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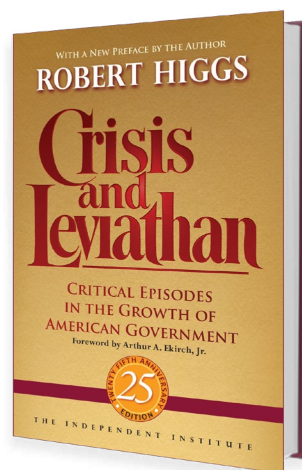

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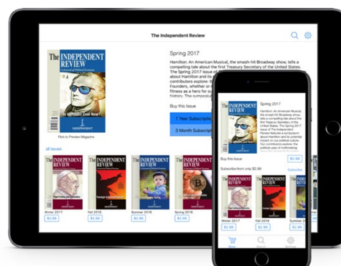

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Revolutionary Armies, Labor Unions, and Free-Riders

Organization, Power, and In-kind Benefits

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JERRY K. ROHACEK

Three paradoxes inspired me to write this article: (1) Activists within groups such as revolutionary armies and labor unions often make extraordinary sacrifices even when they receive the same benefits as do nonactivists. (2) Groups often seek in-kind benefits even when they could have pursued monetary benefits of greater value. (3) Groups often oppose democratic decision making even when their members have democratic values. In this article, I will resolve these paradoxes by explaining the organization and the division of power within various groups.

Purposive Groups, Public Goods, and Free-Riders

Peter B. Clark and James Q. Wilson (1961, 145–66) classify groups as purposive when the incentives that motivate group members come from the goods that the groups seek. For example, the Audubon Society is a purposive group. Members are motivated by the goal of the group, the protection of birds. In contrast, the incentives of members of nonpurposive groups come directly from the benefits given to individual members. For instance, a college study group is a nonpurposive group. The group's members are motivated by the special and various knowledge each member expects to receive.

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The goals of purposive groups are often "public goods" in the economist's broadest sense of the term. For example, once the Sierra Club succeeds in its efforts to protect the environment, it is impossible to provide the benefits of environmental protection to club members without also providing those benefits to nonmembers. Moreover, it is impossible to provide the benefits to some club members without also providing them to all club members.

Occasionally the attainments of purposive groups accrue only to group members but are nevertheless public among the members. That is, once goals are attained, access to the benefits created cannot be selectively and differentially distributed among group members. For instance, when a baseball team wins a game, even though outsiders receive little benefit, all team members share in the team's success. To at least some degree, pure capitalist "unanimity without conformity" cannot be achieved.

When the benefits of large purposive groups are public goods, the groups often encounter a serious "free-rider" problem. This occurs when nonmembers of the large purposive groups can receive the same benefits as members and can do so without incurring the costs of membership. Individuals then have an incentive to avoid becoming members.

In his classic book *The Logic of Collective Action* (1965), Mancur Olson presented an excellent discussion of the nonmember free-rider problem and an explanation of how it can be avoided in the special case of a large purposive political group. Olson's solution is that, in addition to providing public goods, the groups provide private goods restricted to group members.

However, most large purposive groups also must avoid a second free-rider problem, which arises when the benefits of the goods that the groups create are public among the members of the group. Under such conditions, nonactivist members of the groups can obtain the same benefits as activists without making the sacrifices for the groups that the activist members make. Members then have an incentive to avoid becoming activists.

Avoiding the nonactivist free-rider problem is often as crucial to the creation and survival of purposive groups as avoiding the nonmember problem. Large purposive groups usually need activists as well as members. Without activists, most purposive groups could not survive.

My purpose in this article is to explain how large purposive groups avoid the nonactivist free-rider problem. The explanation shows how activists can be selectively rewarded even if their eventual benefits come from public goods. Note that the rewards to activists are public goods, not private goods, as in Olson's solution.

Perhaps because analysts have focused on the nonmember problem, they have not directly discussed the nonactivist problem. It appears that sometimes they have assumed that avoiding the one is tantamount to avoiding the other. Nevertheless, in dealing with how *small* political groups avoid the nonmember problem, the analysts have provided some hints about how groups may avoid the nonactivist problem.

Olson (1965, 35–37), for example, recognized that small political groups can solve the nonmember problem when recipients unequally value the public goods that the groups obtain. The values that accrue to some members can then be sufficient to cover membership costs. However, because of his focus on the nonmember problem, his discussion deals with cases in which the goals of the groups are given and the only problem is to motivate individuals to become members. The theory presented here shows that the very process of selecting large-group or small-group goals can create the necessary incentives for individuals to be members of purposive groups and, more importantly, activists in those groups.

Taking a different approach, Richard B. McKenzie and Gordon Tullock (1978, 222–23) imply that small political groups can solve the nonmember free-rider problem by converting public goods into purely private goods. They use truck and airline regulations as examples. In this case, lobbying associations can seek truck and airline regulations that limit truck and airline routes exclusively to association members. Nevertheless, although the regulations mentioned by McKenzie and Tullock may have arisen as they hypothesize, it is unnecessary to convert public goods to purely private goods.

My theory emphasizes a method by which individuals can be motivated to become activists even though they receive only the same access to *public* goods as nonactivists. This theory demonstrates that avoiding the nonactivist free-rider problem can largely determine the goals of purposive groups and how the groups are organized. In fact, avoiding the problem may have more of an effect on the objectives and structures of purposive groups than any other consideration, including avoidance of the nonmember free-rider problem.

In addition to explaining the goals and organizations of purposive groups, the theory yields some particularly important and interesting implications, including the following: (1) Activists in purposive groups may have the groups seek in-kind rather than monetary benefits so that the activists can thereby surreptitiously increase their wealth at the expense of nonactivists. (2) Corruption may be a necessary condition for the existence of many purposive groups, whereas democracy may destroy such groups. (3) The extent of rent-seeking by purposive political groups may be limited by their inability to circumvent the nonactivist free-rider problem. (4) The method for avoiding the nonactivist free-rider problem can sometimes be used to avoid the nonmember free-rider problem. (5) Avoiding the nonactivist free-rider problem may explain why unionization sometimes increases the ratio of fringe benefits to monetary compensation.

Avoiding the Nonactivist Free-Rider Problem

Purposive groups seeking public goods can sometimes solve the nonactivist free-rider problem by paying activists wages and other selective benefits to compensate them for

their extraordinary sacrifices. But although some activists in purposive groups may be paid, many are not. And those who receive monetary compensation often receive far less than normal market rates for their efforts. If monetary and other selective incentives are insufficient, some or all of the benefits to activists must come via the public goods that the large purposive groups seek. The nonactivist free-rider problem therefore arises. To avoid the nonactivist free-rider problem, the groups (1) focus on obtaining a complex package of benefits, (2) try to obtain in-kind as well as monetary benefits, (3) divide their activist members into small subgroups, and (4) allow each of the subgroups some authority over the contents of the package or how the package is to be obtained, that authority being proportional to the sacrifices of the activist members.

The authority granted to the subgroups is great enough and the subgroups are small enough that each activist member believes he or she has some chance of changing the composition of the final package, the probability of obtaining the package, or the costs associated with seeking the package. Moreover, the authority is great enough that each activist values the expected changes that result from his or her inputs more than the sacrifices the activist makes for the group.

In effect, selective compensation takes the form of power (the authority to make decisions). The value of that power is derived from the difference between the individual's valuation of expected group benefits and costs with that power, and the individual's valuation of expected group benefits and costs without that power.

The theory doesn't require that purposive groups be composed of individuals who have strictly selfish goals in mind. Some activists in groups such as Earth First!, the United Way, and the March of Dimes may be motivated almost totally by a desire to do the right thing. Nevertheless, opinions on what is right are subjective. An activist with power may, therefore, obtain a selective reward if he or she thinks that the public goods obtained because of his or her efforts are sufficiently better than the public goods that would have been obtained otherwise.

An Example: Unions

We can illustrate the theory by examining how labor unions circumvent the nonactivist free-rider problem.

The benefits of unions are not naturally public goods. Normally, they would accrue only to union members and could accrue even selectively and differentially to the members if individual members were dealt with separately by union contracts. Nevertheless, the National Labor Relations Act makes the benefits of unions public among nonunion members of bargaining units as well as among all union members. It does so by extending union contracts to all workers in bargaining units and requiring ratification by voting majorities. As a result, unions encounter both free-rider problems.

The nonactivist free-rider problem occurs because union activists who plan rallies, attend union meetings, act as shop stewards, and so forth are covered by the same

contracts as other union members even though they incur more than their share of the costs of union activities. Because activist union members generally incur disproportionate costs, their actions are economically rational only if the activists receive disproportionate benefits.

The union can provide the disproportionate benefits by first dividing union activists into subgroups based on their sacrifices for the union. The subgroups must be small enough for individuals to have some influence over decisions; they often consist of ten or fewer members. Each subgroup is then given authority to make specific decisions regarding a complex package of in-kind as well as monetary benefits to be negotiated in collective bargaining.

Union activists who make more sacrifices than other union activists are usually given more decision-making authority. For example, the decision on the contents of the health-care package to be sought in collective bargaining may be made by a bargaining committee composed of very active union members. However, the chair of the committee may be a union leader who has "earned" his seat by donating more of his time or money to union efforts than other committee members.

In this way, individual activists can change the package obtained by the union to increase the expected value they place on the package and thereby obtain selective compensation for their special sacrifices. A member will sacrifice for the union if he or she thinks that the value of the eventual package to him or her will be sufficiently greater than the value of the package that would have been negotiated otherwise.

In other words, although the benefits of a collective bargaining agreement will accrue to all bargaining-unit members, a worker has an incentive to be a union activist because he or she may obtain a *particular* collective bargaining agreement only by active personal involvement in the union. Many different collective bargaining agreements are possible, and each has a different value to each worker. As a result, selective compensation with public goods becomes possible.

The same motivations drive individuals to form and actively participate in other large groups that seek public goods. Individual doctors actively participate in the American Medical Association to obtain a *particular* package of medical regulation. Individual manufacturers make extraordinary contributions to industry lobbying efforts to foster a *particular* package of tariffs. Individual peasants march with a revolutionary army to fight for a *particular* form of communism. And individual environmentalists join groups and militate for their *favorite* environmental protections.

Just as activists can affect the contents of the collective bargaining agreement, a variation on the same theme occurs when subgroups of union activists make decisions regarding union tactics. By causing their unions to act differently, activists can increase what they perceive as the probabilities of obtaining favorable union contracts, and thereby increase the present values of those contracts. For example, the timing of a strike can greatly affect the probabilities by which various union activists discount the future benefits of a collective bargaining agreement. Also, the use of different tactics

can change the personal costs that individual activists incur. Relative to other union tactics, a strike may be less painful for senior union members than for recently hired workers.

The public explanation of the division of a union's decision making and the assignment of particular members to powerful positions and committees may be that decision making by small groups and specialization in decision making based on special skills and information make for better decisions. Indeed, this explanation may often serve as a concurrent rationale for the division of decision making among individuals and small groups and the assignment of particular members to positions of power. However, a more fundamental reason may be that a union is rewarding activists lest they cease making their sacrifices for the union and the union cease to exist. That reason is more fundamental because unless activists are rewarded, the union can't survive. Making decisions efficiently serves no purpose unless the union itself survives.

In-Kind Benefits

The theory specifies that in-kind benefits will be included among the packages of benefits that large purposive groups seek. This stipulation is paradoxical, because whenever money can be substituted for in-kind benefits, recipients generally prefer to receive money. Money gives them more options. For example, many poor people would prefer to receive a hundred dollars in cash rather than a hundred dollars in the form of rent subsidies, because they could use the money to pay rent or, should they value some other good more, to purchase an alternative good. Nevertheless, an enormous amount of casual evidence reveals that large purposive groups have obtained at least some in-kind benefits. The auto industry receives aid in the form of trade restrictions, the poor obtain food stamps, doctors benefit from the regulation of medicine, and so forth.

Two usual reasons are given to resolve the paradox. First, the value of giving is often greater to contributors when in-kind benefits are provided. The public at large, for instance, may feel better if its taxes provide the poor with food. If the poor were to receive money, they might spend it on alcohol. Second, unlike money (a unit of account), in-kind benefits may hide from contributors how much the contributors must sacrifice and how much the recipients gain. Few voters know how much they must pay via price increases so that individuals in wheelchairs can have access to public facilities. Nor do most voters know the amount of wealth that manufacturers gain from protective tariffs.

The requirement that large purposive groups avoid the nonactivist free-rider problem provides additional reasons for the existence of in-kind benefits. First, the addition of in-kind to monetary benefits increases the complexity of benefit packages. A purposive group can then reward more activists, because the possible combinations of benefits that can be achieved increase. Second, and more important, if either the contributors to large purposive groups or the members of the groups would object to extraordinary

monetary payments to group activists, then in-kind benefits might be sought by the groups as a means of surreptitiously providing high rewards to activists. In-kind benefits, rather than being merely associated with large purposive groups seeking public goods, may become necessary conditions for avoiding free-rider problems and, therefore, necessary conditions for the existence and survival of the groups.

For example, suppose a group of ten Alaska Native leaders wants the federal government to increase the wealth of the Alaska Natives in a small area in Alaska where ten thousand Natives reside. To obtain the wealth, the leaders must organize meetings, decide how to lobby Congress, raise money to fund lobbying efforts, write letters to newspapers, submit editorials to various publications, and so on.

Let us assume the value of the sacrifices incurred by the ten leaders is $10,000 each, for a total of $100,000. If the benefits of the effort were $500 to each of the ten thousand Natives in the region, for a total of $5 million, then the total benefits to Natives would far exceed the total costs to Natives. Nevertheless, the lobbying effort would not commence, because by the lobbying each of the leaders would incur personal costs of $10,000, far greater than each one's personal benefits of $500.

Of course, in the foregoing example it is assumed that the Native leaders are motivated by direct personal rewards rather than by altruism. A desire to benefit others or to do "right" often does motivate many activists in large purposive groups. Nevertheless, selective rewards would still be necessary if the value of altruism were insufficient to cover extraordinary costs. Also, in any case selective rewards might be sought if they could be obtained without much of a sacrifice of altruism. Absent altruistic motivations, for the lobbying effort to begin, a method would have to be found to distribute benefits unevenly among Natives, with $10,000 or more in prospective value going to each of the leaders.

Distributing $5 million in cash unevenly among the Natives would be difficult if taxpayers and nonactivist Natives strenuously objected. The nonactivist Natives might provide the most significant resistance. Taxpayers may not care how benefits are distributed among Natives, because their personal losses would be the same in any case. Taxpayers might be reacting more to the political power of Alaska Natives than to their own altruism. The nonactivist Natives, on the other hand, would be more affected by the unequal distribution, because their shares of the total wealth transfers would be reduced so that the leaders' shares could be increased.

To provide themselves with significant selective rewards, the Native leaders might lobby for in-kind benefits rather than money. In-kind benefits could yield them, in a manner hidden from view, more value. For instance, Native leaders might fight for the construction of airstrips near Native villages, at a construction cost of $5 million. Airstrips might benefit all Natives in the villages to some degree, but they would certainly benefit the Natives who owned airplanes more, and those Natives might be the leaders.

Five million dollars spent on airstrips would force taxpayers to sacrifice $5 million

but would generally yield benefits to recipients worth far less than $5 million. Natives might value the airstrips at only $1 million, for a net social loss of $4 million. Nevertheless, if the airstrips were worth $20,000 to each of the Native leaders, the leaders would have an incentive to lobby for the airstrips, whereas they would not have a sufficient incentive to lobby for $500 in cash.

Clearly, in cases where contributors and nonactivist members of large purposive groups would have prevented a greater distribution of money to activist members, in-kind benefits may be more than just associated with large purposive groups. In-kind benefits may be a necessary condition for avoiding a free-rider problem that would have prevented the successful organization and maintenance of the groups.

Greater Rewards for Activists

It is sometimes possible to compensate some activists in large purposive groups with money rather than in-kind benefits. Some activists for large purposive groups are salaried employees of the groups. For example, the Teamsters Union, the Democratic Party, and the American Association of Manufacturers have paid presidents and other employees.

Why not pay all activists at market rates for their contributions? One reason has been explained already: nonactivists members and contributors to purposive groups often object to paying money to activists who they believe should be motivated by high ideals rather than personal compensation. Another possible reason is that the activists themselves may want to be paid in kind if they think that hidden compensations will be more valuable compensations. In terms of the earlier example, Native leaders would be willing to form a Native lobbying group if they were paid $10,000 each in wages, but they would lobby more readily if they were seeking airstrips and the value of the airstrips to each of them would be $20,000.

Normally, activists control both what types of goods are obtained by large purposive groups and how individuals in the groups are compensated. Activists will opt for in-kind benefits rather than monetary payments if thereby they can receive in-kind benefits worth more to them than the money that could have been obtained otherwise. The lower values of in-kind benefits relative to money, dollar for dollar, can be offset by the receipt of greater quantities of in-kind benefits.

The benefits that accrue to nonactivists need not be significant if the benefits to activists are sufficient to compensate the latter for their sacrifices. In the case of the Alaska Natives, the group might be formed even if the value of the airstrips to all Natives were, say, $210,000, with $200,000 in value going to activists and only $10,000 accruing to nonactivists. The continued existence of some labor unions that generate few benefits for rank-and-file members and large benefits for activists can be explained in this way. The use of in-kind benefits may allow the survival of purposive groups even if the groups exist almost exclusively for the benefit of group activists.

We should not be surprised if activists try hard to skew benefits toward themselves at the expense of nonactivists. Sometimes the only constraint on such intragroup competition is resistance from contributors and nonactivist members, and such resistance can be greatly reduced by activists who hide their rewards by making them in-kind rather than monetary.

Corruption and Democracy

If we define corruption loosely as a reallocation of wealth between individuals without the knowledge and explicit consent of the individuals from whom the wealth is shifted, then corruption may become a necessary condition for the creation of many large purposive groups.

For example, many citizens of Nicaragua wanted a communist revolution to eliminate Somoza's regime. But why join the Sandinistas and make extraordinary sacrifices if the benefits of communism accrue to all, regardless of participation in the revolution? No doubt some people joined the Sandinistas solely out of a sense of social responsibility. However, others may have done so because they also expected extra rewards; and the greater their sacrifices, the greater their expected extra rewards.

Resistance from the public and from nonactivist Sandinistas may have prevented monetary rewards that would have compensated the activists according to their special sacrifices. As a result, the Sandinistas may have had to hide the extent of their unequal rewards by creating a particular communist system. In that system, the "people" obtained in-kind benefits, but the benefits had far more value to some Sandinistas than to either the public at large or the Sandinistas who made fewer sacrifices.

Although corrupt behavior may be frowned on or condemned by many observers, it may be a necessary condition for the creation of many large purposive groups, such as the Sandinistas. Without the selective and exceptional rewards that accrue to activists within large purposive groups, free-rider problems may prevent the creation and maintenance of such groups.

If corruption is a necessary condition for the successful formation and continuation of large purposive groups, then the elimination of corruption will cause the demise of such groups. For example, if pure democracy takes away from activists the special decision-making authority they enjoy as members of powerful subgroups, then special compensations of the subgroup members may become impossible. The larger purposive groups will then confront serious free-rider problems.

Extreme democratic practices may eliminate political organizations. For example, extensive democracy may cause the failure of unions if it eliminates their ability to compensate union activists for extraordinary sacrifices. The resistance of labor unions to the provisions of the National Labor Relations Act that increased union democracy may have sprung from the recognition that extensive democracy would lead to union failure if it prevented selective compensation of various union activists.

The claim that large political groups are sometimes corrupt is hardly new. What is surprising is the implication that corruption may be a necessary condition for the organization of large political groups and that democracy may be anathema to such organizations.

The corruption within large purposive groups need not have a strong self-serving dimension. It can occur even when activists have highly altruistic motivations or a desire to "do right." For example, the Libertarian Party may obtain few benefits that accrue directly to individual members. Nevertheless, to avoid free-rider problems, the party may need to divide into small subgroups and give each activist some authority over a package of goals, authority sufficient to compensate the activist for his or her extraordinary sacrifices. Although the party may in any case improve society, by being an active member a particular individual may succeed in, say, shifting the party's focus from abortion rights to drug decriminalization, and the subjective value of the shift may compensate the individual for his or her sacrifices. Although the corrupt actions have no strong self-serving character in such cases, they nevertheless represent corruption in the sense that the benefits obtained by activists would often be opposed by the membership at large. Indeed some nonactivists might drop their membership upon learning that an activist had succeeded in causing the Libertarian Party to shift its focus from advocating abortion rights to seeking the decriminalization of drugs.

Limits on Rent-Seeking

Since Gordon Tullock (1967) made his rent-seeking observation and Anne Krueger (1974) named it, the rent-seeking literature has focused on rent seeking by large political groups. In *The Economics of Special Privilege and Rent Seeking* (1989), Tullock asks why rent seeking in the form of lobbying is not more extensive, given the apparent benefits of lobbying relative to the costs. He presents a number of possible explanations.

The explanation of how large purposive groups organize to avoid the nonactivist free-rider problem provides an additional possible explanation for the limited extent of rent-seeking behavior. The necessity of selective rewards to activists may imply that the rule for efficient behavior is not that the marginal benefits of lobbying must be equal to the marginal costs, but that the marginal benefits of lobbying that accrue to activists must be equal to the marginal costs incurred by the activists. Even when the political groups would receive benefits in excess of sacrifices, lobbying will not occur if the activists who sacrifice disproportionately for the groups cannot obtain sufficient selective compensations.

Consider, for example, the case of the Alaska Native lobbying group discussed earlier. If Native leaders cannot obtain sufficient authority over the final composition of benefits or cannot package benefits so that the leaders obtain sufficient selective rewards, then lobbying will not occur. And it will not occur even though the recipient group as a whole might obtain benefits far in excess of the group's cost of lobbying.

The Nonmember Free-Rider Problem Again

As noted previously, Olson (1965) has explained how large political groups avoid the nonmember free-rider problem, the problem that both nonmembers and members have the same access to the public goods that the groups seek. In that explanation, the groups organize to obtain private goods and then use the resulting organizations to obtain public goods as by-products. In the case of agriculture, for example, farmers organize farm cooperatives to aid in the production and distribution of their products, and then the cooperatives assess fees to fund lobbying efforts aimed at desirable farm legislation—laws that benefit all farmers.

Richard Wagner (1966) has identified another method of avoiding the nonmember free-rider problem. He claims that politicians can act as entrepreneurs to provide public goods to constituent groups in exchange for votes or political contributions. A politician may identify, say, a need for an environmental control and fight for the necessary legislation so that he or she can obtain the votes or contributions of environmental political groups.

My theory of how large purposive groups avoid the nonactivist free-rider problem provides an additional solution to the nonmember free-rider difficulty. Relative to nonmembers, members may be selectively rewarded by being allowed some influence upon group decision making. That is, members may be given selective rewards for their special sacrifices by being given small amounts of power (and the potential to obtain more). The value of that power (and potential) may be sufficient to compensate for the relatively small costs of membership. More specifically, voting rights and other sources of influence may be the rewards of membership and may reduce, if not overcome, free-rider difficulties.

Empirical Evidence: Unions

My objectives in this article are more theoretical than empirical. However, some indirect empirical evidence already exists that tends to support the theory that large purposive groups avoid the nonactivist free-rider problem by dividing into subgroups and seeking benefit packages that include in-kind as well as monetary benefits. That evidence comes from studies of union activities.

As noted before, labor unions confront free-rider problems when they organize to obtain collective bargaining agreements. The agreements generally provide bargaining-unit members with both monetary and fringe benefits. Of course, employees not working under union contracts also receive both monetary and fringe benefits. However, in an empirical study of unions, Richard B. Freeman (1981) showed that, compared to unorganized workers in similar jobs, unionized workers have generally obtained *more* fringe benefits relative to monetary benefits.

Ronald G. Ehrenberg and Robert S. Smith (1987, 397–98) identify four possible reasons for that difference: (1) Unions may know better than employers do the values

that workers place on fringe benefits relative to money; (2) by raising wages, unions put workers in higher tax brackets, making fringe benefits more desirable from a tax perspective; (3) by raising wages, unions make workers more attached to firms and thereby increase the value of fringe benefits; (4) unions may be more responsive to older workers, who value fringe benefits more than younger workers do.

The need to avoid the nonactivist free-rider problem provides an additional and more fundamental reason for the greater extent of fringe benefits: unions negotiate for more fringe benefits because those benefits surreptitiously reward union activists for their extraordinary sacrifices for the unions. By giving more to union activists than to rank-and-file union workers, unions can avoid free-rider problems. That reason is more fundamental that those cited by Ehrenberg and Smith because successful bargaining for fringe benefits may be a necessary condition for the very existence of unions.

My theory, however, does not necessarily imply that fringe benefits will be more extensive when unions negotiate contracts. It is sufficient that unions negotiate different fringe benefits than would have existed otherwise, benefits shaped so as to benefit union activists disproportionately.

Conclusion

The contribution I seek to make in this article does not lie in pointing out that groups divide into subgroups, that subgroups have power over certain large-group decisions, that packages of benefits are obtained by large purposive groups and the values of those packages differ among members, that corruption is present in large purposive groups, or that rent seeking is limited. Those phenomena have all been recognized and explained (although differently) elsewhere. My contribution lies in presenting a general explanation that systematically links those phenomena. The theory explains how, by shaping complex in-kind and monetary benefit packages and by making strategic divisions of power, activists can be surreptitiously and selectively rewarded for their sacrifices, even when the rewards take the form of public goods to whose benefits all group members (and even nonmembers) may have equal access.

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