Marginal lobbying cost and the optimal amount of rent seeking

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1. Introduction

When carefully discussed, rent seeking refers to those activities motivated by the desire to capture private gains which, once captured, have non-positive impacts on social wealth. For example, rent seeking aimed at receiving a monopoly grant from government will, if successful, impose a welfare loss on society quite apart from the resources dissipated by the rent seeking activity itself. But activities designed to capture a pure transfer also qualify as rent seeking with the only cost in this case arising from the direct resource cost of rent seeking. If, on the other hand, the attempt to capture rents is wealth creating, it is not rent seeking as currently defined. When, for example, rents take the form of higher than competitive salaries for government officials it is ‘excessive expenditure on education to prepare for civil service examinations,’ that qualifies as rent seeking. Educational competition creates net wealth up to a certain point and this competition is not rent seeking until it becomes excessive.

It is easy to classify certain activities as rent seeking, (for example, lobbying for monopoly privileges) when the outcome is clearly inefficient over all activity levels. But as is clear from the education example, for some activities it is difficult to determine when ‘profit seeking’ ends and rent seeking begins. As another example, consider the fact that Western farmers engage in political competition aimed at securing funds for water projects. Although the competition is motivated by the desire of farmers to increase their wealth at the expense of the general taxpayer, up to some point the construction of water projects may be efficiency enhancing. It would only be when political activity resulted in the construction of dams that cost more than they are worth that this activity would be considered rent seeking.

In an ideal world the structure of government would be such that political activities that are efficiency enhancing would not be discouraged; political profit-seeking cost would be zero. But as soon as political activity pushed a government program to its efficient level, lobbying cost, which has now become rent seeking cost, would become prohibitive. Obviously, such an
ideal political structure does not exist, and is never likely to exist. Political procedures can be adjusted in such a way as to raise, or lower, the marginal lobbying cost across the board, but there is no practical way to keep this cost at zero (or at the minimum level) until all efficiency increasing lobbying has taken place, at which point they increase into the prohibitive range.

The inability to realize the ideal suggests the second-best problem of choosing the uniform level of marginal lobbying cost that maximizes the net return from a government activity. This uniform marginal cost should obviously not, in general, be set so high for each government activity that it chokes off all lobbying. While this would eliminate rent seeking cost and wasteful government spending, it would also eliminate the net social benefits that are only available through some government activities. On the other hand, assuming for the sake of argument that this lobbying cost could be reduced to zero, it would not be a good idea, in general, to do so. Rent seeking cost would be eliminated, but there would be no restraint on the inefficiencies that could be imposed through government activities.

In the next section we consider a simple model in which the net social return to a government activity depends on the uniform marginal lobbying cost. Obviously, if the net social return (ignoring lobbying cost) is non-positive over all positive levels of activity, then the marginal lobbying cost should be prohibitive. However, even if this net social return is positive over some levels of activity, it is still possible that the efficient solution calls for a prohibitive marginal lobbying cost. On the other hand, it is also possible to find the efficient lobbying cost set so low (possibly zero) that the political activity will be pushed into the range typically considered to be excessive. In this case, a positive amount of rent seeking (employing resources to achieve socially inefficient outcomes) will be efficient. Brief concluding remarks are offered in Section 3.

2. Optimal rent seeking

Although it is straightforward to develop our model mathematically and consider its implications in a general framework, the important points to be made are more easily, and just as effectively, presented with a graphical approach.

It is assumed that the government is providing some good or service, with the marginal value potential beneficiaries place on the good given by a demand curve, $D$. The marginal, and average, production cost is assumed to be constant and is given by $MC$. It is also assumed that only those receiving the service benefit from it, but that they incur none of the production cost of making it available. However, the benefiting group does have to engage in lobbying activity to acquire the service, with the marginal cost of lobbying