

## Chapter 16

# Rent Seeking

Public Choice begins with two assumptions about members of a collective. First, while they appreciate the wealth-producing potential of a market economy, they have wants for public goods. Second, they believe that they can benefit by making a collective agreement to cause the supply of these goods. In contemplating the agreement they will make, they are immediately confronted with high costs of making collective decisions. To avoid or reduce these costs, they agree on a rule of less-than-unanimity for making laws. In addition, they elect agents (legislators) to make laws in their behalf.

This combination gives people an incentive to try to influence the actions of legislators and enforcers. Sometimes the people aim to correct for market failure. Sometimes they promote laws and administration that benefit themselves at the expense of other members of the collective. Actions of the latter sort are called rent seeking.

Rent seeking pertains to laws and/or administrative actions that most people would regard as harmful, or wasteful, *in net*. In a

Two types of rent seeking in a market democracy:

1. Market privilege rent seeking.
2. Redistribution rent seek.

system where the conditions of the market economy already exist, there are two kinds of such laws or administrative actions. The first grant

special market privileges to some people while taking privileges away from others. By interfering with free enterprise, the granting of such privileges reduce the market economy's wealth generating capacity. It reduces economic efficiency. The second redistribute wealth. This kind does not interfere with free enterprise, although it affects incentives to produce wealth. Thus we distinguish between two kinds of rent seeking: (1) market privilege rent seeking and (2) redistribution rent seeking. Most of the discussion in this text will be about the first kind.

There is a variety of ways that an individual can try to influence laws and their administration. For example, when you vote, you hope to elect a candidate who will vote for laws that are in your interest. And, if you are a typical voter, you probably pay very little attention to whether those laws harm others. However, ordinary voting is not rent seeking. *Rent seeking consists of legitimate, non-voting actions that are intended to change laws or administration of laws such that one individual and/or group gains at the same or greater expense to another individual or group.*

Consider a real-world example of market privilege rent seeking. Suppose that a U.S. steel company is losing money because of competition from Asian or European steel.<sup>1</sup> Suppose further that the company bosses believe that they can eliminate the losses in two ways. First, they can modernize by building a new factory. Second, they can hire a lobbying company and make campaign contributions to legislators in order to persuade them to pass a law blocking imports of foreign steel. If the lobbying and campaign contributions cost less than the factory, the company would choose the lobbying.

Rent seeking: non-voting, non-criminal actions that are intended to change laws or administration of laws such that one individual and/or group gains at the same or greater expense to another individual or group.

If the lobbying succeeds, people in the society would be worse off for two reasons. First, there would be an increase in the price of steel. In the typical economic model, this means inefficiency because the benefits to the gainers are less than the losses to the losers. Second, resources that would otherwise be used to produce useful products would have been used in activities intended to produce the law. In other words, the resources used to promote the law would be wasted.

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<sup>1</sup>This example was used by Tullock (1989: 55-56).

Many large companies today in the more developed democracies employ resources to seek market privilege. The result is

Defensive lobbying: lobbying aimed at avoiding the harm that other peoples' lobbying and other rent seeking actions are likely to cause.

a large lobbying industry. The lobbying industry is even larger than otherwise because of what we might call *defensive lobbying*. This is lobbying aimed at avoiding the harm that other peoples' lobbying and other rent seeking actions are likely to cause.

In the U.S., many large firms make a contract with a professional lobbying firm or they hire people directly in order to influence legislators, the president, and voters. In the newer democracies, the relationship between politicians and firms is often more direct. The companies simply bribe the politicians or assure with their campaign contributions that the politicians are reelected, that their families are cared for, etc.

We define rent seeking to be a legal act. Accordingly, if bribery is illegal, the act of bribing a legislator to vote for a law is not rent seeking. In some societies, however, the distinction between the legal and illegal acts is not so clear. Where bribery laws exist but are not enforced or are not enforced vigorously, it is not easy to distinguish legitimate rent seeking actions from corruption.<sup>2</sup>

In economic models, we can define rent seeking precisely. This is because we can define efficiency precisely in our models. In practice, it is not so easy to tell the difference between rent seeking and other actions that aim to influence laws.

In everyday life rent seeking can become extremely complex and each case is different. We cannot describe it fully here. Our purpose in this chapter is to describe the basic idea and to give some simple examples. Parts one and two discuss rent seeking that is aimed at achieving market privileges. This is the kind of rent seeking about which Public Choice scholars have written the most.<sup>3</sup> Part one presents two types of market privilege rent seeking: the case of a single firm wanting a monopoly and

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<sup>2</sup>This definition corresponds to that used by Susan Rose-Ackerman in her classic book on corruption. See Rose-Ackerman (1978: 7-8).

<sup>3</sup>For additional references, see Aranson's excellent discussion (Aranson 1989: 110-6). Also see Robert Tollison's 1982 survey. The term "rent seeking," as it is now understood, was first used by Anne Krueger (1974). Many of the important academic articles on this subject are contained in two collections, one edited by Buchanan, Tollison and Tullock (1980) and the other edited by Rowley, Tollison, and Tullock (1988).

the case of domestic firms wanting protection from foreign competition through a tariff. Part two uses Buchanan's example of taxi services to illustrate different levels of market privilege rent seeking. Such a procedure is necessary in order to analyze more complex rent seeking cases. Part three presents an example of market privilege rent seeking. Part four describes redistribution rent seeking. Part 5 discusses rent seeking in a broader context in which the conditions of the market economy are not initially established. This is the situation present in many less developed economies and in so-called rentier economies, in which the government is financed by selling collectively-owned natural resources.