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Politics as exchange: the classical liberal economics and politics of James M. Buchanan

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Abstract James Buchanan advocated the market mechanism for allocating resources because it is based on voluntary exchange. People engage in market transactions only when they believe they benefit from doing so. Buchanan depicted the political process the same way. People engage in collective activities to accomplish together ends that they would be unable to accomplish individually, or through bilateral exchange. Buchanan's vision of politics as exchange is a normative framework for evaluating the rules within which political activity takes place. Rules that meet the criterion of agreement are desirable constitutional rules, and Buchanan recognized that not all government activity satisfies that criterion. Buchanan is the father of the subdiscipline of constitutional political economy, and his "politics as exchange" approach provides the foundation for much work in that area. Buchanan has created a foundation that is rich in ideas, but leaves behind a number of unanswered questions that point the way toward a further development of the research program in constitutional political economy.

Keywords James Buchanan · Constitutional economics · Classical liberalism · Economic freedom · Politics as exchange · Public choice

JEL Classification · H1 · H4

James Buchanan's academic work stands on a classical liberal foundation, something he shares in common with other great classical liberal economists of the twentieth century, including, among others, Milton Friedman, Friedrich Hayek, and Ludwig von Mises. Buchanan's academic work stands apart from most other

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classical liberal economists because whereas their work focused primarily on the operation of markets, or the way that government policy affected markets, Buchanan's academic work focused primarily on the operation of government. Buchanan (2000) makes it clear that he not only views himself as a classical liberal, but views his classical liberal agenda as an important undertaking. The limits of liberty, according to Buchanan (1975), lie between anarchy and Leviathan. Buchanan followed the analysis of Hobbes (1651) by arguing that anarchy would bring with it a war of all against all, but also followed the ideas of the American Founders who believed that while government was necessary to preserve liberty, it is also the greatest threat to individual liberty.

Social organization based on voluntary action through mutual agreement is the way to preserve individual liberty, both in markets and through government. Buchanan's classical liberal ideology strongly supports individual exchange in the marketplace, as Buchanan (1954b) explains, and he used public choice analysis to extend this idea to government by depicting the political process as based on exchange. A liberal political system is one in which individuals agree to accomplish collectively ends which they would be unable to accomplish individually, or through bilateral exchange. This paper describes Buchanan's support for market exchange on classical liberal grounds, explains the parallel he draws between market exchange and political exchange, especially at the constitutional level, and then discusses some unanswered questions that remain in Buchanan's constitutional political economy.

1 Economic freedom and the scholarly work of Buchanan

As Buchanan sees it, the foundation of liberty—both economic freedom and political liberty—is the ability to deal with others through voluntary exchange for the mutual benefit of everyone involved in the exchange. Economic freedom implies that individuals have a right to decide how they will use their time and talents. In a liberal society, people do not have a right to take things from others or demand that others provide things for them. Economic and political systems that do that are the Leviathan that Buchanan (1975) said went beyond the limits of liberty. Voluntary agreement is the key element in Buchanan's vision of classical liberalism. Buchanan consistently argued that agreement and voluntary exchange were essential for the preservation of individual liberty, in both markets and through government. He also believed that they provided the framework for sensible analysis of both markets and political institutions. Thus follows Buchanan's vision of politics as exchange.

Buchanan's advocacy of economic freedom and market allocation comes across strongly in his work. In his first book, a co-authored volume written for the introductory principles of economics college course, Allen et al. (1954: 373)[1] state,

> It is conceivable that a completely socialist state, in which all or most economic decisions would be centrally made, could prove as 'efficient' in

[1] We note with some pride, as members of the Florida State University economics department, that Allen, Buchanan, and Colberg were all members of our department when they wrote that book.

> practice as the free-enterprise system. (We do not think this would be the case, but let us assume that it might be.) The case for a private-enterprise system would still be strong. The socialist state or other type of centrally planned economy (*e.g.*, the fascist states of Hitler and Mussolini) secures such efficiency as it achieves only at the cost of freedom of the individual. … The free-enterprise system is the only one that guarantees a maximum degree of freedom for the individual along with a high degree of productivity efficiency.

This passage clearly illustrates Buchanan's preference for freedom of exchange over government coercion.

In a passage that echoes Hayek (1944) and anticipates Friedman (1962), Allen et al. (1954: 373–374) go on to say,

> A government that is required to make most of the economic decisions cannot long remain effectively democratic in any meaningful sense. As government becomes more powerful in economic affairs, legislators and administrators are increasingly subjected to pressure by organized groups seeking economic gain. Democratically chosen officials who wield great economic power are especially unlikely to be champions of the rights of the people as a whole. In a fundamental sense, therefore, the competitive economy may be considered a necessary condition for the maintenance of political democracy.

They introduce an element of public choice by depicting government as subject to influence by interest groups, rather than as an institution that works to promote the common good.

These passages illustrate both the support of economic freedom through voluntary exchange in markets and the fundamental ideas of public choice. Unlike most economics textbooks (even today!), Allen, Buchanan, and Colberg do not consider government to be an organization that implements optimal public policy, but rather one in which people face their own incentives which often work against the public interest. Noting that a market economy is a prerequisite for democratic government, Allen, Buchanan, and Colberg recognize that too much government interference with the market economy will push a society beyond the limits of liberty.

The same year the textbook was published, Buchanan (1954b) offers a series of now-familiar arguments explaining why people's preferences are better satisfied through market exchange rather than through voting. He does not look at the institutions that underlie either markets or voting in any detail. But the idea that the advantages of markets come from individuals being able to make their own choices for their own benefit comes across clearly. Buchanan's ideas in this article foreshadow Friedman's (1962) support of markets, and lay the foundation for a more thorough investigation of the institutions that allow markets to better satisfy individuals' preferences. This work also provided the foundation for our own research on measurement of economic freedom and analysis of how it influences the performance of economies. See Gwartney et al. (1999, 2004, 2012) for examples.

Buchanan has consistently examined the market mechanism as an institution that allows individuals to cooperate with each other to improve their welfare. Buchanan

(1979: 26, emphasis in original) says that economists should "… concentrate on *exchange* rather than *choice*." The subject matter of economics should focus on the process by which individuals cooperate to achieve their ends, rather than on maximizing behavior of individuals and firms. An economy consists of individuals who work together to their mutual advantage, not individuals taking the actions of others as data to maximize utility or profit. Economic problems are social problems, not technological problems. Comparing an analysis of an individual choosing among alternatives to a group of individuals engaging in economic activity, Buchanan (1979: 28) says, "The fact of association requires that a wholly different, and wholly new, sort of behavior take place, that of exchange, trade, or agreement." This illustrates Buchanan's basis for the easy transition from exchange in markets to his vision of politics as exchange, using the same criteria to evaluate collective action that he uses to evaluate bilateral exchange.

Buchanan focuses on the process of exchange rather than the outcome that results from the exchange, so the characteristics of individual preferences that economists often assume (transitivity, diminishing marginal rates of substitution, and so forth) are of limited relevance. The relevant aspect of the exchange is that the parties are engaged in a transaction for their mutual benefit, and the focus is on the institutions that facilitate the exchange. Buchanan takes this same framework forward when looking at collective decision-making, where the emphasis is on the process by which the collective exchange takes place, and on the institutional framework that sets the parameters of potential collective action.

Buchanan (1962b) takes an institutional approach to economic exchange when he argues that little insight is gained by applying the Pareto principles to simple exchanges of goods and services. Individuals have an incentive to engage in mutually advantageous exchange as long as institutions do not create transaction costs that are too high, so with a given institutional framework, a Pareto optimum is produced almost tautologically. Buchanan (1962b: 341) says "… the Pareto criterion is of little value when employed solely to classify 'results' defined with respect to the orthodox economic variables… the criterion must be extended to classify social rules which constrain the private individual behavior that produces such results."

The Pareto concepts make more sense when applied to rules and institutions. Much of Buchanan's work involved the analysis of public sector institutions and collective decision-making, but those ideas apply to the analysis of market institutions as well. One can see a direct connection between Buchanan's analysis of markets as exchange rather than maximizing behavior, and his analysis of the institutions of collective decision-making. Buchanan (1962b: 353) says

> … the operation of alternative rules can only be evaluated in terms of predicted results, and the Pareto construction can be helpful in this process. At the level of application to the social constitution, to the evaluation of the 'rules of the game,' the Pareto criterion serves, however, a function that it cannot possibly serve in the more standard usage. Unless the observing economist is

> assumed to be omniscient, his classification of a final position as nonoptimal can never be more than a conjectural hypothesis that is impossible to test.[2]

This points toward an institutional approach to economic analysis.

People will engage in exchange as long as it is in their mutual advantage to do so, but sometimes institutional constraints may stand in their way—transaction costs, to use the term popularized by Coase (1960). With a given set of institutions, resources will be allocated Pareto optimally tautologically: people will exchange when it is mutually beneficial to do so. If institutional constraints stand in the way, then a Pareto improvement can be made by changing those constraints: by modifying the rules of the game. Buchanan's focus is on the institutions that allow exchange rather than the outcome one might expect from market exchange. The key element is agreement among individuals involved. Connecting Buchanan's analysis of markets and government, in both cases agreement provides the evidence on whether outcomes are welfare enhancing.

Sometimes it might appear that economic outcomes are nonoptimal when the institutional context of the outcome is not taken into account. Buchanan (1962b: 348) uses the example of traffic signals. It appears nonoptimal for a driver to stop at a red light if no other traffic is approaching the intersection, but traffic signals provide order for potentially conflicting traffic, enhancing welfare. Buchanan's institutional approach contrasts with the outcome-based approach taken by the general equilibrium framework for evaluating welfare. Optimal results are generated by an institutional structure allowing individuals the economic freedom to engage in mutually advantageous exchange.[3] Buchanan's framework emphasizes the importance of individual choice, which focuses on the institutions that allow exchanges that improve the welfare of those who are party to the exchange.

When Buchanan discusses economic freedom, it is to emphasize the advantages of individual choice that allow people to engage in market exchanges for their mutual benefit. The market allows people to cooperate to accomplish their mutual ends. This cooperation requires an institutional framework that facilitates exchange, both by protecting participants' rights to engage in mutually advantageous exchanges and by protecting individuals from having their rights violated by others. In a sentence, a market economy enhances individual welfare by facilitating mutually advantageous exchanges.

2 Political liberty: politics as exchange

Sometimes people have ends that require collective action: the cooperation of many people. Buchanan applies the same methodology used to analyze individual exchanges through markets to the collective decision-making process. Groups of

[2] This passage is related to Buchanan's (1969) book on the subjective nature of cost. One can never know what the results might have been of an option that was foregone.

[3] Buchanan (1990) depicts his constitutional political economy research program as analyzing the choice among constraints, contrasting it with models of individual behavior in which individuals make choices subject to constraints.

individuals can collectively agree to further their individual interests through collective action when bilateral exchanges cannot accomplish those ends. Buchanan (1949: 498) says "The state has no ends other than those of its individual members and is not a separate decision-making unit. State decisions are, in the final analysis, the collective decisions of individuals." Discussing political exchange, Buchanan and Tullock (1962: 4) say, "In a genuine sense, economic theory is also a theory of collective choice, and, as such, provides us with an explanation of how separate individual interests are reconciled through the mechanism of trade or exchange." The idea here is that both markets and politics are mechanisms for individuals to engage in cooperative behavior so that, working together, they all can be better off.

Reviewing Arrow (1951), Buchanan (1954a: 116–117) states, "… the individual is the only entity possessing ends or values. … A social value scale as such simply does not exist. … Arrow's analysis appears to consist … in proving that the decision-making processes themselves define no social welfare function…" As Buchanan has often argued, there is no such thing as social welfare beyond the welfare of individuals, and viewing politics as exchange, government is a mechanism that allows individuals to act collectively to accomplish their individual ends.

Further explaining their conception of politics as exchange, Buchanan and Tullock (1962: 13) argue, "Collective action is viewed as the action of individuals when they choose to accomplish purposes collectively rather than individually, and the government is seen as nothing more than the set of processes, the machine, which allows such collective action to take place." Just as the market mechanism is the machine that allows cooperation through bilateral exchange, government is the machine that allows cooperation when bilateral exchange is unable to further people's ends. Buchanan and Tullock continue (1962: 19),

> The market and the State are both devices through which co-operation is organized and made possible. Men co-operate through exchange of goods and services in organized markets, and such co-operation implies mutual gain. … At base, political or collective action under the individualistic view of the state is much the same. Two or more individuals find it mutually advantageous to join forces to accomplish certain common purposes. In a very real sense, they 'exchange' inputs in the securing of a commonly shared output.

Buchanan's view of collective action is not that there is some common good that individuals strive to advance through government; rather, individuals have their own ends that they hope to satisfy, and sometimes doing so requires collective action. Building on Wicksell (1967), people cooperate for their mutual benefit. This idea of politics as exchange clearly shows itself in Buchanan's (1965) theory of clubs, where the institutional framework for provision of a public good is depicted as a club rather than a government.

In perhaps the most widely-cited chapter from *The Calculus of Consent*, Buchanan and Tullock (1962: Ch. 6) explain how everyone can be better off agreeing to a less-than-unanimous decision rule for collective action, recognizing that sometimes individual decisions may go against their interests. The traffic light analogy cited earlier offers an example. While it is narrowly not in an individual's interest to stop at a red light when no other traffic is entering the intersection, the general rules for using traffic lights improve everyone's welfare. Similarly, if some collective decisions go against the individual's narrow interests, the overall collective organization enhances everyone's welfare. As with Buchanan's analysis of markets, the exchange takes place to further the individual goals of those engaging in the exchange. There is no "public interest" beyond the interests of the individuals engaging in the collective action. Also as with Buchanan's analysis of markets, the institutions that allow these exchanges to take place are the key to ensuring that they do, in fact, further the interests of the participating individuals.

This idea goes back to Buchanan's earliest published work. Buchanan (1949: 496) objects to analysis that views the state "… as a single organic entity…" and says "… the state is represented as the sum of its individual members acting in a collective capacity. … These two approaches have not been clearly separated or distinguished in the literature of government finance." Looking at that literature on government finance, Buchanan (1949: 497) observes that the revenue and expenditure sides of the government's budget are typically analyzed independently of each other, and says "… that the optimum values for the tax variables cannot be determined independently except for given values for the expenditure variables." People exchange their tax payments for government output, with the anticipation of being better off as a result of the exchange. Buchanan (1949: 500) goes on to say, "Fiscal analysis has proceeded as if all taxes were net subtractions from social income, never to be returned." Taxes are the price we pay for government goods and services, and it makes little sense to analyze the "optimality" of a tax structure without taking into account the benefits those tax revenues provide through government expenditures.

Buchanan would not say that all government action benefits those who are governed, because institutions can be designed in a way that they systematically benefit some at the expense of others. Outcomes that further the interests of the participants in collective action are mutually beneficial when the participants all agree to the procedures that facilitate the collective action. In markets, mutually advantageous outcomes result from an institutional structure based on the protection of property rights and rule of law. Institutions are important. Similarly, in government, institutions must be designed to facilitate mutually advantageous exchange, or Leviathan government can work to the disadvantage of some—and perhaps a majority—of its citizens. Brennan and Buchanan (1985: 2) note, "If rules influence outcomes and if some outcomes are 'better' than others, it follows that to the extent that rules can be chosen, the study and analysis of comparative rules and institutions become proper objects of our attention."

3 Political liberty through hypothetical agreement

The parallel Buchanan draws between market exchange and politics as exchange rests on the idea that participants in collective action consent to the actions of the group in a manner analogous to the way that participants in market exchanges mutually agree to undertake their exchanges. When one looks at the actual operation of government, this parallel clearly breaks down, because everyone does not agree to government actions. Buchanan (1962a) recognizes this, noting that in democratic decision-making, the majority imposes a cost on the minority, so in the absence of actual unanimity, every government action creates an externality. The minority ends up worse off as a result of the government action. Buchanan and Tullock (1962) address this issue by noting that people might agree to the general constitutional framework for making choices, and in the aggregate are better off with the government activity than without it. One innovation Buchanan and Tullock (1962) introduce is the idea that politics as exchange does not require that everyone agrees with every individual action government takes, if they agree with the procedure that leads to those government actions.

The constitutional framework in Buchanan and Tullock (1962) is incomplete because it does not indicate how citizens might demonstrate their agreement with constitutional rules. Buchanan (1975) addresses this issue by devising the criterion of a conceptual agreement in a hypothetical renegotiation from anarchy. The idea, in a few sentences, is to imagine everyone in a situation of Hobbesian anarchy, where there are no rules or institutions, and life is a war of all against all. From anarchy, people negotiate a social contract and agree on the rules within which they will interact, including the rules for collective decision-making and government action. Used as a benchmark for evaluating government action, if people would agree to the institutions that led to some government action in a renegotiation from anarchy, then Buchanan (1975) says that they are in agreement. Buchanan (1975: 53–54) says,

> In order to discuss or analyze possible criteria for modifying the structure of rights, however, some understanding of conceptual origins may be helpful. As has been suggested, the problem is one of trying to explain and understand the relationships among individuals, and between individuals and government. And for this purpose, various 'as if' models of conceptual origins may be necessary, regardless of the facts described by historical records.

Buchanan (1977: 11) says, "I believe that conceptual agreement among individuals provides the only benchmark against which to evaluate the observed rules and actions taken within those rules." Thus, Buchanan justifies his framework of conceptual agreement from anarchy.

Not everyone finds Buchanan's hypothetical renegotiation from anarchy to be an acceptable criterion for agreement. Yeager (1985, 2001) argues that to say that people hypothetically agree means that in fact, they did not agree. Yeager's criticism points directly at Buchanan's idea of agreement to preserve liberty within the political process. Yeager points out that everything the government does is based on coercion, not agreement. This is true regardless of how much people support the actions of their governments. If people would voluntarily exchange their taxes for public services, there would be no reason for the government to back its demand for tax revenues with the threat of force for those who did not comply. If people would voluntarily follow the regulations government mandates, there would be no reason for government to back its regulatory demands with the threat of force for those who did not comply. No matter how much people favor government's mandates, force underlies all of them, and the only reason for government to act is to force people to do things they otherwise would choose not to.

One might use the argument that people agree to be coerced, following along the lines of Hochman and Rodgers (1969). Without government coercion, people can free ride off the public goods provided by others, so people are willing to contribute to the public good as long as everyone else does too. Government enforces this bargain. The problem with this argument in the context of a search for the limits of liberty, Holcombe (2011) argues, is that in fact, people did not agree. The argument suggests that people who say "No, I do not want to contribute to the public good" are free riders, but there is near certainty that for everything government does, some people will genuinely prefer not to pay, and not to have government undertake the activity. The "agree to be coerced" argument gives government license to coerce people who are not, in fact, in agreement with their government's actions. Any argument based on hypothetical agreement rather than actual agreement opens the possibility for government coercion to go beyond the limits of liberty.

4 The role of government: the protective state and the productive state

One way to preserve liberty through constitutional means is to place constitutional limits on the scope of government. The Constitution of the United States was designed this way, giving the federal government enumerated powers, and then specifying in the 10th Amendment, "Powers not delegated to the United States by the Constitution, nor prohibited by it to the states, are reserved to the states respectively, or to the people." Considering the possibility that government might overstep the limits of liberty, Buchanan does not take the approach of constraining government through enumerated powers, but rather considers the appropriate limits on the scope of government to be those limits to which people agree. Buchanan divides the functions of government into the two broad categories of protection and production. Buchanan (1975: 68–69) says the productive state is "… that agency through which individuals provide themselves with 'public goods' in postconstitutional contract. In this latter context, collective action is best viewed as a complex exchange process with participation among all members of the community." There are no limits Buchanan imposes on the scope of the productive state, except the procedural limit that people must agree to it. In Buchanan and Musgrave (1999: 83), Buchanan says, "I am not willing to impose my own preferences on that question [about the optimal size of the public sector]. Whether or not citizens as individuals want to spend their resources collectively through joint action, or whether they want to spend them privately, is for people to decide themselves."

Buchanan takes a procedural approach to the scope of government and the limits of liberty. The determining factor on whether government has overstepped the bounds of the limits of liberty is whether citizens agree to the government's actions. If they do, then the procedural requirement of agreement indicates that government's action is a joint action of all citizens who have chosen to spend their resources collectively. If people are in agreement, their liberty is preserved. Buchanan's work has been remarkably consistent throughout his long career, as

Sandmo (1990) and Meadowcroft (2011) note, and this idea of agreement and exchange in both the public and private sectors goes back to his earliest work (e.g., Buchanan 1949) and extends up through his most recent.

Can people collectively agree to sacrifice their liberty? It does not appear so, in Buchanan's framework. If everyone was to agree to confiscatory taxation, or to have the means of production owned in common, or anything else, that would be the result of an exchange everyone favored, so liberty would be preserved. We would be more comfortable with this idea if instead it was phrased to say that everyone agreed to give up some liberty, rather than Buchanan's implication that anything everyone agrees to remains within the limits of liberty. There is an apparent tension between Buchanan's constitutional benchmark of agreement to collective action and his classical liberal support of free market institutions that might be voted away.

5 Is government the product of agreement?

Yeager's (1985, 2001) objection that in fact all government action is based on coercion, not agreement has already been noted, and Buchanan would not argue that his contractarian model based on agreement is descriptive of the real world. Discussing *The Calculus of* Consent, Buchanan (1975: 6–7) says,

> The framework for analysis was necessarily contractarian, in that we tried to explain the emergence of observed institutions and to provide norms for changes in existing rules by conceptually placing persons in idealized positions from which mutual agreement might be expected. … I have come to be increasingly disturbed by this basically optimistic ontology. … Zero-sum and negative-sum analogues yield better explanatory results in many areas of modern politics…

By this time Tullock's (1967) rent-seeking idea figured prominently in public choice, and Buchanan's more pessimistic view of government was that in actuality government action involved some people using the force of government to extract benefits from others rather than everyone collectively agreeing to joint production.

Buchanan (1975: 8) calls into question the view of politics as exchange, saying,

> So long as collective action is interpreted largely as the embodiment of individual behavior aimed at securing the efficiency attainable from cooperative effort, there was a natural tendency to neglect the problems that arise in controlling the self-perpetuating and self-enhancing arms of the collectivity itself. The control of government scarcely emerges as an issue when we treat collective action in strictly contractarian terms. Such control becomes a central problem when political power over and beyond plausible contractarian limits is acknowledged to exist.

Buchanan (1975: 161) later calls democratic institutions into question, saying, "Democracy may become its own Leviathan unless constitutional limits are imposed and enforced."

Brennan and Buchanan (1980: 20) model government as a revenue-maximizing monopoly, justifying the framework by saying “The monopoly-state model of government may be acknowledged to be useful, not necessarily because it predicts how governments always, or even frequently, work, but because there are inherent tendencies in the structure of government to push it toward that sort of behavior implied in the monopolistic model, tendencies that may emerge in settings where constraints are wholly absent.” Brennan and Buchanan (1985) follow up their work on taxation with a volume sub-titled “constitutional political economy,” where they discuss ways that constitutional rules can create an environment that channels individual actions away from predatory zero-sum and negative-sum action toward action that is positive-sum and mutually advantageous.

While Buchanan offers the contractarian framework as a model of politics as exchange, where people agree to undertake activities collectively for their mutual benefit, he also recognizes that this framework is not always descriptive of real-world government. The challenge Buchanan raises regarding his own constitutional framework is to design constitutional constraints that will direct government toward activities that benefit everyone, away from predatory activities that emerge from rent-seeking and special interest politics.

6 Buchanan’s normative vision: political liberty and politics as exchange

Buchanan (2000) makes it clear that he considers himself a classical liberal, and considers the classical liberal agenda to be important to the maintenance of a free and prosperous society. His depiction of politics as exchange is an application of his classical liberal ideas, as he makes the analogy between voluntary and mutually advantageous exchange in the private sector and collective action that allows groups of people to engage in mutually advantageous activity. As the previous section notes, Buchanan is not arguing that government action actually is agreed upon by the citizenry, or that it creates mutually beneficial outcomes. Recognizing the rent-seeking and special interest politics that provides benefits for some at the expense of others, the politics as exchange framework is a vision for the way government should work, not a description of the way government does work.

Buchanan and Wagner (1977), for example, discuss deficit finance in contractarian terms, arguing that it violates the social contract, and Buchanan and Devletoglou (1970) are critical of the organization of higher education at mostly state-run institutions. It is apparent that Buchanan’s vision of politics as exchange is not meant as a description of real-world political processes. Buchanan’s contractarian framework has a strong normative foundation, indicating that welfare would be increased if collective decision-making worked as the contractarian model describes. He is saying government should work that way; not that it does. Ideally, collective action through government would be characterized by voluntary agreement and mutually beneficial exchange, in the same way that market exchanges are voluntary and mutually beneficial.

7 Political liberty and the contractarian framework: three issues

Buchanan's view is that liberty resides somewhere between anarchy and Leviathan. Buchanan (1975: 3) says, "The anarchist utopia must be acknowledged to hold a lingering if ultimately spurious attractiveness. Little more than casual reflection is required, however, to suggest that the whole idea is a conceptual mirage." At the other end of the continuum lies Leviathan: the oppressive government that suppresses liberty. Buchanan's contractarian vision of liberty is to have a constitutional government in which the constitutional rules are agreed to by all. Mutual agreement is the common element that links market exchange with unanimous agreement on the constitutional rules, and that agreement, in markets and in politics, signifies a mutually advantageous exchange.

However, this vision does not line up with the facts of the real world. In markets people actually do voluntarily agree to the exchange, but with government most people do not actually agree to the rules. Regardless of whether they approve of them, government's rules are imposed by force without giving people the choice of whether to enter into the bargain. So, Buchanan (1975) creates the device of renegotiation from anarchy to argue that if people would agree to the terms government imposes on them in a renegotiation from anarchy, then they can be said to be in agreement. Consider three issues that present themselves in this framework.

First, in a constitutional framework that applies to everyone, nobody will get the first-best set of rules that he or she would most prefer. Consider something simple like highway speed limits. People will have differing preferences, so the actual speed limit will be a compromise that will be faster than some people would prefer and slower than others would prefer. So, just because a person disagrees with one provision of the social contract does not mean, in Buchanan's framework, that the person would not agree to that contract in a renegotiation from anarchy. The result must be a compromise.

Consider another example. Buchanan and Wagner (1977) argue that deficit financing violates the social contract. Does that mean that Buchanan would prefer anarchy to the actual state of affairs where there is police protection, courts, and a budget deficit? The framework in which agreement is depicted as a hypothetical renegotiation from anarchy leaves substantial ambiguities regarding what are legitimate constitutional rules. Buchanan's procedural theory does not indicate what specific constitutional rules would meet his procedural test.

Second, as Yeager (1985, 2001) notes, Buchanan's device of hypothetical agreement means that people did not, in fact agree. In the context of finding the limits of liberty, Buchanan's device can be used to argue that people who do not agree are, in fact, in agreement. If a person objects to some provision of the constitutional framework, one response is to say that the person would agree in a renegotiation from anarchy. How could one disprove this assertion about a hypothetical event that is far-removed from reality? Despite Buchanan's concern about the limits of liberty, Buchanan creates a framework that can be used to justify violations of individual liberty by resorting to an argument about a hypothetical and unrealistic state of the world.

Third, Buchanan's social contract provides justification for any provision to which people would agree. It does not rule out cases where people would agree to give up their liberties. People might agree to give up all their property, give up the right to the product of their labor, and to follow the commands of a charismatic leader. Setting aside whether this might reasonably happen, it is not ruled out by Buchanan's benchmark of agreement.[4] If Buchanan is really concerned about the limits of liberty, the framework he develops is not sufficient to preserve liberty.

8 Conclusion

James Buchanan's classical liberal values show up in his analysis of both markets and government, and in both, those classical liberal values are operationalized through institutions that are based on agreement and exchange. The agreement and exchange that obviously forms the basis of market transactions can also occur in government activities, if people agree to the rules under which those activities take place so that the activities produce mutually advantageous outcomes. With market transactions, exchange is voluntary and therefore agreement provides the basis for them. Further, the agreement of the trading partners provides evidence that the exchange is mutually advantageous. Political liberty means that collective action through government takes place within an institutional structure that meets with the general agreement of the citizens governed by those institutions. This is Buchanan's framework of politics as exchange.

The parallel Buchanan draws between market exchange and political exchange holds up only as long as political institutions can be said to satisfy the criterion of agreement, and because there is no actual agreement to those institutions—governments impose them on people regardless of their consent—a part of Buchanan's research program was to offer explanations for how political institutions might meet with criteria of implied agreement. Buchanan and Tullock (1962) explain how people could consent to less-than-unanimous decision rules, and Buchanan (1975) explains how people might conceptually agree to a social contract without the requirement of actual agreement.

Buchanan clearly believes people are better off with a government that both protects their rights and produces public goods, so he recognizes the potential benefits of government, and it follows that people should agree to institutions that provide them benefits and improve their welfare. That is, people should agree to a government that protects their rights and produces public goods. Buchanan also clearly believes that government can be either suboptimally small or excessively large and oppressive, so liberty lies between anarchy and Leviathan. As with market exchange, the criterion for producing political liberty is consent. When people agree, transactions result in mutually beneficial exchange. This is the straightforward logic underlying Buchanan's framework for political liberty.

[4] Indeed, Hayek (1944) and Schumpeter (1947) both made arguments that people were consenting to give up their liberty.

We raised three questions about this framework. First, because people must agree on a collective set of rules that apply to everyone, nobody will get his or her most preferred outcome. In light of this, there is some ambiguity as to the exact terms of the social contract. Second, because Buchanan's criterion does not require actual agreement, his arguments could be used to support government programs and actions that would not actually command agreement. In theory, people could agree to be coerced, but in practice, if people have no choice but to be coerced, there is no way to tell whether a conceptual criterion of agreement is satisfied. Third, in the context of Buchanan's classical liberal view on the importance of preserving liberty, his criterion of agreement leaves open the possibility that people could agree to collective rules that reduce or eliminate liberty. Agreement and liberty seem to be uneasy partners in Buchanan's framework, and this is one issue Buchanan did not address in his work.

Buchanan is the unquestioned father of constitutional political economy, and he has left behind a framework rich in ideas. His emphasis on agreement, his analysis of the importance of constitutional constraints, and his clear recognition of the threat Leviathan government poses to liberty and economic well-being provide a foundation for constitutional analysis and a roadmap for the future development of the field. The issues we raised were intended only to suggest that while Buchanan has started us on that road, there are still unanswered questions, and that there is more work to be done in constitutional political economy.

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