Innovating Governance with Startup Cities

How an Entrepreneurial Approach to Community Development Can Build a Better Future for Politics

Outside of Stockholm, vandals and vines have taken over Eastman Kodak's massive factories. The buildings are cold metal husks, slowly falling down and surrendering to nature. The walls are covered in colorful (and sometimes vulgar) spray paint. In the words of one graffiti artist: It's "a Kodak moment."

After its founding in 1888, Eastman Kodak became the uncontested champion of photography for almost a century. But in early 2012, the once $30-billion company with over 140,000 employees filed for bankruptcy.

Kodak was the victim of innovation—a process that economist Joseph Schumpeter called "the gales of creative destruction." Kodak could dominate the market only so long as a better, stable alternative to their services didn't exist. Once that alternative—digital photography—had been created, Kodak's fate was sealed. The camera giant slowly lost market share to upstarts like Sony or Nikon until suddenly "everyone" needed a digital camera and Kodaks were headed to antique shows.

How does this happen? Christian Sandström, a technologist from the Ratio Institute in Sweden, argues that most major innovation follows a common path.

From Fringe Markets to the Mainstream

Disruptive technologies start in "fringe markets", and they're usually worse in almost every way. Early digital cameras were bulky, expensive, heavy, and made low-quality pictures. But an innovation has some advantage over the dominant technology: for digital cameras it was the convenience of avoiding film. This allows the innovation to serve a niche market. A tiny group of early adopters is mostly ignored by an established firm like Kodak because the dominant technology controls the *mass* market.

But the new technology doesn't remain on the fringe forever. Eventually its performance improves and suddenly it rivals the leading technology. Digital cameras already dispensed with the need to hassle with film; in time, they became capable of higher resolution than film cameras, easier to use, and cheaper. Kodak pivoted and tried to enter the digital market, but it was too late. The innovation sweeps through the market and the dominant firm drowns beneath the waves of technological change.

Disruptive innovation makes the world better by challenging monopolies like Kodak. It churns through nearly every market except for one: law and governance.

Social Technology

British Common law, parliamentary democracy, the gold standard: It may seem strange to call these "technologies." But W. Brian Arthur, a Santa Fe Institute economist and author of *The Nature of Technology*, suggests that they are. "Business organizations, legal systems, monetary systems, and contracts…" he writes, "… all share the properties of technology."

Technologies harness some phenomenon towards a purpose. Although we may feel that technologies should harness something physical, like electrons or radio waves, law and governance systems harness behavioral and social phenomena instead. So one might call British common law or Parliamentary democracy "social technologies."

Innovation in "social tech" might still seem like a stretch. But people also once took Kodak's near-total control of photography for granted (in some countries, the word for "camera" is "Kodak"). But after disruptive innovation occurs, it seems obvious that Kodak was inferior and that the change was good. Our legal and political systems, as technologies, are just as open to disruptive innovation. It's easy to take our social techs for granted because the market for law and governance is so rarely disrupted by innovations.

To understand how we might create disruptive innovation in law and governance, we first need to find, like Nikon did to Kodak, an area where the dominant technologies can be improved.

Where Today's Social Techs Fail

Around the world, law and governance systems fail to provide their markets with countless services. In many developing countries, most of the population lives outside the law.

Their businesses cannot be registered. Their contracts can't be taken to court. They cannot get permission to build a house. Many live in constant fear and danger since their governance systems cannot even provide basic security. The ability to start a legal business, to build a home, to go school, to live in safe community—all of these "functions" of social technologies are missing for billions of people.

These failures of social technology create widespread poverty and violence. Businesses that do succeed do so because they're run by cronies of the powerful and protected from competition by the legal system. The networks of cooperation necessary for economic growth cannot form in such restrictive environments. The poor cannot become entrepreneurs without legal tools. Innovations never reach the market. Dominant firms and technologies go unchallenged by upstarts.

Here's our niche market.

If we could find a better way to provide one or some of these services (even if we couldn't provide *everything*better than the dominant political system), we might find ourselves in the position of Nikon before Kodak's collapse. We could leverage our niche market into something much bigger.

Hacking Law and Governance with Startup Cities

A growing movement around the world to build new communities offers ways to hack our current social tech. A host nation creates multiple, small jurisdictions

with new, independent law and governance. Citizens are free to immigrate to any jurisdiction of their choosing. Like any new technology, these Startup Cities compete to provide new and better functions—in this case, to provide citizens with services they want and need.

One new zone hosting a Startup City might pioneer different environmental law or tax policy. Another may offer a custom-tailored regulatory environment for finance or universities. Still another may try a new model for funding social services.

Startup Cities are a powerful alternative to risky, difficult, and politically improbable national reform. Startup Cities are like low-cost prototypes for new social techs. Good social techs pioneered by Startup Cities can be brought into the national system.

But if bad social techs lead a zone to fail, we don't gamble the entire nation's livelihood. People can easily exit a Startup City—effectively putting the project "out of business." If a nation chooses to use private capital for infrastructure or other services, taxpayers can be protected from getting stuck with the bill for someone's bad idea. Startup Cities also enhance the democratic voice of citizens by giving them the power of exit.

Looking at our niche market, a Startup City in a developing nation could offer streamlined incorporation laws and credible courts for poor citizens who want to become entrepreneurs. Another project could focus on building safe places for commerce and homes by piloting police and security reform. In reality, many of these functions could (and should) be combined into a single Startup City project.

Like any good tech startup, Startup Cities must be small and agile at first. They will not be able to rival many things that dominant law and governance systems provide. But as long as people are free to enter and exit, Startup Cities will grow and improve over time. What began as a small, unimpressive idea to serve a niche market can blossom into a paradigm shift in social technologies.

Several countries have already begun developing similar projects, and many others are considering them. The early stages of this movement will almost certainly be as unimpressive as the bulky, toy-like early digital cameras. Far-sighted nations will invest wisely in developing their own disruptive social techs, pioneered in Startup Cities. Other nations—probably rich and established ones—will ignore these "niche market reforms" around the developing world. And they just might end up like Kodak—outcompeted by new social techs developed in poor and desperate nations.

The technology hacker finds vulnerabilities in dominant technology and uses them to create something new. In a sense, *all* disruptive innovation is hacking, since it relies on a niche—a crack in the armor—of the reigning tech. Our law and governance systems are no different. Startup Cities are disruptive innovation in *social* tech. The future is just beginning. Social entrepreneurs and far-sighted political leaders can lead the way to safe and prosperous communities.

Those interested in learning more about the growing Startup Cities movement should visit startupcities.org or contact startupcities@ufm.edu

Zachary Caceres is Executive Director of Startup Cities Institute.