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Size, fungibility, and the strength of lobbying organizations

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ABSTRACT

How can a small special interest group successfully get an inefficient transfer at the expense of a much larger group with many more resources available for lobbying? We consider a simple model of agenda setting where two groups of different size lobby a politician over a transfer from one group to the other, and the group which sets the agenda can choose the size of the proposed transfer. The groups have resources which are used to pay the politician and to overcome the public goods problem within the group. Our key result is that which group prevails in the agenda setting game depends crucially on whether the transfers can also be used to pay the politician – in which case we say they are *fungible*. If the transfer is fungible, as in the case of a monetary payment, the smaller group prevails. If the transfer is non-fungible the result depends on whether it is rival or not – civil rights for example are non-rival. In the case of a rival non-fungible transfer depending on circumstances either group may prevail. In the non-rival case the large group prevails. Our results explain the apparent paradox that when it comes to special financial favors small groups seem very effective, but when it comes to large non-financial issues – such as minority rights – large groups are more effective.

1. Introduction

We analyze two groups of different sizes lobbying a politician over a transfer payment between the two groups. We are particularly interested in how the agenda is set: that is, not just whether the transfer takes place and in which direction, but how the size of the transfer is determined. In particular, we ask when a small group might be successful in lobbying against a larger opponent. Why do bankers and farmers "win" over taxpayers? Why, on the other hand, do minorities find their rights suppressed?

To place our work in the context of the extensive literature on lobbying, there is a basic puzzle about lobbying: how can a small special interest group successfully get an inefficient transfer at the expense of a much larger group with many more resources available for lobbying? Olson (1965, 1982) and others such as Becker (1983) originally argued in favor of the proposition that small groups are likely to be more effective than large groups. A large literature both empirical and theoretical has grown out of this. The empirical results on the relation between group size and strength are mixed, see, for example, the survey by Potters and Sloof (1996). Much of the theoretical literature has focused on the issue of lobbying as a public good arguing with voluntary contribution and depending on excludability a small group may have an advantage because it faces less of a public good problem – see for example Chamberlin (1974), Pecorino (2009) and the recent surveys by Sandler (2015) and Pecorino (2015). We focus here on the important and common case where exclusion from the benefits of the transfer are not practical. In this case a theory of voluntary public goods provision runs into the problem known in voting theory as the paradox of voting: with some noise in observing individual behavior

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when the group is large the free-rider problem dominates and there will be little or no individual contribution to the lobbying effort. Such a model also predicts that it is the absolute rather than relative size of groups that matters. This seems inconsistent with the fact that lobbying groups are effective in countries of very different sizes. Hence we take a different approach grounded in the Olsonian idea that large groups face greater organization costs. Specifically we assume that the public goods problem can be overcome by monitoring and punishing individual group members for failing to contribute and that this organizational effort takes the form of a fixed cost per member.[1] A formal model of monitoring leading to this result can be found in Levine and Modica (2016) and a similar approach is used in the study of voting by Levine and Mattozi (2016). In this context it is the relative not absolute size of groups that matters and the advantage of a small group arises not because it faces a smaller public good problem, but because it faces a lesser organizational cost.

In analyzing a small versus a large group there are two forces at work. On the one hand the small group has an organizational cost advantage. On the other hand the large group has more resources to use for lobbying. Hence if the stakes are large, the large group may find it worthwhile to pay the additional cost and exploit its resource advantage to succeed in the lobbying contest. This in turn suggests that if the smaller group controls the agenda they may wish to moderate their demands so that the large group does not find it to their advantage to pay their higher organizational costs. We find that the extent to which this works depends crucially on the nature of the transfer. Our main finding is that fungibility – whether the prize can be used to pay for itself – plays a key role. For example monetary subsidies such as farm subsidies are fungible since they can be used to pay the politicians who provide the subsidies, while benefits such as civil rights are not fungible as they do not increase the resources available for lobbying. When the prize is fungible it is indeed the case that the small group prevails – and it does so by making a modest demand. When the prize is non-fungible but rival the situation is more mixed: the small group may still prevail but only if resources available for transfer are relatively small and the cost of organization relatively high. If the prize is non-fungible but non-rival – for example rights which benefit each group member equally regardless of the size of the group – then the small group never prevails – the combination of limited resources and the fact that the larger group benefits more from the transfer cannot be overcome.

Our model potentially provides an explanation of the following paradox: Olson (1965) and others provide substantial evidence that small groups are effective at winning subsidies while larger groups are not. However we also observe frequently the suppression of minority rights by a majority; here the larger group trying to deny rights seems much more effective than the smaller group trying to keep their rights. We propose that the reason is due to the role of fungibility – small groups are effective in garnering small prizes regardless of fungibility, while large groups are effective only in garnering large non-fungible prizes – and civil rights seem to be in that category. In our conclusion we present some evidence that indeed small groups are much more effective at garnering fungible than non-fungible prizes.

In analyzing an endogenous agenda we suppose that the politician chooses an agenda setter, the agenda setter chooses an agenda (in our case the transfer size), then the two groups bid to determine whether the agenda will be implemented. There are a variety of models of the final stage of lobbying: for example Dixit et al. (1997) and Rama and Tabellini (1998) study lobbyists who purchase influence in a menu auction.[2] We show that the crucial feature of the mechanism by which influence is purchased is whether it is done by some form of auction or by a take-it-or-leave it demand by the politician. We take an agnostic position on this, arguing that the bargaining strength of the politician determines which the form of mechanism will be and allowing varying degrees of bargaining power. Our main results are not sensitive to the level of politician bargaining power. Although we focus is on the case where the politician must affiliate with one of the lobbies prior to agenda setting we also consider the possibility the politician might try to "extort" the lobbies by threatening each with the agenda of the other if they do not pay up. In practice this is probably dangerous, and we show that in some circumstances it will result in the lobbies colluding to get rid of the politician.

The literature on lobbying and other interest groups is large. Models such as ours of "politicians for sale" have fallen into four categories. Some treat the strength of the group as a black box and proceed with a working assumption, generally one in which strength decreases with size (Olson, 1965; Becker, 1983, 1986), or in the case of Acemoglu (2001) that strength increases with group size for a relatively small and a relatively large group.[3] A second class of models treats collusive groups as individuals – effectively ignoring internal incentive constraints – and focuses instead on information differences between the groups: examples are Nti (1999), Persson and Tabellini (2002), Kroszner and Stratmann (1998), Laffont and Tirole (1991), Austen-Smith and Wright (1992), Banks and Weingast (1992), Damania et al. (2004), Green and Laffont (1979), Laffont (2000) and Di Porto et al. (2013). Dixit et al. (1997) is similar, but allows the endogenous possibility that groups either act non-collusively, or collusively as a single individual. A few papers assume that leaders of the group can distribute benefits differentially (this may or may not be what Olson (1965) has in mind by "selective incentives"[4]) so that there is no public goods problem: see for example Nitzan and Ueda (2011) and Uhlaner (1989). Finally Pecorino (2009), Lohmann (1998), Esteban and Ray (2001) and Esteban and Sakovics (2003) treat the problem of

[1] See Pecorino (2015, pp. 253–254) for some related efforts to incorporate fixed costs.

[2] Those papers do not analyze the effect of group size. Other work such as Dixit (1987) examine contests with random outcomes. Those models are well-suited to analyzing conflicts but less well-suited to studying lobbying where the politician selling favors can determine the winner.

[3] This is consistent with our results, since we show that strength increases with size for a small group, and for a relatively large group, the opposition is small, and therefore weak.

[4] Olson's concept is a bit slippery. He may have in mind people who are not in a group benefiting from the activity of the group – although this view of voluntary group participation runs somewhat counter to his notion of what constitutes a group. He argues that the group should devise auxiliary services (free lawyers, insurance) which "selectively" benefit only group members. It is not entirely clear why it would not be better to free ride on the group and pay directly for the auxiliary services, unless the group has some cost advantage in providing those services. In our setting members do not have the option of leaving the group – which is to say that they cannot avoid being punished by group members. For example, farmers cannot avoid being shunned by neighboring farmers by refusing to join a farm association. There are some useful efforts summarized in Pecorino (2015, pp. 255–258) to clarify this notion of Olson's.