
The Political Economics of Campaign Finance

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The public debate over campaign-finance reform is often framed as necessitating an unfortunate tradeoff between the liberal ideals of free speech and association on one side and the democratic ideals of equal representation and participation on the other. But despite frequent calls for dramatic action, the terms of the tradeoff are not well-understood. In this regard as in others, the study of the political economics of campaign finance is more notable for its faults and oversights than for its contributions. Scholarly work on campaign finance provides little basis for a cost-benefit analysis of proposed campaign-finance reforms.

First, no one has analyzed systematically the effects of campaign-finance regulations on freedom of speech or association. Are such regulations enforced in an even-handed or a haphazard manner? Are they enforced at all? How do campaign-finance regulations affect the nature of citizen participation and public debate? Are corporate, labor, and other interest groups equally constrained? Are organized interest groups less hampered by regulation than more ad hoc coalitions? It is difficult to evaluate the desirability of either current laws or proposed reforms when the potential costs of various policies have been completely ignored by scholars and policy makers alike.

Second, we do not know much about the supposed benefits of campaign-finance regulations. Despite a plethora of research on how money affects either electoral or policy outcomes, the quality of those studies is often wanting. Recently, important methodological advances have been made in the empirical analysis of the electoral consequences of campaign spending, although no strong consensus has been reached on the importance of money in elections (e.g., Grier 1989; Levitt 1994; Ansolabehere

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and Snyder 1996b; Erickson and Palfrey 1998; Gerber 1998; Milyo 1998a). In addition, several admirable empirical studies of campaign contributions focus on the allocation of funds by political action committees (PACs) to congressional incumbents (e.g., Snyder 1990, 1992 and 1993; Grier and Munger 1991a, 1991b; Grier, Munger, and Roberts 1994). Though not unimportant, PAC contributions represent a small and declining share of total campaign contributions—down to about 15 percent of all contributions to federal candidates in 1996. Further, no consensus exists in the research literature as to whether campaign contributions are the functional equivalent of bribes (Lowenstein 1996; Milyo 1998b). Finally, several relevant insights from the theory of social choice have not been applied to the question of how campaign finance affects the democratic process.

In this article I deal primarily with the last two questions: Are campaign contributions interested, and if so, should we care? I argue that contrary to the apocalyptic rhetoric of some reformers, interested money plays a less deleterious role in American politics than is commonly held.

The Conventional Wisdom

The corrupting influence of money in politics is a staple of media pundits, public-interest advocates, and even many politicians. The basic claim is that interested money perverts the democratic process in three ways: (1) campaign contributions buy legislative favors, (2) campaign expenditures buy elective office, and (3) popular disgust with the dominant role of money in politics causes ordinary citizens to withdraw from participation in the political process. Consequently, the current system of campaign finance is thought to undermine the twin democratic principles of representation and participation.

It is not difficult to find lurid examples and descriptive statistics consistent with the claim that money is the driving force in American politics (Stern 1991, 1992; Morris and Gamache 1994; Makinson and Goldstein 1996). For example, usually in electoral contests the candidate who spends more money wins. Further, when incumbent officeholders run for reelection, they usually spend far more than their challengers, and they usually win reelection easily. Also, PAC contributions flow disproportionately to incumbents, and those incumbents often vote in ways that please the sponsors of their donor PACs. The funding advantage of incumbents is compounded because the absence of serious competition permits many incumbents to build up large stockpiles of unspent campaign funds. To the extent that those war chests deter future challengers, the incumbents become more securely entrenched in office. Finally, turnout in elections has been generally decreasing and campaign spending generally increasing. Yet, notwithstanding the foregoing familiar facts, more systematic evidence and more sophisticated analysis tend not to corroborate the conventional wisdom.

Empirical Studies of Campaign Finance

The conventional wisdom on the role of money in politics stands in disturbing contrast to the findings of most academic research on the topic (to the great frustration of those of us doing the research). In short, most academic experts would agree that it is very difficult to find consistent and convincing evidence that interested money buys either elections or policy favors (e.g., Sorauf 1992; Levitt 1995).

One important implication of recent empirical research on campaign finance is that the marginal value of a campaign contribution is quite small, both to the recipient and to the donor, because current law limits the size and source of contributions and because marginal campaign spending appears to have little effect on electoral outcomes (Levitt 1994; Milyo 1998a). Corroborating evidence comes from studies that demonstrate that neither candidate wealth nor campaign war chests deter challengers (Ansolabehere and Snyder 1996a; Milyo and Groseclose 1998). Therefore, it is not surprising that there is little evidence that PAC contributions influence the roll-call voting behavior of legislators (e.g., Bronars and Lott 1998; Levitt 1998).

These findings are consistent with the fact that relatively little money flows into political campaigns. For example, aggregate contributions to federal candidates and parties during the 1995–1996 electoral cycle totaled just over \$2 billion (Miller 1997). This amount is equivalent to about 0.02 percent of GDP, or roughly one-third of the amount contributed to the United Way during the same period. Note that Americans donated over \$300 billion to charitable causes during that period, and corporations alone gave more than \$15 billion. Further, case studies of major corporations suggest that the funds spent on charitable activities by major firms are about ten times greater than the combined total amount devoted to political activities by those firms, their associated PACs and their employees (Milyo 1998b). If campaign contributions were the functional equivalent of bribes, we might expect much more money to flow into political campaigns. Consequently, most political contributions should be considered relatively *uninterested* money.

Soft Money

An important distinction must be made between campaign contributions to candidates and PACs, which are limited by the Federal Election Campaign Act, and those to parties or issue-advocacy campaigns, which are not currently limited. Money raised in accordance with federal contribution laws is known as “hard money”; such contributions may be spent on any type of political advertisement. “Soft money” includes any donation to a party or other group that does not qualify, by either amount or source, as hard money. Soft money may be used for generic issue-advocacy advertisements but not for advertisements that explicitly advocate voting for or against a particular candidate. Of course, the generic issue-advocacy activities are sometimes close substitutes

for campaign advertisements. Further, soft money contributions to the state and national political parties allow those parties to transfer more hard money to candidates (Dwyre 1996). Consequently, soft money contributions have been the target of numerous recent reform efforts.

Soft money contributions are more likely to be effective “bribes” than are direct campaign contributions to individual legislators, because soft money contributions are unlimited in amount and because political parties have various methods of disciplining their members and delivering political favors. Nevertheless, soft money contributions to the two major national parties amounted to less than \$275 million during the 1995–1996 electoral cycle, equivalent to 15 percent of the hard money spent during that period. Further, 93 percent of all soft money was raised in amounts of less than \$20,000 (www.fec.gov).

It is difficult to reconcile the relative dearth of soft money with the notion that such contributions constitute effective bribes. But it is consistent with the claim that most hard money contributions are uninterested and that the sheer volume of those contributions drives the marginal value of campaign contributions down so far that interested money has little incremental value to politicians. Thus, so little interested money flows into politics because it does not buy much legislative action. However, an important caveat must be made here: no one knows how much money is spent on generic issue-advocacy campaigns or more subtle attempts to manipulate popular opinion (e.g., the content of popular entertainment programming). Consequently, it is difficult to assess the degree to which interested money affects American politics through this soft money “loophole.” Nevertheless, we have good reason to doubt the popular understanding of the role of money in politics.

Moreover, even if interested money does play an important role in American politics, it does not follow that the basic principles of democracy are being ill-served, because interested money also has some salutary effects on majoritarian politics.

Lessons from the Theory of Social Choice

The most significant conclusion of social choice theorists in the last half century is that no collective decision rule can always satisfy a certain reasonable set of “rationality” conditions (Arrow 1963). Further, given a collective of heterogeneous individuals, several different methods can be used to aggregate their individual preferences into a collective preference, each method being arguably consistent with the democratic ideals of representation and participation, but those methods produce different collective choices (e.g., Riker 1982).

In light of the foregoing conclusions, it is not obviously undesirable for interested money to produce deviations from what would otherwise occur under simple majority rule. After all, pure majority rule is irrational, inasmuch as a pure majority-rule equilibrium almost never exists (Plott 1967). Worse yet, under majority rule,

agenda setters wield extreme influence over outcomes (McKelvey 1976). Finally, in large elections voters have little reason to vote responsibly (Brennan and Lomasky 1993). It is therefore not unreasonable to view interested money as a check on the power of political agenda setters or the whims of a less interested and temporary majority (Hayek 1960).

What Is Democracy?

In common parlance, democracy has come to mean simple majority rule. Institutions that hinder action by simple legislative majorities, whether they be internal to the legislature (the filibuster, the committee system, party leadership, supermajority rules) or external (executive vetoes, judicial overrides)—are often decried as undemocratic. In this perspective, outside pressure from special interests in the form of lobbying or campaigning is undemocratic because it may change the legislature's choice. However, deviations from simple majoritarianism are widely accepted, even strongly preferred, in certain venues. For example, supermajority rules are used for altering the Constitution and for jury decisions, although plurality rule is used to decide the outcomes of most elections. Clearly, the frequent equation of democracy and simple majority rule in common parlance signals imprecise language and intellectual laziness more than it evinces a popular consensus for such a narrow understanding of democratic decision making.

A more sensible definition would denote as democratic any institutions that limit the inevitable inequalities of representation and participation to some tolerable level. Of course, having accepted such a definition, one cannot draw a bright line between democratic and undemocratic institutions. Consequently, once we adopt a more expansive understanding of democracy, it becomes more difficult to maintain that the presence of interested money in politics is necessarily undesirable.

Control of the Legislative Agenda

The intransitivity of pure majority rule is more than just a theoretical curiosity. The inherently chaotic tendencies of pure majority rule lead legislatures to adopt rules of procedure that constrain legislative choice and empower agenda setters. Procedural rules typically limit the feasible set available to the legislature, dictate the order of consideration of the feasible options, and restrict the mechanism of choice to a series of binary (yea, nay) votes. The ability to manipulate the content and ordering of the legislative agenda permits party leaders to wield significant influence over the outcomes of legislative choice (Cox and McCubbins 1993). However, free and open public debate can focus the attention of the electorate and raise the cost of agenda manipulation.

For example, issues such as campaign-finance reform, term limits, and balanced-budget restrictions are typically far less popular among legislators than among the

general public. Party leaders often block such issues from even coming up for debate. However, in many instances, special-interest groups have successfully raised public awareness of and concern about these issues and forced them onto the legislative agenda. Thus, allowing interested persons to lobby their representatives and fellow citizens reduces the power of agenda setters. At the same time, participants in the public debate come to consider new information and arguments. Of course, some misinformation and illogic will also be injected. But it is hardly self-evident that the social costs of issue advocacy and lobbying outweigh their social benefits.

Representation of Intense Interests

Even if we ignore the pervasiveness of intransitivity, pure majoritarian institutions are deeply flawed on normative grounds. Simple majority rule is the most direct implementation of the principle of “one person, one vote,” and although this principle is held in great esteem, its appeal stems partly from the implicit assumption that all persons have an equal stake in the collective outcome. That is clearly not the case in what we might call “private” matters; indeed, a generic right to privacy is so well accepted that few Americans would find that the existing constitutional guarantees of their individual liberties are “undemocratic.” The great flaw in majoritarian institutions is that each individual’s preference is weighted equally, even though individuals differ enormously in the intensity of their preferences.

Supermajority requirements are one common method of accounting for the intensity of individual preferences. Such rules permit the votes of an intensely concerned minority to outweigh those of a less concerned majority. However, such rules may also permit an unconcerned minority to thwart the desire of an intensely concerned but insufficiently large majority.

A second method of incorporating intensity of preferences in the collective choice process is to give disproportionate weight to the preferences of intense minorities. The committee system in Congress can be viewed as an attempt to do so: preference outliers seek membership on committees with narrow policy jurisdictions, and the rules of the House and (to a lesser extent) the Senate permit committee members disproportionate influence over legislation in their jurisdiction (Weingast and Marshall 1988).

A third method of incorporating the intensity of interests is simply to permit deliberation and debate. By communicating their positions, intensely interested persons can better inform the collective about any disproportionate effects of a policy or, at least, appeal to the magnanimity of the less intensely interested. Because not all interests will be well represented in a given legislature and because effective persuasion may be quite costly, groups will naturally form around common interests and pool their resources for the purpose of influencing the decisions of the legislature or the opinions of citizens at large. Consequently, special-interest lobbying and issue-advoc-

cacy activities serve a socially desirable function: they permit at least some minority interests to inform the collective about the intensity of their preferences.

A final method of incorporating information on the intensity of individual preferences into the collective choice process is vote trading. Within legislatures, such exchanges are known as log-rolls. Being voluntary, these vote trades necessarily work to the expected advantage of the interests entering into them. Further, in majoritarian institutions, vote trading necessarily involves minority interests, as otherwise the majority would simply pass its preferred legislation directly. Consequently, through log-rolling, minority interests improve their lot by “buying” legislation dear to them at the cost of supporting legislation relatively unimportant to them (but dear to some other minority interest). In this way, majoritarian institutions become more responsive to minority interests.

An indirect form of vote trading occurs through campaigning and elections. Intense interests provide support to candidates in exchange for political favors. However, candidates who cater only to special interests risk alienating large segments of the electorate. Consequently, candidates must expend resources to inform and persuade the electorate. Thus, candidates serve as arbiters, both between competing groups of intense special interests and between intense special interests and the unconcerned majority. If the interests of minority groups are sufficiently intense, then those groups will provide enough support to candidates that the candidates can then afford to ignore the interest of the majority on the issue in question. Of course, it is easy to envision contexts in which such an outcome is normatively either appealing or appalling, but the same is also true of pure majoritarianism.

Voter Participation

Rational-choice theories of voter participation posit that individuals weigh the benefits of voting against the costs. The benefits of voting consist of the satisfaction of the act itself and the expected change in the outcome of the election that results from one vote. The costs of voting include the time and effort required to actually cast a ballot; for example, registering to vote, becoming informed about candidate positions, finding the appropriate polling place, and queuing to vote. It is widely appreciated that in large elections the probability that a single vote will be decisive is essentially nil, so the decision to vote turns on a simple weighing of the intrinsic value of the act against its costs.

It is often claimed that public disgust with campaign finance helps to account for declining voter participation. The main evidence for this claim is the fact that campaign spending and turnout have been moving roughly in opposite directions over the last fifteen years. This observation is consistent with the claim, but it is scarcely convincing evidence of a causal relationship.

Does campaign spending cause voter apathy by lowering the intrinsic value of voting? If so, we might expect that individuals with more cynical views on campaign

finance, party politics, and government would be less likely to vote. A recent poll of voters and nonvoters commissioned by the League of Women Voters suggests that is not the case: nonvoters hold views very similar to those of voters (www.lwv.org/lwus/mellsumm.html). The major difference found between voters and nonvoters is that the latter have a higher opportunity cost of time and are less likely to feel strongly that they have a duty to vote. This evidence is consistent with the rational-choice theory of voting but gives no support to the claim that the prevalence of interested money in politics reduces voter participation.

It may be, however, that interested money depresses turnout in a more indirect fashion. Because interested money flows primarily to incumbent officeholders, the dramatic increase of campaign spending may have reduced the competitiveness of elections and thereby lowered turnout. But this argument has two serious flaws.

First, as I have shown elsewhere (Milyo 1997), congressional elections have actually become more competitive as campaign spending has jumped. Despite an increase of real incumbent spending and no change in the proportion of experienced challengers, House races have become closer, incumbents have drawn down their war chests, defeats have increased, and the proportion of unopposed incumbents has dropped. The increased competition for partisan control of Congress is surely one of the primary causes of the upward trend of aggregate campaign spending. Further, the failure of increased competitiveness to cause a similar increase in the voter-participation trend is consistent with the view that the instrumental value of voting does not drive an individual's decision to vote.

The second flaw in the logic is the presumption that electoral competitiveness would raise turnout in large-electorate contests. It is true that empirical studies of elections repeatedly find that turnout is significantly correlated with the closeness of the electoral race. It is also true that many rational-choice theorists have interpreted this finding as evidence consistent with the rational-choice theory of voting, the idea being that an individual's vote is more likely to be decisive in a close race. However, in large elections, the probability of casting a decisive vote, even in a close election, remains negligible. Consequently, changes in the expected closeness of an election should not have a significant and direct effect on turnout.

The observed correlation between turnout and closeness is not evidence of a proximate causal relationship. Rather, greater electoral competition causes increased spending, which in turn causes increased turnout. Electoral competitiveness raises campaign spending for two reasons. First, the expected closeness of the election increases the propensity of donors to give to candidates and causes candidates to expend more effort on raising funds. Second, because campaign spending is used largely for campaign advertisements, voter interest is peaked in districts bombarded with numerous advertisements. In fact, voter turnout is significantly related to campaign spending even when controlling for the closeness of the race (Milyo 1998c).

In sum, there is little support in either theory or empirical analysis for the claim that the presence of interested money in American elections has caused the general decline in voter turnout.

Conclusion

Participants in the public debate over campaign-finance reform have generally assumed that interested money corrupts democratic politics. However, recent empirical studies indicate that interested money does not play an extremely influential role in federal elections. More importantly, the theory of social choice informs us that the net effect of interested money on the democratic ideals of representation and participation is ambiguous. My appraisal places a greater burden on reformers: a cost-benefit analysis of campaign-finance reform must consider not only the real costs of regulation on free speech and association; it must also demonstrate a net positive effect on democratic procedure.

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