

Design of Constitutions

Edited by

Stefan Voigt

*Director, Institute of Law and Economics
University of Hamburg, Germany*

ECONOMIC APPROACHES TO LAW

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Direct Democracy: Designing a Living Constitution

Bruno S. Frey and Alois
Stutzer

2.1 Introduction

In this chapter we analyze the competition between various interests to control the state, including the power to change its basic laws. We apply a comparative view to evaluate initiatives and referendums as mechanisms for institutional change. The reference standard is a purely representative democratic system (as is still dominant in most countries) in which members of parliament decide on constitutional issues such as basic rights, the scope of democratic decision-making and of market exchange, and the organization of the judiciary and federal structure of the country. Section 2.2 briefly describes direct democratic decision making in general, and lists where it has been applied. Section 2.3 analyzes the effects of providing for direct citizen involvement through initiatives and referenda. We focus on three aspects: (1) the difference induced in the principal-agent relationship between citizens and politicians, when citizens have agenda control via initiatives and can ask for a referendum on new legislation; (2) the process of direct democratic decision making; and (3) the protecting influence of referenda against the risk of overcentralization. Empirical evidence for all three aspects is provided in section 2.4. Section 2.5 discusses arguments for and counterarguments against direct democracy. Issues for designing a constitution that includes direct participation rights for the citizens, especially in the context of the European Union, are taken up in section 2.6. Last section 2.7 offers some concluding remarks.

Direct democracy fundamentally changes the *process* of political decision making. It is not only that politicians are more restricted to follow citizens' preferences, but the direct involvement of the people changes their motivation when they act as voters, taxpayers or fellow citizens (Frey 1997). This can explain systematic differences as to how

well aware of political issues people are, whether they can build up a relationship based on trust to public authorities, and whether they have a preference for, and gain procedural utility from, direct democratic participation rights as such.

The Proposal by the Convention of the European Union delivered in June 2003 presents a *unique chance to write a constitution for this century, and for those to come*.¹ It represents a rare window of opportunity for designing a constitution for one of the major political units of the world. It is very likely that few, if any, ground rules of such relevance can be written in the near future. The Convention could not start from scratch—no designers of any constitution ever can. In the case of the European Union there are various previous treaties, such as those of Maastricht, Nice, and Amsterdam, as well, of course, as the founding Treaty of Rome in 1956, that have to be taken into account. Nevertheless, the entry of ten new member states in 2004, as well as the likely future entry of five or so additional countries, should have allowed the Convention to draft pathbreaking new rules for the future European Union.

This opportunity was missed. The Convention understood its task quite differently, namely as an *exercise in compromise*. Granted, the Convention had a difficult task to fulfill. The new EU constitution has to meet with the agreement of all the member countries. So the support of the existing 25 members must be sought. This is no small task, considering that the interests of the nations can differ in a great many respects. Most important, two fundamentally different interpretations of the European unification clash with each other. The *first* interpretation sees the European enterprise as essentially an *economic* one. The Union is to guarantee *free trade* in terms of the movement of goods, services, labor, and capital. Political interventions should only serve to keep the borders open, to prevent trade distortions by subsidization, and other interferences distorting relative prices. The *second* interpretation sees the goal of the European enterprise as a *political* one. Europe is to move to “an ever closer union” (in the words of the former president of the Commission, Jacques Delors) and end up as a “United States of Europe.”

Accepting the “necessity” of a compromise, the focus should already today lie on the development of the European constitution in the future, namely on the question of *amending constitutions*. This chapter suggests that direct democracy should play a central role in every constitution’s amendment process.

2.2 Direct Democratic Decision Making and Its Diffusion

There are many different meanings, conceptions, and also misunderstandings about what “direct democracy” is. The two crucial features of the term “direct democracy” are discussed here.²

Referenda and Initiatives as Additional Rights

Direct democracy (or, more precisely, semi-direct democracy) does not substitute for parliament, government, courts, and all the other features known in representative democracies. Instead, it shifts the final rights in determining issues to the citizens. The extent of direct participation rights may vary, but they always include constitutional changes, normally by an obligatory referendum. Optional referenda and initiatives (allowing citizens to put issues on the political agenda) require a predetermined number of signatures by the citizens before they can take place.

From a historical perspective, three main stages of democracy may be distinguished:

- Classical democracy, first developed in Athens and other Greek city-states. Participation rights were restricted to male citizens, thereby excluding a large number of the population, and extended only over a small area of a town. Yet the principles of democracy still revered and used today were developed there.
- The French Revolution extended democracy over a large area. The principle of representation made it possible to introduce indirect political participation to the nation state.
- Direct democracy combines these two earlier types of democracy by giving every citizen the right to decide on certain issues. The extreme (classical) form of having citizens decide on each and every issue is practiced nowhere today, but the number of issues on which citizens may vote varies widely between countries.

Over the period 1990 to 2000, no less than 405 popular referendums on the *national level* were recorded (see Gross and Kaufmann 2002; Butler and Ranney 1994). More than half took place in Europe, namely 248 (and again half of them in Switzerland); 78 in America, 37 in Africa, 26 in Asia, and 16 in Oceania.³ In the decade before (1980 to 1990), there were only 129 national referenda. Up until August 2002

issues of European integration led to no less than 30 national referenda.⁴ There are a very large number of popular referenda at lower levels of government. In the German state of Bavaria, there were as many as 500 since its adoption. In Switzerland, there are thousands of referenda at all three levels of government: local, cantonal, and federal. In the United States, the initiative and referendum process is available to citizens in 24 states. Since 1904 when the first statewide initiative appeared on Oregon's ballot, approximately 2,021 measures have been placed on the voting agenda and many more referenda (Waters 2003).

Most democracies do not allow the general electorate to participate in taking important decisions. Nowhere (except in Switzerland and Liechtenstein) are popular referenda used in a regular and systematic way at the national level. In the United States, despite its many local popular decisions, and its frequent use in some states, such as California and Oregon, there is no referendum at the national level. Many important decisions shaping a country's fate for decades to come are not subject to a popular referendum. A telling example is Germany. The citizens had no say either with respect to the conditions for the integration of the former GDR or the dumping of the deutsche mark and introducing the euro. Directly democratic decisions are in many cases not taken seriously by the politicians in power. A revealing example is the Irish vote on the Nice Treaty of the European Union. The citizens rejected it in June 2001. Before the second vote on the issue, due to take place in August 2002, EU politicians made it clear that they would go ahead with the Treaty's program, regardless of whether the Irish vote be positive or negative (though unanimity within the European Union is required).

Referenda and Other Forms of Consultation of Citizens

Referenda are a right given to the citizens by the constitution. Government and parliament are bound by these rights: they are not free to ask the opinion of the citizens only when it suits them. This distinguishes referenda from plebiscites undertaken by governments to ex post sanction a decision already taken by them. With plebiscites, the citizens are not asked to decide on an issue, but only to express their support of the government. Referenda also fundamentally differ from opinion surveys, which are on the spot views of people, without any consequences for the government: they can choose to act in accordance with the results or disregard them. In contrast, when citizens have taken a deci-

sion in a referendum, the constitution obliges the government to put the corresponding policy into practice.

2.3 Working of the Direct Democratic Process

Direct Democracy against the Politicians' Cartel

Politicians against the Voters

Persons acting within the confines of the political system have incentives to exploit it to their advantage. Politicians are not "bad," or any worse than other persons, but they tend to be—as everyone else—self-regarding. They endeavor to further their own interests, which consist not only of material wealth but also of recognition and prestige.

In a democracy, politicians can use three main ways of gaining benefits at the citizens' expense, or "exploiting" the general population:

- Politicians may take decisions that they know to *deviate from the voters' preferences*. Political actors may do so because they have an ideology of their own, because they reap material and nonmaterial advantages by so doing, or because they have insufficient information. For instance, politicians systematically prefer direct interventions in the economy to employing the price system because regulations generally allow them to derive larger rents.
- Politicians secure themselves *excessive privileges* in the form of direct income for themselves or their parties, pensions, and fringe benefits such as cars and houses.
- Citizens' exploitation may take the form of *corruption*, namely of direct payments for special services provided to payers but not to others.

Politicians have a common interest to protect and extend these rents where possible. That means they have an incentive to form a *cartel* against the ordinary citizens. There is, however, a public good problem involved: an individual politician has an incentive to break out, if such action is positively sanctioned by the electorate. Such action can regularly be observed in democracies, but it is rarely of much consequence for the cartel. The politicians in many countries form a close-knit group of people clearly differentiated from the rest of the population. Their main contacts are within the group, so that the social disapproval of the few who dare to break out of the cartel is acutely felt and carries a

high cost. Moreover the cartel is administered by the leaders of the parties so that in most countries and time periods, only a small number are involved, and the breakout of a politician is quickly and effectively sanctioned by the other members of the cartel, for instance, by restricting access to parliamentary positions (in particular membership of powerful commissions) or by reducing the monetary support provided by the state to the parties. Individual politicians find it equally hard not to be a part of the cartel because the leaders of their parties have many means at their disposal to control their politicians, including enforced resignation.

Constitutional Provisions against the Politicians' Cartel All the actors involved, in particular the voters, are well aware that there are strong and ubiquitous incentives for the politicians to form a cartel and to exploit the voters. In response, one finds three quite different forms of institutions in democratic constitutions designed to check such action:

1. Rules prohibiting the (excessive) appropriation of rents by the politicians, the most stringent ones being to prevent corruption. Obviously such rules are only effective if they cannot easily be circumvented and if they are well enforced. Such provisions are completely useless against the first type of exploitation mentioned, namely the systematic deviation from citizens' preferences. As the privileges accorded by the politicians to themselves are of an extremely varied kind and are difficult to detect (especially with respect to pensions), experience shows that politicians' rent seeking can thereby scarcely be prevented. With respect to corruption, only the most blatant cases are found out. It must be concluded that while such rules are of some use, they certainly are not able to prevent the exploitation of citizens to any significant extent.

2. The establishment of special *courts*, with the task of preventing citizens' exploitation. All democratic countries know some institution of courts of accounts, but it may well be shown that they fulfill their role only to a limited extent. They are obviously the less effective, the more directly they depend on the politicians they are supposed to control. In this respect it does not help much if the members of the court of accounts are elected and must answer to the parliament (instead of to the government) because the cartel includes politicians inside and outside the government. Even courts of accounts, formally independent of

government and parliament, have little incentive and possibility of checking the exploitation of the citizens by the politicians. This applies particularly to the deviation from citizens' preferences; it may indeed be shown that courts of accounts, which necessarily have to focus on the formal correctness of politicians' and administrators' behavior, in some respects tend to widen the gap between what politicians provide and what the people want.

3. *Competition between parties* is the classical institution in representative democracies to prevent politicians from pursuing their own goals at the population's expense. Constitutions include various devices to further competition and make a coalition between the politicians more difficult. One is the division of power among the executive, legislative, and jurisdictional branches. Another is the establishment of two houses of parliament. Because of the many types of interactions existing, and the well-defined gains to be expected, these devices are rather ineffective in checking the interests of the *classe politique*.

An important constitutional device for stimulating the competition among parties is to guarantee, and to facilitate, the entry of new politicians and parties into the political system. While this certainly forces the established parties in a democracy to take better care of the people's wishes and to be more careful with regard to privileges and corruption, the effects tend to be short-lived. The previous outsiders quickly realize that many advantages are to be gained by tolerating the politicians' cartel, and even more by participating in it. The experience of many countries supports this theoretical proposition. An example are the "Green" parties, who at first fought against the political establishment, but within a surprisingly short time learned to take advantage of the taxpayers' money for their own purposes.

On the basis of these arguments, it is concluded that neither party competition, nor constitutional rules, nor courts, are particularly successful in reducing the possible exploitation of the general population by the politicians. It is not argued, of course, that the constitutional features elaborated are useless, but that they do not provide a sufficient safeguard against politicians' rent seeking. It is therefore desirable to search for, and to seriously consider, other constitutional means of fighting the politicians' cartel.

Referenda as a Constitutional Provision against the Politicians' Cartel A referendum, which allows all citizens the possibility of

participating, meets the crucial requirement that it gives decision-making power to people *outside* the politicians' cartel. The individuals making the decision are not integrated into the *classe politique*, and they avoid the control of politicians. In an *initiative* the demands are explicitly directed against the political establishment represented in parliament and government. Initiatives allow putting issues on the political agenda that members of parliament prefer not to discuss. *Optional* and *obligatory* referenda serve more of a controlling function because, if successful, they overrule the decisions taken by the executive and the legislative bodies.

A popular referendum (in the widest sense of the word) can only serve its purpose if the *classe politique* cannot block it. In many countries the Supreme Court or, even worse, the parliament, has the power to decide whether a referendum is admissible. The criteria appear to be purely formal, but in fact the members of the *classe politique* have a considerable number of possibilities and incentives to forbid referenda threatening the position of the politicians' cartel. Often vague concepts, based on what *they* consider to be the "raison d'état," are employed. In other countries, such as Switzerland, almost no such possibility exists, and therefore issues may be brought to the vote that are not desired, and are sometimes even strongly disliked, by the politicians.

Empirical evidence shows that referenda can break the cartel among the politicians by getting through constitutional provisions and laws totally against the interests of the *classe politique*. The following cases refer to Switzerland, the referenda nation par excellence. The first two cases concern important historical episodes (Blankart 1992).

CASE 1 During the nineteenth century the house of representatives (*Nationalrat*) was elected according to the majority rule. The largest party greatly benefited from that throughout seven decades, the Radical-Democratic Party secured a majority of the seats. When the idea was raised that the elections should follow proportional representation in order to allow small parties to enter parliament, the then *classe politique* among the executives and jurisdiction strongly rejected this proposal for obvious reasons of self-interest. Nevertheless, in 1918, the corresponding referendum was accepted by the majority of the population and the cantons. In the subsequent elections the Radical-Democratic Party lost no less than 40 percent of their seats.

CASE 2 Until the Second World War, Urgent federal laws (*dringliche Bundesbeschluesse*) were not subject to (optional) referenda. In order not

to have to seek the people's approval, and in order to pursue policies in their own interests, the *classe politique* in the government and parliament often declared federal laws to be "urgent," even if that was not in fact the case. In 1946 an initiative was started with the objective of preventing this disregard for the interests of the population. Again, the executive and legislative bodies urged the voters to reject the initiative, which was clearly one of self-interest. However, the initiative was accepted by the voters, and the politicians are now forced to take the citizens' interests into account when they decide on federal laws.

The history of Swiss voting provides many more examples of such clashes between the opinions of the leaders and the citizens. The politicians have to make great efforts to endorse as quickly as possible any movements originating from outside the cartel. Sometimes it is established parties (but usually at the fringes of the cartel), or associated interest groups, that initiate referenda. If this strategy is to be successful, the politicians have to at least partially take into account the population's preferences, and have to reduce the extent of their rent seeking. The institution of referendum in this case leads indirectly to the desired outcome that the cartel of politicians has less leeway.⁵

Politicians are well aware that the institution of popular referendum severely restricts their possibility of "exploiting" the citizens/taxpayers, and they therefore oppose introducing elements of direct democracy.

Referenda as a Process

It would be mistaken to consider a referendum just to be a vote. Indeed two important stages before and after the vote need to be considered.

The Pre-referendum Process

The constitutional setting determines to a large extent which issues are put on the political *agenda* and which are prevented from appearing. In representative democracies, politicians are often skilled at not letting problems, which are to their disadvantage, be discussed in the democratically legitimized institutions. As has been shown, both theoretically and empirically, agenda setting power has a significant effect on voting outcomes.⁶

An important feature of referenda is the *discussion process* stimulated among the citizens, and between politicians and citizens.⁷

Pre-referendum discussions may be interpreted as an exchange of arguments among equal persons taking place under well-defined rules. This institutionalized discussion meets various conditions of the "ideal discourse process," as envisaged by Habermas (1983). The relevance of discussion for politics induces citizens to participate, depending on how important the issue in question is considered to be. The experience of Switzerland shows indeed that some referenda motivate intense and far-reaching discussions (e.g., referenda on whether to join the European Economic Space with a participation rate of almost 80 percent, compared to an average of roughly 40 percent). Other referenda considered to be of little importance by the voters engender little discussion and low participation rates (as low as 25 percent). This variability in the intensity of discussion and participation overrides the much studied "paradox of voting" (Tullock 1967; Riker and Ordeshook 1973).

The main function of the pre-referendum process is certainly to raise the level of information of the participants (for empirical evidence, see the next section). It may moreover be hypothesized that the exchange of arguments also forms the participants' preferences. What matters most is that this preference formation can be influenced by, but not controlled by, the *classe politique*.⁸

A further important aspect of the referendum process is going beyond outcome considerations. Citizens may benefit from the process as such, as it is well established that people have a preference for participation in decision making because it enhances individuals' perception of self-determination (e.g., Pateman 1970; for an extensive survey, see Lane 2000, ch. 13). With regard to direct democracy, Cronin (1989, p. 11), for example, notes, that "giving the citizen more of a role in governmental processes might lessen alienation and apathy." Moreover the political discussion induced by initiatives and referendums generates a common understanding for different political opinions and positions. This strengthens the social contract based on consensus and motivates people to go beyond acting out of narrow self-interest. Participation possibilities are thus considered an important source of perceived procedural fairness, shaping individual behavior.

Post-referendum Adjustments

In a referendum a political decision is formally made, but this does not necessarily mean that the politicians and the public administration take the appropriate action to implement it. In fact there is substantial vari-

ation on how they react to winning referendums and in particular to initiatives (Gerber et al. 2001, 2004; Bali 2003). Initiatives that are drafted in order to overcome inaction of the government or the parliament often face opposition from the latter actors in the post-referendum process. The groups who launch and support winning initiatives are not authorized to implement and enforce them. They must rather delegate these tasks to the members of parliament or the administration. The position of the initiators is relatively stronger if they are linked to a political party represented in the legislature or if they can rely on an existing and permanent infrastructure. It is most difficult (or impossible) to oversee the implementation and enforcement of initiatives for ad hoc groups and committees that disband after the ballot. The costs for the legislatures and the bureaucrats to oppose winning initiatives in the post-referendum process thereby are the higher, the more legitimate the constitution is taken to be in a political system. The politicians may in particular fear of not being reelected by the voters if they undermine citizens' democratic rights. However, ultimately the extent of implementation depends on whether the constitutional rules are voluntarily obeyed by the persons in power.

The question of which side gets a majority in a referendum is not the only thing that matters. A referendum also clearly reveals how the population feels about the matter, and where and how large the minorities are. Groups dissenting from the majority are identified; their preferences become visible and become part of the political process (see Gerber 1997). This makes it more likely that particular parties start to champion their cause in order to win additional support, and for referenda to take place in particular regions.

Switzerland again provides a suitable example. In 1989 a popular initiative demanded that the Swiss Army be completely disbanded. Many Swiss considered this to be an attack on one of the almost "sacred" institutions of the country. The *classe politique* was totally against the initiative, and the generals threatened that they would retire if the initiative was not overwhelmingly rejected (they spoke of a percentage of no-votes between 80 and 90 percent). The referendum outcome was a surprise to everybody, because one third of the voters (and a majority among the young voters eligible for military service) voted for the dissolution of the army. After a short period of shock, several parties suggested changes in the army which were implemented within a short time—changes which, before the referendum, were considered by everyone to be impossible to achieve.

Referenda and the Protection of Federalism

The institution of citizens directly deciding on an issue and the decentralization of decision making are closely connected. On the one hand, federalism is an *alternative* means for better fulfillment of the voters' preferences: individuals tend to turn away from unsatisfactory jurisdictions, while they are attracted to those caring for the people's preferences at low cost. The possibility to vote with one's feet (Tiebout 1956; see also Buchanan 1965; Hirschman 1970) tends to undermine regional cartels by politicians.

Federalism is, at the same time, *facilitating* effective referenda rather than substituting them. In small communities much of the knowledge *needed for informed political decision making is acquired in everyday life*. The citizens are well aware of the benefits and costs of particular public programs (see also Mueller, chapter 8 in this volume). As taxpayers they have to carry the burden, provided that there is a sufficient amount of fiscal equivalence (Olson 1969, 1986).

It is crucial for the beneficial functioning of federalism that the constitution explicitly assigns competence to spend money, *as well as* to levy taxes, to all the different levels of the state. However, this is not enough, because politicians oppose federal competition as it restricts them in following their own interests. Therefore subcentral governments try to form tax and expenditure cartels that are protected by the central government. As a result there is a tendency toward government centralization beyond the point where citizens benefit the most (e.g., Blankart 2000). The problem of overcentralization also exists for other reasons (see Eichenberger 1994; Vaubel 1994) and is difficult to control. Rather than protect the federal system in the United States, the Supreme Court allowed a broad interpretation of activities assigned to the federal level that led to substantial centralization (Niskanen 1992). A referendum system, in contrast, is the constitutional provision that is most likely to protect a decentralized government.⁹

2.4 Empirical Evidence on the Consequences of Direct Democracy

Direct democracy changes the political process in three important ways, compared to a purely representative democracy, as was argued in the last section: (1) Due to a restriction of established politicians' power, an *outcome* of the political process can be expected that is closer to the citizens' preferences. (2) The participatory character of direct

democratic decision making provides incentives to voters to inform themselves about political issues, and changes their relationship to authorities and fellow citizens. The referendum *process* might thus be a source of procedural utility. (3) Direct democracy affects *institutional* change, and protects rules that favor the citizens; in particular, it is a safeguard against the risks of overcentralization.

In order to substantiate these hypotheses, systematic empirical analyses are necessary. A number of studies exist for both Switzerland and the United States (e.g., for surveys, see Bowler and Donovan 1998; Eichenberger 1999; Kirchgässner, Feld, and Savioz 1999; Gerber and Hug 2001; Matsusaka 2004). The two countries are particularly suited for comparative empirical analyses because direct democratic rights are developed to a very different extent at the level of Swiss cantons and US states respectively. While we briefly mention a wide range of results, some particularly important findings are presented in greater detail.

Effects on Policy Outcomes

In order to study whether direct democracy makes a difference to the outcomes of the political process, a natural starting point is to begin with public expenditures and revenues. Fiscal decisions are the central activities of most governments, and policy priorities are to a large extent formed in the budgeting process.

In a study covering the 26 Swiss cantons and the years between 1986 and 1997, Feld and Kirchgässner (2001) measure the effects of a mandatory fiscal referendum on aggregate expenditure and revenue. In 217 cases of the totally 312 annual observations, cantons adopted a mandatory referendum on new expenditure above a given threshold. It is found that expenditure and revenue in cantons with fiscal referendums are lower by about 7 and 11 percent respectively, compared to cantons that do not have this institutional provision.¹⁰ In a sample of 132 large Swiss towns in 1990, the same authors replicated their test for the mandatory referendum on budget deficits. In cities where a budget deficit has to be approved by the citizenry, expenditure and revenue, on average, are lower by about 20 percent, while public debt is reduced by about 30 percent. With an extended panel data set from 1980 to 1998, the effect of the mandatory expenditure referendum is analyzed, taking the spending threshold into account (Feld and Matsusaka 2003). At the median threshold of 2.5 million Swiss francs (SFR),

spending per capita is reduced by 1,314 SFR, namely by 18 percent for an average expenditure level of 7,232 SFR (compared to cantons that either have an optional financial referendum or no referendum on new public expenditure).¹¹ The difference in overall spending significantly varies between cantons, applying a low threshold of 0.5 million SFR (25th percentile) and a high threshold of 15 million SFR (75th percentile). For the former, expenditure is estimated to be lower by 1,389 SFR, while for the latter the reduction is 845 SFR. Moreover it is found that the mandatory financial referendum has less effect when it is easier for citizens to launch an initiative for a new law or to change an existing law (measured by the signature requirement). Thus there is a substitutive relationship between the two institutions with regard to their consequences on cantonal fiscal outcomes.

Very similar results are found for analyses across US states (Matsusaka 1995, 2004). In a panel from 1970 to 1999, including all states except Alaska, the effect of the initiative right is estimated on public expenditure, as well as on revenue. The institutional variable (a dummy variable) captures any type of initiative, whether it is statutory or for a constitutional amendment. After controlling for the average income in the state, federal aid, population size and growth, the percentage of metropolitan population, and whether it is a southern or western state, initiative states, on average, have lower expenditure, as well as lower revenue, than non-initiative states. States with the initiative spend \$137 less per capita than states that do not provide the initiative, *ceteris paribus*. They also raise less revenue, \$117 per capita compared to non-initiative states. Both effects are about 4 percent, compared to average expenditure and revenue respectively. The effects are, however, significantly different when the signature requirements to launch an initiative are taken into consideration. States with a 2 percent requirement are estimated to levy \$342 less taxes and fees per capita than non-initiative states (for the modal signature requirement of 5 percent, revenue is 6 percent lower and expenditure is 5 percent lower Matsusaka 2004, ch. 3). These effects reflect robust results that can be assigned to the referendum process and not, for example, to the ideology of a state's electorate. Controlling for roll call voting of state senators, as a proxy for voters' conservatism, does not change the results in a substantive manner; if anything, the effects for the institutional variable increase (Matsusaka 2004, ch. 3).

Often these kinds of results are interpreted as clear evidence that direct democracy produces favorable outcomes for the citizens. How-

ever, they mainly provide clear evidence against a simple median voter world, in which representatives implement the preferred expenditure and revenue levels of the median voter, and referendums and initiatives would have no effect.¹² It could well be that low expenditure and revenue levels mainly serve some well-organized interests (e.g., rich people) that rely less on public services. Therefore the efficiency in the provision of public goods has to be analyzed.

The cost efficient use of public money under different institutional settings can be directly studied for single publicly provided goods. In a careful study on waste collection, Pommerehne (1983, 1990) finds that this service is provided at the lowest cost in Swiss towns that have extended direct democratic participation rights and choose a private contractor. If the services are provided by the town instead of a private company, costs are about 10 percent higher. Efficiency losses are about 20 percent in purely representative democratic towns (compared to direct democratic ones). The average cost of waste collection is the highest in towns that rely on representative democratic decision making only, as well as on publicly organized collection (about 30 percent higher than in the most efficient case).

A hint on the efficiency of public services comes from a study that relates fiscal referendums to economic performance in Swiss cantons (Feld and Savioz 1997). For the years 1984 until 1993 a neoclassical production function is estimated that includes the number of employees in all sectors, cantonal government expenditure for education including grants, as well as a proxy for capital based on investments for building and construction. The production function is then extended by a dummy variable that identifies cantons with extended direct democratic participation rights in financial issues at the local level. Total productivity—as measured by the cantonal GDP per capita—is estimated to be 5 percent higher in cantons with extended direct democracy, compared to cantons where these instruments are not available.

Based on an aggregate growth equation, Blomberg et al. (2004) analyze to what extent public capital (utilities, roads, education, etc.) is productively provided and whether there is a difference between initiative and non-initiative states in the United States. Data on gross state product, private and public capital, employment and population, are for 48 US states between 1969 and 1986. They find that non-initiative states are only about 82 percent as effective as states with the initiative right in providing productive capital services, meaning approximately

20 percent more government expenditure is wasted where citizens have no possibility to launch initiatives, compared to states where this institution is installed.

Interesting indirect evidence for the efficiency of referendums and initiatives offers a comparative study of land prices in 91 municipalities in Connecticut (Santene 1986). Property prices are significantly higher in municipalities that provide direct democratic rights, compared to municipalities that do not.

In section 2.3 we outlined a politicoeconomic process in which politicians form a cartel against citizens. Previous results could, however, also be explained by imperfect information that leads benign representatives to implementing inferior policies, which happens less frequently in cantons, municipalities, and states with direct democratic rights. While we do not reject the notion of well-intentioned representatives, differences in the level of efficiency are hypothesized to be due to differences in legislative shirking. Corresponding evidence is provided by a study on corruption in US states in 1998 (Alt and Lassen 2003). The misuse of public office for private gains is measured based on a survey of state house reporters' perception of public corruption. It is found that in addition to a number of control variables, there is a statistically significant effect of voter initiatives on perceived corruption. In initiative states, corruption is lower than in non-initiative states, and this effect is the larger, the lower the signature requirement to launch an initiative. The result is further qualified, as there is only a negative effect on corruption for direct initiatives (but not for indirect initiatives, that have to be approved by the legislator).

Beyond the efficient provision of public goods and services, the consequences of direct political participation rights can be studied for citizens' happiness. Individuals not only have preferences for material affluence but also with regard to freedom, equal opportunities, social justice, and solidarity. Whether, overall, individuals' preferences are better served in direct democracies than in representative democracies can be conjectured, but not deduced, based on the extensive previous evidence. In contrast, the analysis of people's reported subjective well-being (for an introductory survey, see Frey and Stutzer 2002b) can offer important evidence on whether people in direct democracies are happier.

In a study for Switzerland in the early 1990s, the effect of direct democratic participation rights on people's reported satisfaction with life is empirically analyzed (Frey and Stutzer 2000, 2002a). Survey answers

are from more than 6,000 interviews. The proxy measure for individual utility is based on the following question: "How satisfied are you with your life as a whole these days?" People answered on a scale from one (completely dissatisfied) to ten (completely satisfied). The institutionalized rights of individual political participation are measured at the cantonal level, where there is considerable variation. A broad index is used that measures the different barriers preventing citizens from entering the political process via initiatives and referenda across cantons.¹³ The main result is a sizable positive correlation between the extent of direct democratic rights and people's reported subjective well-being (after taking important sociodemographic and socioeconomic variables into account). An increase in the index of direct democracy by one standard deviation raises the proportion of people indicating very high satisfaction with life by approximately 3.4 percentage points (or about 0.14 unit on the 10-point scale). This effect is more than a third as large as the difference in life satisfaction between the lowest income category and the one reporting the highest life satisfaction. As the improvement affects everybody, the institutional factor capturing direct democracy is important in an aggregate sense.

Effects on the Process of Political Decision Making

It is widely believed that well-informed citizens are an essential prerequisite for a well-functioning and stable democracy. If citizens do not have sufficient information about the policies or candidates they vote for, they may be disappointed by the actual consequences of their decisions, which in turn can undermine the acceptance and legitimacy of democracy as a political system. However, collecting information in order to make an informed decision at the poll is a public good that citizens are only willing to make to a limited extent. On the one hand, it can be debated whether a direct democratic decision on a particular issue demands more or less information than the choice of a candidate, given the institutions that lower citizens' information costs.¹⁴ On the other hand, it can be asked whether the level of voter information itself is dependent on the political system in which citizens live. We have theoretically argued in the last section that a political system that gives citizens more political participation possibilities will change the demand for political information, as well as the supply of it. An illustrative example is the introduction of the Maastricht Treaty in various European countries. In the countries where citizens had the right to

vote on it (e.g., Denmark), politicians had to engage much more in explaining the Treaty to the citizens than in countries where no referendum took place (e.g., Germany). For the citizens the incentives to be informed were greater, as the intense discussions before the referendum partly transformed 'having a reasoned opinion' into a private good. Casual observation suggests that as a consequence information levels on the content of the Treaty were high among Danish citizens. While this example offers suggestive evidence that voters are better informed when they have a larger say in the political process, Benz and Stutzer (2004) provide more systematic evidence.

They study voter information in two different contexts. First, survey data from the Eurobarometer series is used to systematically investigate how referenda in several European countries affected citizens' information on the European Union. The results indicate that people in countries with a referendum are in fact "objectively" better informed (according to ten questions about the European Union in the 1996 Eurobarometer), as well as feeling "subjectively" better informed about the European Union after a referendum (Eurobarometer 1992–1997).

Second, they look at voter information in Switzerland. As a proxy measure for citizens' awareness of political issues, the number of correct answers to the following three questions is used: (1) "How many parties are in the Federal Council?" (2) "Who was the president of the Federal Council in 1995?" And (3) "How many signatures are required for an initiative?" Data are obtained from a large survey conducted among the Swiss electorate in 1996. Differences across cantons are explained by a measure for the extent of citizens' participation rights, as well as a number of sociodemographic control variables. In this study the same broad index is used as in the work on direct democracy and life satisfaction in Switzerland (described in the last subsection). A raw correlation is presented in figure 2.1.

As the figure shows, on average, citizens living in more direct democratic jurisdictions are objectively better informed about politics. The result holds in a multiple regression framework and indicates that the effect is sizable. For the full range of the institutional variable, an effect is estimated that is comparable to an increase in education from mere compulsory education to having attended a college providing a diploma at the end.

The study by Benz and Stutzer (2004) also indicates that political participation possibilities raise discussion intensity which, in the literature, is seen as an important transmission channel that leads to higher voter information.

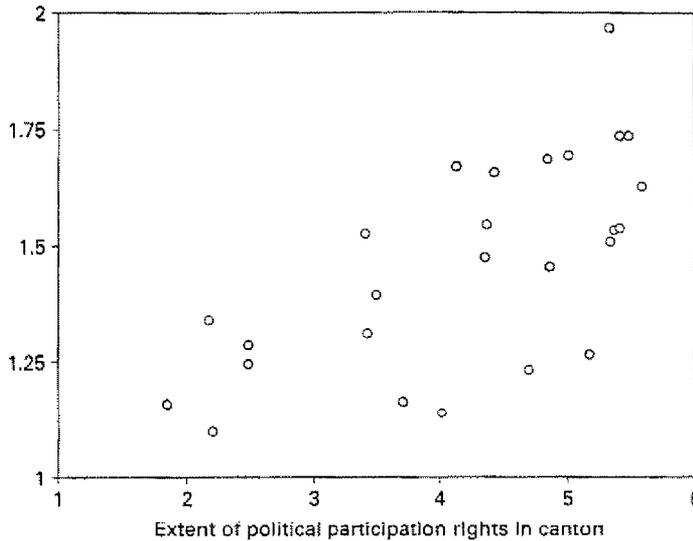


Figure 2.1
Correlation between voter information and political participation rights in Swiss cantons, 1995. Source: Benz and Stutzer (2004), based on Selects 1996.

People's satisfaction with the provision of public services in direct democracies is likely to influence their behavior as voters collecting information or as taxpayers. However, the process of decision making may also change people's trust in authorities (this can be seen as a psychological contract; see Feld and Frey 2002) and their motivation to obey the law. It has, for example, been shown that with more extensive democratic participation rights, people have higher tax morale and evade taxes less. Based on survey data from the World Values Study, Torgler (2003) finds that, in more direct democratic Swiss cantons, citizens are more likely to agree with the statement that "cheating on taxes if you have a chance" is never justifiable. Pommerehne and Weck-Hannemann (1996) directly study tax evasion in Swiss cantons and find that it is substantially lower where citizens have a direct impact on budgetary policy.

Citizens' experience with direct democracy has further been found to form positive attitudes about their abilities to influence what government does (Bowler and Donovan 2002). Thus direct democracy strengthens citizens' feelings of political efficacy.

The evidence mentioned in this subsection leads to the hypothesis that citizens might benefit from the process of direct democracy,

beyond its political outcomes.¹⁵ Frey and Stutzer (2005) extend the study mentioned above on direct democracy and life satisfaction to address this hypothesis. In order to disentangle outcome effects and procedural effects that make for the positive correlation between participation rights and reported subjective well-being, foreigners are used as a control group. Foreigners benefit from favorable outcomes but are excluded from procedural benefits. In fact it is found that the positive effect of direct democratic participation rights is about three times as large for citizens as it is for foreigners.

Effects on Government Centralization

The relation between direct democracy and federalism is not restricted to the common goal of a better fulfillment of citizens' preferences. Rather, the two institutions are mutually dependent. In particular, the citizens are interested in a working federal competition between jurisdictions. In order for the citizens to defend themselves against politicians' interests in the case of centralization, they need strong political rights. Blankart (2000) explains the stronger centralization in Germany, compared to Switzerland, after World War II by the missing direct democratic instruments at the federal level in Germany. He documents the centralization process by comparing Germany's Basic Law in 1949 with the one in 1999. With regard to taxation, for example, tax bases in 1949 were allocated exclusively to each of the three levels of government. In 1999, almost all the relevant taxes are under federal legislation, and separation of taxes is replaced by revenue sharing. This is reflected in a percentage of centralized taxes of 93.0 percent in 1995 compared to 61.2 percent in 1950. While, in Switzerland, a parliamentary system with two chambers exists that is similar to the one in Germany, there is a significant difference in the process of constitutional change. In the case of tax issues, for example, "since 1917, the citizens have been called no less than 23 times to vote on federal income and turnover taxes. Forty percent of the proposals have been declined in the first round" (Blankart 2000, p. 32). Accordingly, centralized taxes account for 47.4 percent in Switzerland in 1995, which is a much smaller proportion than in Germany (although both countries had similar levels in 1950: 60.1 percent in Switzerland and 61.2 percent in Germany).

The effect of direct democracy on government decentralization is also empirically documented for the lower levels of government. In an

extension of the work on spending across US states from 1970 to 1999, Matsusaka (2004, ch. 4) studies how the initiative changes the division between state and local expenditure. While initiative states, on average, spend 13 percent less per capita at the state level than non-initiative states, they spend 4 percent more at the local level. The result is more decentralized spending patterns in states that adopt the initiative. Similar results are obtained for Swiss cantons in a panel over the period 1980 to 1998 (Schaltegger and Feld 2001). Rather than expenditure per capita, the proportion of cantonal expenditure in percent of total state and local spending is related to the development of the financial referendum. It is found that cantons with fewer obstacles to launching a budget referendum are less centralized with regard to expenditure, as well as revenue. The effect on expenditure is to a large extent due to more decentralized spending on education in more direct democratic cantons.

Direct democracy is not only affecting the process of fiscal centralization, but also spatial centralization. Martin and Wagner (1978) find that there are fewer municipal incorporations in US states, where direct democratic processes involve residents in incorporation decisions.

2.5 Arguments against and Counterarguments for Referenda

Systematic evidence has been accumulated that direct democracy is a process and provides outcomes that are more in line with citizens' preferences than are a purely representative democratic process and its outcomes. Nevertheless, referenda can hardly be considered a popular institution in democracies, not to speak of authoritarian systems. Not surprisingly, the members of the *classe politique* are quick to raise many objections because they realize that referenda constitute a threat to their position, by limiting their rent-seeking potential. Many intellectuals—even those who do not share in the spoils of the politicians' cartel, and those opposing the political establishment—also reject referenda, with a variety of arguments. The basic reason is that they consider themselves to be better judges of what is good for the people than the citizens themselves. They tend to see themselves in the role of "philosopher-king," determining what "social welfare" is. Consequently they prefer decision-making systems where they have a larger say. Thus they oppose referenda for the same reasons as they oppose the market.

The following ten arguments are often raised against the institution of the referendum. In addition to the empirical evidence in the last section, we respond to these claims with additional arguments.

Citizens Fail to Understand the Complex Issues

It is argued that the average voter is not well informed nor well educated, so he or she cannot reasonably be allowed to determine political issues. Therefore policy making is the task of a specialized group, the politicians, who represent the voters.

This view can be refuted for various reasons: First of all, it is inconsistent to trust citizens to be able to choose between parties and politicians in elections but not between issues in referenda. If anything, the former choice is more difficult, as one must form expectations on how politicians will decide on future issues. Second, the voters need not have any detailed knowledge about the issues at stake. Rather, they only need to grasp the main questions involved. These main questions are not of a technical nature but involve decisions of principle, which a voter is as qualified to make as a politician. Third, the general intelligence and qualifications of politicians should not be overrated. They can hardly be considered to be consistently superior to other people. Moreover the average member of parliament has little choice; he or she is normally forced to vote according to what the party superiors and a few specialists have decided in advance. Fourth, a number of institutions have emerged in direct democracies, helping citizens to reach reasoned decisions. The parties and interest groups give their recommendations concerning decision making, which the citizens may take into consideration. Even more important, the discourse in the pre-referendum stage brings out the main aspects and puts them in perspective. Finally, as shown in the last section, citizens' information on political issues has to be taken endogenously. Direct democracy provides incentives for the citizens to privately collect information, and for the political actors and the media to provide it.

Citizens Have Little Interest in Participating

Participation in initiatives and referenda is often low and varies with the size of jurisdictions (e.g., see Hansen et al. 1987). Sometimes only a few eligible voters go to the polls. It can be concluded from that that citizens are not interested in the issues to be decided on.

This is, however, a wrong conclusion for three reasons: First, the voting participation is not always so low. When the citizens feel that the issue is important, the voting participation rises considerably. This holds also in large jurisdictions where political mobilization is at a disadvantage. Switzerland provides a good example of this variability: while average participation for all issues at the federal level is around 45 percent, it can be as low as 25 percent. But sometimes it goes up to 80 percent and more, as was the case in 1992, when the Swiss citizens had to decide whether or not they want to join the European economic area.

Second, high voting participation is not necessarily a good thing. Citizens are perfectly rational not to participate when they find the issues unimportant or when they are undecided. It can even be argued that it is socially beneficial that citizens do not participate under these conditions but rather leave the decision to those for whom the issue really matters. Voting participation then reflects citizens' preference intensities, which makes the vote socially more valuable. Third, it is naive to think that *freely chosen* voting participation in parliaments is very different from how citizens behave with respect to popular referenda. Today's members of parliament are highly specialized and seriously consider the pros and cons of only a few issues. In the case of all other issues, they (have to) follow the dictate of the party leadership, so they do not cast a voluntary vote. This is reflected in the often extremely low participation in a parliamentary session. The members of parliament have to be herded together from the lobby or their offices to cast the dictated vote.

Citizens Are Easy to Manipulate

Financially strong parties and pressure groups are better able to start initiatives and to engage in referendum propaganda than are financially poor and nonorganized interests. This cannot be denied. However, the perspective is wrong because it takes an absolute stance: it is *always* true that the rich and well-organized groups wield more power. The crucial question is whether they have *more* or *less* power in a direct than in a representative democracy. It is well known that well-organized and financed pressure groups exert considerable power over the politicians sitting in parliament and in government. It may even be argued that it is cheaper to influence the small number of legislators and government politicians than the total electorate.

Citizens Are Prone to Decide Emotionally

Voters are often supposed to be unduly influenced by emotional considerations. Again, this charge must be considered in a comparative perspective. There is little reason to believe that politicians are less subject to emotions. After all, parliaments are known to have highly emotional debates, sometimes even erupting into fist fighting. For that reason many parliaments have formal procedures to debate a proposal two or even three times, with considerable time elapsing in between. The same holds for popular referenda. Before taking the vote, there must be time for intensive discussion, which allows the various sides of a question to be brought up. This strongly increases the chances of a decision dominated by rational aspects.¹⁶

There Are Too Many Referenda Confusing the Voters

When the citizens have to simultaneously decide on a great many issues (e.g., in California the voters often have to deal with 20 or even more propositions), they focus on a few clear issues. The decisions on all other issues are then haphazard and lack rationality.

This is indeed a situation to be avoided. However, the number of referenda put to the vote can be steered by the number of weekends with ballots over the year and by the number of signatures required for an initiative or optional referendum. If the number of issues to be decided on gets too large, the number of signatures required can be raised. Such a decision should be taken by a constitutional referendum to prevent the *classe politique* from fixing such a high number of signatures that referenda become improbable.

Political Leadership Is Impossible

Politicians are sometimes supposed to make unpopular decisions. An example would be a restrictive fiscal policy, when the budget deficit is getting too high or when inflation soars. Such policy pays off only over the medium or even long term. It is argued that such unpopular policies would be impossible in a direct democracy.

This conclusion, however, does not necessarily hold. In a direct democracy the politicians are forced to explain their policies to the citizens. If they can give good reasons why they propose to undertake such a seemingly unpopular policy, the citizens will not oppose it.

There are many examples in Switzerland where the citizens are prepared to support policies burdening them, provided that the politicians make an effort to explain why the sacrifice is necessary to improve the situation over the long term. Empirical evidence presented in the last section, for example, shows that fiscal stability is higher in Swiss cantons and US states with more extensive direct democratic participation rights.

Referenda Are Inadequate for Major Issues

As the voters are taken to be poorly educated and ill informed, subject to manipulation and to emotional decisions, it is often argued that referenda should only be used for small and unimportant issues. In contrast, issues of great consequence—such as changes in the constitution—should be left to the professional politicians.

The opposite makes more sense. Major issues can be reduced to the essential content. Evaluation is then not a matter of (scientific) expertise but of value judgments. Following methodological individualism, only the citizens may be the final judges when it comes to preferences, and a substitution by representatives is, at most, a second-best solution. As the politicians have a systematic incentive to deviate from the voters' preferences, a substitution leads to biased outcomes.

Referenda Hinder Progress

Asking the population to make a decision is often rejected because it is argued that the "ordinary citizens" do not like changes, and that they prevent the adoption of "bold, new ideas."

It may well be true that many new propositions are rejected in referenda, but this does not mean that this constitutes a disadvantage. The fact that proposals contain new ideas is no proof of their quality. Indeed the citizens are right in rejecting them when they are in favor of the *classe politique*. The concept of "bold, new" solutions is not rarely the result of technocratic thinking and of a planning mentality. They strengthen the politicians' and bureaucrats' position but need not necessarily be in the voters' interests.

Referenda are well proved to break deadlocks in societal decision making and, in this sense, are progressive. There are cases where a referendum helped clear an issue that was difficult to resolve in parliament and government. The prime example is the demands by regions

for more independence. These demands are often accompanied by considerable violence and bloodshed. The Basque country is just one of many cases. In a direct democracy such heated issues may be brought to a resolution acceptable to a large majority. In Switzerland, for instance, the secession of the Jury from the canton Bern was achieved by undertaking a number of referenda. While some minor violence took place, the issue was settled with much less strife and bloodshed than normally occurs in representative democracies, let alone autocratic systems.

Referenda Destroy Civil Rights

One of the fundamental problems of democracy is the "tyranny of the majority." This danger is seen to be particularly acute in the case of referenda where the will of the majority is unrestricted. As a result civil rights may be thwarted. But this is not necessarily the case. Most important, if there are economic, social, and political cross cleavages, no group of citizens is *always* in the majority, and therefore will be careful not to antagonize other social groups. Empirically some evidence for the suppression of civil rights has been found in local and state ballots in the United States (Gamble 1997), but there is also contrary evidence for the United States and Switzerland (Cronin 1989; Frey and Goette 1998). In a study on 51 California ballot propositions, the notion of cross cleavages is supported. Hajnal et al. (2002) find that black, Latino, and Asian American voters are only about 1 percent less likely than white voters to be in the winning majority of the vote.

Referenda Are Expensive

The last argument against referenda is the alleged high cost of undertaking them from an administrative point of view. It is argued that parliamentary decisions are much less expensive and should therefore be favored.

There are two reasons why this reasoning is fallacious: First, referenda are not expensive compared to the large cost of running a professional parliament with its accompanying party system (e.g., see von Arnim 1988 for Germany). As in a direct democracy the final say is with the citizens, and less money needs to be spent on parliament and the parties. Moreover the administrative costs of referenda are not high because several propositions can be dealt with in one weekend, and

citizens can be asked to actively participate in organizing the vote and counting the votes. While the citizens drafted suffer some opportunity cost, such a participation has the advantage of getting them more directly involved in governing their state, which tends to raise their sense for citizens' duties. Second, the administrative cost of running referenda is immaterial compared to their major advantage, namely to significantly reduce the deviation of political decisions from individual preferences.

2.6 Issues for Constitutional Design

The Case of the European Constitution

While the designers of the European constitution are well advised when they are inspired by the US constitution, in particular its revolutionary vision, they should not repeat the mistakes of the founders of the American Republic when dealing with constitutional amendments. The constitutional history of the United States shows that in the case of three major transformations, each has broken the rules for constitutional amendment (Ackerman 1998): (1) The convention that wrote the US constitution ignored the rules that allowed for the amendment of the Articles of the Confederation. (2) The amendments, which freed the slaves and provided them with citizenship, did not result from a procedure designed for amending the constitution. (3) The great extension of the competence of central government vis-à-vis the states in the 1930s was backed by Supreme Court judgments rather than a formal amendment. Article V of the US constitution thus does not seem appropriate to handling constitutional change under the rule of law. The first option, to call a convention in order to amend or replace the constitution, was never chosen. The second option, a two-thirds support for an amendment in both Houses of the Congress, and ratification by three-quarters of the states, was sometimes applied but was disregarded for major changes.¹⁷

The proposal for the new European constitution in Article IV-7 defines the "Procedure for revising the Treaty establishing the constitution." The process is designed as follows:

1. The government of any Member State, the European Parliament or the Commission may submit proposals to the Council of Ministers for the amendment of the Treaty establishing the Constitution.

2. If the European Council, after consulting the European Parliament and the Commission, adopts by a simple majority a decision in favor of examining the proposed amendments, the President of the European Council shall convene a Convention The European Council may decide by a simple majority, after obtaining the consent of the European Parliament, not to convene the Convention, should this not be justified by the extent of the proposed amendments.
3. The Convention shall examine the proposal for amendments and shall adopt by consensus a recommendation to the conference of representatives of the governments of the Member States
4. The conference of representatives of the government of the Member States shall be convened by the President of the Council of Ministers for the purpose of determining by common accord the amendments to be made to the Treaty establishing the Constitution.
5. The amendments shall enter into force after being ratified by all the Member States in accordance with their respective constitutional requirements.

These citations capture the most relevant aspects of article IV-7. Two characteristics are essential. There is *no direct role for citizens* in deciding on the basic law to which they are supposed to adhere. *Unanimous consent* (in the Convention and in the conference of representatives of the governments of the member states) is the only principle for a formal constitutional amendment.

The fact that the European constitution has to meet the *unanimous consent* of all member states means that it can practically *not be changed*. Such unanimity is correct behind the veil of ignorance. But most member countries are far from ignorant about what their interests will be in the future. The requirement of unanimous consent means that formal adjustments and amendments to the constitution will not occur.¹⁹ But such changes are crucial in order to prevent the ossification of the fundamental rules guiding the Union.

Citizens' preferences and the economic and social conditions of the European Union will certainly evolve in the future. If the EU constitution is immutable, due to the exclusion of citizens' direct involvement and unanimity requirements, the necessary changes will take place *outside* the constitution, as has been observed in the United States. Three decision-making bodies will gradually adjust the rules actually followed in the political process. Contrary to a constitutional process geared to fulfill citizens' preferences, these three groups of actors will change institutions and laws more in the direction of their own ideologies and interests. Common tendencies will be the exclusion of "disturbing" influences on the part of the citizenry and the restriction of

competition between regions and nations within the Union, resulting in centralization.

The *European Constitutional Court* will form the ground rules by interpreting the existing constitution in a particular way. The respective constitutional developments may well be superior to an immutable set of rules. But the decisions taken will have special features. The members of the Constitutional Court being elected by representative bodies are far from being responsive to citizens' preferences. Even if the members are elected for long terms, or for life, their incentives are unlikely to be directed to meeting citizens' desires. Experience with the US Supreme Court supports this conclusion. Judges do not effectively protect citizens from government intervention. In contrast, the Court tends to support centralization and governmental action against citizens' rights.

The members of the *European Parliament* (MEPs) are elected directly, but the corresponding elections are generally considered to be unimportant. The MEPs do not really have to convince the citizens about their position, but they are elected on the basis of their belonging to a particular party. Nevertheless, MEPs see themselves as the "true" representatives of "Europe." They tend to identify with the European bodies and support the European centralization process, even if it is inconsistent with the voters' wishes. They fight hard to prevent their legislative powers being eroded, in particular, if they are intended to be curbed by the direct participation rights of the citizens.

The *European Commission* and the *European public service* have a direct and strong interest in interpreting and adjusting the constitution in a way that provides more competence for them. Increased centralization of decision making raises their importance and power. For the same reason, both bodies resist direct interventions in decision making by the citizens.

The development of the rules outside the written European constitution thus disregards the interests of the citizens. Binding rules favor the interests of the particular bodies able to informally establish these rules.

While a living constitution is important, its development must be based on the *rule of law*. This means that a crucial part of a constitution is making provision for how to change it. The procedures must not be left to whatever body is trying to capture them. Rather, the procedures for changing the constitution must give the *citizens well-defined rights to*

participate in that process. A straightforward way would be to require a double simple majority, both among all the voters in the European Union *and* among the member states.¹⁹ It is, of course, also possible to require qualified majorities, either among the voters or member states, or both. According to our point of view, the essential requirement is that the citizens' participation is fully guaranteed and, in particular, that they (and not the federal government) have the power to assign legislative competence to bodies and state levels, the so-called competence competence. This includes the right to start constitutional changes via popular initiatives, with the courts and parliament having only minor, and clearly delineated, possibilities of intervention with respect to the issues proposed. The right must also extend to accepting or rejecting constitutional changes suggested by the parliament.²⁰

Precondition in Society

There are many politicoeconomic obstacles to introducing political institutions that restrict the competence and influence of established interests. However, in societal crisis, or after a revolution (like in the former communist countries in Europe), there is a window of opportunity for institutional change and new basic rules for society. In order to successfully introduce direct democracy during these periods of time, a civic culture is necessary that facilitates the use of referenda and initiatives. It is impossible to successfully run directly democratic institutions where there is no adequate basis in society. One condition under which direct democracy²¹ works well is when there are strong cross-cutting cleavages (e.g., with respect to per capita income, religion, and culture or language). This guarantees that it is not always the same group of persons that finds itself in the minority and therefore feels exploited. As has also been emphasized, the citizens must have sufficient trust in the politicians that they actualize the referendum decision, and the politicians must trust that the citizens take reasonable decisions when voting on issues. This trust must develop over time and cannot simply be instilled from outside. Therefore the "grand" solution of jumping from a representative democracy straight into a fully developed direct democracy is both unrealistic and undesirable. Rather, direct participation rights for the citizens should be gradually introduced²² so that a *learning process* can take place between the citizens, parliament and government. The use of initiatives and referenda by the citizens is, however, also a major factor in raising civic culture,

especially in the form of the trust citizens have in their government. Direct democracy thus helps to create the necessary conditions for its own smooth functioning, provided that the learning effect does take place.

Gradual Introduction

There are several ways in which directly democratic rights can be gradually introduced. Most of them restrict the application of direct democratic decision making and constitute a considerable danger for direct democracy. Most important, the restrictions introduced may stay for good. In the case of several of the restrictions this would amount to destroying the whole idea of citizens' participation in political decision making. The institutions of direct democracy cannot develop their strengths. The outcome of politics would not correspond more closely to citizens' preferences than under a traditional representative system. Moreover the citizens are unable to learn the special features of direct democracy properly. Five approaches for a gradual introduction are briefly discussed.

Size of Majority

Passing a proposal in a popular vote may require a *super majority*, for instance, two-thirds of the participants. Alternatively, one may require a simple majority of the *whole* electorate, including those abstaining. Such quorums exist in Italy and many transition economies. In several of these countries referenda received a majority of the votes cast but not of the electorate. In Italy these quorums led to the perverse situation that opponents of a referendum called people to abstain from voting and were thus undermining the institution of direct democracy as such.

A strong restriction on popular initiatives and optional referenda is the number of signatures required. A balance between requiring a low number (and therefore having many referenda) and a high number (and therewith excluding citizens) is needed.

Issue Domain

Some questions can be excluded from direct voting or can be protected with the use of qualified majorities, for fear of "irresponsible" or "uncontrollable" outcomes. One could restrict the domain in the following way:

- Basic parts of the *constitution*, such as those referring to human, political, and civil rights, could be excluded.²³
- Supposedly *sensitive* issues could be removed from citizens' voting. This may refer to problems relating to particular minorities, ethnic, or religious groups but also, for example, to the death penalty (as in Germany).
- Issues that are thought to be beyond the *competence* of the citizens. This could, for instance, be assumed to hold for economic problems, such as taxation. (In Germany the recent proposal to introduce national referenda excluded tax issues from the very beginning).

These restrictions are probably most dangerous for a successful application of direct democratic decision making, since they undermine the institution from the beginning. If only very unimportant issues are put to the vote, or if the number of signatures required for an initiative or optional referendum is far too high, the citizens cannot experience the advantages of direct democracy. On the other hand, the politicians can always claim that they gave direct democracy a chance but that it did not work. In the case of tight restrictions a vicious circle may develop. The way popular participation is introduced leads to unsatisfactory results and experiences, providing the opponents of direct democracy (in particular, the politicians in power) with a good reason to introduce even more severe restrictions. Of course, under these circumstances direct democracy cannot work.

Decision Level

Direct democratic elements can be restricted by initially granting them only on a particular level of the state.

One possibility is to start at the *local level*, giving citizens the right to launch initiatives and vote in referendums in political communes. This allows the citizens to benefit from everyday or impacted information in order to form a reasoned opinion. Moreover the issues are often of immediate relevance to the population. But this procedure only makes sense if the political communes have a sufficient amount of autonomy. Preferably they should be able to decide both on taxes and public expenditures. Recently, in the case of EU member states, there have been introduced quite extensive referendum rights in some of the German Länder (in particular, in Bavaria and the new Länder; e.g., see Luthardt und Waschkuhn 1997).²⁴

Another possibility is to start at the *national level* when major issues are at stake. This has indeed happened in several European countries, where the decisions of whether to join the European Union or to join one of the several treaties have been relegated to the citizens as a whole. As these decisions are of crucial importance, the citizens are well aware of their relevance and will certainly be inclined to participate in the vote.

The limitations on the levels at which elements of direct democracy are to be introduced make most sense. The rights for initiatives and referenda should first be introduced at the local level, and at the same time at the national level, and perhaps only later at the regional level. At the local level the citizens tend to be well informed about the issues in question, while at the national level the decisions to be taken are of obvious importance. These are indeed the levels where direct democratic elements have been introduced in several transition economies, though only to a limited extent (Gross and Kaufmann 2002).

Time

The referendum process may be shaped by requiring a sufficient amount of time to pass between the start of an initiative or referendum process, the actual vote and the resulting decision becoming effective. This is a move toward the constitutional idea (e.g., Mueller 1996) of putting people behind the veil of uncertainty, and therefore inducing them to take a more "objective" position.

A more innovative idea is to proceed, as (many) parliaments do, namely to have a first, second, and sometimes even a third reading of a law. In a direct democracy one could first have an *informative* vote, and after sufficient time has elapsed to allow for a discussion of the outcome, a *decisive* vote could be cast.

Co-determination

The citizens' decision may only become effective if it is supported by a corresponding vote in the parliament (and perhaps even in the two houses). This would, however, reduce referenda to a plebiscite. Another possibility would be to accord a veto right either to the citizens or to the parliament. One could also consider a double majority in the form of the popular vote and votes in the regions (cantons or states). This latter requirement applies, for instance, in Switzerland, where both the majority of all the Swiss voters and the majority of the cantons must approve a constitutional referendum.

2.7 Concluding Remarks

The crucial question is *who governs* the step by step introduction of directly democratic instruments. Ideally it would be a constitutional assembly. Its members are not directly involved in current politics, so they take a more objective stance. They do not have to fear a reduction in their own power if direct democracy is introduced in the future. In reality, however, a considerable number of the members are likely to belong to the *classe politique*. They either served in political decision making in the past, currently do so, or hope to do so in the future. In all cases they tend to oppose popular participation in political decision making.

For these reasons the active involvement of the citizens in amending the constitution, as well as in more general political decision making, cannot be substituted by resorting to representation. Giving citizens rights to directly participate in political decision making can be based on two different types of reasoning. The first takes such political rights as a *value as such*, which must not be legitimized any further. Direct democracy is then taken as the next logical major step from the introduction of democracy in the classical Athenian city-state and its broadening over whole nations in the wake of the French Revolution. The second type of reasoning considers the favorable consequences of giving the citizens the right to directly participate in political decision making. This chapter identifies two sources of benefits:

1. *Procedural utility*. Direct participation rights raises citizens' utility, quite independent of the outcomes reached. Empirical evidence suggests that citizens' subjective reported well-being (*ceteris paribus*) is the higher, the more extensive their participation rights are.
2. *Outcome utility*. When the citizens are allowed to directly participate in political decisions, the policies undertaken yield more favorable results for them.

Extensive empirical evidence for Switzerland and the United States (the leaders in direct democracy) suggests that more extensive participation rights via popular initiatives and referenda lead to a lower tax burden and lower public expenditures, to higher efficiency and productivity in the provision of public goods and services, and to higher overall satisfaction (happiness) of the population.

The following arguments are often raised against direct democratic institutions: the citizens fail to understand the complex issues, they

have little interest in participating, they are easy to manipulate, they tend to decide emotionally, the large number of referenda lead to confusion, leadership is made impossible, and direct democracy is inadequate for major issues, hinders progress, destroys civil rights, and is very expensive. This chapter shows that these arguments should be rejected, in particular, if a comparative stance is taken, that is, if decision making in direct democracy is contrasted with that in representative democracy.

Elements of direct democracy can be introduced gradually, and there are many possibilities for varying the required majority, the issue domain, the time, and the extent of codetermination of citizens and parliament, as well as whether to start at the local, national or supranational level.

The chapter concludes that increasing the direct democratic political participation rights of the citizens is an important step for a future democracy. It is, in particular, a crucial requirement for a future European constitution committed to democracy.

Notes

1. The draft of the European Constitution is electronically available at <http://european-convention.eu.int/>, July 31, 2003.
2. See, for example, Magleby (1984), Cronin (1989), Butler and Ranney (1994), Frey (1994), Dubois and Floyd (1996), Kirchgassner, Feld, and Savioz (1999), and Frey, Kucher, and Stutzer (2001).
3. Some of these referenda certainly do not meet the requirement of leaving the (final) decision on an issue to the general electorate, but are rather plebiscites, meaning votes where the government wants the support of the population for a decision already taken.
4. An up-to-date account of the referendum experience around the world is provided by C2D—Research and Documentation Centre on Direct Democracy at the University of Geneva (<http://c2d.unige.ch/>, August 6, 2003). Additional information about direct legislation in the United States is collected by the Initiative and Referendum Institute in Washington (<http://www.iriinstitute.org/>, August 6, 2003). Its partner organization in Europe (<http://www.iri-europe.org/>, August 6, 2003) provides information on the state of direct democracy in European countries (with a special focus on transition economies).
5. Citizens' initiatives also allow an "unbundling" of issues, compared to the bundled issues typical for representative democracies. This induces policy outcomes that have a closer relationship with popular preferences (see Besley and Coate 2000).
6. See Romer and Rosenthal (1978, 1982) for Oregon school budget referendums, and Weingast and Moran (1983) for congressional committees. The two groups of researchers do not consider the general role of referenda in agenda setting, but concentrate on its

effect on bureaucratic decisions. Our emphasis is on its role as a means to break the politicians' cartel.

7. The essential role of discussion in direct democracy is more fully discussed in Frey and Kirchgaessner (1993) and Bohnet and Frey (1994). For democracy in general, see Dryzek (1990).

8. The quality of the discourse process is, however, periled if multiple initiatives on the same issue are drafted and put on the ballot simultaneously. The strategic drafting of initiatives, for example, as observed in California, makes it difficult for voters (1) to catch on the meaning of the proposals from the title or wording of the initiatives and (2) to anticipate the actual policy change if more than one measure on the same topic passes (Silva 2000).

9. In their proposal for a "New Democratic Federalism for Europe," Frey and Eichenberger (1999) develop a model of federalism that is based on functional overlapping competing jurisdictions (FOCJ) that rely to a large extent on direct democracy.

10. While these findings imply larger deficits and higher public debt in cantons with a fiscal referendum, *ceteris paribus*, the respective empirical results neither show statistically significant effects on the former measure nor on the latter one (Feld and Kirchgaessner 2001, p. 354).

11. In the regression equation the following are controlled for: income level in the canton, federal aid, age structure of the population, population size, population density, unemployment rate, as well as whether people are German-speaking or not.

12. In contrast, Pommerehne (1978) provides strong evidence that the median voter model performs better in Swiss towns with extended direct democratic rights than in representative democratic cities. While, for the former category containing 48 of the 110 towns in the data set, a statistically significant demand elasticity for aggregate public expenditure with respect to income is estimated in 1970, this is not the case for representative democracies. Thus public expenditure seems to match median voter's preferences better in direct democratic jurisdictions.

13. The index is based on the four main legal instruments for directly influencing the political process in Swiss cantons: (1) the initiative to change a canton's constitution, (2) the initiative to change a canton's laws, (3) the compulsory or optional referendum to prevent new law or the changing of law, and (4) the compulsory or optional referendum to prevent new state expenditure. Obstacles are measured in terms of (1) the number of signatures necessary to launch an instrument (absolute and relative to the number of citizens with the right to vote), (2) the legally allowed time span in which to collect the signatures, and (3) the level of new expenditure per head allowing a financial referendum. Each of these restrictions is evaluated on a six-point scale: "one" indicates a high obstacle, "six" a low one (compulsory referenda are treated like referenda with the lowest possible obstacle). Average nonweighted ratings represent the measure used for direct democratic rights in Swiss cantons.

14. Voters can use party ideologies to proxy for the consequences of their vote. They also pay attention to the previous performance of a government, they judge the reputation of candidates (Lupia and McCubbins 1998), they evaluate voting recommendations by interest groups (Schneider 1985; Lupia 1994), or they collect political information as a by-product of mass media consumption.

15. For a general account on procedural utility, see Frey, Benz, and Stutzer (2004).

16. In July 2002 the German Bundestag debated (and rejected) a proposal to introduce elements of direct democracy at the federal level. For fear of emotional decisions, the introduction of the death penalty was excluded right from the very beginning as a subject for a referendum. This overlooks that an extensive discussion among the citizens, and with experts and politicians, brings to the fore all sides of the issue. A purely emotional decision is unlikely to occur. Moreover many countries using the death penalty follow the representative principle (e.g., the United States), while the country with most extensive direct democracy (Switzerland) prohibits the death sentence.

17. For a discussion, see Mueller (1999).

18. If the veil of ignorance is lifted and transaction costs are taken into account, unanimity is not an optimal decision rule (Buchanan and Tullock 1962). Instead, an optimal majority has to be found that is minimizing the sum of costs due to externalities composed of minority and transaction costs.

19. This corresponds to the rules in the Swiss constitution requiring that constitutional changes must be approved by the simple majority of the Swiss voters and the Swiss cantons. This has resulted in a great number of constitutional changes over the course of time and has contributed to ground rules adapting to evolving requirements. The many changes are partly due to the fact that at the federal level, popular initiatives are possible only for changes in the constitution but not for changes in laws. Therefore the constitution became overburdened with issues of lesser importance better suited for the level of laws. Recently this provision has been changed, and it is now possible to undertake general popular initiatives that leave the decision to the legislator whether the initiative is formulated as a constitutional amendment or as federal law.

20. We are, of course, not the only ones who are proposing elements of direct democracy for the new European constitution. See more recently, for example, Feld and Kirchgässner (2003), Mueller (2002, 2003), or Hug (2002, ch. 7) for a survey on previous proposals.

21. This condition is not only specific to direct democracies but also holds for all types of democracy.

22. To gradually introduce direct democratic elements in a political system dominated by the government may, however, induce the risk that the government on purpose undermines its functioning in order to "demonstrate" to the citizens that it cannot work.

23. Such restriction may make sense also in fully developed direct democracies, but it should be noted that this is not the case in Switzerland. It should immediately be added that the Swiss voters have had no inclination to cheat where such basic rights are concerned.

24. The referendum experience in other European countries is described in Gallagher and Uleri (1996).

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