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Political Property Rights and Governance Outcomes: A Theory of the Corporate Polity

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Abstract
I present a theory of political property rights that complements familiar Tiebout mechanisms in explaining governance outcomes. I argue that when the structure of political property rights is such that the polity most closely resembles a corporation, governance will be largely productive. In contrast, when the structure of political property rights is such that the polity is characterized by a tragedy of the commons, governance will be largely predatory and will promote rent seeking. I illustrate my theory with reference to two corporate-like polities, Singapore and the United Arab Emirates, as well as the literature on private city planning on urban development. I also discuss the assumptions to which my analysis is sensitive. I conclude by exploring possible future trends in governance in light of my theory.

JEL Codes: D72, H11, H77, P14, P16
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I. Introduction

This paper develops a theory of incentive alignment in formal governance institutions based on the structure of political property rights. It also explores how this structure affects the quality of governance as perceived by a representative polity dweller. By combining factor mobility (Tiebout 1956) with well-aligned political property rights, I arrive at a powerful incentive-alignment mechanism for rulers. I define a political property right as one that guarantees an individual or a group the right to participate in political decision-making and a claim to the revenues generated therefrom (see, e.g., Salter 2014). Differing political property rights structures incentivize

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differing governance strategies, as implicitly shown by rational choice analyses of political structures (see, e.g., Buchanan and Tullock 1962; Tarko 2014). The framework I develop will ultimately be oriented toward increasing the intelligibility of governance institutions, but it is still consistent with standard methodological practice (e.g., Friedman 1953) provided that an appropriately broad conception of prediction is adopted.

Similar to Olson (1993), I will classify the state as a corporate body, and specifically as a corporation in the "business" of maximizing appropriable rents. While the Weberian definition of a state is mostly satisfactory for my purposes, I alter the definition slightly to consider the behavior of an organization (whether executive-dominated or council-dominated) that is sovereign, in that it is de facto the final enforcer of the specific sets of rights-claims within its purview (see, e.g., Salter 2015b). Considered this way, there is always a sovereign; the issue lies in specifying the range of rights over which the sovereign claims authority. This focuses the analysis squarely on the underlying property rights arrangement, which again is the institutional structure determining how rational agents will behave. Some property rights arrangements will cause agents to behave in a manner conducive to widespread flourishing: they will protect subjects' property rights and engage in some collective goods provision. However, other property rights arrangements will cause agents to behave in a manner that results in widespread malaise: they will prey on subjects and promote rent-seeking behavior. In both cases, agents with political property rights will act according to their own self-interest—that is, engage in wealth-maximizing behavior. Whether this behavior results in the "productive state" or the "predatory state" (Buchanan 1975) depends on whether the incentives afforded by the political property rights structure result in harmony or a conflict of interest with the public at large.[1] The interests of subjects must be evaluated with respect to their preferences, but these preferences must be confronted with real trade-offs. The desire for goods and services provided by holders of political property rights cannot be considered without reference to these trade-offs. Choice divorced from cost is meaningless (Buchanan 1969).

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[1] Ideally, there is some property rights structure that results in an implicit generality norm—governance in the interests of a supermajority of subjects, and conceptually unanimously so (Wicksell 1958; Buchanan and Congleton 1998; Salter 2015a).

In addition to the work already cited, my framework contributes to two related literatures. The first focuses on "inclusive" governance institutions and their effects on social, political, and economic outcomes (see, e.g., Acemoglu and Robinson 2005, 2012; North, Wallis, and Weingast 2009). The main theme running throughout these works is that by expanding the inclusiveness of political decision-making processes, elites' propensity to use and promote governance institutions that benefit themselves at the expense of the public at large are curtailed. However, what is less often emphasized is that there is such a thing as excessive inclusiveness—the point at which, because there are so many political decision-makers, each individual decision-maker rationally refrains from acquiring information that can improve the quality of political decision-making. This excessive inclusiveness also can result in the capture of political processes by groups that use political machinery to benefit themselves at the expense of the public, due to concentrated benefits, dispersed costs mechanisms. These mechanisms probably explain why a recent meta-study of the empirical literature on democracy and growth (Doucouliagos and Ulubaşoğlu 2008) failed to find a clear relationship. A corporate polity, in order to govern in a (social) wealth-maximizing manner, and thus in the interests of subjects as well as rulers, must discover a way of navigating the trade-offs associated with the inclusiveness of political decision-making.

The second literature studies private governance (Anderson and Moroni 2014; Beito, Gordon, and Tabarrok 2004; Leeson 2014; Salter and Hall 2014; Salter and Hebert 2014; Stringham 2015; see also Powell and Stringham 2009, and the references therein). I contribute to this literature by further drawing out the structure of political property rights that will result in wealth-producing governance. Private governance solutions to social problems typically involve both residual claimancy and jurisdictional competition as responsibility mechanisms, which also are important in the generation of governance-relevant feedback concerning the efficacy of a given governance strategy. My analysis of political property rights also makes use of these mechanisms.

I organize the remainder of the paper as follows. Section 2 discusses the foundational concepts on which my economic analysis of the corporate polity relies. Section 3 uses these concepts to highlight important features of the underlying political property rights structure, drawing support from two case studies and a related literature. Section 4 discusses issues of scope and scale that will influence the structure of the corporate polity. Section 5 concludes by discussing the analysis in light of future trends in global governance, with special attention on how changing decision-making costs, relative to other costs, influence the makeup of the optimal corporate polity.

II. Prices, Politics, and Predation—Peculiarities of the Corporate Polity

The conception of the state as a corporation—albeit an unusual one—is commensurate with Wagner's (2016) analysis of politics as a peculiar kind of business. Politics is exchange (Buchanan 1987, section 4), but the peculiarities of political exchange must be explored in order to understand the implications of political bargains on social wealth. One of these features is that political bargainers and entrepreneurs frequently engage in exchanges that impose on third parties obligations to which they did not consent. Varying slightly the themes of Podemska-Mikluch and Wagner (2013), market exchange is dyadic; the "ideal type" of market trade is two parties engaging in a mutually preferred exchange of property rights. In contrast, the ideal type of political exchange is triadic; it involves unwilling third parties who are coerced into the exchange and who serve as the source of the gains between the main parties to political exchange. In this scheme, the political analog of market prices are tax prices. Market prices emerge as the outcome of voluntary trades of private output; tax prices emerge as the outcome of voluntary and involuntary trades of public output (Eusepi and Wagner 2013). Thus, the political pricing process possesses some aspects that are fundamentally predatory.

The key feature driving this result is the political commons, as exists in modern democratic polities (Wagner 2007, 2012b, 2016). In the political realm, the tax base is a common pool resource, the use of which no political actor has an incentive to economize. While elections do offer some constraint, their ability to discipline political actors is greatly vitiated by familiar public choice problems such as rational ignorance. This weak constraint provides a corridor within which holders of political property rights can use these rights to stake claims to the economy's social product (Salter 2014, pp. 15–19).[2]

[2] Although the modern state is a commons, it is still meaningful to speak of political property rights holders as agents who possess de facto rights of control, with accompanying informal claims to the economy's social product. Some property rights always exist, whatever the de jure status of these rights.

Even when political property rights holders in this environment cater to constituents, they have an incentive to do so by providing local benefits, the costs of which are borne by nonconstituents. In this case, the incentives afforded by the environment of state-as-commons direct political actors to advance their self-interest through creating exchange relationships that, while privately beneficial to the actor and his direct counterparties, are globally costly for society at large. The bottom line of Governance, Inc., and thus that of political property rights holders, is best served by productive governance only up to a point, beyond which predatory governance is preferred at the margin.

Another example of how the corporate polity differs from a traditional business organization is with respect to internal harmony of interest. Firms are typically modeled as profit maximizers. Despite the information and incentive frictions that exist within firms, such as principal-agent problems, that need to be overcome to meet this goal, it is reasonable to reduce the goal of those who make up the firm to a single maximand. A single objective function is appropriate, since the firm is an institution for joint production to achieve a shared goal. Reducing the goals of those who make up the corporate polity to a single value function is not reasonable, however. This is not to say that political property rights holders do not seek to maximize appropriable rents. It is to say that political property rights holders, in seeking to maximize appropriable rents, can and do find that their plans are not mutually consistent. A harmony of interests cannot be assumed to exist within the corporate polity. In Hayek's (1973) terminology, the corporate polity is an order (*cosmos*), but not an organization (*taxis*). This, too, is a function of the underlying property rights arrangements. That holders of political property rights often find their rights, and the claims these rights afford to the economy's social product, in conflict is due largely to the inherently fluid boundary between de facto political property rights. Because modern states are largely a political commons, political property rights cannot be sufficiently well-defined to ameliorate these conflicting plans.

One last difference between the corporate polity and the traditional corporation merits discussion. Because political property rights in modern democratic nation-states are largely informal, arising as a mechanism to cope with an otherwise even more severe tragedy of the commons, there is no ordinary secondary market in which they can be traded, and hence priced.[3] When combined with the above insight concerning the peculiarity of the political pricing process for public output, the link between internal and external incentive alignment that characterizes a well-functioning joint stock corporation is noticeably absent. Given this, it should not be surprising that political property rights holders find it most profitable to negotiate exchanges that are privately beneficial, the costs of which are passed on to others. The rent-seeking society of Tullock (2005) and Olson (1965) is ultimately the result of poor incentive alignment due to the underlying property rights scheme, just as low-quality management is a result of poor incentive alignment in a traditional corporate environment. Governance that is not in the public interest, in that it is predatory rather than productive, ultimately has its roots in basic economic insights concerning the importance of property rights. The role of nonmarket constraints, notably the economic justification of checks and balances (Buchanan and Tullock 1962) and polycentric federalism (Ostrom 1997, [1971] 2008a, [1973] 2008b), in limiting predatory governance are well known in the political economy literature. In contrast, the role of market constraints, and property rights in particular, receives less attention. However, the analysis here suggests that proper definition of political property rights will also better align the incentives of political property rights holders with the goal of social wealth maximization, and hence the welfare of the ruled.

III. Property Rights in the Corporate Polity

The account of the differences between a traditional corporation and a corporate polity yields a concrete prediction: the more closely a polity resembles a traditional corporation, in terms of its underlying property rights arrangements, the more likely holders of political property rights will be to govern prudently. Again, in this context, "prudently" refers to the propensity for political property rights holders to promote the productive state and to avoid the behaviors of the predatory state. In some sense, even hypothetically responsible governance on the part of the corporate polity is predatory, in that it claims final control over a well-defined set of rights within its territorial jurisdiction (sovereignty), and it defends these claims through the use or threat of coercion, not unlike Olson's (1993)

[3] Various informal markets negotiate the exchange of political property rights among political property rights holders.

stationary bandit (Salter and Hall 2014, pp. 8–11). However, when compared to the situation of the state-as-commons, as with Olson's roving bandits, the situation is a marked improvement in terms of wealth-producing governance.

Since few polities resemble the corporate polity I have described, the possibility of empirical analysis is limited. However, two cases illustrate the theory: the city-state of Singapore and the individual emirates that comprise the United Arab Emirates (UAE). In addition, taking a broader view, the literature on private city planning and urban development also supports my theory. Each will be considered in turn.[4]

A. Singapore

The governance arrangements in Singapore have resulted in the city-state receiving the tongue-in-cheek label "Singapore, Inc." The label perhaps contains more truth than its users realize. Founded in the early nineteenth century by the British Empire as an outpost of the East India Company, it has long been associated with a culture of "unhindered international trade and investment," (Siddiqui 2010, p. 3; see also Formal and Wojtera 2013, pp. 8–11, 21–24) policies which were then in the empire's regional interests. Since its independence in 1963, income per capita (in current dollars) has grown spectacularly, from $428 to $52,052 in 2012. In addition, Singapore has always been ranked fourth or higher on the Fraser Institute's ranking of polities in terms of economic freedom.[5]

Singapore's economic success has been coupled with governance that can perhaps justly be labeled authoritarian, but not totalitarian. While it is nominally a democracy, the People's Action Party (PAP) has exercised continuous political control since 1965. The PAP can be characterized as the "firm" that exercises sovereign governance rights in Singapore, with separate "personhood" from those who hold official positions, as with other traditional corporations. On the order-organization continuum, it is much closer to an organization than are corporate polities characterized by the state-as-commons. Combined with the de facto exclusive control over political property rights possessed by the PAP, and exercised by its members, Singapore's policy with respect to ministerial salary is perhaps the most convincing piece of evidence that Singapore, Inc., is a reality.

[4] The subsections on Singapore and Dubai are largely adapted from the relevant subsections of Salter and Hall (2014).

[5] The complete series of reports can be found at the Fraser Institute's website.

First, Singapore explicitly links the salary of civil servants with the wage conditions in the private sector, with the compensation of the former tracking the latter with an automatically updating formula (Low 2006, pp. 356–57). Second, civil servants' bonuses are directly tied to the rate of economic growth (World Bank 2001). Third, pay for civil servants (and especially top officials) is high and aimed at attracting talented administrators.

For example, in 1996, the salary paid to the President of the United States was $200,000. Singapore's chief executive that year was paid $812,858. Also, senior civil servants in Singapore made $292,714 on average, as compared with senior civil servants in the United States, who made $118,118 on average. This is even more pronounced when compared to the pay of legislators. Singaporean legislators made $65,174 on average, whereas US legislators made $133,600 on average (Low 2006, p. 359). This pay structure suggests that Singapore heavily emphasizes the execution of governance strategies, but values relatively little the legislative process as a source of such strategies. When combined with Singapore's well-known harsh punishments for shirking and corruption (Salter and Hall 2014, p. 17, n. 11), the result closely resembles the standard efficiency wages model for aligning worker incentives: significant rewards for agents who perform the duties prescribed by principals, combined with significant punishment for those who use their position, and the associated corporate resources, to further their interest at the expense of principals' interests.

One more general policy category merits discussion: Singapore's attitude toward taxation. Low (2006), in perhaps the most detailed study of the political economy of Singaporean governance, writes of the city-state's tax policy: "the substitutability between the two [types of revenue, tax-derived and nontax-derived] reflects the business, capitalistic, or entrepreneurial tendencies *of the state*" (p. 119, emphasis added). Singapore's operating expenditures are primarily derived from taxation, 84.1 percent in 2003, with fees and charges for publicly provided services making up 14.6 percent, and all other sources making up a mere 1.3 percent (Low 2006, p. 121). Its tax rates are, unsurprisingly, extremely low for the developed world. In 2004, the corporate tax rate was 22 percent, with only Hong Kong, Ireland, and Switzerland having lower rates. It began reducing top marginal tax rates on personal income in 2007, aiming to achieve "one of the most competitive personal tax regimes in the world" (Low 2006, pp. 134–35). These policies make sense in light of the

Laffer relationship between tax revenue and rates, and they fit closely with rule by political property rights holders who are confronted with a time horizon significantly longer than political property rights holders in a familiar, Western democracy, subject to the short-term electoral cycle.

B. The United Arab Emirates

If Singapore is modeled as a conglomerate in the business of providing governance, broadly defined, then the polities which comprise the United Arab Emirates (UAE) should be modeled as "family businesses" that provide similar services. The UAE is a confederacy of several smaller principalities (emirates). Most political authority is retained by the individual emirates, which are ruled as quasi-absolute monarchies. Some pooling of resources and delegation of authority takes place for certain key collective goods, such as national defense. The wealth of the UAE's member polities is well-known and frequently attributed to rentierism due to their significant oil holdings. While oil is certainly a cause of their material prosperity, it cannot be the sole cause: many other polities have abundant natural resources but remain poor, a phenomenon long recognized by development economists (e.g., Sachs and Warner 1995, 1997). As in all exercises in applied political economy, an institutional source of the member polities' wealth should be put forth. This source is the nature of political property rights.

Two features regarding the nature of political property rights in the individual emirates merit explanation. The first is the internal organization of each emirate as a family business. Of particular interest is that, contrary to the popular image of absolute or near-absolute monarchies, the ruling family is where political authority is primarily vested. The monarch has great power, but he is expected to rule in a manner that maintains the family's monopoly on political authority. The eldest male is not necessarily the monarch, or even the crown prince; instead, succession is determined by family consensus, itself a result of bargains over political power. This institutional structure, known in the context of Middle Eastern monarchies as "dynastic monarchism," (Herb 1999, chap. 2; Davidson 2005, chap. 2) arose contemporaneously with the rise of the Middle Eastern monarchies as "petro-states." Before the realization of oil wealth, state capacity in these monarchies was quite weak. Rulers frequently had to appoint relatives to bring order to defiant territories on behalf of the monarch, but frequently the result of this arrangement was the appointed relative solidifying his authority in the outlying territories to undertake a coup d'état. However, the growing value of oil rents changed the choice calculus of prominent royal family members jockeying for authority. Historical circumstances allowed the ruling family to monopolize these rents, which makes it in the interests of various family members, who still jockey for power, to limit their competition if it risks damaging the political authority and legitimacy of the ruling family. In exchange for limiting their political infighting, which has negative externalities for the ruling family, prominent nonruling family members are granted high-level political appointments and shares of oil rents (Herb 1999, pp. 30–31).

The second way to highlight the effects of political property rights on socioeconomic outcomes is by comparing governance in the emirates to governance in neighboring polities. Consider Dubai, perhaps the most well-known emirate. Dubai has managed to diversify its economy away from oil, with tourism, real estate, and financial services now comprising a significant portion of its economic activity (Salter and Hall 2014, p. 18). Although hit hard by the 2007–08 global financial crisis, Dubai continues to succeed at producing wealth-generating governance. In contrast, Kuwait, another Middle Eastern monarchy, has stagnated in recent decades. Part of the explanation for Kuwait's troubles undoubtedly lies in the Gulf War, but this is not sufficient to explain many of the long-term trends observed in the country. In particular, Kuwait's largely dysfunctional political sector has rendered economic progression increasingly difficult. Kuwait is known to be an especially difficult place to develop a business, especially compared to Dubai: "What takes one year to accomplish in Dubai takes ten years in Kuwait," Herb writes (2009, p. 381). In addition, Kuwait has fallen behind significantly in attracting foreign direct investment. Kuwait's merchandise exports were 86 percent of the UAE's in 1980, but by 2006, they had fallen to 5 percent. Tourism and transportation statistics tell a similar story. In 2005, the UAE had six-and-a-half times as many airport passengers, and fourteen times as much freight container traffic at its ports (Herb 2009, p. 337; Salter and Hall 2014, p. 21).

The differing political property rights arrangements in Kuwait and the UAE explain the significant difference in economic outcomes. While much of the Middle East was once a colony or outpost for the British, Kuwait has a unique experience as a British suzerainty, and thus a distinctive tradition with political forms that resemble liberal democracy. In contrast, the emirates that comprise the UAE, as already mentioned, are near-absolute monarchies. This suggests key differences in the structure of political property rights across polities. In Kuwait, a constitutional parliamentary monarchy, the state is a commons. In the emirates, it is privately owned, with rights to governance revenues made quite explicit. "In the UAE, in the absence of a parliament, political power resides primarily in the hands of those who have an interest in private-sector growth" (Herb 2009, p. 384). Thus, it is unsurprising that politics in Kuwait is characterized by a significant degree of rent seeking, whereas this particular kind of socially costly behavior is strongly checked by the institution of the ruling family in the emirates. Herb (2009, p. 385) explicitly likens governance in the Middle Eastern dynastic monarchies to that of corporations, whose largest shareholder is the ruling family. My analysis suggests that this is more than an analogy; it is a meaningful characterization of actual governance arrangements, in light of the underlying political property rights structure (Salter and Hall 2014, pp. 21–22).

C. Private Community Planning and Development

Singapore and the UAE are specific examples of polities that characterized corporation-like governance arrangements. Broadening our perspective, the literature on private city development and urban planning (e.g., MacCallum 1970; Boudreaux and Holcombe 1989; Foldvary 1994; Beito, Gordon, and Tabarrok 2004; Andersson and Moroni 2014) also supports the themes stressed in previous sections. In brief, the following themes of this literature are of particular interest:

1. Claims to governance rents. The success of privately led city planning and urban development arrangements rests heavily on private parties' claims to profits from development. These profits depend on, at least in part, land prices arrived at via voluntary exchange. Thus, the information-generating and incentive-aligning features of the price system in an environment of private ordering (e.g., Wagner 2002) are applicable to governance institutions as well, at least on the scale of a city. This is the cornerstone for the following two features.
2. Collective goods provision. The standard economic theory of pure public goods becomes significantly less interesting once it is realized that the externalities associated with public

goods almost always are spatially demarcated. Coupled with the insight that the pecuniary benefits or burdens of these externalities are endogenous to the size of the group, it becomes obvious that many public goods are really club goods (Buchanan 1965). Since these goods are, in virtue of the above elements, exclusionary, private governance arrangements are able to supply them. Examples abound, from elevators in malls—"public transportation"—on a relatively small scale, and security and private property rights protection in Walt Disney World on a relatively large scale (see, e.g., Wagner 2012a). Governance profits are the relevant information feedback and incentive-alignment mechanism relating to the provision of collective goods.

3. Stability of meta-rules. The vast majority of developed nations are nominally constitutional republics. Constitutions are supposed to lay down the rules for rule-making: the meta-rules. However, constitutions do not enforce themselves. Political actors and private actors both frequently find it in their interests to alter, or in some cases outright ignore, the meta-rules when it is in their self-interest to do so (Martin and Thomas 2013). The case of the United States is particularly striking: what was originally a system of polycentric federalism has since evolved into a system of monocentric nationalism (Ostrom 1997, 2008a, 2008b). However, private organizations, such as country clubs and homeowners associations, also frequently have constitutions. Importantly, these organizations are characterized by claims to the revenues derived from organizational operation according to the stated meta-rules (Leeson 2011). This makes their constitutional contracts self-enforcing, and thus helps protect against undesirable "constitutional drift." Whereas the meta-rules for public polities are frequently opaque and only loosely constrain those in positions of authority, the meta-rules for private polities that offer similar services tend to be clear and thus firmly delimit these organizations' activities.

Several other categories could be listed, but the above three are most important for comparing the governance outcomes within corporate polities. Corporate polities that are most explicitly corporate, in the business sense, exhibit the above traits, which are all founded upon political property rights holders' claims to governance rents—a rejection of the political commons. Corporate polities that are less explicitly corporate do not, and thus are plagued by, commons problems.

IV. Scope, Scale, and Market Share

Despite the differences between a corporate polity and a traditional corporation outlined in section 2, corporate polities characterized by explicit claims to governance rents tend to be most like traditional corporations and also to engage in productive as opposed to predatory governance. This result was sensitive on a few key assumptions, which I will now discuss. First, and most importantly, the effectiveness of a corporate polity relies on a competitive market process (contestable markets) in the provision of governance services. In other words, between corporate polities, labor and capital are sufficiently mobile as to flow to better-governed polities from worse-governed polities, and thus polities compete for market share in the form of residents.[6] Even without an explicit secondary market for shares, political property rights that link the payoffs of the rulers with the wealth created in their polities should facilitate standard price-theoretic accounts concerning incentive alignment and information feedback. Productive as opposed to predatory governance in this scheme is, in addition to a particular arrangement of political property rights, a matter of external checks—Singapore is a well-governed corporate polity in part because residents can potentially move to Dubai. This is the standard Tiebout story.

The lack of a competitive market process in governance completely invalidates the results concerning a corporate polity's tendency to deliver good governance, even if holders of political property rights are still de facto owners. This can be seen in the limit by considering the hypothetical case of a single world government. In such a case, the most corporate-like polity arrangements would be an instrument of predation, rather than production. The CEO of "Earth, Inc." has no prospect of clients and their capital exiting the polity for another. In this case, the privately optimal point arrived at by maximizing appropriable rents would almost certainly diverge from the socially optimal point. This is the case where an analog to standard neoclassical theory is appropriate: Earth, Inc. will behave as a monopolist, with the usual results concerning social wealth destruction that follow (Stringham 2006; Leeson 2007). If a single world government had to exist in some form, then it would be a firm

[6] The costliness of moving labor and capital must also be taken into account.

case where Earth, Inc., is dominated by the Constitutional Federal Republic of Earth. In this case, the standard internal checks on formal governance outcomes promoted by scholars and fellow travelers of the Virginia School become much more attractive: rather than an imperfect mechanism for aligning the incentives of rulers with those of the ruled, they are the only possible way to prevent the rulers from preying on the ruled. Since factor mobility is no longer a possibility, the only recourse would be attempting to increase the inclusiveness of governance institutions, as suggested by Acemoglu and Robinson (2005, 2012) and by North, Wallis, and Weingast (2009). That this situation would encounter the same problems concerning a lack of self-enforcing meta-rules in this scenario is beside the point—the choice is not between perfect and imperfect constraints, but between imperfect constraints and nothing. If a corporate polity is most like a traditional corporation when it is hierarchical and authoritarian—situations that are desirable from an efficiency standpoint *when a chief goal is economizing on decision-making costs*, that is, executing a given strategy—then the optimal form for the corporate polity when exit is not an option is to make it as unlike a traditional corporation as possible. In such an environment, executing a given strategy should be made much more difficult, given that external costs relative to decision-making costs in such an environment would be quite large.

The other extreme would be a world comprised of thousands of small city-states and micro-polities. In this environment, the wealth-producing governance form would be as much like a traditional corporation as possible—"let a million Singapores bloom." Highly hierarchical-authoritarian decision structures within each are not nearly as worrying as in the case of a hypothetical world-polity, or any polity with high exit costs, since protection is afforded by standard Tiebout mechanisms. Preventing predatory governance is overwhelmingly a function of exit, rather than voice plus internal constraints, whereas in the case of a single monolithic polity, voice plus internal constraints are the only remaining options.

V. Conclusion: Future Trends in Governance

In concluding, I will briefly discuss how the theory I developed relates to future trends regarding existing formal governance institutions. The arguments in section 4 relied on a generalization of the framework for discovering an optimal decision threshold as a function of decision-making costs and costs of imposed decisions, first discussed by Buchanan and Tullock (1962). Tarko (2014) expands this model into a general theory of federalism, polycentricity, and self-governance. My aim here is much more modest: to use the *Calculus of Consent* framework to discuss the relevance of the political property rights structure to real-world governance outcomes.

Due to the feasibility of exit, the external costs associated with governance decisions by rulers were seen to be quite low, relative to decision-making costs. All else being equal, this suggests the efficiency of a hierarchical-authoritarian decision structure, just as the possibility of switching from one cellphone carrier to another suggests the efficiency of a hierarchical-authoritarian decision structure within the traditional business corporations responsible for the provision of cellular services. Of course, this only makes sense if political property rights holders' claims to governance rents exist as a background condition. If it is the case that technological advances are lowering external costs relative to decision-making costs, then the spectrum of "optimal" polities, while there will obviously still be significant heterogeneity given the idiosyncrasies of each polity, should become more corporate-like over time. Given the increased prevalence of high-speed internet, cloud computing and storage, and other technologies and social practices that undermine the monolithic infrastructural monopoly of the modern, centralized nation-state (see, e.g., Easterling 2014), which increases the mobility of labor and especially capital, it does seem the optimal formal governance unit should become smaller and be characterized by fewer internal checks. However, one can also argue that these developments lower decision-making costs, which would cut against the shrinking scale-scope-market share narrative.

Observing trends in existing governance institutions may shed light on how, if at all, the optimal formal decision structure is changing, but there are reasons why optimal formal governance does not currently exist and should not be expected to exist in the future. The most important underlying assumption concerns whether there is an efficiency criteria applying to governance institutions. Prominent scholars such as Kirzner (see, e.g., 1987) and Buchanan (see, e.g., 1977) have argued that there is a tendency toward efficiency within a set of institutions, but no mechanism that ensures the tendency toward efficiency of underlying institutions themselves. Polities that are currently quite corporate-like, an arrangement resulting from a complex historical process of political bargaining that was not intended ex ante with the goal of creating good governance, do seem to have a strong incentive to adapt to changes in governance conditions that result from changes in external costs relative to decision-making costs. But polities that are least corporate-like, especially due to the tragedy of the political commons, would only have an incentive to adjust internal decision structures due to changes in external economic forces if doing so was in the self-interest of current political property rights holders, which, as we have seen, are currently not aligned with social wealth creation.[7]

In fact, it is plausible that inefficient corporate polities (i.e., Western liberal democracies) that find themselves losing market share to more efficient corporate polities due to fleeing labor and capital may respond by engaging in even more predatory governance, rather than by moving toward productive governance, at the margin. Given the political and economic ignorance of voters (see, e.g., Caplan 2007; Somin 2013), democracies may respond to worsening economic conditions by enacting policies that are popular, but wealth-destroying. Instead of falling market share providing the feedback necessary for poorly managed corporate polities to become better managed, it may provide political property rights holders with incentives to expand predatory governance, given the tragedy of the political commons. In democracies, it may very well be that worsening economic conditions produce bad ideas, which bring about even worse economic conditions (see, e.g., Caplan 2003).

We should be skeptical that changing economic conditions can cause corporate polity structures that produce predatory governance to become corporate polity structures that produce productive governance. It is unclear what forces can result in a political property rights structure that affords rulers the current use value of political machinery, but not capitalized value, changing to one that affords rulers both current and capitalized value, thus forcing them to internalize the trade-offs associated with securing governance rents by productive means, versus securing governance rents by predatory means.

I should offer a few cautionary remarks regarding what implications do *not* follow from my theory. First, my theory should not be interpreted as a necessary endorsement for modifying existing governance institutions to make them more corporate-like. At this stage, such a recommendation would be premature, because it is still unclear to what extent such regimes can be designed, or whether they

[7] This can be thought of as a large-scale transitional gains trap (Tullock 1975).

must be "grown"—arising organically out of the underlying sociopolitical institutions, formal and informal, that exist in each case. The only way to shed light on this issue is careful historical analysis of the relevant cases. Even if design is possible—and some of the cases I discuss above suggest it is—we next must consider issues of scope, especially since we are not building polities de novo, but starting from a concrete arrangement where parties to the political bargains necessary to begin the transition may, understandably, be disinclined to renounce their (currently privately beneficial, but socially costly) rents. Furthermore, issues of institutional transition naturally impel the question of whether institutional regime change generates benefits in excess of costs. My theory does not shed light on this question.

Next, my theory does not imply that the corporate-like arrangement of a polity, with political property rights structured as has been described in previous sections of this paper, is a necessary condition for good governance. Institutional structures can and have existed that retained the feature of state-as-commons but also were characterized by significant internal checks on abuse of power. I have in mind here the Western liberal democracies, which were sufficiently well-governed to become the wealthiest nations in the world.[8] Although several of these polities saw tremendous growth during a time when wielders of political power still possessed some claim to governance rents (Salter 2014), the structure of political property rights was far from corporate-like.

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[8] Given the continuous cycle of "deficits, debt, and debasement" (Boettke and Coyne 2011; see also Buchanan and Wagner [1977] 1999) that has characterized governance in these polities since the First World War, it is questionable that they continue to be well governed.

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