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Delegation, Agency and Competitive Representation

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ABSTRACT

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Traditional agency models focus on the conceptual line of delegation running from principal to agent. The more information about agents’ preferences and actions, the better able the principals to use selection and sanctioning to achieve desirable outcomes. Following this conventional wisdom, institutional transparency is viewed as an unequivocal good and representative democracy as built on delegation and control. However, this is an incomplete picture at best.

Game-theoretic and case analysis shows that the elevation of the elected European Parliament as a legislative chamber coequal to the intergovernmental Council of the European Union may be a ruse to undermine lobbyist influence by diluting formal responsibility. Less transparency in decision-making may help align EU policy closer to broader societal objectives. The Commission, perhaps most heavily influenced by special interests, and not Council has lost clout in the legislative process as a result of the changes.

In several generalized noncooperative formal settings with information asymmetries, delegation can work for principals only if the set of potential agents is diverse. Not only does selection dominate sanctioning as a control mechanism, but the very existence of compliance equilibria is contingent upon the a priori arrangement of candidate agents’ policy preferences relative to one another and to the principals’. The principal–agent relationship is dependent on and may be only secondary to between-agent competition. This insight has far-reaching implications for a number of research programs within political science.
Schumpeter viewed modern democracy as a system where elites compete for the support of the masses. This conceptualization suggests a new path towards sustainable democratization. Building elite capacity in undemocratic conditions through institutionalized, if unfair, competition may be a more effective approach than parachuting fully democratic institutions in an unreceptive environment. Empirical analysis of over two hundred years of data shows that states with competitive political institutions, regardless of whether those are democratic, are most likely to develop and sustain full-fledged democracy.
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Chapter 1

Transparency and Institutional Choice
in the European Union

“As in life, it is much easier to know the maternity than the paternity of amendments.”

– Michael Schackleton

This chapter proposes a rational-choice theory of institutional change which provides an informational rationale for the member-states’ empowering of the European Parliament (EP) as a partner in European Union (EU) decision-making. The first section of the chapter introduces the issue by highlighting the EP’s uniqueness and its significance for the broader comparative study of political institutions. Section 1.2 reviews the veto-player and integration literature on the evolution of EU decision-making and demonstrates that the EP’s empowerment remains largely unexplained.

As a necessary step towards resolving that puzzle, Section 1.3 outlines distinct types of institutional transparency and the ways in which they can be useful to mobilized interest groups and the general public. Based on the idea that not all transparency is created equal, the following Section 1.4 develops a simple formal model showing that decreasing structural transparency and the dissemination of targeted policy information by the EP to the general public can

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1 As attributed by Simon Hix (see Hix and Høyland 2013, 176).
be powerful instruments in reducing the impact of special interests upon the policymaking process and in improving the quality of EU legislation.

Section 1.5 details the EU’s legislative processes to show that while Parliament’s formal power expanded dramatically towards the beginning of the 21st century, effectively it did so at the expense of the Commission, not of Council. Because they can still exert control through the power of the purse and domestic politics, the member-states’ governments remain the true masters of the process while the EP may serve as a front for legislation unpopular with powerful domestic and transnational lobbies. Consistent with the mechanisms suggested by the theory, the EP has established itself as a vocal and active proponent of transparency, while Council and the Commission have remained staunchly opposed to letting light shine on their decision-making. In a case study of over a decade of EU lawmaking on new-vehicle emissions standards, the Commission appears heavily influenced by lobbyists while the governments in Council posture to placate their demands, then still adopt legislation adverse to the lobbyists’ goals under the political cover of Parliament’s “equal” legislative powers.

Section 1.6 summarizes the findings and their implications for the further development of the rational-choice literature concerning institutional design in the context of transparency and the broader field of agency theory. The paradox that a legislative body such as the EP, whose electoral connection is tenuous at best, can be a tool to increase policy responsiveness to the public interest motivates a new approach to understanding democratic representation – one focused on elite and institutional competition rather than electoral selection and control.
1.1. INTRODUCTION

The European Union rarely appears on the scholarly radar of comparativists when thinking about parliamentary democracy. However, the EU has evolved in the span of just about a half-century from an essentially intergovernmental organization to an emergent confederation of sovereign states with parliamentary government. The empowerment of the EP is perhaps the most significant institutional change that has taken place during this period, the EU’s first truly supranational institution and “the only directly elected supranational assembly in the world” (Hix and Høyland 2013). The EP is a unique case where such a rapid transformation can be observed in a nonviolent democratic setting, which can help illuminate more general mechanisms of political-institutional change. In understanding the latter, informational concerns have rarely taken a prime spot, but the EP’s growing role can be explained in precisely such terms.

The approach is twofold. On one hand, there is a latent conflict between two growing literatures regarding the impact of institutional transparency on representation and policy responsiveness. To comparativists, information problems are a pervasive obstacle to effective institutional delegation – from coordinating electoral behavior in order to ensure representative outcomes to monitoring coalition partners in order to secure stable government. In international relations, however, there has been a small but evolving body of research arguing that a veil of secrecy may improve the effectiveness of treaty bargaining and deliver domestic benefits to constituents who may otherwise be sidelined by the insertion of disproportionally powerful mobilized interests. Situated substantively at the intersection of these two disciplines, the EU is a most apposite institutional backdrop to examine and adjudicate the veracity of such seemingly incompatible views.
On the other hand, neither neofunctionalists nor intergovernmentalists have been able to provide a convincing explanation for the creation and empowerment of the EP by the EU member-states. While the Council of the European Union (previously known as the Council of Ministers, hereafter simply “Council” or “the CEU”) and the European Commission are both directly dependent on the will of the national governments and are responsible for much of the lawmaking process, the EP is directly elected by the citizens of the member-states. Thus, from an intergovernmentalist perspective, it is puzzling as to why the member-states would encumber the process with another body that is independently elected and therefore circumvents their “line of command” (or, at least, appears to). Meanwhile, the neofunctionalist view does not provide a compelling rationale for institutional spillover in this particular case. Again, the sticking point is that, even before the creation of the EP, there was plenty of institutional capacity within the Commission to legislate and enforce EU law. The addition of another legislative institution and the subsequent expansion of its powers, making it an effective veto player in many policy areas, including the all-important budgeting process, appears counterproductive from a functional-integrationist perspective.

Instead, the rational-choice theory advanced here contends that institutions have a strategic informational function that affects the policy process indirectly through the channel of responsiveness to constituents. Because of specialization and the revolving door, bureaucracies such as those of the Commission usually become captive to powerful concentrated interests. Although Commission appointments are made in concert by the member-state governments, the EU’s executive has quickly grown into a separate center of power with its own agendas and interests. Parliament is electorally incongruent with both Council and the
Commission, so its interests are likely to be distinctly different.\(^2\) The potential for policy conflict between Parliament and the Commission puts the EP in a dual oversight role. For the member-states, it may work as a watchdog over the EU bureaucracy’s legislative and regulatory proposals, as the member governments are much more focused on their domestic politics and dedicate relatively few scarce resources to monitoring moral hazard in EU institutions. For EU governments, the EP is also an independent source of information for domestic publics on important issues requiring specialized knowledge, where lobbyists have a particularly strong competitive advantage in the policy process. EP oversight reduces information costs for the member-states and domestic audiences in organizing resistance to Commission proposals that run against the public interest. The EP can mobilize public opinion where member-state governments may not want to take positions to avoid intergovernmental conflict or because of interest-group pressures. Because the EP is directly elected rather than appointed by member-states’ governments, it can also be used by them as political cover in implementing unpopular reforms or resisting the demands of domestic or transnational interest groups.

1.2. TRANSPARENCY, BARGAINING AND REPRESENTATION

The conventional wisdom holds that the transparency of the political process is an inseparable feature of representative democracy – and, furthermore, a beneficial one. There are at least two justifications for this view. From a normative perspective, the argument generally goes, democracy cannot fulfil its purpose if the actions of political leaders cannot be subjected to rigorous scrutiny. Constituents should be given maximal access to the nitty-gritty of the policy-

\(^2\) It is an altogether separate matter as to whether it can act on those divergent interests.
making process in order to be able to exercise effective electoral control and align policy as closely as possible to their preferences (Stasavage 2004). Lack of transparency attenuates this mechanism and allows politicians to pursue their own agendas at the expense of the public good, which ultimately defeats the putative rationale for democratic governance. The expected result in such circumstances is that policy outcomes will be skewed away from their “social optimum”, thereby deviating public welfare and social equity from their desired path. Such normative concerns are particularly pertinent in Europe, where the welfare state is still conceptually dominant as a favored form of social organization, and even more so with the accession of formerly communist countries to the EU (cf. Hawkins et al. 2006).

The more pragmatic basis for promoting political-institutional transparency is that it facilitates cooperation by making commitments (domestic or international) more credible and by reducing information asymmetries in bargaining. Both of these benefits are directly contingent upon the ability of constituencies to exercise electoral control, which inevitably requires access to information about government policy-making. As far as bargaining is concerned, an electoral leash tightened by enhanced citizen scrutiny can communicate to international partners a fairly narrow notion of the reservation point of the government, thus reducing the potential for breakdown in negotiations and/or war onset (Hug and König 2002; Fearon 1994; 1995; 1998; M. Svolik 2006). Schneider and Cederman (1994) specifically use information asymmetries to model the stop-and-go nature of European integration. Domestic audience costs affecting credibility have been persistently evoked in studies of both international

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3 See the next chapter for a more detailed discussion of the comparative literature on transparency in the context of principal-agent relationships.
cooperation and international conflict (e.g., Choi 2004; Goldstein and Martin 2000; Putnam 1988; Schultz 1998; 1999; Smith 1996; Tomz 2007). Meanwhile, constituent control can also act as a deterrent from defection – either because the latter is considered intrinsically undesirable by the constituents or because its consequences have a detrimental effect on the interests of the polity as a whole (e.g., Dai 2005; 2006).

Claims that EU integration subverts long-established democratic traditions by empowering opaque and unaccountable international institutions have long become an integral part of the repertoire not only of anti-integration parties, but also of genuinely disquieted nongovernmental organizations (Pollack 2003). Seemingly in response to such concerns (Taggart and Szczerbiak 2004), European leaders have been increasing the powers of the EU’s sole directly elected body – Parliament. However, the member-states’ strengthening of anticorruption practices at the union level and their bolstering the Court of Auditors and the European Court of Justice (ECJ) only faced even further accusations of foisting an essentially undemocratic and antidemocratic international regime on their citizens.

The opponents of further EU institutionalization may be on to something. The treaty bargaining and enforcement literature has suggested that the supranationalization of the EU might be conducive to the purposes of representative democracy and the welfare state precisely because it inhibits accountability by making the policy-making process less susceptible to outside scrutiny. On occasion, this can even be the sole benefit of bringing a particular policy within the jurisdiction of a supranational institution such as the EP. In particular, member-state governments may decide to engage in cooperation and supranationalization even if that does not provide benefits such as economies of scale or gains from trade – i.e., with the sole purpose of domestic redistribution.
Institutional transparency may have long been an object of interest for comparativists, but it has been drawing ever more attention from students of international relations (e.g., Finel and Lord 1999; Nielson and Tierney 2003), some of whom are challenging the conventional view that transparency has an unequivocally positive impact on institutional output (e.g., Fox 2007; Stasavage 2004). Dai (2005; 2006) suggests that providing domestic audiences with greater access to policy information can be a double-edged sword. According to her analysis, such access could provide ammunition to mobilized interest groups opposing compliance with international agreements and thereby result in a deterioration of states’ ability to realize cooperative gains. Furthermore, the openness of domestic institutions and the bargaining process may allow special interests to emasculate international agreements as early as the negotiation stage (e.g., Hug and König 2002; Mayer 1992; Stasavage 2004). Goldstein and Martin (2000, 630) posit that “legalization leads to more and better information about the distributional effects of proposed agreements [so] that it could actually deter the conclusion of cooperative deals” because it can provide incentives to resistant interests to mobilize effectively.

The strategic behaviors of governments in avoiding such adverse interference usually take the form of either diversion or appeasement. The latter normally involves providing side-payments to domestic groups in the form of direct compensation or policy concessions in other issue areas (Mayer 1992). For example, Davis (2004) shows how issue linkages have helped Europe and Japan liberalize agricultural trade in the face of belligerent domestic lobbies. Diversionary tactics, which are more relevant to the topic at hand, reduce policy transparency by obfuscating the decision-making process or hiding the distributional effects of international agreements (cf. Friman 1993). Allee and Huth (2006), for example, argue that political leaders use international adjudication as
cover for domestically unpopular dispute settlement (cf. Sandholtz 1993). In his analysis of informal international agreements, Lipson (1991, 538) makes a strong case that “[i]nterstate bargains are frequently designed to be hidden from domestic constituencies [and] to avoid legislative ratification” (cf. Chayes and Chayes 1993; Drezner 2000). Abbott and Snidal’s (2000) theoretical treatment of regime legalization yet again puts forward the idea that the ambiguity and formality of international law is informed by concerns about the political influence of domestic interests and used strategically to minimize their interference.

So which one is it? Does the insertion of the EP into the decision-making mechanisms of the EU slow down the process of integration and reduce policy agility and responsiveness? Veto-player theory and some of the bargaining theories would support this view on the grounds that electoral incongruence with the other EU institutions and the added transparency make logrolling more difficult. Or does the EP facilitate lawmaking and improve representation by adding an extra source of information and expertise (other than the Commission) thus helping mobilize domestic audiences? Probably the answer is in the affirmative. But before outlining the informational theory of institutionalization that substantiates that answer, it is necessary to delve deeper into the notion of transparency itself because not all types of transparency are created equal.

1.3. RECONCEPTUALIZING INSTITUTIONAL TRANSPARENCY

The conventional view is driven by an implicit assumption that more transparency translates into more information about the policy process, which in turn results in pressure on policymakers to adjust course if they veer away from the public interest. This serene image dissipates quickly under closer scrutiny. The specific impact of information about the policymaking process is mediated by the
relative influence of interested constituents and their ability to act on that information. Thus, it may well be the case that the availability of information disproportionately benefits special interests rather than the general public.

Access to decision-making processes allows interest groups to partake, often directly, in deliberations and policymaking. Hearings, public meetings and invitations to interest groups to file briefs on policy proposals are just a few formal methods for lobbies to exert influence. It is fairly safe to assume that, because of their ability to mobilize resources, special interests would be better able to take advantage of access than the general public would. Flows of rewards to obedient policymakers are well-documented in the literature. For example, Nollen and Quinn (1994) find a strong relationship between campaign funding from interest groups and roll-call votes in the US Congress (cf. Fordham and McKeown 2003). While research has been by no means conclusive on whether funding pressure induces compliance or simply promotes the political survival of individuals who would act favorably to special interests (Fortier and Malbin 2013, 457), in either case information about policymakers’ behavior is likely to facilitate lobbyist influence. Often lobbyists may (in)directly participate in drafting legislative language even when no avenues for that are formally available. Researchers in American congressional politics have suggested that the bulk of lobbyist influence is likely to “occur earlier in the process, when committees and leaders shape the agenda, and when members can add little-noticed provisions to larger bills or take preventive actions to block items before public votes need ever be taken” (Fortier and Malbin 2013, 458).

Additionally, the availability of information does not necessarily mean that audiences will become more informed. The relationship between the availability of information and the quantity of information acquired by each constituent group is mediated by the attendant acquisition costs. Special interests may again be in a
better position to acquire and process available data to obtain actionable policy knowledge, whereas the costs of doing so may be prohibitive for the general public. Individuals are much less likely to invest resources in information acquisition than lobbyists are (cf. Hüller 2007) because the costs do not justify the benefits. The advantage of special interests is dual. Typically organized by formal groupings, they enjoy economies of scale on the acquisition-cost side. By definition, they also benefit disproportionately from moving the political needle in the specific policy area (which is why they are called special interest groups). The implication is that fluctuations in transparency may have a similarly disproportionate effect – in one direction or another – upon organized interests. Rather than being direct and monotonic, any relationship between transparency and constituents’ ability to affect policy must more likely be subject to jump conditions mediated by resource endowments, mobilization levels as well as institutional constraints such as electoral rules, election cycles, campaign-finance restrictions, decision-making procedures and so on. In some cases marginal changes in institutional transparency may have similarly marginal effects on policy outputs but in other situations they may serve to exclude completely previously powerful constituencies.

Finally, “transparency” may refer to distinctly different aspects of the policymaking process. In the context of the EU, there are at least two distinguishable subspecies of transparency, which are not necessarily prominent in the literature. Indeed, this distinction is a significant substantive contribution of this analysis because, even if they do have similar effects on policy outcomes, different aspects of transparency may function in entirely different ways, with implications for institutional design.

On one hand, deliberative transparency encapsulates the propensity of each institution participating in the process to invite outside scrutiny into its decision-
making by holding open meetings, televising roll calls and publicizing reports, among other features. Deliberative transparency may be a product of both formal procedure and informal legislative practices. For example, a designated member must make a formal recommendation before a bill can move out of committee in the EP; it has become standard practice to publish those reports online even if there is no procedural requirement to do so. Overall, deliberative transparency tends to reveal credible and/or actionable information about policymakers’ beliefs and activities – e.g., whether a committee member delivered a supportive report on a piece of legislation or how a legislator voted in a roll call.

On the other hand, structural transparency is not directly determined by any one rule or practice, but implied in the totality of the decision-making process. For example, most legislation must clear committee review, make it to the floor agenda and be approved by both chambers of the US Congress before it can become law, inhibiting the attribution of responsibility for any particular provision in the final version of the bill. Information costs can be expected to increase as the structural transparency of policymaking decreases – i.e., as the number, institutional complexity and legislative equality of the decision-makers increases. The multi-level governance of the EU almost certainly impairs structural transparency, as does the empowerment of the EP in many policy areas. This impairment can be amplified or attenuated by the deliberative transparency of each decision-making body (e.g., whether committee meetings are open to the public or whether decisions are taken by roll call). But it is by no means a foregone conclusion that the addition of the EP, which tends to exhibit higher levels of deliberative transparency than Council, as a coequal chamber offsets the concomitant dilution of structural transparency.
1.4. TRANSPARENCY AND POLICY CHOICE IN A SIMPLE FORMAL MODEL

To elucidate the disparate effects of transparency on the policy impact of special interests relative to the general public, this section develops a formal model that incorporates deliberative and structural transparency as separate aspects of political institutions and takes into account the political clout of constituents and their information-acquisition costs.

The utility $W$ that political elites derive from staying in office can be defined as a function of the rent-extraction base, captured by total national wealth $\Omega \in \mathbb{R}$, and the government’s electoral popularity $Q \in [0,1]$:

$$W = \Omega^Q \quad (1.1)$$

This objective function is consistent with the prevailing view in the democratization literature: that governments’ ability to extract rents is contingent on available resources and constituents’ compliance with or resistance to rent extraction. An armed insurgency or even minor terrorist activity may destroy capital, impede economic activity and disturb the elite’s ability to harvest rents. Coming out on top in the struggle for power is therefore far from a license to appropriate everything, particularly in a complex technologically advanced economy. On one hand, excessive demands for rents are likely to result in growing resistance by the affected parties so that beyond a certain point an increase in the demand actually reduces the amount obtained. The greater the popular support for the government, the farther afield that inflexion point is likely to be. On the other hand, rent extraction reduces the ability of constituents to generate value that can be extracted in the future.
This initial specification can be simplified to make mathematical manipulation easier. Taking twice the natural logarithm of both sides of (1.1) produces

\[ \ln \ln W = \ln \ln \Omega + \ln Q \]  

(1.2)

which, after substitution \( w := \ln \ln W, \omega := \ln \ln \Omega \) and \( q := \ln Q \), yields the affine transformation

\[ w = \omega + q \]  

(1.3)

In other words, maximizing \( W \) is equivalent to maximizing \( w \) so that rent-seeking and welfare-seeking aspects of the policy-maker’s preferences can be represented additively.

To differentiate their power, let constituent groups \( i \in K = \{k, -k\} \) be characterized by political influence \( \eta_i \) such that \( \eta_i \in [0,1] \) and, without loss of generality, \( \sum_{i \in K} \eta_i = 1 \). Let the wealth component \( \omega \) of the government’s utility function be the sum of the utilities of all the constituents so that \( \omega = \sum_i u_i \). Further let constituent support \( q \) for the government be determined by the total amount of support received from the members of society, which are not required to put all their resources behind a single politician. That lobbyists often support competing candidates is a fact of life. If \( \pi_i \) is the probability that a constituent supports the government, then its total popularity is given by

\[ q = \sum_{i \in K} \eta_i \pi_i \]  

(1.4)
Let the policy space be two-dimensional so that the ideal points \( x_k, y_k \) of constituent \( k \) define a policy utility function

\[
u_k(x, y) = \alpha_k (x - x_k)^2 + \varepsilon_k^x + \beta_k (y - y_k)^2 + \varepsilon_k^y \tag{1.5}\]

Together with the cost of acquisition of information \( c_i \), the policy utility \( u_i \) adds up to the total utility of the constituent:

\[
U_i = u_i - c_i = \alpha_i (x - x_i)^2 + \varepsilon_i^x + \beta_i (y - y_i)^2 + \varepsilon_i^y - c_i \tag{1.6}
\]

The significance of the policies for each of the constituents is captured by the coefficients \( \alpha_i, \beta_i < 0 \). Constituents can observe directly only their total utility policy utility and the institutional structure, but not the policies implemented by the incumbent \( x, y \). The cost of acquiring information is \( c_i \) and \( \varepsilon^j \sim N(0, \sigma_i^j) \) are independent normally distributed random shocks to the utility signal in each policy area \( j \in \{x, y\} \) with standard deviations \( \sigma_i^j > 0 \). In other words, the utility signal differs in its clarity in each policy area and among constituents. If \( \varepsilon_i := \sum_j \varepsilon_i^j \), then by normality \( \varepsilon_i \sim N\left(0, \sigma_i = \sqrt{\sum_j (\sigma_i^j)^2}\right) \), and if \( f^j \) is the probability density function (PDF) of \( \varepsilon^j \)'s distribution, then the PDF of the total error \( \varepsilon \) is given by

\[
\varphi\left(\cdot \mid \sum_i (\sigma_i^j)^2 \right) = \prod_j f^j(\cdot \mid 0, \sigma^j) \tag{1.7}
\]

where \( \varphi(\cdot \mid \sigma) \) is a normal density with mean \( \mu = 0 \) and a finite standard deviation \( \sigma \geq 0 \). For brevity, it makes sense to write \( \varphi(\cdot \mid \sigma_i) = \varphi_i(\cdot) \). The dispersion of \( \varphi_i \) can be interpreted as the obscurity of the decision-making process – the larger the
standard deviation, the more unclear the actions of the government to the specific constituent \( i \).

To make it possible to reduce policy obscurity by acquiring more information, let \( \sigma_i = (1 - h_i)\bar{\sigma} \), where \( \bar{\sigma} > 0 \) is the reciprocal of structural transparency \( 1/\bar{\sigma} \). Meanwhile, let the information level \( h_i = \min\{\tau, c_i, \lambda_i\} \) be a function of the deliberative transparency level \( \tau \in [0,1] \) explicitly set by the government, the constituent’s resource endowment \( \lambda_i \in \mathbb{R}_+ \) and the acquisition cost \( c_i \in \mathbb{R}_+ \) expended by the constituent. In other words, constituents can invest in becoming informed, but they cannot learn more than the information \( \tau \) that the government makes available and their research is constrained by their available resources \( \lambda_i \). The constituents do not know the utility function of the government, assuming instead that it maximizes its political support \( q \).

The game proceeds in the following order:

1. The government chooses whether to delegate policy \( y \) to a supranational institution, which would constrain the policy to some specific value \( \bar{y} \), which is known to the government but not the constituents.
2. The government then picks policies \( x, y \) to implement with \( y = \bar{y} \) if it chose the international institution in the previous step.
3. The constituents decide on their information expenditure and observe their individual policy utilities \( u_{ki} \); the government observes the subsequent wealth level \( \omega \).
4. The constituents choose a level of support for the government and the latter receives its payoff.

The political support for the government by individual constituents can be defined as a univariate function of their observed utility relative to some performance metric \( M_i \) based on observed utility so that the support of constituent
for the government equals \( J(u_i \geq M_i) \), where \( J(s) \) is the indicator function – i.e., \( J(s) = 1 \) when statement \( s \) is true and \( J(s) = 0 \) otherwise. Therefore, it is possible to derive the probability that constituent \( i \) supports the government given a pair of policies \( x, y \). Specifically, \( \pi_i = P(J(u_i \geq M_i) = 1) = P(u_i \geq M_i) = P(\alpha_i(x - x_i)^2 + \beta_i(y - y_i)^2 + \epsilon_i \geq M_i) = 1 - \Phi(M_i - \alpha_i(x - x_i)^2 - \beta_i(y - y_i)^2|\sigma_i) \) such that \( \Phi(\cdot |\sigma_i) \) is a normal cumulative distribution function (CDF) with standard deviation \( \sigma_i \) and mean \( \mu = 0 \):

\[
\Phi \left( \frac{n|\sigma_i = \sqrt{\sum_i (\sigma_i')^2}}{\int_{-\infty}^{\infty} \prod_i f_j^i(\cdot |0, \sigma_i') \, dt = \int_{-\infty}^{\infty} \varphi(\cdot |\sigma_i) \, dt} \right) (1.8)
\]

The solution concept for the purposes of this chapter will be subgame-perfect equilibrium (SPE) and, whenever they are not provided directly, proofs will be available in Appendix I.

1.4.1. **General Results in a Domestic Game**

First, consider only a purely domestic version of the game, where the first step of the game is omitted and there is no delegation of policy-making to a third party. The results in this subgame will inform the equilibrium conditions in the larger game, which includes the potential for outsourcing some portion of policy-making to a supranational body.

**Proposition 1.1.** In the subgame-perfect equilibrium of the domestic game, the best-response strategy of the incumbent is:
\[
\begin{align*}
\bar{x}^* &= \frac{\sum_i x_i \alpha_i \left(1 + \eta_i \left(\sigma_i \sqrt{2\pi}\right)^{-1}\right)}{\sum_i \alpha_i \left(1 + \eta_i \left(\sigma_i \sqrt{2\pi}\right)^{-1}\right)} \\
\bar{y}^* &= \frac{\sum_i y_i \beta_i \left(1 + \eta_i \left(\sigma_i \sqrt{2\pi}\right)^{-1}\right)}{\sum_i \beta_i \left(1 + \eta_i \left(\sigma_i \sqrt{2\pi}\right)^{-1}\right)}
\end{align*}
\]

**Proposition 1.2.** In the subgame-perfect equilibrium of the domestic game, the optimal information level of each constituent is:

\[
h_i^* = J \left(\frac{\partial u_i}{\partial h_i} \geq \frac{\partial c_i}{\partial h_i}\right) \min\{\tau, \lambda_i\}
\]

**Proposition 1.3.** In the subgame-perfect equilibrium of the domestic game, the government’s chosen policy is closer to a group’s ideal (the constituent’s expected utility increases) if that group has higher political influence, higher equilibrium information levels and a larger impact on social welfare, as well as if the ideal point of the other group is closer.

Overall, these generic equilibrium results of the domestic game conform to standard expectations. Proposition 1.1 simply states that the implemented policies fall somewhere between the ideals of the constituents. Proposition 1.3 reflects the idea that these equilibrium policies are tilted more strongly in favor of groups that are economically larger – in the absolute values of parameters \(\alpha, \beta\); politically more influential – in \(\eta\); and face a better clarity of responsibility \(\varphi_i(0) = 1/\sigma_i \sqrt{2\pi}\), which hereafter is denoted simply as \(\varphi_i\). By Proposition 1.2, constituents choose to get informed only if their marginal utility of doing so is at least as high as the cost of acquiring the information. This separating condition leads to two diametrically opposite types of behavior. When the condition is met, constituents absorb all information they can up to their resource endowment \(\lambda\) or the transparency ceiling \(\tau\) set by the government, whichever is more constraining. Otherwise, they
rationally choose to remain completely ignorant of the policy process. This result is consistent with the earlier suggestion that information availability is distinct from information acquisition.

The next step is to evaluate how the equilibrium conditions compare to two potential social optima – the maximum wealth and the most equitable distribution of it.

**Definition 1.1.** If \((x, y) \in \arg \max \omega(x, y)\), then the policy \((x, y)\) is economically optimal.

**Definition 1.2.** If social equity is \(\Theta(x, y) := -|E[u_k(x, y)] - E[u_{-k}(x, y)]| = 0\), then the policy \((x, y)\) is socially equitable.

**Proposition 1.4.** The economically optimal policy levels are:

\[
\begin{align*}
\bar{x}^* &= \frac{\sum_i x_i \alpha_i}{\sum_i \alpha_i} \\
\bar{y}^* &= \frac{\sum_i y_i \beta_i}{\sum_i \beta_i}
\end{align*}
\]  
\[(1.11)\]

**Proposition 1.5.** Any economically optimal policy is socially equitable and, in equilibrium, an improvement in total welfare cannot result in a reduction of social equity.

**Proposition 1.6.** The subgame-perfect policies \(x^*, y^*\) converge to the wealth-maximizing and socially equitable policies \(\bar{x}^*, \bar{y}^*\) as the ratio of the groups’ policy clarity levels \(\frac{\varphi_k}{\varphi_{-k}}\) converges to the reciprocal of the ratio of their political influences \(\frac{\eta_k}{\eta_{-k}}\).

**Proof.** This result follows directly from evaluating the limit of the equilibrium solution for either policy:

\[
\lim_{\varphi_k \to \varphi_{-k} \to \varphi_k \eta_k \to \varphi_{-k} \eta_{-k}} x^* = \lim_{\varphi_k \eta_k \to \varphi_{-k} \eta_{-k}} \frac{\sum_i x_i \alpha_i (1 + \eta_i \varphi_i)}{\sum_i \alpha_i (1 + \eta_i \varphi_i)} = \frac{(1 + \varphi_k \eta_k) \sum_i x_i \alpha_i}{(1 + \varphi_{-k} \eta_{-k}) \sum_i \alpha_i} = \frac{\sum_i x_i \alpha_i}{\sum_i \alpha_i} = \bar{x}^*. \quad \blacksquare
\]
The bottom line is that the disparity of political influence leads, just as in the real world, to economically suboptimal and socially inequitable policies. And, assuming that an organized interest group has not just more clout $\eta$ but also a better grasp $\varphi$ of the goings-on of policymaking, these lopsided outcomes are even more skewed towards powerful lobbies. Defining the political clout arising from a constituent’s policy clarity level $\varphi$ and political influence $\eta$ as $\psi = 1 + \eta \varphi$, it can then be stated generally that the group with greater political clout $\psi$ enjoys more favorable government policy.

**Proposition 1.7.** As constituent $k$’s advantage $\psi_k / \psi_{-k}$ in political clout increases, the equilibrium policy moves towards that constituent’s ideal point; the government’s equilibrium policy is always skewed away from the optimum $\bar{x}^*, \bar{y}^*$ towards the constituent with the greater political clout.

In other words, it may be normatively desirable to aim for a reversal of the information ratio relative to the influence ratio, as in Proposition 1.6, by means of institutional design. Policy can move towards the optima if the relationship between political influence and information levels is moved towards reducing the lobbyists’ informational advantage. Substantively, this can be achieved by restricting their access to information, increasing the information levels of the general public or both. From a practical perspective, the former seems much more feasible than the latter, but a combination of both would probably be the most effective approach. To a large extent, this combined impact is visible in the workings of the EP (see Section 1.5 below), so the effects of deliberative and structural transparency deserve to be analyzed in greater detail, which is the subject of the following subsection.
1.4.2. INSTITUTIONAL TRANSPARENCY AND POLICY-MAKING

Assuming that, in equilibrium, information is valuable to the constituents (i.e., that \( \partial u / \partial h > 1 \)), in order to obtain a more comprehensive understanding of the implications of transparency, it is necessary to consider its impact on constituents’ payoffs in different configurations of the transparency parameters: deliberative transparency \( \tau \), structural transparency \( 1/\bar{\sigma} \) and the information resource endowments of the constituents \( \lambda \). For the remainder of the analysis, let \( k \) be the mobilized interest group so that \( \lambda_k > \lambda_{-k} \) and \( \eta_k > \eta_{-k} \). Without loss of generality\(^4\), also let \( x_k > x_{-k} \).

**PROPOSITION 1.8.** If political clout is distributed unequally among the constituents, decreasing structural transparency \( 1/\bar{\sigma} \) brings policy closer to the social optimum \( \bar{x}^* \).

**PROPOSITION 1.9.** If political clout is distributed unequally among the constituents and \( h_k \leq \lambda_k \), decreasing deliberative transparency from \( \tau \) to \( \tau' < h_k \) brings policy closer to the social optimum \( \bar{x}^* \).

Together, Propositions 1.8 and 1.9 show that structural and deliberative transparency can be used to manipulate the equilibrium outcome and bring it closer to the social optimum – which ultimately benefits the less powerful constituency. Notably, structural transparency seems to be the more reliable of the two methods because the deliberative-transparency pathway requires (i) that in equilibrium constituents actually bother to gain information (i.e., that \( \partial u / \partial h > 1 \)) and (ii) that deliberative transparency falls below the equilibrium consumption and the resource endowment of the more powerful constituent. The blunter instrument of reducing structural transparency needs no such special conditions to work.

\(^4\) Subsequent proofs can be replicated with the opposite assumption.
Furthermore, the EP may have a role much more significant than being just another paperweight in a pyramid of veto players. Through their reports, hearings and media activities, members may be able to “subsidize” the information consumption of the public, particularly on subjects with substantial lobbyist pressures. Almost by definition such subsidization would take place at a very basic level – it would aim not to overshoot the informational sophistication of the lobbyists themselves because in that case much of the redistributive effect may be lost. Thus, it can be expected that if issue-specific information is subsidized, the target level would be somewhere between the information levels of the special interests and the general public, which is captured by the following:

**Proposition 1.10.** If political clout is distributed unequally among the constituents, setting an information floor $h$ such that $h_k \geq h > h_{-k}$ moves the equilibrium policy towards the social optimum and towards the preferred policy of the less influential group.

Observe that the empirical implications of this proposition are domain-restricted to policy (not valence) messaging; it would be focused on specific issues and have somewhat more factual and more sophisticated content than typical (mostly symbolic) political messages. It would likely also have a prospective rather than retrospective character and take place during the actual legislative process rather than in election campaigns. In other words, MEPs’ being secretive about their own affairs and Parliament’s proceedings cannot be counted as empirical evidence against this mechanism. Rather, the EP will be open on debates where specific policy decisions are at stake and those decisions are known to involve powerful interest groups with influence over the Commission and (some) member-state governments. Thus, Parliament can be expected to be vocal on a policy issue when public attitudes are congruent with those of the EP (or at least members who specialize or care about the particular policy area) and there is
conflict with the Commission; parliamentary action must be contingent on tacit approval by the member-states because they are the ones who decide which policy falls within the legislative jurisdiction of the EP.

1.4.3. **Supranational Institutions and Domestic Redistribution**

Moving one of the policy areas to the supranational level entails replacing the domestic mechanism with some expected value for the collective policy $\bar{y}$ and the assumption that adding an extra institution will decrease structural transparency $1/\bar{\sigma}$. Thus, there are two factors simultaneously at work – moving policy out of the domestic domain and getting another institution involved in that external domain. This is largely consistent with what happened after the adoption of the Treaty on European Union (TEU) and its various revisions, which created new collective legislative procedures newly including the EP in a stronger role, but also made the EU’s legal jurisdiction ever broader in terms of the policy areas involved.

**Proposition 1.11.** In the supranational equilibrium where policy $\bar{y}$ is set externally and $1/\sigma'_i$ is the constituent’s structural transparency level under the new institutions, where $\sigma \ll \sigma'$, the government’s best-response residual domestic policy is

$$x^{**} = \frac{\sum_i x_i \alpha_i \left(1 + \eta_i \left(\sigma'_i \sqrt{2\pi}\right)^{-1}\right)}{\sum_i \alpha_i \left(1 + \eta_i \left(\sigma'_i \sqrt{2\pi}\right)^{-1}\right)} \quad (1.12)$$

It is reasonable to assume that structural transparency will decline with supranationalization. While the *acquis communautaire* of the EU has direct effect in the member-states, much of the law is subject to interpretation and regulation at the local level; in many cases EU directives only outline objectives to be achieved
and leave to the member-states to find their own way to the goal by whatever domestic law they choose to implement. In creating the EP, the member-states may have been applying just that blunt instrument for obstructing the clarity of decision-making that benefits powerful lobbies, but rarely everyday constituents. Encumbering the decision-making process with the inclusion of the EP, even in cases when that role is just marginal, can improve outcomes for less mobilized and politically influential groups. Specifically, Proposition 1.8 implies:

**Proposition 1.12.** In the supranational equilibrium where policy \( \tilde{y} \) is set externally and \( 1/\sigma'_i \) is the constituent’s structural transparency level under the new institutions such that where \( \sigma \ll \sigma' \), residual domestic policy \( x^{**} \) will be closer to the social optimum than without supranationalization.

**Proposition 1.13.** In the global game, the government will choose to move policy-making to the supranational institution whenever

\[
(x^* - x^{**}) \sum_i \alpha_i (x^* + x^{**} - 2x_i) + y^* \sum_i \beta_i (y^* - 2y_i) < \tilde{y} \sum_i \beta_i (\tilde{y} - 2y_i)
\]

where \( x^* = x^*(\tilde{\sigma}), y^* = y^*(\tilde{\sigma}) \) and \( x^{**} = x^*(\tilde{\sigma}') \).

The unexpected implication of the global game is that if moving policy \( y \) to the supranational institution makes sense (i.e., condition (13) is satisfied), then policy improves also along the dimension of the residual domestic policy area \( x \). In other words, the model captures an indirect redistributive effect in domestic welfare. For instance, integration in the area of fisheries should increase women’s real incomes, assuming that women are not as organized as (and that few of them work as) fishers. This domestic spill-over theoretically guarantees policy improvements even in areas where no integration has occurred – which was part
of the reason why the EU rushed in Spain, Portugal and Greece long before they were objectively ready for accession (cf. Dinan 1994). These effects may extend far beyond the institutional organization of the EU itself; Baccini and Urpelainen (2014) argue that leaders in developing countries use preferential trade agreements, particularly with the EU, in order to commit to and entice support for domestic economic reforms.

Thus, more than anything else, the main reason for supranationalization may have been to use the directly elected EU institutions as political cover against powerful interest groups. The Single Market and other elements of the EU treaty framework that indubitably benefit the member-states do not necessarily require such supranationalization. Cooperative agreement could have been – and for a considerable time was – reached and implemented without the interference of an independently constituted supranational body such as Parliament. If the model’s intuition is correct, somehow the introduction of more EP-leveraged decision-making must have disturbed the balance of information between more and less influential groups in favor of the latter. On one hand, the EP can be viewed as an additional decision-maker diluting responsibility across the board and decreasing structural transparency $1/\bar{\sigma}$; on the other, it does have a different internal organization and is much more open than the Commission and Council, which may allow it to engage in subsidizing public information on EU policy to the detriment of lobbyists by setting an information “floor” similar to that put forward in Proposition 1.10.

1.5. Empirical Experience

In evaluating the extent to which the informational rationale for the formal elevation of the EP as a (nearly) coequal legislative chamber finds empirical
support, three sets of issues merit consideration. At the outset, it is important to track the development of the EP’s authority within different policy areas and types of legal acts within EU law, as well as the dynamics of its interaction with the other legislators – Council and the Commission. The main goal is to show that, consistent with the theory, Parliament’s formal legislative prerogatives have indeed expanded dramatically over the past quarter-century, but other aspects of the EU’s legal framework such as the budget process have ensured that in practice the power of the member-states (and of Council) remains undiminished. Additionally, patterns of bill adoption within and between the two chambers have become even more consensual and informal than before, making it nearly impossible to identify empirically consistent defiance by Parliament of Council positions, which supports the theory’s conjecture about the conditional nature of the EP’s new powers: Parliament is more likely to oppose the Commission’s draft language and does so mostly when its amendments can pass in Council. Such a finding is in tune with the idea that member-states use Parliament as a political cover to modify legislation heavily influenced by interest groups. In terms of deliberative transparency, the internal disclosure rules and legislative practices of each of the three institutions and their behavior during the adoption of the EU’s transparency regulations add yet another piece of evidence revealing the EP’s distinct informational role and that role’s conditionality on implicit member-state consent.

Next, it is vital to contemplate competing explanations for the creation of the EP and the expansion of its power, whether they are logically and empirically compelling, and to what extent they complement or contradict the proposed informational theory. If there is a viable complementary explanation, then it is important to evaluate the relative importance of the mechanism and especially whether both of them are necessary or they are merely additive – reinforcing one
another but capable of inducing the outcome on their own. If there is a strong case for any theory that contradicts the model of informational balancing proposed in the prior section, then it is necessary, at a minimum, to identify empirical pathways for adjudicating which one is more likely to be valid.

Finally, it is helpful to provide an example of the legislative process at work when powerful special interests are pitched against what can be viewed as the public interest on an issue that affects most of the member-states and is technically complex and preferably fact-based (i.e., possibly not an issue with a prominent “values” dimension such as religion or immigration). Such an important policy decided at the EU-level is the regulation of vehicular emissions of greenhouse gasses, which is an important point of contention between car companies and their labor unions on one side and environmental groups on the other. Whereas the EU is generally considered among the most aggressive polities in tackling global warming, the cost and effectiveness of climate policy has frequently been a subject of considerable controversy nonetheless. If the EP acted largely in concert with Council and the Commission and adopted their non-public mode of decision-making, then the mechanism of the informational theory would simply be absent and the theory itself would not find support as a viable explanation of Parliament’s creation. If, on the other hand, the EP’s legislative organization exhibited a greater degree of openness to public scrutiny and if legislators’ behavior involved actively using media channels to disseminate policy information in order to oppose Commission or Council positions, that would be an indication in favor of the informational model.

1.5.1. Development and Transparency of EU Legislative Processes

EU law comes in a variety of flavors, which are created and function differently (Fig. 1.1). The treaties act as the Union’s de facto constitution. They are
the legal basis for all EU law and mostly deal with arranging the institutions of the EU, their decision-making procedures and the extent of the EU’s jurisdiction over various policy areas. Since the treaties have to be ratified by the member-states, by definition they cannot contradict any of their national constitutions (which is why treaty revisions have triggered domestic constitutional changes more than once). However, EU law below the treaty level takes precedence over national law. The Treaty on the Functioning of the European Union (TFEU) extends treaty amendment initiative to Parliament and the Commission, not just the member states, but recommendations have to be adopted and specific language drawn up by an intergovernmental conference (IGC) before being submitted for ratification by the member states. Regardless of the formal power of initiative, an IGC cannot be convened without a decision by the European Council (or, in some cases, the EC may adopt the proposal and submit directly for ratification), thus supranational institutions can hardly claim even agenda-setting power at the constitutional level.

Figure 1.1. EU Law and Legislative Procedure under the TFEU\(^5\)

<table>
<thead>
<tr>
<th>EU Legal Category</th>
<th>State Equivalent</th>
<th>Initiative</th>
<th>Adoption</th>
</tr>
</thead>
<tbody>
<tr>
<td>treaties</td>
<td>constitution</td>
<td>member-states,</td>
<td>European Council,</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Commission,</td>
<td>then member-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Parliament</td>
<td>states</td>
</tr>
<tr>
<td>budget</td>
<td>federal law</td>
<td>Commission on opinion by</td>
<td>Council,</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Parliament</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>EU Legal Category</th>
<th>State Equivalent</th>
<th>Initiative</th>
<th>Adoption</th>
</tr>
</thead>
<tbody>
<tr>
<td>directives</td>
<td>federal law</td>
<td>Commission</td>
<td>Council, (in most cases) Parliament</td>
</tr>
<tr>
<td>regulations</td>
<td>federal, state and local law and regulations</td>
<td>Commission</td>
<td>Council, (in most cases) Parliament, (rarely) Commission</td>
</tr>
<tr>
<td>decisions</td>
<td>typically issue-specific executive orders and pronouncements</td>
<td>Commission</td>
<td>Commission by delegation from Council, (rarely) Parliament</td>
</tr>
</tbody>
</table>

The EU’s budgetary procedure is similarly complicated. It takes place in two stages. With the assent of Parliament, Council unanimously adopts a seven-year financial framework, which caps the revenues at 1.23% of union-wide gross national income and expenditures at 1.29% for the 2013-2020 period. The funding comes from collections of the Common Customs Tariff and assessments on national value-added tax, with various state-specific transfers and exemptions. The annual budget then allocates resources for EU institutions and policy, with the latter funds allocated by issue area and member-state, thus its effect is indirect and requires implementation by member-states’ institutions and, typically, special legislation at the state and, often, regional level. The Commission is responsible
for approving and monitoring how member-states disburse the funding through their own programs.

Whereas the Commission drafts the annual budget proposals based on opinions submitted by the EP and CEU beforehand, the member-states still dominate the process. The Commission proposal goes through a single reading, first in Council, which adopts by qualified majority voting (QMV), and then in Parliament, before typically ending up in the conciliation committee, composed of 28 members each of the EP and Council. This is in sharp contrast to most other important legislation, where the EP reads the proposal first and conciliation rarely becomes necessary. Even though Parliament can unilaterally adopt the committee decision within two weeks, it seems unlikely that the member-states would let out of committee anything they have not agreed en bloc in Council beforehand. The relatively convoluted procedure retained for the budget process is suggestive of its persistent contentiousness – among the member-states and between the participant institutions – because of its redistributive nature (Kardsheva 2013, 860).

Regulations are the most powerful form of EU law as they have direct effect within the member-states and can be enforced by local courts, not just EU institutions. Both regulations and directives are drafted by the Commission and in some cases Council can entirely delegate its legislative authority to the Commission. Directives typically set goals and intentions of varying specificity, but leave the methods of achieving them in the hands of the member-states’ governments and legislatures. Although directives require transposition into national law, the ECJ ruled as early as 1991⁶ that they can have direct effect in that individuals (not just member-states and EU institutions) can seek redress if

---

⁶ See Francovich et al. v Italy, European Court of Justice 1991.
directives are not implemented within the set timetables. Decisions often involve the Commission’s making pronouncements on (i) EU law violations by member-states such as excessive budget deficits under the Maastricht criteria for fiscal stability and (ii) commercial matters such as (multinational) mergers and implementation of tariffs and duties.

With the obvious exception of the budget discussed earlier, the adoption of legal acts of any particular type is not limited to a specific procedure. Rather, procedural rules are determined by the policy area that they affect, which creates a peculiar restriction on logrolling, as potential omnibus legislation has to remain within the same adoption procedure (Fig. 1.2). This makes it extraordinarily challenging to measure logrolling activity within and between institutions when conflictual issues within different procedures are being considered.

**Figure 1.2. Adoption Rules in Council**

<table>
<thead>
<tr>
<th>Nomenclature</th>
<th>Adoption Rule</th>
<th>Applicability</th>
</tr>
</thead>
<tbody>
<tr>
<td>unanimity</td>
<td>all member-states must agree for adoption</td>
<td>most CFSP and some PJCC issues, accession, association agreements, taxation</td>
</tr>
<tr>
<td>QMV</td>
<td>a blocking minority must include at least four member-states and 35% of population</td>
<td>most policy areas</td>
</tr>
</tbody>
</table>

7 European Union 2012.
### Nomenclature

<table>
<thead>
<tr>
<th>Adoption Rule</th>
<th>Applicability</th>
</tr>
</thead>
<tbody>
<tr>
<td>simple majority</td>
<td>informational and procedural issues as well as other non-essentials</td>
</tr>
<tr>
<td>more than half the present members must agree for adoption</td>
<td></td>
</tr>
</tbody>
</table>

The EU is also exceptional among parliamentary systems in that its executive – the Commission – is the only institution which can draft legislation, which confers it unusual agenda-setting power, worthy of a Westminster-style system. This consistency of initiation explains why legislative procedures are typically classified along two dimensions: the decision rule in Council (the upper house) and the involvement of Parliament (the lower house) past Council’s decision (Fig. 1.3).

### Figure 1.3. EU Legislative Procedures

<table>
<thead>
<tr>
<th>TFEU Procedure</th>
<th>Superseded Procedure(s)</th>
<th>Summary of Process</th>
<th>Main Areas of Applicability</th>
</tr>
</thead>
<tbody>
<tr>
<td>ordinary legislative procedure</td>
<td>cooperation, co-decision I, co-decision II</td>
<td>three readings by EP and CEU each, with conciliation</td>
<td>most EU legislation under Communities and PJCC pillars</td>
</tr>
<tr>
<td>assent</td>
<td>consent</td>
<td>up or down vote by EP on CEU-adopted legislation</td>
<td>international, accession and association agreements; financial framework</td>
</tr>
</tbody>
</table>

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Council is essentially an intergovernmental forum composed of representatives of the member-states. In practice, the composition of the upper chamber varies with the subject matter and the rise and fall of member-states’ cabinets. Typically, the minister with the relevant national portfolio will represent the member-state in a Council meeting. For example, agriculture law will be decided in a meeting of the agriculture ministers of the member-states, although others may substitute. Since the adoption of the Treaty on the European Union, unanimity has been in retreat as Council’s main de jure decision rule; the annual budget and most new issue areas within the EU’s jurisdiction, including many in the traditionally sensitive Common Foreign and Security Policy (CFSP) and Police and Judicial Co-operation in Criminal Matters (PJCC) pillars of the Union. While higher agreement thresholds are needed for certain proposals not initiated by the Commission, Art. 16 (4) of the TFEU stipulates, in rather convoluted language, that

[a]s from 1 November 2014, a qualified majority shall be defined as at least 55% of the members of the Council, comprising at least fifteen of them and representing Member States comprising at least 65% of the population of the Union.

A blocking minority must include at least four Council members, failing which the qualified majority shall be deemed attained. (Council of the European Union 2008, 31)
This iteration of QMV rules follows earlier – less proportional and more restrictive – versions, but empirically it is only a tool to drive consensus. In very rare instances do member-states’ object or even abstain in Council votes. Despite expanding the domain of QMV and the more-than-doubling of its membership since the adoption of the Maastricht Treaty, most decisions in Council are still taken by consensus and roll calls – let alone public debate – rarely occur. One explanation for this phenomenon is based on member-states’ efforts to build blocking coalitions, which may ultimately lead to logrolling or compromise on contentious policy proposals (Häge 2013). Meanwhile, simple majority voting is formally allowed only on inessential matters such as requesting legislation or information from the Commission (which it is not obliged to provide it by the treaties). The bottom line is that bills rarely appear in Council meetings unless their unanimous adoption is a foregone conclusion.

With the Lisbon Treaty, the ordinary legislative procedure (OLP), based on its predecessor “co-decision”, covers most policy areas just like QMV has come to be the main formal method of Council decision-making. With more member-states and divergent interests, effective logrolling requires more omnibus bills which potentially increases bill complexity (Aksoy 2012). Thus, putting most legislation under the same rule facilitates logrolling, while increasing the EP budget enables the development of much-needed analytical capacity to handle omnibus legislation. However, package deals “make the legislative process less transparent, as they are usually agreed upon informally between a select group of representatives” (Kardasheva 2013, 860). Thus, a potential logroll on steroids engendered by the dominance of OLP plays right into the hands of state governments looking to gain political cover by claiming that some issues had to be surrendered to Parliament’s demands.
Formally, the broad implementation of OLP also undercuts the Commission’s agenda-setting power because Parliament is the first to review and amend the proposal. Since about 2003, most legislation has been adopted on first reading and only about 10% on second or third reading taken together (Hix and Høyland 2013, 174). This means that Council typically approves any amendments made on Parliament’s first reading. It is hard to tell whether this is despite or because of the fact that if the EP fails to reject or amend a Council position on second reading it becomes law – or simply because of the consensual legislative model, where Council and Commission representatives are often invited by the EP’s presidency to comment before plenary votes. Only in very rare cases under the OLP’s predecessor procedures has Parliament outright rejected Council positions – e.g., the unsuccessful software patentability directive which was killed in 2005 and the first attempt at passage of Directive 98/44/EC on biotechnology patents in 1995. Thus, the EU’s legislative process draws a sharp contrast to other multicameral systems, especially those under presidentialism, not as much for its formal complexity as for its practical outcomes. In the United States, for instance, the legislative process involves plenty of ideological posturing and is very often adversarial, with any one of the three legislative bodies – House, Senate and president – routinely proposing bills that cannot conceivably be approved by the other two. By contrast, the legislative process in the EU is one of extensive consultation and consensus-building (Yoshinaka, McElroy and Bowler 2010; Kardasheva 2013; Häge 2013) that frequently seems to begin long before even a single word of the draft bill has been written.

One may easily lose sight of whether these outcomes are a product of a consensual or a highly regimented and informally controlled process (or, indeed, whether the distinction between those categories is itself purely semantic). At any rate, it is important not to overplay or overestimate the power of Parliament after
the Lisbon Treaty. “Parliament is less powerful than the Council – even under the revised co-decision procedure [i.e., OLP], where the formal powers of the two institutions are identical” (Hix and Høyland 2013, 177). The EP still cannot initiate legislation and, even though it has to approve the president of the Commission, the member-states still are the true masters – de facto if not de jure – of the nomination and approval process for the commissioners as well as the Commission’s president. In some respects, though, this disjuncture between Parliament and the executive prevents the EP from becoming subservient to the Commission as the legislature would be to the cabinet in a true Westminster-style system.

Within this legislative framework, the most important actors that can set transparency levels in the EU continue to be the member-states. In the sphere of constitutional change, the veto power that individual states hold over amendment of the treaties grants them overwhelming agenda-setting advantage over the EP despite that the latter has to approve future agreements. Even proponents of the multi-level governance approach do not challenge the notion that member-states have retained an overwhelming proportion of the decision-making authority within the union and hold an even tighter grip on constitutional changes (viz., Hix 1999; Hooghe and Marks 2001; Peterson and Shackleton 2006; Pollack 2005; Wallace and Wallace 1996; cf. Dinan 1994; Garrett 1992; Moravcsik 1993). There is abundant evidence that not only have member-states retained most of their legislative leverage vis-à-vis the Union’s supranational institutions, but also used institutional changes strategically to maintain the balance of power within the Council in anticipation of the Fifth Enlargement (König and Bräuniger 2004).

That “independent” European institutions still operate under the shadow of (the disapproval of) the member states is anything but an uncommon argument. There is good reason to believe that even the ECJ is strongly influenced by the
latent threat of noncompliance or retribution by the member-states (Carruba, Gabel and Hankla 2008; 2012). König and Bräuniger’s (1998) empirical analysis of EU legislative dynamics shows that shifts to qualified-majority voting (QMV) have resulted in bringing the Council even closer to a run-of-the-mill bargaining forum. Large states have increased their authority through the redistribution of votes under this procedure. Thus, QMV appears even more consistent with “power politics” than unanimity does and its adoption in a wide variety of areas does not necessarily imply that supranational institutions will acquire a particularly dominant position by acting as an independent power center. The conjecture that states are still firmly in command is supported by empirical evidence even in the most integrated area – international trade (Meunier 2000). Ironically, this is where the unabated institutional power of Council and the member-states comes from. Through the multiannual financial framework, only the member states can approve revenue not just for EU programs, but for the Union’s administrative expenses as well. And if Parliament wants to be funded or have any new EU policy adopted at all, it better assent to what the member-states’ governments have agreed among themselves on budgetary matters. The power of the purse is the only real power in town, and the member-states both de jure and de facto firmly hold its strings. The implication is that constitutional changes empowering the EP in the legislative process are unlikely to have produced better policy than what Council would have done on its own – if the “brute force” of the formal decision-making mechanisms is the only explanatory variable.

Rather, the extent to which the EP’s position has been enhanced is visible in the growth of its overall budget and in the expansion of its policymaking domain, particularly as it relates to the application of OLP even to such traditionally sensitive areas as agriculture. Parliament’s general appropriations increased to nearly €1.8 billion for FY 2015 from €1.53 billion in FY 2009, whereas
the Commission’s budget shrank from €3.57 billion to €3.26 billion over the same period (European Parliament 2009; European Commission, n.d.). These fiscal trends indicate a buildup in institutional capacity at the EP and a relative increase of its administrative resources as compared to the Commission’s still dominant position. Meanwhile, the CEU’s budgeted expenditure (together with that of the European Council) has remained about €600 million per annum. These figures suggest at least two trends consistent with the informational theory: (a) Parliament is building up its own capacity and therefore must be informationally less dependent on the Commission’s bureaucracy and (b) Council budgets do not exhibit an upward trend, suggesting that it relies on its existing resources and national governments’ administrative capacity to inform its decision-making.

Explicit changes in EU procedural and structural transparency have also been largely confined to the EP’s own evolution. The right of access to EU documents was first enshrined in Art. 255 of the 1997 Treaty of Amsterdam (later TFEU Art. 15). Paragraph 3 of the article states that “[a]ny citizen of the Union, and any natural or legal person residing or having its registered office in a Member State, shall have a right of access to […] documents” (European Union 2012, 54–55). However, the text leaves it up to each institution to determine its own rules of procedure. In other words, the provision is little more than a generic statement of intent. The 2007 Treaty of Lisbon introduced the only binding constitutional provision – Paragraph 2 of Art. 15, according to which, “the European Parliament shall meet in public, as shall the Council when considering and voting on a draft legislative act” (European Union 2012, 54). No mention is made of access to documents that Commission and the Committee of Permanent Representatives

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9 The Commission’s shrinking budget is in part related to the reduction of its enlargement activities.
(COREPER) supply to legislators or any other private information that they have. That is, drafting bills, legislative deliberations and the information they are based on remain undisclosed without action from interested parties, and even if such action is forthcoming, institutions essentially can arbitrarily deny access by claiming exceptional circumstances. In other words, there is negligible constitutional constraint on deliberative transparency, if any (cf. Dodge 1994; Heitsch 2003).

These vague constitutional provisions are reflective of a strong governmental preference against deliberative transparency (cf. Dodge 1994). The requirement for open Council meetings cannot have a discernible impact on because those votes mostly rubber-stamp decisions already made in COREPER and in informal discussions (Peterson and Shackleton 2006; esp. Hayes-Rehnshaw and Wallace 1997; Van Schendelen 1996). Making Council meetings public contributes little information about states’ true positions because bargains are struck long before the actual meetings, where consensus is the standard outcome, if a formal vote is taken at all.

Contrastingly, it took five years to pass Regulation 1049/2001 governing deliberative transparency (implementing TFEU Art. 15), whose content and adoption are a testimony to the value institutional players place on policy information, access to the legislative process and its overall transparency – or, rather, the lack of the latter. EU member-states had first asked the Commission to draft a report on improving public access to information on the work of the institutions in an addendum to the Maastricht Treaty of 1992. While Regulation 1049 took 10 years to pass, the entire Single Market legislation and accompanying treaty amendments were agreed by the member-states in less than half the time – between 1987 and 1991. Given that the Commission (at least publicly) and Parliament supported better disclosure, only two possible explanations exist for
this staggering fact: (1) member-states were not particularly enthusiastic about the regulation and (2) the issue was so important that member-states wanted the legislation to be precise in order to avoid any creative interpretation by other institutions, particularly by the ECJ.

The regulation itself follows very closely the letter and spirit of Art. 15 – in that it is essentially a statement of good intentions that allows arbitrary exemption of internal documents from disclosure. Tellingly, the regulation’s longest article is titled “Exceptions” and stipulates a variety of ways to render it irrelevant. For example:

Access to a document containing opinions for internal use as part of deliberations and preliminary consultations within the institution concerned shall be refused even after the decision has been taken if disclosure of the document would seriously undermine the institution’s decision-making process, unless there is an overriding public interest in disclosure. (European Union 2001, 45)

Of course, no clear criteria are set for the special circumstances allowing exceptions to disclosure rules. And, anyway, requesting EU documents or accessing publications on the Internet is always costly. The general public is much less likely to use this readily available resource than mobilized interests, which have gone to great lengths to establish their presence in Brussels (B. Wessels 2005; W. Wessels 1997).

The worthlessness of Regulation 1049 probably reflects even more the preferences of the Commission that drafted it than those of Council. The Commission’s secretive deliberative processes and expert groups, which draft and implement most legislation alongside Council representatives in the comitology, has been object of criticism much more than the intergovernmental smoked-filled
room that are Council negotiations (which practically never take place during official sittings of the chamber). To believe that the political appointees composing the College of Commissioners have a high degree of control over the permanent bureaucracy and the directorates-general (the EU equivalent of ministries) would be naïve at best – and potentially dangerous. Thus, there is a latent tension between the Commission, whose administrative apparatus has taken on a life of its own, and the member-states, which want to reassert their control but without compromising the secretiveness of their own institution – Council. Expanding Parliament’s budget and prerogatives is a shrewd way to create a counterweight and watchdog for the Commission’s growing clout without ticking off the lobbies that inhabit its corridors or allowing them more access to Council. Rather than hobble the Commission’s ability to develop and deploy policy expertise, they create a rival center of expertise (cf. Thomson and Torenvlied 2011 on the expert value of the Commission to Council). In a push to begin reining in the comitology, Council and Parliament passed Regulation 182/2011 that includes a requirement for detailed record-keeping of committee meetings and reports, but only makes the data available to the EP and CEU (European Union 2011, 17). EP representatives remain excluded from the comitology process, a longtime cause of frustration for MEPs and Regulation 182’s public-access rules are subordinated to Regulation 1049. In other words, public access to such these mandatory reports increases by just about zero. After much prodding by Parliament, the Commission produced a proposal for a new regulation in 2008, which “has received much criticism by the European Ombudsman, who believed that it would allow for access to fewer rather than more documents” (Augustyn and Monda 2011, 18).

Measuring the consequences of Regulation 1049 versus the status quo ante and comparing it to the legal systems of some European states, Heitsch (2003) finds that for the most part the regulation far from compensates for the ambiguity of
treaty Art. 15. According to him, Art. 16 of the regulation effectively contradicts the principle of transparency. Riemann’s (2004) discussion on the same subject not only reaches similar conclusions but also argues that the pro-forma improvements that the regulation introduced are carefully balanced out by an extra “weighing of interests” with respect to whether a particular document should be released (cf. Deckmyn 2002). That is, they effectively preserve the right to arbitrarily withhold information yet again. It should also be noted that the provisions would put under greater scrutiny the private information of Parliament and Commission, which would certainly benefit the ability of Council to monitor their activities – as well as that of member-states. In short, the loophole-ridden regulation is a “concession” on the part of Council that in practice allows it to keep sensitive information away from prying eyes, just as predicted. Member-states seem to have chosen the most advantageous balance of being able to monitor each other and EU institutions while preserving the opaqueness of much of Council’s own decision-making.

Council has systematically maintained the honored tradition of outsourcing most of its decision-making to COREPER and the underlying comitology, which is nearly impenetrable to any sort of outside scrutiny (Dinan 1994; Hayes-Rehnshaw and Wallace 1997; Jacobsson and Vifell 2003; Peterson and Shackleton 2006; Van Schendelen 1996). Council’s dominant form of policy-making is the Open Method of Coordination (OMC). The key here is that it is really “open” only to the member-states and their administrations, and by invitation only to other EU institutions which may be relevant to the topic at hand. Armstrong and Bulmer (1997) highlight the overwhelming importance of informal rules in the most institutionalized and supranationalized area of EU policy-making – the Single Market. The logic behind their idea is quite straightforward: if deliberation takes place in a long pipeline of hearings and reports, that increases the costs of acquiring any private information that decision-makers might have; looking for a
needle in a stack of hay is much less costly than looking in several stacks. Delegation to high-profile institutions such as the Commission is likely to draw the attention of interest groups and involves the cession of considerable decision-making authority because the Commission can rely on its powerful bureaucracies. Meanwhile, transferring the deliberative process down the line in informal meetings or in the Council’s functional committees provides much better cover. The ad-hoc committees operating under OMC are then an encumbrance of the decision-making structure as far as transparency is concerned because permanent committees still can have their say on the draft legislation (i.e., no decision-makers are effectively subtracted from the mechanism).

In sum, member-states have done little to increase the deliberative transparency of decision-making mechanisms in the Commission and Council. If anything, member-states have taken every step possible not just to preserve, but also to increase the structural costs of acquiring information. The only usable and functioning constraint is the infamous Regulation 1049, taking advantage of which is very costly and already has produced several ECJ suits. But it requires an amount of effort that remains too constraining without resources to invest in information gathering or sufficiently high stakes in a particular policy – the sort of characteristics that an influential lobby is much more likely to have than the general public.

Meanwhile, the inclusion of the EP by expanding the OLP’s domain increases lobbying costs without impinging on member-states’ private information. First, by adding a veto player to the process, OLP increases lobbyists’ monitoring and bargaining costs, potentially weakening their influence and resulting in better policy relative to less powerful groups. Even though the EP certainly is a target of lobbying, just like any governmental institution, its process is very different from the Commission’s, where lobbyists are directly embedded
in expert committees and bureaucrats rely on the revolving door for career advancement. Analyzing lobbyism in Denmark, Pedersen, Binderkrantz and Christiansen highlight interest groups’ privileged position as “existing, close and institutionalized relationships with political decision makers” (2014, 204). Even though the Danish open consultation procedures are very inclusive – unlike those of the Commission, – they still work on the initiative of the bureaucrats, and it is important to have a strong position in the political system to be alerted of or invited to an administrative consultation. In contrast, it is not necessary to be privileged in order to engage in the parliamentary arena (Pedersen, Binderkrantz and Christiansen 2014, 219). This dynamic, when amplified manifold, resembles closely what happens as legislation is tossed back and forth in informal bargaining between Parliament and the Commission.

Second, expanded OLP furnishes the dual scapegoat of Parliament itself and of increased public scrutiny if the EP takes an adversarial stand in the media, providing political cover for governments when they do not necessarily want to indulge lobbyists’ demands. The mechanism is clear: “politicians […] may exploit the existence of complex institutions and in-group biases to seek to attach credit to their own institutions and shift blame to other institutions” (Hobolt and Tilley 2013, 810). These two institutional changes increase the structural policy risk $\tilde{\sigma}$ in the model, triggering a move of equilibrium policy towards the optimum. Beyond a certain point, increases in deliberative transparency benefit only mobilized groups because they are the only ones that have the resources to make use of the improvement. In such conditions, the only way to disturb the informational balance favorably is to directly subsidize the information consumption of the less mobilized constituents so that they can force more balanced decisions. The EP is the only institution that can take that role within the EU’s policymaking
framework, as is clear from the foregoing analysis of decision-making and transparency preferences among the EU’s legislative actors.

Third, by wielding the power of the purse, Council has the option of using the EP as a decoy on a case-by-case basis – if there is genuine disagreement between the EP and the CEU, the latter can exert pressure in informal consultations not just to ensure passage but also to suppress amendments and public reports that cast the legislation in unfavorable light with the public. Thus, the EP subsidizes public knowledge of lawmaking \( h \), but only when there is tacit agreement between the member-states to allow that. This mechanism is supported by the intracameral organization of the EP, which has a very powerful presidency and committee system. This structural power is due not just to restrictive rules but particularly to the informal negotiations with the Commission and Council, where “the EP can be represented by the committee rapporteur, shadow rapporteurs, committee chairs, as well as political group leaders who can exercise party discipline in plenary” (Kardasheva 2013, 859). These gatekeepers are the points of contact with Council, thus pressure need not be exerted on Parliament as a whole or parties, pivots or majorities, but instead on individual committee members and rapporteurs. “Many proposal-stage coalitions form around policies that differ from the median-voter outcome” (Hix and Høyland 2013, 179) and “one member even claimed that ‘the rapporteur can theoretically decide to block legislation’” (Yoshinaka, McElroy and Bowler 2010, 462). This is where Council’s agenda-setting power under the OLP also comes in handy. If the rapporteur on a piece of legislation is incentivized just enough to produce an unimpressive report, it becomes exceedingly difficult to gather the absolute majority which is required by OLP to reject the legislation in the plenary vote (cf. Yoshinaka, McElroy and Bowler 2010), even if one takes place. Tellingly, “the committees are largely representative of national party delegations” (Hix and Høyland 2013, 183) and
those tend to be responsive to national parties rather than party groupings within the EP. Since national parties can exert substantial influence over MEPs’ careers, there is yet another convenient avenue whereby member-states’ governments can control Parliament’s actions.

Using a single institution such as the EP at the international level is certainly less costly than an additional chamber for each member-state’s parliament. In this way, states realize economies of scale in decreasing structural transparency. Meanwhile, the fact that the EP is a supranational institution, rather than intergovernmental, makes it much more difficult to blame a single member-state’s government or party for policy output. MEPs are uniquely positioned to be more resistant to lobbyism than national governments and the commissioners they appoint. The first reason for that is that EP elections tend to be proportional and highly uncompetitive – their results depend on the domestic popularity of the MEP’s party and are highly correlated with the results of domestic elections. The actions of the MEP in Parliament are thus divorced from the electoral process at home; with strict campaign-finance restrictions, fundraising is much less of a channel for influence by lobbyists than in the US, for example. Another structural problem is that a party that is a domestic opposition may be part of the plenary majority in a particular EP vote, giving even more credence to the political cover provided by Parliament. Finally, the issue of geographical remoteness should not be forgotten – Polish farmers’ access would be much less costly if the EP sat in Lodz instead of Strasbourg. All these problems are much more likely to constrain lobbyists than the general public simply because the general public was prohibitively cost-constrained even before the EP was empowered under OLP.

What is really dramatically different in terms of deliberative transparency between the EP and the other legislative institutions of the EU is that the EP’s proceedings are widely publicized by the EP itself and often by the media.
Committee meetings, reports and plenary sessions are for the most part open to public scrutiny. Indeed, Parliament does not have at its disposal the vast resources of the national or the Commission’s bureaucracies, but its members often are seasoned politicians with experience in policy-making and enough staff to be able to make trouble. The EP’s most powerful tool in this respect is not just its increased formal power under OLP, but the virtual megaphone lent to it by the media. MEPs can publicize details of proposed legislation and assessments of its impact in ways that the Council and the Commission may not be willing to or may be interested in suppressing. Meanwhile, the media have fairly unrestricted access to formal deliberations in committee or in the plenaries, which certainly does not make decisions less transparent. This channel of subsidizing the public’s awareness of a certain policy’s implications is, however, quite restrictive. MEPs cannot overuse it in trying to influence policy and can depend on it only when they can actually rely on being able to sway public opinion. Because they depend on national parties, not on electoral popularity, for their seats in Strasbourg, MEPs can leverage this tool more effectively against the commission than against the governments in Council. The conditional nature of MEPs’ media power becomes manifest in the case study in Subsection 1.5.3.

1.5.2. OTHER EXPLANATIONS OF EU SUPRANATIONAL INSTITUTIONS

In sum, the actions of Council and the Commission with respect to transparency legislation, their preferred legislative practices, the legislative outcomes (very few failed bills) and even the internal organization of Parliament are consistent with the informational theory. There is also indirect evidence that divided government may have a negative impact on lobbying efforts. Engstrom and Ewell (2010), for example, find that political contributions to members of dozens of US legislatures are strongly correlated with party government; party
misalignment between the (typically) bicameral legislature and the state executive leads to a decline in campaign donations. As becomes clear from the case analysis in the next subsection, the main source of public institutional conflict should be sought between the EP and the Commission rather than between Council and Parliament (cf. Aksoy 2012; Kardasheva 2013). Apart from sociological explanations (see Goetze and Rittberger 2010), there are a couple of alternative arguments for the empowerment of the EP that must be considered.

Neofunctionalism is the prevalent academic explanation for the expansion of the EU’s policy jurisdiction, but does not provide a compelling rationale for moving policy from the intergovernmental (Council) to the supranational arena (the EP). Neofunctionalists would suggest that the expansion of Parliament’s formal powers is a natural continuation of spillover effects in institutional integration elsewhere. The causal path for this argument, however, is tenuous at best. Even if there is demand for an institution that would help manage increasingly intricate and interconnected policy areas, the Commission already is the locus and main source of such transactional efficiency within the EU institutional framework (Thomson and Torenvlied 2011). It is hard to see how more integration would lead governments to create an institutional rival of the Commission under this causal mechanism (which does not imply or require competition and counterbalancing between the two).

Meanwhile, veto-player theory suggests a high cost for the empowerment of the EP, which makes the process even more puzzling from a traditional rational-choice viewpoint. The addition of the EP to the policymaking process may reduce EU lawmaking’s agility and effectiveness, which has not been enviable anyway (Garrett and Tsebelis 1996; 2001; Tsebelis et al. 2001; esp. Tsebelis and Money 1997). This implication reveals an inherent deficiency in veto-player theory, which does not typically take into account the internal structure and factionalization of
political institutions, thereby ignoring the dynamics of intracameral competition. Adding another veto player to the mix may force factions to compromise in order to present a united front against an incongruent chamber. Or factions, gatekeepers and agenda-setters can form alliances and logrolls across chambers, negating the mechanical (gridlocking) effects of adding more institutions to the chain of legislative approval. Such workarounds are by no means guaranteed, but they certainly are a possibility. Gehlbach and Malesky (2010) even argue that the addition of veto players may in fact speed up reform in the face of powerful interests. There is evidence that EU member states’ negotiators understand and take seriously the role of structure-induced bargaining power (McKibben 2013). Hence it is unlikely that they would engage in costly power-sharing without the expectation of some benefit, but veto-player theory does not make a compelling case for what that might be. The threat of increased EP committee hearings and reports, which are more likely to be publicized, may induce interested parties fearful of such publicity to compromise at earlier stages and speed up the process so that further scrutiny is avoided.

Using the EP as a commitment device is the only explanation for the expansion of its powers consistent with the veto-player approach: the member-states may rely on the EP as a mechanism to tie the hands of future Council members as well as their own hands in order to enforce long-term bargains (cf. Melo, Pereira and Werneck 2010). However, the commitment hypothesis does not square well with the empirical reality surrounding the EU’s legislative processes. First, the Commission is equipped much better to monitor compliance by member-states, enforce the treaties and keep Council bargains stable. Second, there is some evidence that Parliament was able to exert pressure even under consultation by threatening to block progress on co-decision legislation. By linking proposals from the two legislative procedures and requiring their simultaneous resolution, the EP
was able to negotiate package deals with Council including policy covered by the consultation procedure (Kardasheva 2013, 861). Furthermore, logrolling may not always be necessary for the EP to exert power under consultation. If the committee reviewing the proposal rejects it, the president may ask the Commission to withdraw the proposal, which would prevent Council from adopting it. A similar outcome is possible if the proposal (potentially as amended by the committee) is rejected in plenary. If rapporteurs and other gatekeepers could already act as tripwires for defections from Council bargains, why make things more complicated – and potentially unwieldy – by bringing the plenary into the mix through expansion of OLP?

According to Berliner (2014), transparency laws such as the US Freedom of Information Act are a method of protection against uncertainty about future political control in competitive political environments. He and Erlich (2015) find evidence that Mexican parties adopted state-level access-to-information laws more rapidly in more politically competitive states. In a similar vein, MEPs can act as fire-alarm oversight for member-states’ compliance with EU law, which could ultimately facilitate cooperation in Council. For example, opposition-party MEPs are seen as more likely to alert the Commission of their own governments’ infractions, which shifts enforcement conflict outside Council (Jensen, Proksch and Slapin 2013). But all of these enforcement mechanisms – targeting Commission bias or defection by individual member-states – had already been in place before the Lisbon Treaty, so why extend Parliament formal legislative power through OLP? The reasonable explanation is that while the EP was already acting on behalf of Council as a corrective for the Commission’s potential bias, the informal nature of that power did not provide Council and the member-states with political cover to act upon the EP’s signals given that the Commission is typically backed up by lobbyists with access to COREPER and the comitology under Council itself.
1.5.3. Case in Point: Regulating Vehicular Emissions of CO$_2$

Environmental legislation provides a telling case of the EP’s being the only institution that makes a serious effort to address the informational imbalances of decision-making – and the limitations of that effort. The first legislation adopted by the European Communities on the topic of car exhausts dates back to 1987 (Council Directive 220/70/EEC). Nevertheless, no formal caps on CO$_2$ emissions for new vehicles had been in place until 2009. In 1998, the car manufacturers’ lobby managed to derail major proposed legislation for mandatory caps on new-vehicle emissions by committing instead to voluntary targets of 140 g/km to be achieved by 2008, down from an average of over 180 g/km at the time. This is when the EP legislated on the topic for the first time (Directive 98/69/EC) and still under co-decision I. By late 2006, it was already becoming clear that, short of a miracle, the car manufacturers will not be able to meet their voluntary targets and emissions would average about 160 g/km for vehicles produced in 2008 (Mahony 2006). The shortfall was particularly large for German-based carmakers Volkswagen, BMW, Audi, Porsche and Mercedes (the latter with 188 g/km!), which tend to have more product lines based on powerful, fuel-hungry engines. By contrast, manufacturers of smaller and more economical cars such as Fiat and Citroën were about to hit very close to the target. In the aggregate, however, the situation seemed dismal – European statistics showed the EU was failing to reduce greenhouse-gas emissions to pre-1990 levels, the transport sector being by far the worst performer with emissions growth of nearly a third above 1990 levels by 2004. Further amendments to 220/70/EEC with mandatory emissions standards for vehicle manufacturing seemed necessary.

With the explicit backing of Commission President Barroso (Portugal), Environment Commissioner Stavros Dimas (Greece) quickly drafted amendments
to the Euro 5 and Euro 6 emissions schedules of Directive 220/70/EEC entering into force in 2008 and 2012 respectively with mandatory aggregate caps of 120 g/km to be introduced by 2012. The bill proposal promptly drew flak from industry commissioner Günter Verheugen (Germany) and the large-carmaker lobbies, who said that the suggested targets would be unsustainable and would result in massive layoffs (Mahony 2007). Interestingly, the German environment minister, Sigmar Gabriel, “told journalists he is surprised that Mr Verheugen is not ready to impose legal measures on the car industry”, taking Dimas’ side against Germany’s own commissioner (Beunderman and Spongenberg 2007). A few days later, Chancellor Merkel entered the fray publicly for the first time, saying that Germany will do everything possible to avoid the setting of aggregate targets and advocating instead different caps for different classes of vehicles (Spongenberg 2007a; 2007c) – a solution that would reduce the burden on German manufacturers.

On the very day after her statement – 31 January 2007 – the Commission officially submitted the bill on fuel-efficiency standards for refineries, which would tighten the caps on a variety of chemical pollutants, while rumors were already circulating that the delayed proposal on new-vehicle emissions caps had been increased to 130 g/km. The backstage power struggle regarding that cap apparently was already leaking into Parliament:

“Focussing on fuel quality alone to address emissions from road transport is like trying to quench a forest fire with a water pistol”, said green MEP Claude Turmes (Luxembourg). “By placing a disproportionate emphasis on fuel quality, the Commission is diverting attention from the real problem – the cars that use the fuel – and creating the illusion that fuel from plants is the panacea for our climate problems”, he pointed out. “Car manufacturers are trying to wriggle out of a target for CO2 emissions that they have agreed to a long time
ago and pass the buck on to others, like the fuel industry.” (Sponenberg 2007b)

When Commissioners Verheugen and Dimas jointly announced the bill proposal on 7 February 2007, the former appeared to have scored a clear victory – as had been leaked, the goal would be 130 g/km by 2012 without any specifics on whose directorate would make the draft and how the caps would be policed. The positions of the main political actors were further “clarified” two days later, when in an interview published in the German daily *Tageszeitung* Minister Sigmar Gabriel backed down from Germany’s opposition to the new legislation, burying it in the context of a number of concessions that Germany would agree upon within a large package of environmental legislation to be drafted by the Commission (Mahony 2007). Apparently, Christian-Democratic Chancellor Merkel had little intention to enter a tough fight on behalf of the automakers – she let her Social-Democratic minister of the environment make the concessions (and take the political fallout domestically), while she paid lip service to the position of Mr Verheugen (another German Social Democrat). The German chancellor had no reason to mount serious opposition in Council to tougher regulations because those would mostly affect supporters of her coalition partner and archrival SPD – labor unions in the German West (mostly former SPD strongholds, then controlled by provincial governments aligned with Ms Merkel), – while an SPD minister (Mr Gabriel) would be the one directly responsible for delivering the bad news. In late June 2007, the Council of Ministers approved unanimously Commissioner Dimas’ original goal of 120 g/km by 2012 (Kubosova 2007) while Minister Gabriel was now the one arguing for diversification between bigger and smaller cars.

After much haggling in the Commission and belligerence by Chancellor Merkel in the media, on 19 December 2007 the Commission finally produced the
bill (drafted by Mr Dimas’ directorate) with a baseline cap on engine emissions of 130 g/km and 120 g/km on final exhaust emissions of carbon dioxide by 2012 with fines of €20 growing to €95 in 2015 for every excess gram, whereat Mr Verheugen boycotted the press conference (BBC News 2007). The proposal was again unanimously approved by the Council of Ministers as presented by Commissioner Dimas several months later (despite that in the interim French and German representatives continued to spar in the media).

In this first stage of adopting the regulation, two facts stand out. First, the original bill proposal of the Commission reflected the car industry’s position. The toughest anti-regulation statements were made by Gunter Verheugen, the industry commissioner, not by the German government itself, whose representatives frequently spoke at odds with one another and appeared strangely out of sync. Verheugen opposed any binding standards and particularly the fines for excess emissions embedded in the proposal, while Chancellor Merkel mostly focused on relaxing the requirement through higher thresholds and averaging across smaller and larger vehicles – relative to environmentalists’ tough 95 g/km standard. The actual bill that reached Council (still under co-decision II) had moved away from Verheugen’s position after being bounced around through the comitology and, presumably, discussed with Parliament. An intergovernmental perspective stating that the process was simply a matter of strategic bargaining between Germany and other member-states (in this case, the southern bloc around France, whose car manufacturers would benefit from tougher standards, and the environmental bloc around Denmark) cannot explain why Verheugen and then the Commission together would take a position more in favor of the car lobbies than the German chancellor herself.

The legislation then went on its formal way through the committees of the European Parliament. Its first hurdle was the legal committee because
automakers’ lobbyists suggested the penalties constituted illegal EU taxes on car manufacturing. After promptly clearing this committee, the bill landed in the transport committee, which introduced amendments that would weaken the regulation by reducing the penalties. But on 26 September 2008 the environmental committee not only approved the Commission proposal in its original form, but also slapped on additional requirements that emissions be cut to 95 g/km by 2020. It is at this point that the draft legislation peaked in media popularity and even produced headline news in major European media outlets. The committee argued in simple terms that its amendments were necessary in order to produce a meaningful reduction in car emissions in view of the fact that car fleets would continue to grow. The bill was adopted in this form by Parliament to the delight of environmental lobbies such as Greenpeace (Phillips 2008c).

Their jubilation was short-lived. The car-emission amendment was attached to the environmental mega-package to be discussed at the yearend European Council. As the global economy headed down the drain and it became clear that the US government will aid its car manufacturers with billions of dollars, the car lobby quickly regained the upper hand. The conciliation committee of Council and Parliament agreed on 2 December 2008 not only on the initial German demand for a weight curve on the emission caps, but also on a more lenient schedule of fines for the first 3 grams of emissions above the target to be in effect until 2018. “As a result of the dilution of the law, emissions by 2012 [were projected to] climb to an average of 164.5 grams per kilometer, and by 2015, 139 grams per kilometer – a reduction of only two percent on [then] current levels according to some estimates” (Phillips 2008a). The conciliation bill did retain the 95 g/km cap to become effective in 2020, but without any specifics on how it would be enforced. This final draft was adopted by Council and Parliament, becoming Regulation 443/2009.
What does the fate of this bill say about the role of the Commission and Parliament in the legislative process? While the first draft was being put forward by the Commission, the manufacturers’ lobbies had a firm supporter in Commissioner Verheugen. A report published by the transparency group Alter-EU in March 2008 lined up the Commission’s climate-change panel among the most heavily influenced by industry, which was allocated 40 of the panel’s 60 members. Two months later Greenpeace alleged that the Commission’s CARS 21 workgroup that had “helped” draft the initial proposal by Commissioner Dimas had seven representatives of the car lobby against only one from an environmental NGO (Phillips 2008b). That proposal included a provision that would allow the carmakers to pool together for the purposes of meeting the aggregate requirements and did not include the long-term 95 g/km target suggested by Parliament’s Committee on the Environment, Public Health and Food Safety. This would result in royalties for more efficient manufacturers, not in emission reductions.

The German government was the most likely opponent of the legislation in Council. However, Chancellor Merkel only paid lip service to the matter until the European Council at the end of 2008 with two strategic objectives: (i) to make a later “concession” on the car-emissions problem to her partners in the European Council in return for diluting other emissions legislation in the environmental package since most of Germany’s electricity comes from combustion-driven power plants; and (ii) to channel the approval of the car-emissions caps through the environmental minister and have her rivals from the SPD take the fall for it in the next election, solidifying the ground gained by the CDU/CSU in the Rhine-basin provinces.

After September 2008, however, the situation changed dramatically. Now all member-states had genuine concerns about the fate of their car industries as
automobile sales plummeted in the wake of the financial crisis. On the other hand, the EP had become more concerned about the general environmental package meant to fulfil the EU’s Kyoto commitments for greenhouse gases. This also reflected a doubtless shift in public opinion from concern about the environment to worries about job security and the economy in general. What is surprising in these circumstances is not that the EP agreed to dilute the legislation, but that the bill survived at all – on top of that, with the 95 g/km commitment still in as a target for 2020. In sum, the presence of the EP in the decision-making process both publicized the issue and provided much more information about it through various committee reports, but also introduced amendments that auto-industry lobbyists had managed to prevent in the Commission’s original proposal and which were strongly supported by public opinion in the member-states. This reliance on the media to draw attention to the issue and distribute information about it proved to be a double-edged sword – as soon as the attention of the public and the media was drawn by the mounting economic woes in the global economy, the capacity of the EP to resist the lobbies dominating Council and Commission dissipated along with public support.

The same dance took place five years later during the next installment of the CO₂ saga. Because the 95 g/km target did not have an enforcement mechanism (the regulation only included fines for the more lenient targets in years until 2020), new-vehicle emissions came up again during general climate policy negotiations in 2012. Germany, led by Angela Merkel, appeared yet again to be attempting to weaken the regulation further, with media coverage painting her as the angel of German carmakers:

European Union environment ministers agreed to German demands to scrap an agreement to cap average EU new-car emissions at 95 grams per kilometer
in 2020 from about 130 g/km now after Berlin argued the target would cost jobs and damage its premium automakers.

After months of forceful lobbying from Germany, the ministers from the 28 EU member states agreed […] to reopen a deal [whereby] EU governments and the European Parliament had agreed in June [2013] a 95g/km target. (Reuters 2013)

Angela Merkel’s government is no longer supportive of the agreement, and a number of green groups said she was under heavy pressure from some German automakers worried that they could not meet the 2020 target[.] A German proposal would delay full implementation of the standard until 2024, but it would need approval from multiple European bodies. [emphasis added] (Motavalli 2013)

On 25 February the following year, the EP passed with 499 votes in favor the amendments to the regulation… with the original 95 g/km standard and substantial penalties for noncompliant manufacturers. The “concession” to the automakers was a one-year phase-in and allowing them to count their cleanest cars for more than the others, but only through 2022, neither of which provisions does much to help luxury and guzzler manufacturers such as BMW and Mercedes. More fascinating than the tough standards are the new procedural rules which take up much of the regulation. While enforcement legislation is delegated to the Commission, it is put on a tight leash, a new Art. 14a stipulating that the delegation can be revoked unilaterally by either Council or Parliament. EP amendments also mandated that the Commission begin a study of emissions measurement methodologies with an eye on imposing tougher standards (European Union 2014). Council unanimously approved what was to become Regulation 333/2014 about two weeks later.

The same general scenario seems to have been played both times. First, governments made a tentative deal amongst themselves and asked the
Commission to draft legislation. The Commission produced a bill proposal that was not consistent with the Council’s bargaining agreement but served lobbyists’ agenda instead. German politicians in Council postured as champions of the luxury carmakers in their country and appeared to gain the upper hand in negotiations with other member-states. The EP “intervened” by adopting a bill that went even further than the Council’s initial intention to cut emissions and more strongly against the lobbyists. Council and Parliament then “compromised” on final language which was by and large consistent with the initial intergovernmental bargain and Council’s original intent.

1.6. DISCUSSION

This chapter has presented an alternative – and complementary – explanation for the supranationalization of the EU. Previous theory had identified economies of scale and scope as the primary reason for states to cooperate and integrate (Bolton, Roland and Spolaore 1996; Fearon 1998; Gruber 2000; Harrop 1992; Henning 1998). The current model has shown that supranational institutions can be a valuable tool for domestic redistribution – more specifically, for attenuating the impact of mobilized interest groups on policy-making. This logic also provides a rational explanation of why the member-states of the EU chose to increase the formal legislative authority of the EP. Member-state governments’ strategic action of empowering the EP under the ever-expanding OLP are typically cast as a puzzling loss of Council power. As the analysis demonstrates, Parliament’s gains are in fact at the expense of the Commission and the lobbyists straddling its expert panels and Council’s comitology.

The EP does emerge a critical player, but rather in its role of political cover for the member-states and as a check on the Commission than through its formal
legislative powers. At the macro-level, the EP is an additional veto point in policy-making that reduces the likelihood of policy skewing towards lobbies, but arguably this can be considered a rather low hurdle given the lobbyist infestation of the EP’s own halls. Parliament’s more important function is carried out at the micro-level, where it helps reduce the informational imbalance between more and less powerful lobbies, if not necessarily by increasing EU institutional transparency itself, and by subsidizing the information consumption of less resourceful constituencies.

Thus, reducing structural transparency may be a means of inducing normatively desirable outcomes consistent with the goals of democratic governance and the welfare state. The model shows that political leaders have strong incentives to seek cover from powerful domestic interest groups, whose pressure distorts policy away from social optima. But open institutions such as the EP also alleviate distortions by supplying free, pre-digested information to the public, so that outsourcing decisions to Parliament allows governments to gain political cover against powerful lobbies.

This oblique role of the EP is particularly jarring in the context of traditional views of democratic representation because MEPs largely bear no electoral responsibility for their activities (Hix and Høyland 2013). The evidence in the literature seems to support the view that the improved representativeness arises from institutional and elite competition: MEPs are motivated to produce good policy by individual career goals or by a desire to increase Parliament’s power, largely at the expense of the Commission, while Council uses parliamentary scrutiny both as an alarm bell for moral hazard in the Commission and as a decoy against powerful domestic and multinational interests.

The formal model suggests that the structural veil of secrecy thrown against disproportionately powerful interest groups helps alleviate problems of domestic
welfare distribution and increases aggregate wealth. Indeed, these conclusions should not be taken in the extreme because they are based on certain assumptions about the motivation of political leaders, domestic preferences and the distribution of political influence. Nevertheless, the model reveals that institutional transparency should only be viewed as a means to an end, not as an end in itself. The blind pursuit of political transparency is likely to reinforce some distortions of policy-making pursuant to imbalances in domestic politics and the collective-action problems inherent in social choice. Naurin’s (2007) comparative study presents empirical evidence that more transparency with respect to lobbyists harms the decision-making process. As the current model shows, absolute transparency provides an opportunity for disproportionately mobilized groups to pursue their interests at the expense of social welfare and equity. This is hardly the goal of representative democracy and even less so in the context of European politics.

Instead, a focus on the quality of decision-makers may be more appropriate. As Hix and Høyland (2013) assert, MEPs with different backgrounds and motivations perform differently. Hobolt and Høyland (2011) suggest that MEPs with national experience tend to receive more votes in elections than do Brussels careerists or inexperienced national politicians looking to jump back to national office. This sort of career differentiation also appears to drive plenary absenteeism, committee appointments and MEPs’ being chosen as rapporteurs (Yoshinaka, McElroy and Bowler 2010), among other performance metrics within Parliament. In other words, even when the electoral link is weak, the quest for power within the EP itself and vis-à-vis other EU institutions can be motivating enough to improve the quality of legislation and engender an institution that is a counterweight to special interests, at least in comparison to the Commission. Elite competition appears to spur better policy in unexpected ways and largely in the
absence of electoral control, particularly of the spatial variety. Chapter 2 delves deeper into the agency problem to explore the implications of this insight for political theory and representation far beyond the institutional and geographical limits of the EU.
Chapter 2
From Strategic Agency to a Political-Capital Theory of Democracy

“All was not flux; final outcomes were not arbitrary.”
– Kenneth Shepsle\textsuperscript{10}

“The need for certainty is the greatest disease the mind faces.”
– Robert Greene\textsuperscript{11}

Chapter 1 identified an interesting case where, despite a weak electoral connection between MEPs and their constituents, the European Parliament has come to play an important role in advancing public rather than special interests. This chapter lays out a more general substantive and formal agency theory in order to seek an explanation for this unexpected phenomenon. As the following introductory section demonstrates, delegation theory has long been integral to the study of political institutions and rational-choice approaches to representation have been focused on the (s)electoral connection as a method of ensuring that agents’ actions are aligned with principals’ interests. Section 2.2 provides a brief summary of some of the formal methods available and of the substantive core of agency theory contextualized within the broader themes of political economy and representation. Section 2.3 proposes a commonsense notion of strategic rationality

\textsuperscript{10} Shepsle 1989, 136.

\textsuperscript{11} Greene 2012, V.
and a rational equilibrium concept consistent with that notion and institutional stability as a basis for developing a formal theory wherein formal methods are logically consistent with the substantive questions at hand. With these tools, Section 2.4 lays out several delegation games eschewing domain-restrictive assumptions as possible in order to provide a most general set of results about selection, sanctioning and bimodal approaches to understanding agent control. The analysis generally confirms and strengthens earlier findings that selection dominates sanctioning as a method of inducing compliance in non-cooperative agency games; moreover, sanctioning alone is not an institutionally stable way of delegation, paradoxically because of principals’ inability to commit to punishing bad behavior under general conditions. In mixed settings, the impact of outcome transparency on compliance levels is entirely contingent on the properties of the pool of potential agents. The implication is that the composition of the set of candidate agents will dominate the attainment of normative goals such as representation and policy responsiveness and, therefore, elite competition may be a more fruitful perspective to understanding those linkages than institutional transparency or electoral control. Section 2.5 briefly summarizes the ramifications of this insight for several prominent research programs in the discipline: parties and elections, party government, majoritarian versus consociational visions of democracy, and differences between presidential and parliamentary systems. Section 6 takes the perspective of competitive democracy further to motivate a solution to a lasting theoretical puzzle: what makes some democratic transitions succeed and others fail. The role of (undemocratic) competitive political institutions is revealed as the missing link in achieving stable democracy and forms the basis of a political-capital theory of democratization. Section 7 concludes with a roundup of the theoretical and methodological questions addressed and the implications for future research.
2.1. INTRODUCTION

The institutional framework surrounding the European Parliament presents a starkly counterintuitive case of democracy without much representation. As Chapter 1 suggested both theoretically and substantively, the empowerment of the EP may be an effective improvement of policy in aligning it better with the public interest, but not because of the electoral connection between its members and the general public in the member states. Instead, Parliament’s power – to the extent that it exists – turns out to be based on elite and institutional competition. The expansion of the EP’s prerogatives diminishes the clarity of responsibility in the policymaking of the EU and makes it easier for the political elites within the member states to pass policy that is less congruent with the interests of powerful lobbies representing other elites.

This finding brings into question two dominant paradigms about conceptualizing and studying democratic political institutions – that more transparency and clarity of responsibility is always unequivocally a boon for better policy and that the delegation channel from voter to political officeholder is what drives effective representation. It becomes necessary to reexamine the theoretical validity of these precepts in order to identify the general conditions under which they should hold and the circumstances that favor the types of mechanisms that are at work in EU policymaking. In particular, it is important to reconcile the traditional channel of electoral control with the dynamics of elite competition that appear to be driving much of responsiveness in the EU case. Is there a more global relationship between them? To answer this query, Chapter 2 deploys a new formal framework to revisit the issues of delegation and control.

Politics is an indispensable part of human life not merely because, like any other animal species, people compete with one another, but because the
advantages of human intellect become distinctly formidable in collaboration. Working together is arduous, especially in conditions of uncertainty, and a special toolset is needed to make it possible. This chapter motivates the concept of strategic rationality, which captures effectively that common ability to anticipate and counteract potentialities as well as tangible events; it recognizes explicitly that rational actors can generate models of the entire interaction as well as others’ strategies. Coupled with rational equilibrium, a refinement on sequential equilibrium that ensures effective coordination of strategies in non-cooperative environments, strategic rationality is a robust vantage point for analyzing principal-agent relationships. A general model of delegation rooted in this framework suggests that a change of perspective may be long overdue in several important research programs in the discipline, including electoral politics, democratization and comparative political economy.

Selection and sanctioning are the established theoretical mechanisms for understanding the principal-agent relationship, two phenomena fundamental to new institutionalism, its rational-choice subspecies and socioeconomic theory more broadly. Both markets and firms are plagued by problems of moral hazard and adverse selection, which stem from asymmetric – and often nonexistent – information (cf. Przeworski et al. 2000; Olson 1993). While political organization and governmental institutions alleviate these problems to some extent, government itself becomes infested therewith (Falaschetti and Miller 2001). Madison’s dilemma (Federalist Papers 51) provides a concise summary of that conundrum at its pinnacle – once society has constituted a government, the former must make sure that the latter does not turn against it; principals must create mechanisms that prevent agents from reneging on their fiduciary duties by
succeeding to special interests, including their own (cf. Lupia and McCubbins 1998; Shugart 2005).12

This intuition was implicitly present in the earliest examples of rational-choice theory in the discipline, which were oriented towards electoral politics (Downs 1957; Riker and Ordeshook 1968). Particularly in the context of representative democracy, elections are typically regarded as the crucial delegation mechanism in a polity. But principal-agent relationships span much further afield across and within political institutions: delegation extends from legislatures to their own committees (Cox and McCubbins 2005; Weingast and Marshall 1988; Hedlund et al. 2009; Wielen 2010), to bureaucracies (Kiewiet and McCubbins 1991; Huber and Shipan 2002; McGrath 2013; McCubbins and Schwartz 1984) and to executives (Carroll and Cox 2012; Martin and Vanberg 2005; Laver and Shepsle 1990; 1994; 1996); from legislative parties to their members (Hedlund et al. 2009; Cox and McCubbins 2005; Rohde 1991; Weingast and Marshall 1988) and ministers (Kam et al. 2010); from backbenchers to party leaders (Ramseyer and Rosenbluth 1993); and from executives to their cabinet members (Martínez-Gallardo and Schleiter 2015; Indridason and Kam 2008; Martin and Vanberg 2005; Martin 2004; Matthews and Valen 1999; Laver and Shepsle 1994), to legislative parties and coalitions (Cox 1987; Ramseyer and Rosenbluth 1993; Hiroi and Renno 2014), and to bureaucrats (Huber and Lupia 2001).

In research and in reality alike, metaphorical arrows of delegation shoot in almost every conceivable direction. This preponderance of the principal-agent schema makes it all the more jarring that there is little consensus on what it ought to encompass, substantively and methodologically. “While principal-agent theory

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12 This conceptualization was gaining some prominence in the early 21st century – e.g., Carroll and Shugart’s (2007) “neo-Madisonian” framework of analysis.
is often invoked heuristically in research, there are only a handful of studies that rigorously apply the theory within the discipline” (Rauchhaus 2009, 873). The historical reason for this state of affairs is perhaps that rational-choice institutionalism emerged as response to the instability of preference aggregation in multiple dimensions that engendered the end of “pure” rational choice (McKelvey 1976). Instead of reexamining the concepts and assumptions that underlay that result, the rational-choice movement saw an easy solution in adopting the view that exogenous institutions set the agenda. But if institutions sort out the preference-aggregation problem, how do rational actors agree on a set of institutions in the first place? This is perhaps the defining chicken-and-egg problem of rational-choice institutionalism, but only one of many unresolved issues it inherited from its public-choice predecessors.

What distinguishes institutions from “mere” behaviors is that they engender repeated and predictable action that affords self-interested actors substantial mental economies in their individual decision-making and helps resolve coordination problems. In a world in flux, institutions conjure (the illusion of) stability and predictability. In light of this essential feature of institutions, formal rational-choice models of institutionalized delegation ought to utilize solution concepts that exclude predictable unpredictability. If a solution concept permits multiple equilibria with widely divergent strategies and outcomes, it is hard to justify applying it in a substantive context whose defining characteristic is consistency. Even objectively dysfunctional institutions tend to be consistently so. The following section contextualizes existing formal methods for the purposes of studying political agency in order to identify any refinements necessary to meet a standard of consistency between subject and method. These methodological concerns include not only solution concepts, but also the way that substantive questions can be framed, hence the discussion comes in two parts.
2.2. Questions of Research and Methodology

In the interest of brevity and generality, the analysis hereafter focuses on principal-agent relationships in the context of elections. A basic formal framework developed by Fearon (1999) to analyze electoral behavior is emblematic of, if not directly invoked by, contemporary rational-choice approaches to the agency problem in the discipline. This model is a handy example of some of the formal-theoretic and the framing issues that have dominated the literature.

2.2.1. formal methodologies and agency theory

Fearon presents three games – a case of selection, a case of sanctioning and a case of both – and uses von Neumann and Morgenstern’s (1944) Nash equilibrium (NE), the first solution concept in game theory, as a basis of his substantive discussion. As often happens with NE, however, Fearon’s games have multiple equilibria, not just the relatively benign one he focuses on. While there is an equilibrium where selection and/or sanctioning may work, there is also a legitimate NE in which agents just follow their own preferences. The arbitrariness of choosing one of these solutions over another is less than appealing and thus conflicts with methodological standard set forth in Section 2.1. Arguing that a non-unique equilibrium, often with radically different sister equilibria, is the appropriate solution to a game naturally raises the question as to whether a truly rational person would partake in institutions that induce such unpredictable outcomes and do not ameliorate coordination problems. Another fundamental issue with NE and many of its refinements is that they do not ensure players can implicitly coordinate strategies – so that best responses match – where information is scarce. If an institution does not provide a credible reduction in behavioral uncertainty, particularly in non-cooperative settings such as electoral representation, then how is it sustainable and not redundant?
Game theorists have made many attempts to develop more robust solution concepts that are not just theoretically elegant, but stand the scrutiny of similar commonsense critiques. One set of solutions was motivated by equilibrium perfection and stability – ensuring that there are no dominated strategies in the equilibrium set and that it is robust to induction. An important advancement in this line of research is Harsanyi’s (1967; 1968) perfect Bayesian equilibrium (PBE), which allows games of incomplete information about players’ types (i.e., their utility functions or other relevant characteristics). Its critical innovation is that it takes into account both a mixed strategy $\pi$ and a belief system $\mu$, which together are called an assessment $(\mu, \pi)$. In a PBE, “[t]he strategy of each player starting from each information set must be optimal starting from there according to some assessment over the nodes in the information set and the strategies of everyone else” (Kreps and Wilson 1982, 871). But even though PBE does take into account some of the beliefs of the players, it is still insufficiently robust because it often results in illogical and implausible results, as equilibrium solutions are not always sequentially sustainable at all decision nodes.

The consistency of beliefs (alongside strategies) has persisted as a central theme in subsequent refinements and even helped motivate the other school of thought, which emerged from the work of Bernheim (1984) and Pearce (1984). Considering perfection concepts too restrictive in some cases – i.e., potentially ruling out plausible actions, – they introduced the concept of rationalizability, “as

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13 Interestingly, among the solution concepts that gained in popularity in the early 21st century are Markov perfect equilibrium and quantal response equilibrium, which are not robust and may even be weaker than NE, depending on certain parameters.

14 See Kreps and Wilson 1982, 871, for a formal definition of $\mu$ and other terms not expressly defined here.
the logical consequence of assuming that the structure of the game and the
rationality of the players (and nothing more) is common knowledge”
(Brandenburger and Dekel 1987, 1391). The big substantive advancement made by
this line of research is that it puts center-stage the problem of coordination
between players operating in conditions of imperfect and incomplete information.

Concept refinements based on perfection or rationalizability included some
mix of these desirable properties, but none has emerged that combines them all
while preserving a tractable, practical solution formulation that would be
appropriate in a political-institutional context. While Kreps and Wilson’s (1982)
sequential equilibrium sought to restrict solutions to assessments robust to
backward induction, Köhlberg and Mertens (1986) showed that, for example,
sequential equilibrium is not sufficient to guarantee solutions that survive the
elimination of weakly dominated strategies and are “stable” to trivial changes in
the extended-form tree of the game. Mertens (1989; 1991) went on to develop a
formal definition of their proposed stable equilibrium, but it is not a concept that is
intuitively appealing or sufficiently practicable. Aumann’s (1987) correlated
equilibrium attempted to reconcile Bayesian-probabilistic with complete-
information approaches such as NE, but did not ensure perfection. Meanwhile,
Brandenburger and Dekel (1987) developed a posteriori equilibrium seeking a point
of convergence between the perfection and rationalizability approaches, but theirs
also did not guarantee robustness to backward induction and coordination issues,
both of which are central to the substantive questions for institutional research.

Apart from being reasonably convenient to determine, an effective solution
concept in the context of institutions must meet some commonsense criteria:

(i) ensure that players cannot improve their payoffs by deviating from
the equilibrium (perfection);
(ii) mandate that in games of incomplete and imperfect information coordination issues are resolved (stability); and

(iii) accommodate player errors by specifying rational strategies in dominated branches of the game, but not at the expense of being overly restrictive (rationality).

To address these methodological requirements, the next section develops a solution concept, *(strategically) rational equilibrium* (RE), which is a refinement on the concept of sequential equilibrium (Kreps and Wilson 1982) and which draws on the more sophisticated belief properties of *self-confirming equilibrium* (Fudenberg and Levine 1993). Sequential equilibrium requires that each assessment be sequentially rational — i.e., that the beliefs of players are derived using Bayes’ rule from their strategies and that no player wants to change strategy given the ensuing beliefs. Figuratively, the strategies have to be best responses not just to each other but to the beliefs as well in every information set (decision stage) of the game. Self-confirming equilibrium further assumes that players have knowledge of the structure of the game and therefore their beliefs have to be mutually consistent, but relaxes some perfection conditions. Using that assumption, the equilibrium concept proposed here adopts a more restrictive approach along the equilibrium-relevant portions of the game, but relaxes some limitations on unreachable branches to accommodate player “mistakes” and ensure solution completeness.

2.2.2. Interpretations of the Agency Problem within the Discipline

The structure of the RE solution concept is motivated by the idea that institutions must solve some collective-action problem for the players — i.e., that any radically different or erratic equilibrium strategies do not make sense and that coordination and aggregation problems are (at least) mitigated. These concerns are
recurrent features of principal-agent analysis within rational-choice institutionalism. There are two established ways to construe the agency relationship: as a mandate to implement a specified menu of policies and as a trusteeship wherein the agent is expected to act in the best interests of the principal without any restrictions on the means to that end. At first sight, it appears that sanctioning bad behavior and selecting good agents, correspondingly, are the appropriate mechanisms for a principal to achieve good outcomes within each one of these perspectives. Both of those mechanisms also seem to require some level of information about (the actions of) the agents.

The problems associated with agency are typically ascribed one of three categories: moral hazard, adverse selection or both. Moral hazard is present when agents cannot commit credibly due to lack of enforcement or transparency of their actions. Electoral democracy is the preeminent case of lack of enforcement – elected officials’ actions cannot be restricted except by the shadow of the next election or, in rare cases, by the threat of impeachment. Criminal prosecutions are rare and often constitutionally restricted or prohibited altogether. The appointed bureaucracies and “independent” agencies that operate under the layers of elected leadership are the paragon of lack of transparency. Although punishments there can be dispensed more readily, their actions and intentions are not easy to monitor, whether because of their sheer number or their much higher level of information and expertise about their area of specialization. A similar dynamic builds in corporations and other institutions – while shareholders may occasionally manage to bring down a senior executive or board member, it is rare that middle managers would be punished by shareholder or even board decision.

Adverse selection occurs in pluralist and competitive institutional contexts. It is rooted in two logical conjectures. Agents with the least skill and good faith are more likely to make recklessly attractive promises to the principals. At any rate,
agents always have an incentive to misrepresent their beliefs and intentions because their goals may not be the same as the principals’. This tendency is reinforced by the competitiveness of the (s)election process, where reasonable and sincere agents are quickly weeded out of the pool of electable candidates. This phenomenon is most acutely expressed in the electoral politics of crisis, where the panicked principals are most willing to throw caution to the wind and entrust high office to people who would never have stood a chance even in moderately improving circumstances (e.g., the rise of far-right parties in Weimar Germany in and post-Soviet Europe).

Even when considered only in the abstract, the issues of moral hazard and adverse selection seem to be deeply intertwined. However, there is a critical distinction in the way they tend to be interpreted and to unravel in reality. Moral hazard involves the actions of elected officials while they are holding the reins of power: Is the incumbent agent faithfully executing the will of the principal? Adverse selection concerns the traits and attitudes of candidates for office: Does the candidate have the right skill set and priorities to be an effective agent of the principal’s will? This dichotomy has not been without some prominence in the study of representation, particularly in the representational conceptualizations of trusteeship versus mandates. But in either perspective, the information available to the principals has been viewed as the critical determinant of their ability to achieve instrumental or normative goals.

The beliefs, identities and general knowledge of voters about politics and politicians have been defining research questions not just for rational-choice theory but for the discipline at large, from the earliest attempts to grapple with the issues of party identity, voting and representation (e.g., Campbell et al. 1960; Mayhew 1974) to later work on the attitudes and involvement of the electorate in the political process (e.g., Zaller 1992; Matthews and Valen 1999). Scholarship has
gravitated around two focal points. On the empirical end, it is a fairly widely accepted fact that, whatsoever the rationale therefor may be, the vast majority of eligible voters are very poorly informed (in terms of specifics) about the activities of their elected representatives. Meanwhile, theorists have contended that selection is a stronger and more widely utilized delegation mechanism than sanctioning (Fearon 1999), even though some authors have argued that sanctioning may be more widely used under presidentialism (e.g., Strøm 2006). The main point of debate is whether their aggregate perceptions of performance, particularly as it relates to the economy, are accurate in some systematic way, even if not always (Duch and Stevenson 2011). The evidence generally points to the conclusion that the electorate is more effective at formulating adequate attitudes and/or punishing bad performance when the policymaking process is more transparent – there are fewer veto players, coalition partners, independent branches of government involved etc. (Powell and Whitten 1993; Duch and Stevenson 2008; Nadeau, Lewis-Beck and Bélanger 2012). In the face of all this evidence to the contrary, transparency is still commonly viewed as a distinguishing feature of democracy (Lupia and McCubbins 1998; Hollyer, Rosendorff, and Vreeland 2011) because of its role as a facilitator of sanctioning and, in most studies, there is a latent presumption that more transparency would result in better representation and performance, a position which Chapter 1 addressed at length.

When studying the impact of this clarity of responsibility on voting behavior, it is common to conceive of the latter mostly in retrospective terms (e.g., Fiorina 1981; Ferejohn 1986; Lewis-Beck 1990; Duch and Stevenson 2008). Forward-looking models have also mostly focused on the electoral rather than the policy outcome (e.g., Downs 1957; Cox 1997), which, with the benefit of hindsight, suggested even in the heyday of spatial-voting theory that valence may instead
account for most of the electoral calculus. Policy-motivated voting is a subject which the relevant research expends little effort on and later authors find even less evidence for (Campbell et al. 1960; Zaller 1992; Edlin, Gelman and Kaplan 2007; cf. Popkin 1994).

Meanwhile, few studies address directly the effectiveness of these mechanisms in terms of representation and policy outcomes, although there are some signs that a new literature on this issue could be emerging (e.g., Duch, May and Armstrong 2010; Indridason 2011; Dewan and Myatt 2012). A similar stasis has developed in the subfield of bureaucratic accountability, where, perhaps due to endemic measurement challenges, scholarship has found it hard to move from the question of what the commonly employed methods of control are – e.g., hearings, appointments and the specificity of legislation – to the more significant question of when and to what extent those methods work to achieve instrumental or normative goals (Clinton et al. 2012; MacDonald 2010).

2.3. RATIONAL EQUILIBRIUM IN NON-COOPERATIVE GAMES

To address the agency problem underpinning these literatures, this section introduces a definition of strategic rationality and develops an equilibrium concept consistent therewith and the substantive requirements of institutional research. While seldom made explicit, the idea that theoretical rigor requires that the solution concept employed be logically as consistent as possible with the nature of the problem itself and the specific model applied thereto is far from novel (e.g., Granato, Lo and Wong 2010). This vital criterion of coherence between subject, theory and method has eluded much of previous research, as many narrow constraints on utilities, outcome probabilities and other aspects of formal models have been transplanted from economics. Fearon (1999), for example,
adopts a very narrow view with a unidimensional spatial utility function and somewhat naïve agents, which undermines the generalizability of his results. To build a less domain-restricted model, it is necessary first to outline a commonsense definition of strategic rationality and then build a formal solution concept that can work effectively with it, while ensuring the relative stability of outcomes.

2.3.1. Strategic Rationality

When talking about rational choice in game-theoretic terms, the focus is typically on the players’ preference structure. To the extent that there is any meaningful debate on this point, it concerns semantic issues such as whether the notion of preferences should be constrained to “tangible” outcomes (e.g., policy payoffs, office rents, monetary transfers) or extend to “warm and fuzzy” psychological considerations (Blais 2000; Edlin, Gelman and Kaplan 2007; Fowler 2006). Or it focuses on theoretical abstractions such as transitivity, which are consistently disconfirmed by empirical evidence and, indeed, everyday experience. In reality, a person who prefers (both in “sincere” and “revealed” terms) apples to pears to grapes to apples is seldom considered irrational. Someone who lends a large sum of money to a perfect stranger, however, could easily fall into that category. What lies behind these everyday intuitions is that the concept of rationality comes to mind not so much in individual behavior – in some atomistic sense – but most commonly in the context of strategic interaction, i.e., situations where several sentient beings engage in economic exchange, in the broadest sense of that term. Perhaps the most widely accepted precondition for rationality is that the subject be self-interested and act in a manner consistent therewith. Ironically, neuropsychologists and philosophers have conjectured that the very self and, consequently, the notion of self-interest arises in social
interaction and an evolutionary imperative to communicate *strategically* with other intelligent individuals (Bruner 1981; Dennett 1987; Pinker 2002; J. Hawkins 2004).

What is an accepted fact is that an indispensable component of selfhood is the “theory of mind” – the ability to make predictions of other selves’ behavior. “Reasoned choice does not require full information; rather, it requires the ability to predict the consequences of actions” (Lupia and McCubbins 1998, 4; cf. Dennett 1987; 1991; Hawkins 2004). Some studies suggest that conditions such as Asperger’s and autism may be related to neurobiological impairments which preclude the individual’s forming expectations about others’ beliefs and intents despite that he or she is perfectly aware of their independent selfhood (Baron-Cohen et al. 1999; Castelli et al. 2002). It is easy to see how autistic behavior can be interpreted as “irrational” and why modelers should not ignore this strategic capacity. The combination of selfhood and theory of mind has proven to be so effective evolutionarily that people are even prone to attributing this “intentional stance” to inanimate objects and phenomena when at a loss about how to make strategic predictions about their behavior (Dennett 1987). Thus, the first desirable property of rationality and of a rational solution concept is that it should be consistent with actors’ (or “players’”) understanding that others are (a) likely to act in a strategic way, including by (b) predicting their own actions.

Common knowledge, and especially the ability to infer it autonomously from a situation, is a defining characteristic that makes these faculties valuable in the context of human interaction (Lewis 1969; cf. Lupia and McCubbins 1998). This is an oft-overlooked element of games. The common knowledge involved in the interaction is essential to predicting other actors’ behavior and strategic choice cannot be effective without it. For example, adequate strategic response necessitates common knowledge of the rationality of other players – i.e., player A knows that player B is rational, player B knows that player A knows and so on ad
infinitum. Because such common knowledge is usually assumed only implicitly, its strategic ramifications are rarely discussed and often omitted, which undermines the credibility (and sometimes the accuracy) of the results. To avoid any pitfalls, the second desirable property must then be that rationality itself is common knowledge (cf. Fudenberg and Levine 1993).

Moreover, it is reasonable to expect that players have common knowledge not only of each other but of the general structure of the game – or, at a minimum, that they may be able to derive such knowledge as the game progresses. That a rational player should be able to use observed behavior not just to estimate the information set of the current decision node automatically presupposes at least some knowledge of the structure of the game and the other players involved – or “meta-knowledge.” Taken together, these ideas form the core motivation for the rationalizability literature (Brandenburger and Dekel 1987, 1391–1392) and a set of characteristics essential to a definition of rational actors as well as self-confirming equilibrium (Fudenberg and Levine 1993).

The ability to model is perhaps the most fundamental distinction between human minds and other animal minds. Human brains are not limited to simply reproducing evolutionarily embedded scenarios or socially transmitted reaction paths; they can build simulations of situations and play out different actions in those contexts, trying to predict the results without always taking the risks and incurring the costs of learning by doing. A critical component of this mechanism is that people are not only cognizant of the characteristics of a situation they find themselves in, but that they can be aware that they are in a situation. The ability to access this state of observational detachment and situational meta-understanding is critical to unleashing the full potential of one’s mind to achieve desirable outcomes and, indeed, to pinpoint what the desirable outcomes really are in the first place.
**Definition 2.1. (Strategic Rationality)** Rational actors can reason strategically to predict the actions and reasoning of others, see other rational actors as such and as cognizant of the structural setting of a strategic interaction, and all of this is common knowledge.

One very prominent example of a very useful solution concept which is not strategically rational is evolutionary equilibrium. If a sufficiently large population (or “type” of player) adopts an evolutionarily stable strategy (ESS), it cannot be invaded (and replaced) by a population with an alternative strategy. The essential understanding here is that the population is defined by the strategy itself more so than by any other aspect of the game (such as the information structure). In other words, the strategy space of each type of player consists of a single strategy. This absence of choice makes reference to rationality redundant, which does not necessarily entail that ESS cannot be applied to human interaction – as long as one explicitly recognizes that the “players” may not be considered strategically rational. ESS can be applied in some pure selection games (discussed below), but one can safely assume that evolutionary equilibrium be best reserved for situations where strategic rationality fails; when that is not the case, other solution concepts typically prove more credible (cf. Smith 2003). In the case of moral hazard, this solution concept presents a fundamental, though not always obvious, contradiction in terms. By its very definition, moral hazard requires that players be able to intentionally (hence “moral”) misrepresent (the “hazard” part) their strategies or their preferences – i.e., that they are self-aware and conscious of their implicit interests so they can engage in strategic choice, which is incompatible with the notion of evolutionary equilibrium. This is precisely the type of conceptual conflict between subject and methodology that ought to be avoided.
2.3.2. **Generic Structure and Sequential Equilibrium of an Extensive-Form Game**

Conversely, the strategic interaction can be formally modeled by a *strategic* game using a solution concept consistent with strategic rationality. While some have argued that normal form ought to be viewed as the native representation of games (Köhlberg and Mertens 1986), extensive form allows for a more direct visualization and intuitive understanding of the interaction. The remainder of this discussion and the game-theoretic analysis that follows are built on an extensive-form game used by Kreps and Wilson (1982) in their development of sequential equilibrium, whose main features with slight modifications in notation are summarized hereafter. 15 Unless otherwise stated, the main assumptions and definitions are maintained. Information on notation, which is important to understanding the extensive form, is summarized in Fig. 2.1.

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**Figure 2.1. Summary of Important Notation**

<table>
<thead>
<tr>
<th>Concept</th>
<th>Symbol</th>
</tr>
</thead>
<tbody>
<tr>
<td>beliefs over initial nodes of the game</td>
<td>$\beta$</td>
</tr>
<tr>
<td>set of nodes/decision points in the game</td>
<td>$T$</td>
</tr>
<tr>
<td>set of initial nodes</td>
<td>$W$</td>
</tr>
<tr>
<td>set of decision nodes</td>
<td>$X$</td>
</tr>
<tr>
<td>set of final/terminal nodes</td>
<td>$Z$</td>
</tr>
<tr>
<td>precedence relation</td>
<td>$&lt;$</td>
</tr>
</tbody>
</table>

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15 For the complete detail of the setup see Kreps and Wilson (1982) from the last paragraph on p. 865 through the top of p. 869.
<table>
<thead>
<tr>
<th>Concept</th>
<th>Symbol</th>
</tr>
</thead>
<tbody>
<tr>
<td>\textit{nth} predecessor of node ( x )</td>
<td>( p_n(x) )</td>
</tr>
<tr>
<td>number of predecessors of node ( x )</td>
<td>( l(x) )</td>
</tr>
<tr>
<td>( k \textit{th} ) successors of node ( x )</td>
<td>( S^k(x) )</td>
</tr>
<tr>
<td>action set at node ( x )</td>
<td>( A(x) )</td>
</tr>
<tr>
<td>player (actor) at node ( x )</td>
<td>( \iota(x) )</td>
</tr>
<tr>
<td>last action taken before reaching node ( x )</td>
<td>( \alpha(x) )</td>
</tr>
</tbody>
</table>

An extensive form \( F \) consists of a tree of nodes \( T \) such that the precedence relation \( < \) completely orders all the predecessors of each node \( t \in T \). The game begins from an initial node in the set \( W \subseteq T \) and ends in a terminal node in the set \( Z \subseteq T \), so that players make decisions (take actions) from the set \( A \) at nodes in the subset of non-terminal nodes \( X = T \setminus Z \). The set of immediate successors of node \( x \) is denoted \( S(x) \) and a function \( \alpha: T \setminus W \to A \) specifies the last action taken to reach a node so that \( \alpha(S(x)) \) is the action set available to the player at node \( x \). There is a finite set of players \( I \) such that the mapping \( \iota: X \to I \) identifies the player whose turn it is at each decision node. The partition \( H \) on \( X \) divides decision nodes into information sets so that the cell \( H(x) \) contains the nodes which player \( \iota(x) \) cannot distinguish from \( x \) (including \( x \) itself). Nodes in the same information set are customarily depicted as connected by a dotted line. Without loss of generality, each action can be taken in a single information set, hence they are disjoint – either \( H(x) = H(y) \) or \( H(x) \cap H(y) = \emptyset \ \forall \ x, y \in T \). The collection \( F = \{ T, <; A, \alpha; I, \iota; H \} \) is an extensive form. To obtain an extensive-form game over \( F \), it is only necessary to add a utility function \( U: Z \to \mathbb{R} \) for the payoffs and a probability mapping.
\(\beta: \mathcal{W} \rightarrow [0,1]\) which describes the players’ beliefs about the initial states (nodes) of the game.

In the analysis hereafter, players are assumed to have perfect recall and remember what they have chosen previously. They also know when it is their turn to choose and which actions are feasible. Thus, it makes sense to write \(\iota(h)\) for \(\iota(x)\) and \(A(h)\) for \(a(S(h))\), the set of feasible actions in information set (“history”) \(h\). Further, \(H\) can be partitioned into sets \(H^i = \iota^{-1}(i)\) and \(A\) can be partitioned into sets \(A^i = \{a: A^{-1}(a) \subseteq H^i\}\), respectively containing the nodes and actions available to each player \(i \in I\).

A pure strategy is an assignment \(\sigma^i: H^i \rightarrow A\) such that \(\sigma^i(h) \in A(h)\). A mixed strategy \(\pi^i: A^i \rightarrow [0,1]\) assigns to each information set \(h \in H^i\) a probability measure over the corresponding set of feasible actions \(A(h)\). Therefore, \(\Sigma_{a \in A(h)} \pi^i(a) = 1\) since trivially an abstention (if available by construction of the particular game) can be added to every decision set \(A(h)\) or probabilities can be normalized to sum up to 1 if they do not and abstention is unavailable.

Given this construction, each feasible strategy \(\pi \in \Pi\) induces a probability measure on the set of nodes \(T \ni t\) such that

\[
P^\pi(t) = \beta p_{l(t)}(t) \prod_{l=1}^{l(t)} \pi^{l(p_{l(t)})}(a(p_{l-1}(t)))
\]

Because this is simply the conditional probability that a node is reached given a particular strategy, it makes sense to call every node \(t \in T\) for which \(P^\pi(t) > 0\) “reachable” in \(\pi\). Notably, \(\pi(\alpha(t)) > 0\) does not guarantee reachability in \(\pi\).

In games of imperfect (when actions are not credibly observable) and incomplete (when not all aspects of the structure of the game are observable)
information, it is necessary to ensure the “perfection” of the solution concept – i.e., that players have no incentive to defect from their equilibrium strategy locally, not just in the overall game. This is in an essential issue in non-cooperative game theory and one of the prerequisite steps in addressing it is to understand the beliefs of the players in each non-singleton information set. (It is also a criterion that rationalizability concepts typically do not meet, even though they focus a lot on the players’ knowledge of the game structure.)

A belief system is a function \( \mu : X \rightarrow [0,1] \) such that \( \Sigma_{x \in h} \mu(x) = 1 \forall h \in H \); it is the probability assigned by player \( i(h) \) to each node in \( h \) once that information set is reached. The sensible way to make such assignments is to use Bayes’ rule to derive \( \mu(x) \) from the strategy \( \pi \) and the probability distribution over the initial states \( \beta \). Thus, the belief system \( \mu(x) \) is simply shorthand for the conditional probability \( P^\pi(x|H(x)) = P^\pi(x)/P^\pi(H(x)) \). Hence, to be able to compute values for \( \mu \) using Bayes’ rule, it is necessary to ensure that \( P^\pi(H(x)) > 0 \). The standard approach to dealing with this challenge is to assume some form of perturbation to the strategy – that is, \( \forall a \in A \) setting \( \pi(a) > 0 \) (e.g., Kreps and Wilson 1982, 872) so that \( \forall x \in X P^\pi(x) > 0 \). This has become a core feature of the equilibrist school since Selten (1975) introduced the notion of trembling-hand perfect equilibrium. A strictly positive provisional strategy \( \pi \) ensures that beliefs within a game \( \Gamma \) can be derived consistently and rationally in all information sets. Taken together, beliefs and the strategies underlying them form assessments \( (\mu, \pi) \). The set of these assessments contains the candidate equilibria for the game, but further specifications are needed.

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\( ^{16} \) To illustrate this point, consider a node \( x \) such that \( P^\pi(x) = 0 \), which happens whenever \( \pi(a(x)) = 0 \). Then, if \( x < x' \), \( P^\pi(H(x')) = 0 \) so that \( \mu(x') = P^\pi(x'|H(x')) \) cannot be computed by Bayes’ rule.
Kreps and Wilson (1982) define sequential equilibrium as an assessment that is both sequentially rational and consistent. An assessment \((\mu, \pi)\) is *sequentially rational* if \(\forall h \in H\) and \(\forall \bar{\pi} \in \Pi\) such that \(\bar{\pi}^j = \pi^j \ \forall j \neq i(h)\)

\[
E^{\mu, \pi}[u^{(h)}(z)|h] \geq E^{\mu, \bar{\pi}}[u^{(h)}(z)|h]
\]

(2.2)

where \(E^{\mu, \pi}[]\) is an expectation in \(P^{\mu, \pi}(\cdot)\). Intuitively, sequential rationality simply ensures that each player’s strategy maximizes the expected payoff in every history of the game given the accompanying beliefs and the other players’ strategies in the assessment. Thus, they hope, players have no incentives to deviate from the strategy in any information set. However, this intuition does not always hold because it does not solve the problem that arises when some player has a strategy that is just as good as another one, which in practice enables defection from the equilibrium by that player. This type of instability is addressed by the refinements in the next subsection.

Consider the interior \(\Pi^o \subset \Pi\) such that \(\pi(a) > 0 \ \forall a \in A\). Any node-specific belief \(\mu(x)\) can be computed using Bayes’ rule as long as \(\pi \in \Pi^o\) because then \(P^\pi(x) > 0\). If \(\Psi^o\) denotes the set of assessments such that \(\pi \in \Pi^o\) and \(\mu\) is defined from \(\pi\) and \(\beta\) using Bayes’ rule, then the assessment \((\mu, \pi) = \lim_{n \to \infty} (\mu_n, \pi_n)\) for some sequence \(\{(\mu_n, \pi_n)\} \subseteq \Psi^o\) is said to be *consistent*. The intuition behind this definition is that even in unreachable branches of the game, there still need to be some best responses which are “minimally absurd”. The convergence can be thought of as process of guessing and fitting a strategy whenever rational beliefs cannot be derived using Bayes’ rule. The assessment is nonetheless contained in the closure \(\Psi\) of \(\Psi^o\) so that \(\pi(a(x)), \mu(x) \in \{0, 1\}\) are still possible equilibrium
values. (For further commentary on consistency of assessments, see Kreps and Wilson 1982, 872–876).

Sequential equilibrium often does not provide solutions such that the players can commit credibly or even “find” the solution. In the example in Fig. 2.2, the game has a unique sequential equilibrium such that Player 1 goes right half of the time and Player 2 always plays left such that both obtain an expected payoff of 1.5. However, the interaction becomes more complicated in a modified version of the game (Fig. 2.3) where Player 1 receives the same payoff of 2 in every terminal node. That makes it impossible for Player 2 to anticipate the strategy of Player 1. And even if there is a credible way for Player 2 to be informed of it, there still are an infinite set of sequential equilibria, which makes the concept less than helpful, especially if this is just a subgame of a larger game. These types of solutions hardly suggest the sort of stability that is typically associated with institutions.

Figure 2.2. Variant of the Coordination Game
This is a critical deficiency of SE as a solution concept in cases when beliefs cannot be formulated unequivocally. It simply allows any belief as long as the corresponding local strategy is consistent with that arbitrary belief. In Fig. 2.3, a belief on the part of Player 2 that Player 1 always plays left and always playing left in response would be an SE as long as Player 1 actually did choose to play left always. But the opposite assessment – a belief on the part of Player 2 that Player 1 always plays right and always playing right in response would be an SE, too, as long as Player 1 actually did choose to play right always. In a sense, SE admits solutions that presuppose perfect information in some cases where in fact there is none. This is certainly not an appealing feature for a solution concept when coordination and commitment are essential challenges that a theory is trying to address (e.g., voting, electoral-coalition strategy).

It may appear easy enough to remedy this problem by requiring uniqueness (in which case the modified game would not have an equilibrium). However, if
applied indiscriminately, such a requirement may eliminate reasonable solutions in other cases. For example, if the modified game is a subgame in a larger game so that the probability of reaching it in that game’s SE is zero, it would be irrelevant from a commonsense perspective that it has no unique local SE. Yet, the local non-uniqueness would render the global SE non-unique, too, invalidating it under those strict conditions. Is it possible to modify SE so as to devise a concept that excludes the “anything goes” cases but without imposing unnecessarily restrictive criteria?

2.3.3. Strategically Rational Equilibrium

Before that question can be answered in the affirmative, it is necessary to flesh out some more structures within the extensive-form game. These additional concepts are not restrictive. In fact, it is possible to relax some of the assumptions of Kreps and Wilson, who assume that the set $T$ is finite. This is not necessary to maintain their results insofar as they are relevant to this discussion. Instead, it is sufficient to assume only that $p_l(z)$ is finite $\forall z \in Z$, which substantially expands the domain of applicability of the solution concept.

To make it possible to distinguish between “important” and “unimportant” segments of the game tree, it is expedient to define a special partition function that divides a game into smaller objects. Let $\tau: \mathcal{Z} \times \mathcal{X} \to \Gamma$ map the product of the power sets $\mathcal{P}(Z) = \mathcal{Z}$ and $\mathcal{P}(X) = \mathcal{X}$ onto $\Gamma$ and its elements so that $\tau(Z,X)$ is an “extensive-quasi-form” “quasi-game”. Formally, for some $\hat{Z} \in \mathcal{Z}$ and $\hat{X} \in \mathcal{X}$ let $\tau(\hat{Z},\hat{X}) = \hat{\Gamma}$ with extensive quasi-form $\hat{\Gamma} = \{\hat{T}, \prec; \hat{A}, \alpha; \hat{I}, \iota; \hat{H}\}$, where $\hat{H}$ is a partition on the decision nodes $\hat{T}\backslash\hat{Z}$ such that for any nodes $x, y \in \hat{T}$ if $x, y \in H(x)$ then $x, y \in \hat{H}(x)$ for the subset of nodes $\hat{T} = \{t \in T: t < z, z \in \hat{Z}\} \cup \{t \in T: t > x, x \in \hat{X}\}$. Defining further $\hat{A} = \{a \in A: a = \alpha(S(t)), \forall t \in \hat{T} \text{ such that } S: \hat{T} \rightarrow \hat{\Gamma}\}$ and $\hat{I} = \{i \in I: i = \iota(t) \forall t \in \hat{T}\}$, the quasi-game $\hat{\Gamma}$ is completed by $\hat{U} = \{u^{(t)} \in U: t \in \hat{T}\}$ and $\hat{\beta} = \{\hat{\beta}^{(t)} \in \beta: t \in \hat{T}\}$.
\{\beta_w: w \in \hat{T}, W\}. Thus, it consists of all the nodes in the arguments \(\hat{X}, \hat{Z}\), all their successors and predecessors respectively and the other elements of \(\Gamma\) “attached” to those nodes (actions, payoffs, etc.). In other words, \(\tau\) cuts through the action sets of the nodes, eliminating actions that lead to nodes which do not have successors or predecessors in the arguments \(\hat{X}, \hat{Z}\). Trivially, the game itself is a tau object on both the set of its initial nodes and the set of its terminal nodes; \(\tau(\cdot, W) = \tau(Z, \cdot) = \tau(Z, W) = \Gamma\) always, whereas \(\tau(\emptyset, Z) = \tau(W, \emptyset) = \tau(W, Z) = \emptyset\).

The \(\tau\) function’s backward component (working backwards from the first argument-set of nodes located in \(Z\)) can cut through information sets in the original game. There is no guarantee that for any set of input nodes \(\tau(\cdot)\) is going to be connected everywhere. Nor is there a guarantee that initial beliefs \(\hat{\beta}\) will be always available since the forward component (working forwards from the second argument-set of nodes located in \(X\)) may well not start in a singleton information set. However, there are two subfamilies of tau objects that are connected everywhere and may have all the components necessary to formulate a game. Any object of the type \(\tau(\emptyset, H(x)) = \hat{\Gamma}\) is a subgame of \(\Gamma\) (this definition is less restrictive than the traditional one). To make \(\hat{\Gamma}\) a proper subgame (i.e., a full-fledged game in its own right), further restrictions are necessary to avoid splitting information sets (i.e., to keep the information consistent with that in the original game \(\Gamma\)). Let \(H_0 = \{H(x): \forall x' > x, x'' \in H(x') \iff x'' > x\}\). If \(H(x) \in H_0\) and either \(H(x) = \{x\}\) or \(x \in W\), then \(\tau(\emptyset, H(x))\) is a proper subgame with root \(x\).

The second interesting type of tau objects is founded on the terminal nodes of the game. For any \(\hat{Z} \in Z(\Gamma)\) the game \(\hat{\Gamma} = \tau(\hat{Z}, \emptyset)\) is a stem of the game \(\Gamma\). In words, a stem is a part of the game tree which “leads” to a specific nonempty set of terminal nodes. Trivially, the stem supporting the entire terminal set of any extensive-form game is the game itself. Further, denote \(Z^\pi = \{z \in Z: P^\pi(z) > 0\}\)
and $\mathcal{Z}^\pi = \{ Z^\pi : \pi \in \Pi \}$. If for some sequence $(Z_n) \in \mathcal{Z}$ \( \lim_{n \to \infty} \tau(Z_n) = \tilde{\Gamma} \) the game $\Gamma$ containing $Z$ is said to be $\tau$-	extit{convergent} to $\tilde{\Gamma}$ in $\pi$. If $(\mu, \pi)$ is a consistent assessment in $\Gamma$ and $\Gamma$ is $\tau$-convergent to $\tilde{\Gamma}$ in $\pi$, the triplet $(\tilde{\Gamma}, \mu, \pi)$ is a \textit{premise} and $\tilde{\Gamma}$ is its stem.

In other words, the stem of a premise is a game including all of and only the nodes which are reachable in $\pi$; it is the part of the original game that “matters” given the strategies of the players.

The objective is to identify a set of premises that reasonably constitute an equilibrium stable to troubling informational asymmetries, so that players can reasonably arrive at a best-response matching for one another’s strategies that achieves predictable outcomes. Ideally, the solution concept should exclude situations such as the game in Fig. 2.3, where a clear Pareto-efficient outcome exists that maximizes both players’ payoffs but there are nonetheless infinitely many sequential equilibria. Clearly, singleton information sets would not be a problem in this respect, but non-singletons might.

In trying to identify conditions for market equilibrium, Léon Walras likened the equilibrating process to grasping – \textit{tâtonnement} – at a solution by the uninformed participants (cf. Mas-Colell, Winston and Green 1995, 778–782). In a game-theoretic setting, such grasping would be innocuous if it did not impact the players’ payoffs – i.e., if the payoffs were stable given the rest of the beliefs and strategies of the players. Thus, if for all pairs $(\mu, \pi), (\tilde{\mu}, \tilde{\pi})$ in a set of consistent assessments $\Theta$ in the subgame $\tau(\cdot, \tilde{h})$ where $\tilde{\pi}^l = \pi^l \ \forall j \neq i(\tilde{h})$ it is true that $\forall i \in I$

$$E^{\mu, \pi}[u^i(\cdot)|\tilde{h}] = E^{\tilde{\mu}, \tilde{\pi}}[u^i(\cdot)|\tilde{h}] \quad (2.3)$$

the payoffs of the set of consistent assessments are \textit{tâtonnement-stable} in information set $\tilde{h}$. 
To understand the effect of this restriction, consider a candidate set of sequential equilibria \((\mu_k, \pi_k)\) in a non-singleton information set \((x_n)\) of a stem game \(\Gamma\). If player \(\iota((x_n))\) can derive beliefs over these nodes using Bayes’ rule, then either there is a unique sub-assessment \((\hat{\mu}, \hat{\pi})\) that is a sequential equilibrium in the subgame \(\bar{\tau}(\emptyset, (x_n))\) onto \(\bar{\Gamma}\) with \(\hat{\beta} = \mu(x_n)\) or the player is indifferent between strategies because his or her payoffs are the same everywhere in \(Z^n = \{z \in Z : z > x_n\}\). Neither of these cases presents a coordination challenge as long as the payoffs of downstream players are not affected by the unpredictability generated in the indifference case. If, however, \(\mu(x_n)\) renders indeterminate or non-singleton sets and the player’s decision is nontrivial to the payoffs, it is hard to speak of an equilibrium as it would be impossible to lock onto an optimal choice even in mixed strategies. Tâtonnement stability of payoffs removes the need for grasping at an optimal strategy regardless of whether the player is informed (by Bayes’ rule and the structure of the game, including its information assumptions) or not.

**Definition 2.2. (Rational Equilibrium)** A rational equilibrium is a premise whose assessment is any sequential equilibrium which is unique in every information set of the premise’s stem where payoffs are not tâtonnement-stable relative to the stem’s terminus. A rational equilibrium is recursive if it also is a rational equilibrium in every non-stem subgame, in every non-stem subgame of a non-stem subgame and so on.

Formally, a premise \((\bar{\Gamma}, \mu, \pi)\) is a rational equilibrium (RE) of game \(\Gamma\) if and only if all of the following conditions are satisfied:

(i) \(\pi \in \Pi^\circ, \mu\) is derived from \(\pi\) and \(\beta\) using Bayes’ rule and \((\mu, \pi) = \lim_{n \to \infty} (\mu_n, \pi_n)\) for some sequence \((\mu_n, \pi_n)\) \(\subseteq \Psi^\circ\);

(ii) \(E^{\mu, \pi}[u^{(h)}(z)|h] \geq E^{\mu, \tilde{\pi}}[u^{(h)}(z)|h] \forall h \in H\) and \(\forall \tilde{\pi} \in \Pi\) such that \(\tilde{\pi}^i = \pi^j \forall j \neq \iota(h)\);
(iii) \( \bar{\Gamma} = \lim_{Z_n \to Z} \tau(Z_n) \) for any sequence \( Z_n \in \mathcal{Z} \); 
(iv) \( E_{\mu, \pi}[u^{(\bar{h})(\cdot)}|\bar{h}] > E_{\mu, \bar{\pi}}[u^{(\bar{h})(\cdot)}|\bar{h}] \) for \( \bar{\pi}^j = \pi^j \ \forall j \neq i(h) \) in every \( \bar{h} \in \bar{H} \) where \( \exists (\mu, \bar{\pi}) \in \Psi \) such that \( E_{\mu, \pi}[u^j(\cdot)|\bar{h}] = E_{\mu, \pi}[u^j(\cdot)|\bar{h}] \) for some \( j \neq i(\bar{h}) \) for \( \bar{\pi}^j = \pi^j \ \forall j \neq i(\bar{h}) \).

In words, these conditions can be stated as:
1. \((\mu, \pi)\) is a consistent assessment;
2. \((\mu, \pi)\) is a sequentially rational assessment;
3. the game is \( \tau \)-convergent in \((\mu, \pi)\) to the stem \( \bar{\Gamma} \);
4. \((\mu, \pi)\) is uniquely sequentially rational in every information set of \( \bar{\Gamma} \) where the set of all consistent assessments is not tâtonnement-stable.

RE is a strengthening of SE beyond sequential rationality to ensure its logical robustness, both backward and forward, in games of incomplete and imperfect information. One of the motivations for developing RE was to “exclude” games like the one in Fig. 2.3, where what can be seen as rational behavior does not result in something that looks like a reasonable strategic outcome that can be termed an “equilibrium”. In that game, Player 2 simply would not be able to “equilibrate” credibly with Player 1. Existence everywhere is not necessarily a desirable property of a solution concept applied in formal-theoretic analysis of institutions. An RE can exist only in games whose stems are composed only of subgames with tâtonnement-stable payoffs or where backward induction and connectedness over \( \bar{\Gamma} \) induce a unique optimum in \( \pi \). An RRE exists only in the very unlikely case that the same conditions apply to the non-stem branches of the game as well.

As an example, the following dictator game (Fig. 2.4) has infinitely many REs of the type \( \{\pi_1 \in [0,1], 1,0\} \), where \( \pi_i \) is the probability of \( i \) playing “left”, and the game is its own stem in most of those equilibria (whenever \( \pi_1 \notin \{0,1\} \)). The
multiplicity of solutions does not invalidate the equilibria because they are tâtonnement-stable in all three information sets since \( \mu = 1 \) everywhere.

Figure 2.4. A Game with Tâtonnement-Stable Payoffs in Its Initial Node

Operating in the absence of credible commitments and information exchange is particularly relevant to sociopolitical theory because commitment and delegation problems not only are endemic, but usually are the very object of investigation. They are especially acute in the study of institutions because, unlike microeconomists, the political scientist normally cannot avail oneself of exogenous enforcement of contracts by the legal system. In the case of international relations, it is even hard to regard \textit{any} institutions as fixed (Morrow 1999). The conditions added beyond SE ensure that any RE is also rationalizable and admissible everywhere – that is, that the rational-equilibrium best response of each player is not dominated by any other decision function.
To assess the implications of this formulation, consider again the two-period imperfect-information game proposed by Fearon (1999), where a principal selects from a pool of identical office-seeking agents. Each period there is an “election” by the principal followed by an implementation of “policy” by the appropriate agent. Nature then interferes with the realization of the policy. In the derived Nash equilibrium, the principal sets some cutoff-point rule on observed performance at the end of the first period in order to decide whether to reelect the incumbent for another term. Intuitively, this equilibrium solution does not provide a strategically rational equilibrium of the game. From the setup it is clear that whoever gets the second (and final) term is going to implement his or her ideal policy. Thus, there is an infinite set of SPEs (which are also NEs) such that the agent implements one’s own ideal point in every period and the principal does *anything* in the feasible strategy space (e.g., picking agents at random). Being reasonably capable of backward induction, the principal is indifferent as to which of the agents will be selected because they are all identical, and so the principal, in turn, cannot credibly commit to any selection outcome in the second period. Note that this result is robust even in mixed strategies, as the agents are identical, and no probability distribution over the principal’s nodal strategy space can be derived. The specific action of the principal in this instance would pertain to a special cause outside the parameters of the model.\(^\text{17}\) Accordingly, that game has no rational equilibrium and does not seem to reflect a credible institutional arrangement.

\(^{17}\) See further Keynes 1921.
2.4. A General Model of Rational Agency

Nevertheless, Fearon’s setup does present a general starting-point for designing a more robust rational-choice model of delegation and control. An agency game structure can be fleshed out on the general foundation of the extensive-form game used heretofore, so it is convenient to preserve the notational conventions established in the previous sections of this chapter. Within this framework, let there be a finite set of principals $V$ who collectively (s)elect agents from $C = I \setminus V$ (therefore also a finite set). There are no restrictions on the selection rule as long as it is nontrivial – i.e., that the action of the actors in $V$ have an effect on the selection outcome in a predictable way. Formally, it can stated as a function $v: A^V \to C$ that maps the principals’ actions onto the set of candidates thereby producing a (set of) winner(s). In terms of predictability, the requirement is just that if a disinterested third party had all the information about the principals’ actions $a^V \in A^V$ as well as the way they are aggregated into a winset, said party would be able to predict the outcome “reasonably well” – i.e., a sequence of informed rational predictions $\hat{c}_n$ would converge to the actual winner(s):

$$\lim_{n \to \infty} \hat{c}_n = v(a^V) \in C$$ (2.4)

The other option is that principals’ intent has no impact on who the selected agent is. In that case, the agency designation becomes tenuous at best, but such instances do exist in the history of political organization. For example, in the heyday of Athenian democracy, the city’s legislature was elected by lot from the ranks of the entire free male citizenry. While modeling such arrangements should be done with additional caution, they are a perfectly legitimate object of interest in the political economy of institutions. However, this analysis is limited to voting
rules that lead to strategic interaction between principals and agents and therefore it is necessary to assume that voters’ actions do have an impact on the electoral result.

Let the following sequence of events characterize a period $k$ in the game (Fig. 5 visualizes two consecutive periods):

1. The principal(s) choose an agent $\iota(k)$ from the set $C$ and the result becomes known to everybody.
2. The appointed agent $\iota(k)$ undertakes policy action $a \in A^{(k)}$, which is not observable by the principal(s) (imperfect information).
3. Nature maps that action into the periodic outcome space $\Omega_k \supseteq A_k$ according to some rule $\omega: A \rightarrow \Omega$ such that $\lim_{n \rightarrow \infty} \omega_n(a) = a$ for all $a \in A$.
4. Principal(s) and agent(s) observe outcome $\omega_k$ and periodic payoffs are received.

Because all principals have to act every period, it makes sense to make a change in notation so that henceforth the identity function $\iota(k)$ denotes the agent incumbent in period $k$ rather than the decision maker at some node $k$ of the extensive form.

Figure 2.5. Two Periods of a Generic Agency Game
Information is rather scarce in this setting. Players know that agents’ action sets are in the outcome set, but there are other known events in the outcome set that may be in none of the action sets (formally, $A^{(k)} \subseteq \Omega$) – i.e., outcomes are uncertain. Additionally, agents and principals cannot observe the other group’s actions and principals do not know agents’ preferences (i.e., their “type(s)”). Neither group can make credible commitments as there is no third-party enforcer and this information structure is common knowledge.

**Definition 2.3. (Pure Sanctioning)** If and only if all agents have the exact same characteristics (actions sets, information, utility functions, preferences, policy skills, etc.) and that is common knowledge, the agency game is of pure sanctioning.

**Definition 2.4. (Pure Selection)** If and only if agents differ in their competency but sincerely try to implement the principals’ preferred policy and that is common knowledge, the agency game is of pure selection.

**Definition 2.5. (Fully Strategic Agency)** If and only if agents have diverse characteristics (actions sets, information, utility functions, preferences, policy skills etc.), are able to misrepresent their actions and intentions, and that is common knowledge, the agency game is of fully strategic agency.

While it is conceivable that common knowledge of the players’ characteristics may not be the best or only feasible theoretical premise, these three definitions seem to provide the most interesting – yet sufficiently general – settings from an empirical perspective. At this stage it is helpful to outline some assumptions that may be necessary in analyzing some of the three possible variants of the model and to discuss their potential impact on the results.

There are other aspects of the players’ beliefs which could have an impact on their behavior, materially altering the theoretical results. One such difference is office seeking. An office-seeking actor values power – the state of being an agent for another party – for its own sake, not just because that puts him or her in a
position to affect policy. In practice, an assumption of office seeking may be justified with the status that often comes with public office or other rents associated therewith, such as gifts from supporters, patronage or income from corruption. Let $U(\cdot)$ denote the total utility function and $u(\cdot)$ be the policy utility function for some period $k$ (subscripts are generally dropped for brevity). Formally, an agent can be distinguished as office-seeking by adding a positive quantity $b$ to the periodic utility if office has been won – i.e., for agent $i(k)$, $u^{i(k)} = u(\omega) + b$, whereas for any other agent or principal $j \in I$, $u = u^j(\omega)$.

Another potentially important assumption relates to players’ beliefs about their world. If they believe that the world is ergodic, they can construct probabilities in time and use inference based on the Law of Large Numbers. In short, an ergodic milieu allows them to use frequentist methods. If the world is non-ergodic, however, the future cannot be assumed to be like the past and the Problem of Induction becomes the dominant paradigm for determining optimal strategies. Different players may have different ergodicity beliefs about different aspects of the game.

In the context of the generic game, ergodicity would mean that any conditional distribution of policy outcomes $f: A_k \times \Omega \rightarrow [0,1]$ remain the same throughout all the periods of the game. For example, the probability of outcome $\omega$ given policy $\omega'$ should remain the same: $f_k(\omega | \omega') = f_n(\omega | \omega')$ for any periods $k, n > 0$. It also means that if $f$ is not known, it may be possible to approximate it legitimately by observation of outcomes over time. There are no significant restrictions on the topology of $\Omega$; it can be non-discrete, where singletons have nonzero mass in probability and continuous regions with nonzero densities are contained in some subset $\tilde{\Omega} \subset \Omega$, with disjoint subsets $\tilde{\Omega}_i$. If an analytical expression for $f$ is available, the conditional expected utility of a yet unobserved outcome provided a known policy $\hat{\omega}$ would then be obtainable as
\[ E[u(\tilde{\omega})] = \sum_{\tilde{\omega}_i \in \tilde{\Omega}} \int f(\omega_k | \tilde{\omega}) u(\omega_k) d\omega + \sum_{\omega_k \in \Omega \setminus \tilde{\Omega}} f(\omega_k | \tilde{\omega}) u(\omega_k) \]  

(2.5)

Having shown this generalization is available, for the sake of brevity it is assumed that \( \forall \omega \in \Omega \ E(\omega | \tilde{\omega}) = \omega \) whenever \( \tilde{\omega} = \omega \), so that it makes sense to write \( u(\omega) \) instead of \( E[u(\omega)] \) etc.

Finally, heuristic preferences may also introduce substantial differences in results. Office seeking may be regarded as a heuristic preference for holding an office. A much more interesting heuristic preference, however, may relate to the principals’ deriving utility from punishing or rewarding agents’ behavior or results. Most significantly, they may obtain some satisfaction from disposing of poorly performing agents. This sort of preference is “heuristic” in the sense that the evolutionary benefit it provides is indirect; while it may not improve an actor’s odds of survival directly, it may do so by helping induce compliance from the actor’s agents. Like office seeking, such a heuristic preference has a readily available evolutionary rationale – punishing undesirable results (whether the punishment is deserved or not) can improve the survival odds of the group by ostracizing individuals who are ill-equipped for office and by discouraging strategic misbehavior by officeholders.

For the purposes of the analysis that follows, it is necessary to specify two additional concepts within the sequential form. Two terminal nodes \( z_1 \) and \( z_2 \) are said to be symmetric (denoted as a relation \( \sim \)) if for nodes \( x_1 = S^{-1}(z_1) \) and \( x_2 = S^{-1}(z_2) \) all the following are satisfied:

- \( u^t(x_1)(z_1) = u^t(x_2)(z_2) \);
- \( u^t(x_2)(z_1) = u^t(x_1)(z_2) \); and
- \( u^t(z_1) = u^t(z_2) \ \forall i \in I \setminus \{t(x_1), t(x_2)\} \).
Symmetry is not necessarily transitive, but can be expanded to other (sub)elements of $\Gamma$. If all the nodes in terminal subset $Z_1 \subseteq Z$ are symmetric to a node in $Z_2 \subseteq Z$ and vice versa, then $Z_1 \sim Z_2$. Every node is trivially symmetric to itself, i.e., $z \sim z$, and so is every terminal set, i.e., $Z \sim Z$.

Two decision nodes are symmetric if their and their successors’ terminal sets are symmetric: $x_1 \sim x_2 \iff Z(x_1) \sim Z(x_2) \forall x_1', x_2' > x_1, x_2 Z(x_1') \sim Z(x_2')$. This ensures implicitly that every information set and every part of the tree beyond the nodes are essentially mirror images. Similarly, two sets $X_1 \subset X$ and $X_2 \subset X$ are symmetric if all the nodes of one have a mirror element in the other: $X_1 \sim X_2 \iff \forall x_1 \in X_1 \exists x_2 \in X_2$ such that $x_2 \sim x_1$ and vice versa. A pair of identical players have completely symmetric decision sets and identical utility functions. That is, if and only if $X(i) = \{x \in X : i(x) = i\}$ and $X(i) \sim X(j)$, then $i \sim j$ if $u^i(\cdot) = u^j(\cdot)$.

**Identity-Consistency Theorem.** In any rational equilibrium of a sequential-form game, identical players have identical strategies: $i \sim j \iff \pi^i = \pi^j$.

**Proof.** Let $Z(X(i)) = Z$ and $Z(X(j)) = Z'$. From symmetry, $\forall z \in Z \exists z' \in Z'$ such that $u^i(z) = u^j(z')$ and vice versa. From symmetry again, $P^\pi(z) = P^\pi(z')$ for any feasible $\pi$, but $E^\pi[u] = \Sigma_{z \in Z} u(z) P^\pi(z)$, therefore $E^\pi[u^i] = E^\pi[u^j]$. Hence if $\pi$ is suboptimal for one of the players, i.e., if $\exists \pi \neq \pi$ such that $E^\pi[u^i] > E^\pi[u^j]$, then it must be suboptimal for the other one, too: $E^\pi[u^j] > E^\pi[u^i]$ since $E^\pi[u^i] = E^\pi[u^j] \forall \pi \in \Pi$. ■

**2.4.1. Pure Sanctioning**

**Game 1.** To consider first the case of pure moral hazard with a finite number of terms available, let the game consist of at least two sequential periods of the generic type described at the beginning of Section 2.4. (A one-period case is not worth analyzing in detail because it has only one logical solution and does not seem to reflect most interesting delegation situations.) No heuristic preferences are
assumed for this game and the results hold in both an ergodic and a non-ergodic realization of the policy choice. Let further the principals know that the agents are identical, but do not necessarily know their ideal policy set $\Omega$.

**Proposition 2.1.** In any finite game of pure sanctioning (pure moral hazard) without office seeking, agents’ rational-equilibrium strategy is to implement their ideal policy in all periods.

**Proof.** Because agents are identical, it is evident that there is no loss to them from not being in office; agents are indifferent about who is appointed because everyone is identical and by Definition 2.1 they must know that the Identity-Consistency Theorem holds. Without office seeking or any indirect incentive to keep office, in any RE the incumbent must simply implement a point in his or her ideal set $\omega \in \Omega$. Again by complete information, this is common knowledge so there is a unique belief system $\mu$ that reflects $\pi(\omega) = 1$ for any period. The agents’ strategy and this belief system form a sequentially rational assessment with any selection strategy by the principals (given that they cannot affect the outcome, any action on their part is utility-maximizing in every information set). Since the expected payoffs $u(\omega)$ are tâtonnement-stable in every period, these SEs are also REs.

The equilibrium solution to this group of games can be interpreted to reflect situations where two conditions are present simultaneously: the pool of potential candidates is confined to a uniform cadre or screened for dissenting opinions; and the power of the office being elected is restricted by a third party, thus nearly eliminating any specific benefits of office. The closest real-world situation to such unusual theoretical setting is perhaps Iran in the first years after the Islamic Revolution. Only candidates from among the most loyal to the clergy were allowed to run for office and, by virtue of that association, they probably already had most of the advantages that holding a public title would afford them. The first
president of the Islamic Republic, Abolhassan Banisadr, was impeached after just a year in office for “subverting” the power of the clergy and had to flee the country. His successor was killed in a bombing by anti-Islamist plotters days after taking office. The clergy finally ran their own candidate Ali Khamenei, who won “landslides” in 1981 and 1985 and unleashed a reign of terror to crack down on both the official and the armed opposition. The clergy had allowed nearly a hundred candidates in the first election, but only a handful in those that followed, amid suspicions of widespread rigging and voter suppression, having learnt from the election of the dissident Banisadr. However, even in those circumstances it is hard to imagine a situation where office would not confer at least some benefit that would encourage office seeking by some candidates.

**Game 2.** Now consider a setting identical to Game 1, only this time with some positive rents \( b \) coming from office such that the payoff of the agents is 

\[
u^T(k) = u(\omega_k) + b\text{ if in office in period } k.
\]

Let there also be a known conditional probability mapping \( f: \Omega \times \Omega \to [0,1] \) providing a conditional estimate of future policy outcomes.

**Proposition 2.2.** In any finite ergodic game of pure sanctioning (pure moral hazard) with office seeking and risky outcomes, either agents’ RE strategy is to implement their ideal policy in every period or there is no rational equilibrium.

**Proof.** In any RE strategy \( \pi \), it must be the case that \( \pi(\omega) = 1 \) in the last period as there is no other way to maximize \( E^\pi(u) \) for the incumbent.

Consider a potential agents’ strategy \( \pi(\omega) = 1 \) in the penultimate period. If the strategy of the principals was to reward performance with reappointment after observing an outcome \( \omega \) in some winset \( \Omega^* \) and \( \omega \notin \Omega^* \), then an incumbent’s response \( \pi(\omega) = 1 \) would be suboptimal because it could be possible to gain office rents by ceding some policy ground and increasing the probability of being
reappointed for the last period. Formally, the agent would have a better expected payoff for any policy \( \hat{\omega} \) such that

\[
u(\hat{\omega}) > u(\omega) - b\left(P(\omega \in \Omega^* | \hat{\omega}) - P(\omega \in \Omega^* | \omega)\right)
\]

(2.6)

If \( \hat{\omega} \) does not exist, agents implement their ideal policy in any RE. This completes the first part of the proof.

If, however, \( \hat{\omega} \) exists, that rules out setting everywhere \( \pi(\omega) = 1 \) as an equilibrium strategy. Suppose then that in optimum \( \pi(\hat{\omega}) > 0 \) outside of the last period and recall that identity of agents implies identity of \( \pi(\hat{\omega}) \) by the identity-consistency theorem. Against this strategy, the principals are indifferent between playing a strategy where they reward with reappointment every time they observe outcome \( \omega \in \Omega^* \) and a strategy where they defect from this principle in the last period; formally, \( \forall h, E^{\mu,\pi} [u^v | h] = E^{\mu,\bar{\pi}} [u^v | h] \), where \( \bar{\pi} \) involves defecting in the last period by, say, picking an agent at random. Thus, the SE is not unique in the final-period election, but payoffs are not tâtonnement-stable in that information set (changing the principals’ strategy to “defect” from reward/punishment cutoff rule would alter the expected payoffs of the agents because of the bonus \( b \) for holding office). Therefore, no \( \pi(\hat{\omega}) > 0 \) can be an RE strategy either.■

The policy \( \hat{\omega} \) that could improve the expected payoffs of both agents and principals is not achievable because the principals cannot commit to reappointing the incumbent from the penultimate period, knowing that defection to \( \omega \) will inevitably follow. By backward induction, the last-period incumbent will implement his ideal point (Fig. 2.5) as there are no subsequent rewards and punishments for doing otherwise. Therefore, any action by the principal(s) at node \( D \) is sequentially rational since their payoffs will always be determined by the ideal policy of the agent in the last period and all agents and their ideal policies are
identical by definition of pure moral hazard. In other words, the principals cannot commit to re-electing agent \( i(k - 1) \) regardless of outcome \( \omega_{k-1} \). Hence, \( i(k - 1) \) cannot expect any benefit from selecting anything but one’s own ideal point in the penultimate period.

This result is robust to ergodicity considerations and office seeking. It makes evident that adding officeholder rewards does not change the equilibrium dynamic in pure moral hazard (identical agents). While agents have more of an incentive to do good by the principals, the latter still cannot commit to rewarding them because of the imperfect information and the inexorable reversion to the agent’s ideal point in the last period. The principals’ inability to commit to rewarding good behavior overwhelms any other considerations, whether or not ergodicity holds.

**Game 3.** Now consider a setting identical to Game 2, only this time with a heuristic preference on the part of principals to punish bad results and/or reward good. There are different ways to render heuristic preferences within utility theory. They may be ranked lexicographically so that they always take precedence over normal ones or reverse-lexicographically so that they become relevant only when regular utility implies indifference (or does not apply at all). The preference itself need not be symmetric – e.g., it could give different weights to positive and negative stimuli. In this case, the heuristic preference is introduced on a par with the existing utility function and is only relevant to punishing bad performance so that for any principal \( u(\omega) = u^*(\omega) + \chi \) such that \( \chi_k > 0 \) whenever both \( \omega_{k-1} \notin \Omega^* \) and \( i(k) \neq i(k - 1) \) are satisfied or both \( \omega_{k-1} \in \Omega^* \) and \( i(k) = i(k - 1) \); otherwise \( \chi = 0 \). That is, principals receive a direct utility boost from dislodging an underperforming incumbent (from the prior period) or reappointing one that performs well.
**Proposition 2.3.** In the RE set of any finite ergodic game of pure moral hazard with office seeking where principals exhibit a heuristic preference for penalizing underperformance, agents may deviate towards the principals’ preferred points.

**Proof.** The proof of Proposition 2.2 largely applies here. If the agents’ strategy is to set \( \pi(\omega) = 1 \) in every period, given a known set \( \Omega^* \), an alternate policy \( \tilde{\omega} \in \Omega^* \) would provide a better expected utility whenever condition (2.6) is satisfied. To analyze the existence of such a policy before the penultimate period, it is necessary to define a probability of reelection and an analytical expression for the utility of holding office in any period.

Hereafter, let \( \theta_k(\iota(k)|\omega_k^i) \) denote the probability of agent \( \iota(k) \) being reappointed to office in period \( k + 1 \) if he implements policy \( \omega_k^i \) in period \( k \). The shorthand \( \theta(k) \) will be used instead of \( \theta_k(\iota(k)|\cdot) \), wherever that does not cause confusion. The probability of reelection can be formally defined as \( \theta(k) = P(\iota(k) = \iota(k + 1)|\omega^i(k)) = P(\omega \in \Omega^*|\omega^i(k)) \) where \( \omega \) is the policy realization, so it is necessary to assume that this probability can be derived from \( f \). Thus, the conditional probability \( \theta: \Omega \to [0,1] \) is an implicit function derived from \( f \) and the heuristic-preference winset of the principals \( \Omega^* \). The heuristic preference ensures that \( E^{\mu,\pi}[u^v|h] > E^{\mu,\tilde{\pi}}[u^v|h] \) for the principals, where \( \tilde{\pi} \) involves defecting from punishing the incumbent. However, the existence of a compliance RE is contingent on the existence of accommodative policy \( \tilde{\omega} \), which in turn depends on the utility functions of the principals and the agents.

To make the incumbency benefit explicit, define an office-value function \( \delta: \mathbb{N}_1^\kappa \times \mathcal{L} \to \mathbb{R} \) such that \( \delta^i(k) \) is agent \( i \)'s value-added for holding office in period \( k \). In other words, \( \delta^i(k) \) is \( i \)'s opportunity cost of not being in office in period \( k \). The candidates’ dominant strategy must still be to shirk if appointed in the last period. Since in an RE all agents would implement the same policy by the Identity-
Consistency Theorem, the value added to \( i(k - 1) \)'s utility from keeping office in the \( k \)th and last period is simply

\[
\delta^{i(k-1)}(k) = b
\]  
(2.7)

The value-added for keeping office in the \( k - 1 \)th period would then be the sum of the office rent \( b \) and the probability of being reelected times the value added for being in office the following period less the opportunity cost of being in office, which is the probability of being elected to replace another incumbent in this period \( \lambda = (|C| - 1)^{-1} \):

\[
\delta^{i(k-2)}(k - 1) = b + \theta \delta(k) - \lambda \delta(k) = b + (\theta - \lambda) \delta(k)
\]  
(2.8)

Observe that the difference \( \theta - \lambda \) simply reflects the increase in probability to be appointed in period \( k \) if an agent is appointed in period \( k - 1 \). The value of office-holding develops further to earlier periods of the game as follows:

\[
\begin{align*}
\delta(k - 2) &= b + (\theta - \lambda) \delta(k - 1) \\
\delta(k - 3) &= b + (\theta - \lambda) \delta(k - 2) \\
&\vdots \\
\delta(1) &= b + (\theta - \lambda) \delta(2)
\end{align*}
\]  
(2.9)

Hence the general expression for the value-added of office-holding in period \( t \) of a game with \( k \) periods is

\[
\delta^i(t) = b \sum_{s=t+1}^{k} \prod_{r=t+1}^{s} (\theta(r - 1) - \lambda)
\]  
(2.10)
A policy \( \hat{\omega}_t \neq \omega_t \) in period \( t \) would be sequentially rational only if it satisfies

\[
u(\hat{\omega}) > u(\omega) - \delta(t+1)(\theta(t|\hat{\omega}) - \theta(t|\omega)) \tag{2.11}\]

That is, the policy concession made by the incumbent must be less than the marginal gains in office rents obtained through increased probability of being appointed in subsequent periods. To be sequentially rational, \( \hat{\omega} \) must also be at least as good as any other policy \( \tilde{\omega} \) that satisfies (2.11), i.e., \( \forall \tilde{\omega} \neq \hat{\omega} \):

\[
u(\hat{\omega}) \geq u(\tilde{\omega}) - \delta(t+1)(\theta(t|\hat{\omega}) - \theta(t|\tilde{\omega})) \tag{2.12}\]

Thus, two sets of possible REs exist and in both of them the principals’ strategy is to vote the incumbent out when they observe \( \omega_k \notin \Omega^* \) and keep him in when they observe the opposite. If \( \nexists \hat{\omega} \) that meets the separating condition (2.11), there is a non-compliance RE in which the agents’ strategy is to implement their ideal policy \( \omega \) in every period; otherwise they implement \( \hat{\omega} \) that satisfies both (2.11) and (2.12), complying to some extent to the principals’ desires.

Thus, when even fairly weak heuristic preferences are introduced, the agents’ ideal policy \( \omega \) no longer necessarily dominates the RE set; they render even the non-compliance equilibria rational. The other important observation from this variant of the pure moral hazard game is one that will become recurrent. For post-electoral control to be effective without diversity of choice in candidates, the interests of agents and principals \( \Omega \) and \( \Omega^* \) need be aligned to some extent, otherwise there may be no \( \hat{\omega} \) that satisfies condition (2.11). Alternatively, the office rents \( b \) need to be high enough to induce agents to benefit sufficiently from retaining office in order to deviate from their ideal set of policies. The model appears to suggest that if agents are not interested in policy, the availability of
social status, bribery and patronage may be a way to incentivize them to implement (if only slightly) better policy. This is yet another initial observation that will emerge again in other circumstances.

In a compliance equilibrium, principals’ estimated total utility for Game 3 would be

$$U^v = \chi(k - 1) + \sum_{t=1}^{k} u^v(\hat{\omega}_t)$$

(2.13)

where $\hat{\omega}_k = \omega_k$. Even excluding the first term $\chi(k - 1)$, which represents the utility impact of the heuristic preference, the principals are still better off than in Games 1 and 2, where, at best, the agents would implement $\omega$. Of course, this improvement is contingent upon an acceptable level of congruence in the preferences of the principals and the agents. To underscore this point, it is helpful to note that a regime such as the Chinese which holds elections with vetted candidates (thus ensuring they do not diverge much in their $\Omega$ from the party’s) would function very differently if everyone in Politburo and on the list of candidates for municipal office had the policy preferences of a Pol Pot.

Meanwhile, any agent’s total expected utility in a compliance RE of Game 3 is given by

$$U = \sum_{t=1}^{k} u(\hat{\omega}_t) + \frac{bk}{|C|}$$

(2.14)

where the last term is the expected payoff from holding office. The expected office rents are completely independent from the dispersion of the conditional probability $f$. After further examination, this surprising result is perfectly logical:
since all agents must have the same equilibrium strategies and in every period someone has to hold office, the expected amount of office rents captured by every agent is the periodic amount $b$ times the number of terms available $k$ divided by the number of candidates for office $|C|$.

The separating condition (2.11) seems to confirm Fearon’s (1999) insight that, depending on the properties of $f$ (which in turn determines the conditional probability of reappointment $\theta$), there will be a “sweet spot” where the principals may be able to induce compliance by the agents. The impact of the conditional is thus contingent on its exact specification, making this a clear case of a model where the initial assumption (of the precise shape of the distribution) would decidedly affect an important part of the substantive results. Depending on that assumption of the shape of the conditional and the position of $\omega$ and $\hat{\omega}$, it may well be the case that less transparency (i.e., more dispersion in some region of the domain of $f$) leads to more leeway for a better policy without increasing office rents.

The type of constraint and the dispersion will also have an equivocal impact on the likelihood of retaining office. As a simple example, suppose that outcomes are real-valued, continuous and normally distributed with mean $\hat{\omega}$ (the policy implemented by the agent). If the rejection set of the principals is $\Omega \setminus \Omega^* = [-1, \infty)$ and the agent’s implementation is some $\hat{\omega} > -1$ that satisfies (2.11) and (2.12), an increase in the variance may increase the likelihood of being reelected because the normal tail area $\Phi(-1|\hat{\omega})$ will increase (which relaxes the constraint (2.11) and may make further concessions possible). Contrarily, decreasing the variance would at some point thin the tail enough to rule out that $\hat{\omega}$ could meet (2.11), which would result in a non-compliance equilibrium. Thus, even purely static analysis does not lend consistent support to the idea that transparency would improve performance and officeholders’ chances of reappointment in these conditions.
But the ambiguous effects of the outcome conditional $f$ are just about the least consequential property of the equilibrium set. Upon inspecting the separating condition (2.11) and the value of office (2.10) together, it is clear that increasing office rents in order to boost the allure of future office $\delta$ may increase the likelihood of a compliance equilibrium if other parameters (such as $f$ and $\Omega$) preclude it. To be sure, this is not necessarily an intuitive conclusion, but one that should be viewed cautiously because in the model rents are assumed to be costless for all parties and in reality they probably could not have that property.

Another interesting observation is that $\delta$ become larger and the constraint relaxes further if the constant $\lambda$ is smaller. This prior probability of being picked for office is inversely proportional to the number of candidates $|C|$, which suggests that even in an environment where agents are identical, more competitiveness may help induce more compliance. As $|C|$ increases and $\lambda$ decreases therewith, it becomes more difficult to be appointed if one is not an incumbent (i.e., engenders an incumbency advantage of sorts), which increases an incumbent’s implicit cost of not being reappointed.

Finally, the separating condition (2.11) becomes tighter for all agents as time passes, regardless of whether they have held office or not. Further into the game, there are fewer periods left to collect office rents and not being reappointed becomes less costly because $d\delta(t)/dt < 0$. As a result, the likelihood of compliance equilibrium policies will decline and those policies will become less attractive for the principals (if there is leeway in $\Omega$ to adjust away from $\hat{\omega}$ without jumping directly to the agents’ ideal $\omega$).

Overall, the pure sanctioning (moral-hazard) setting proves to be somewhat bizarre and dysfunctional. Without heuristic preferences punishing poor performance, there either are no rational equilibria or they involve always implementing the agents’ ideal. Even when heuristic preferences are introduced,
equilibrium policies are dependent on office rents, the disparity in preferences between principals and agents, and the clarity of the policy outcome captured by \( f \). The strength \( \chi \) of the heuristic preference itself does not have an impact on the equilibrium value of \( \omega \). It appears that in conditions of pure moral hazard, without real choice from a pool of distinct candidates, principals cannot credibly benefit from more transparent institutions. This result is robust to increasing the amount of heuristic utility \( \chi \), requiring it to reward good behavior or strengthening the heuristic preference to be lexicographic (i.e., to override other sources of utility).

Substantively, the ramifications are threefold. First, in circumstances where one-party rule or other forms of screening are present, high office rents and a politically activated populace, willing to go to the ballot box just to punish an incumbent, both are necessary conditions to ensure some level of responsiveness from the ruling elite. It is easy to imagine that such conditions would be extremely unusual and likely not sustainable for any considerable period. Ultimately, policies would be completely lopsided or the political framework would simply collapse.

Second, this is a prominent example of how non-essential assumptions can almost completely shape the results of a theoretical model. Granted that the effects of institutional transparency on political responsiveness are an object of critical research interest, they decidedly should not be analyzed in this theoretical setting (pure sanctioning). With a careful selection of the conditional outcome probability function and the preferred points of principals and agents, one could argue either way. The methodological lesson to be learnt is that perhaps assumptions should be made as late in model development as possible in order to make their impact on the results more transparent – or avoid making them altogether.

Finally, and perhaps this is the strongest implication, theory development based on pure moral hazard would be either misguided or unfruitful, particularly
when trying to understand the impact of institutions on agency control. With pure moral hazard, they simply do not appear to have much of one. Furthermore, the absence of rational equilibria in most environments and the weak results produced by heuristic preferences suggest that such conditions would not be sustainable in reality; a more diverse pool of candidates would have to come into play if policy responsiveness is to be guaranteed and improved.

**Observation 1.** Even in settings where the pool of eligible candidates is restricted to individuals with identical or constrained policy preferences or intentions, a more competitive field (a greater number) of candidates may induce better policy outcomes.

### 2.4.2. Pure Selection

Pure selection requires sincere agents – i.e., they genuinely attempt to implement some policy in the principals’ ideal set $\bar{\Omega} \ni \bar{\omega}$, – which entails a shift from a game-theoretic to a decision-theoretic mode of analysis. Agents have different skill levels, so that they end up implementing some policy $\omega^i$, which may not necessarily be the same as $\bar{\omega}$.\(^{18}\) Each agent is completely defined by his or her individual policy skill point $\omega^i \in \Omega$. The discrete set $\Omega$ containing the possible skill levels of the agents is common knowledge and each skill set is unique so that $|\mathcal{C}| = |\Omega|$.\(^{19}\) The type space can then be mapped by the prior probability mass function $m: \Omega \rightarrow [0,1]$ such that $m(\omega^i) = |\mathcal{C}|^{-1} \forall i \in \mathcal{C}$. Using this prior and observing a series of outcomes $\omega^j = \{\omega^1_j \ldots \omega^t_j\}$ over the $t \leq k$ periods when agent $j$ is

---

\(^{18}\) An alternative interpretation, where agents do have the same expected value of the policy outcome but different levels of dispersion of $f$ around it, yields similar results.

\(^{19}\) Overlapping and non-singleton skill sets can be reduced to this assumption, so it entails no loss of generality.
incumbent, a principal can generate a posterior probability $\gamma: \Omega \times \Omega \rightarrow [0,1]$ for $j$'s identity (i.e., the skill level or point $\omega^j$) using Bayes’ rule:

$$\gamma(\omega^i|\omega^j) = \frac{m(\omega^i)f(\omega^i|\omega^j)}{\sum_{\omega^i \in \Omega} f(\omega^i|\omega^j)} = \frac{f(\omega^i|\omega^j)}{|C| \sum_{\omega^i \in \Omega} f(\omega^i|\omega^j)}$$  \hspace{1cm} (2.15)

The total number of candidate agents $|C|$ is the reciprocal of the prior probability of picking any one agent in the first period $m(\omega^i)$; absent information about the identity of any individual agent, that choice will be random even if it is not intended as such. As before, to be able to compute a distribution over the possible identities for each agent, the principals must have the conditional probability $f$ for outcomes given policies implemented. The notation $\gamma(\omega^i|\omega^j)$ is equivalent to $P(j = i|\omega^j)$, where $i,j \in C$.

At the beginning of each period (except the first), the principals can choose from a smorgasbord of experienced agents as well as any agents who have not yet held office. Using the posterior (2.15), it is possible to compute an expected utility for the current period (denoted by $k$) from choosing some experienced agent $j$ by summing over the products of the probability that $j$ is $i$ and the principals’ expected utility $u^v(\omega^i)$ from the skill level of $i$. Denoting for brevity that $\bar{u}^v_k(\pi(i(k+1) = j) = 1) = \bar{u}^v(j)$, this estimate translates into the formula

$$\bar{u}^v(j) = \sum_{i \in C} \gamma(\omega^i|\omega^j)u^v(\omega^i) = \frac{\sum_{i \in C} u^v(\omega^i)f(\omega^i|\omega^j)}{|C| \sum_{\omega^i \in \Omega} f(\omega^i|\omega^j)}$$  \hspace{1cm} (2.16)

Since $\Omega$ and $m$ are assumed to be known, observations of incumbents’ results also provide information about inexperienced candidates. As the probability that a particular experienced candidate $j$ is of skill level $i$ increases, the
probability that any of the inexperienced candidates are that same type decreases. Thus, if the set \( \hat{C} \subseteq C \) contains all candidates who have held office \( j \in \hat{C} \), each with performance vector of observed policy outcomes \( \omega^j = \{\omega_1^j \ldots \omega_t^j\} \), then after observing \( k = \sum_{j \in \hat{C}} t^j \) outcomes, where \( t^j \) is the number of times candidate \( j \) has held office up to that point, the “residual” periodic expected utility of hiring an untested candidate \( c \in C \setminus \hat{C} \) would be

\[
\bar{u}^v(c) = \frac{1}{|C| - |\hat{C}|} \sum_{j \in \hat{C}} \sum_{\omega^i \in \Omega} \left(1 - \gamma(\omega^i | \omega^j)\right) u^v(\omega^i)
\]  

(2.17)

Therefore, before every (s)election, the principals will have available a \( |\hat{C}| \)-tuple of experienced candidates’ expected performances estimated through equation (2.16) and an expected utility for appointing an inexperienced candidate (2.17). Making appointments on the basis of these estimates (choosing the agent \( i \) with the highest estimated \( \bar{u}^v \)) would maximize expected utilities for the principals as a group within each information set, thus making such a strategy sequentially rational (the estimates are also consistent because the beliefs are derived using Bayes’ rule). Assuming consistent expectations, the total expected utility for a principal in a \( k \)-period game would be

\[
U^v = \frac{k}{|C|} \sum_{\omega^i \in \Omega} u^v(\omega^i)
\]  

(2.18)

The rationale reconciling (2.18) with all the information seemingly derived from (2.16) and (2.17) is counterintuitive but simple. Because the prior \( m \) in the first round of elections is uniform, the expected value of the principals’ first-period utility is just the average of the possible utilities from the different skill levels
known to be available. But observing an average first outcome does not provide any new information, so the first-period posterior is expected to be the same as the prior, hence the second-period expectation remains the same and so on. This is a paradox inherent in the widely used assumption of consistent expectations; it is practically equivalent to actors’ believing that they are omniscient.

**Proposition 2.4.** *Without an informative prior on the agents’ types (skill levels), principals in a pure selection setting are as well off making appointments on the basis of performance evaluation as they are picking appointees at random.*

This compares unfavorably with the principals’ expected payoff from the pure moral hazard setting with heuristic preferences (2.14), assuming that letting individual agents to their own devices would result in the same average expected utility for each of the two groups (i.e., that the average expected utility from the skill points of the agents in the selection model equals the expected utility from the ideal point of the agents in the sanctioning model). Even ignoring any utility from the heuristic preference, the principals in the pure moral hazard context would most periods expect to receive something closer to their preferred set than the average ideal point of the agents. Sinister but strategic one-party rule with office rents appears to be a better option than sincere incompetence.

**Proposition 5.** *Without an informative prior on the agents’ types, a pure selection model produces less desirable outcomes for the principals than a pure moral hazard model with heuristic preferences, even after controlling for any heuristic utility.*

**Observation 2.** *Naïve (non-strategic) candidates may produce worse results for the principals than strategic candidates with the same skills and/or preferences.*

### 2.4.3. Strategic Selection and Control

The mixed environment where both moral hazard and adverse selection come into play seems most promising for understanding principal-agent...
relationships. In such a setting, both agents and principals are strategically rational and there is diversity in the ideal policy outcomes of the agents (at this stage, no such assumption is made regarding the principals). Such strategic environments can become unwieldy and complex quite quickly. Finding an RE in this case is contingent on a larger number of parameters and assumptions about the game. The requisite level of specificity would inevitably restrict the domain of applicability of the theory. To avoid imposing undue limitations, it is better to flesh out the decision structure a little further but without new assumptions, rule out certain strategies and behaviors based on strategic rationality (Definition 2.1), then find the conditions for existence of RE and examine the properties of those RE sets and the separation conditions between them.

To analyze the strategic delegation setting, first it is needed to overlay its distinctive features over the generic agency game structure. The information structure is the same as in the pure selection case, but agents are strategic and, rather than by skills, they are completely defined by unique individual preferred-policy points $\omega^i \in \Omega$ and utility functions $u^i: \Omega \to \mathbb{R}$. Both agents and principals have knowledge of the ideal set of the candidates $\Omega$ and the familiar conditional probability distribution $f$ of outcomes given certain policies. Analogically to the pure selection case, it is helpful to define an office-value function $\delta: \mathbb{N}_1 \times C \to \mathbb{R}$ such that $\delta^i(k)$ is agent $i$’s value-added for holding office in period $k$. In other words, $\delta^i(k)$ is $i$’s opportunity cost of not being in office in period $k$.

**Game 4.** Consider a game of $k = 2$ periods. As with pure moral hazard, candidates’ dominant strategy must be to shirk if appointed in the last period – i.e., in any RE, it must be the case that $i(2)$ implements policy $\omega^{i(2)}$. If the principals dislodge agent $i(1)$ so that $i(2) \neq i(1)$, then the expected utility of any $i(1)$ for the second period would be
\[ \tilde{u}_{2}^{(1)} = \frac{1}{|C| - 1} \sum_{i \neq i(1)} u^{(1)}(\omega^i) \]  

(2.19)

Hence, \( \iota(1) = j \)'s expected value-added from holding office in the last period is

\[ \delta^j(2) = u^j(\omega^j) - \frac{1}{|C| - 1} \sum_{i \neq j} u^j(\omega^i) \]  

(2.20)

To be sequentially rational, any policy sacrifice by the first-period incumbent must be justified by a commensurate future benefit – in this case, an increase in the probability of being selected times the net benefit of being in office in the next period. Therefore, any optimal policy \( \hat{\omega} \) in period \( k = 1 \) would have to satisfy the constraint

\[ u^i(\omega^i) - u^i(\tilde{\omega}^i) \leq \left( \theta(\tilde{\omega}^i) - \theta(\omega^i) \right) \left( u(\omega^i) - \frac{1}{|C| - 1} \sum_{i \neq j} u^j(\omega^i) \right) \]  

(2.21)

where \( \theta \) is the probability of being reappointed for period 2. Any sequentially rational strategy of the incumbent in period 1 must therefore be to implement a policy in the set of admissible policies \( \tilde{\Omega} = \{ \omega \in \Omega: \omega \in u^{-1}(\tilde{u}), u(\omega) \geq u(\omega') \, \forall \omega' \in u^{-1}(\tilde{u}) \} \), where

\[ \tilde{u} \geq u^i(\omega^i) - \left( \theta(\tilde{\omega}^i) - \theta(\omega^i) \right) \left( u(\omega^i) - \frac{1}{|C| - 1} \sum_{i \neq j} u^j(\omega^i) \right) \]  

(2.22)

Using Bayes' rule as in equation (2.15), principals can derive a posterior probability function \( \gamma: \Omega \rightarrow [0,1] \) for what \( \iota(1) \) played given observed outcome \( \omega_1 \). Obtaining the posterior \( \gamma \) makes it possible to construct an estimator \( \epsilon^l \) of the
expected utility from the policy implemented – the utility $\bar{u}$ in condition (2.22) – for each possible type of incumbent $i \in C$:

$$
\epsilon^i(\omega_1) = \sum_{\omega^j \in \Omega} u^j(\omega^j) \gamma(\omega^j | \omega_1) = \frac{1}{|C|} \sum_{\omega^j \in \Omega} \frac{u^j(\omega_j) f(\omega_1 | \omega^j)}{\sum_{\omega^j \in \Omega} f(\omega_1 | \omega^j)} \quad (2.23)
$$

The estimator for the set of admissible policies is $\hat{\Omega} = \{\omega \in u^{-1}(\epsilon) : u^v(\omega) \geq u^v(\omega^j), u^v(\omega) \geq u^v(\omega') \forall \omega' \in u^{-1}(\epsilon)\}$, where $u^v$ is the principals’ utility function and the correspondence $u^{-1} : \mathbb{R} \to \Omega$ is the inverse of the agent’s utility function. In words, the estimated admissible set is the subset of the inverse of the estimated boundary utility by (2.22) that provides the greatest strictly better utility to the principals than the agent’s ideal $\omega^i$. Without loss of generality, let $|\hat{\Omega}| \in \{0,1\}$, so it makes sense to write $u^{-1}(\epsilon^i(\omega_1)) = \bar{\omega}(\epsilon^i)$. On this basis, the principals can assign a probability for the type of the first-period agent by using Bayes’ rule:

$$
P(\omega_1 | \epsilon^i) P(\epsilon^i) = P(\epsilon^i | \omega_1) P(\omega_1) \quad (2.24)
$$

Noting that $P(\epsilon^i)$ is just the prior probability of type $i$ and similarly $P(\epsilon | \omega_1) = P(\omega^i | \omega_1)$, expression (2.24) leads to the posterior probability mass function $M(\omega^i | \omega_1) = P(\omega^i | \omega_1)$ for the type of $i(1)$ given first-period observation $\omega_1$:

---

20 Should an agent have a non-singleton set of admissible policies, the RE prior probability of any one such policy having been implemented would be $|\Omega|^{-1}$, so it would be easy to substitute some average probability for $f(\cdot | u^{-1}(\epsilon^i))$ in the following equations.
The only sequentially rational decision rule is to reappoint \( \iota(1) \) if

\[
\sum_{i \in C} u^v(\omega^i) M(\omega^i|\omega_1) > \sum_{i \in C} u^v(\omega^i) \left( 1 - M(\omega^i|\omega_1) \right)
\]  

(2.26)

and to pick an agent from the pool \( C \setminus \{\iota(1)\} \) otherwise. In words, condition (2.26) simply states that the expected utility from reappointing the incumbent has to be larger than the expected utility from picking an agent at random from the rest. This condition translates further into the best response function

\[
\pi^v_2(\iota(1) = \iota(2)|\omega_1) = f \left( \sum_{i \in C} u^v(\omega^i) \left( M(\omega^i|\omega_1) - \frac{1}{2} \right) > 0 \right)
\]  

(2.27)

where \( J(s) \) is the indicator function such that \( J(s) = 1 \) if statement \( s \) is true and \( J(s) = 0 \) otherwise. Hereafter the notation \( \pi_2(\cdot) \) is used as equivalent to \( \pi^v_2(\iota(1) = \iota(2)|\cdot) \).

Thus, the RE strategy of the principals must be to pick an agent at random in period 1 and reappoint that agent if they observe \( \omega_1 \) such that (2.27) is satisfied, otherwise to pick a different agent at random for period \( k = 2 \). However, to show that an equilibrium may exist for some distribution of utility functions and also to be able to estimate expected RE payoffs, it is necessary to find the best-response function of the agents as well.

If \( \Omega_2 = \{ \omega \in \Omega: \pi_2(\omega) = 1 \} \) is the set of all outcomes that qualify an incumbent for a second term in office, then \( \theta(\omega) = P(\iota(1) = \iota(2)|\omega) = \)
Now that $\theta$ is computable, it is possible to find the sequentially rational set $\bar{\Omega}$ that also satisfies condition (2.22). Observe that $\bar{\Omega}$ cannot be empty; even if there is no admissible compliance equilibrium strategy, that just means there is an RE where agents play their respective ideal policy $\omega$ in every period. Dropping the scripts and substituting $\theta = \theta(\hat{\omega})$ in the admissibility condition (2.22) yields the first-period optimal policy condition for each type with solution set $\bar{\Omega} \ni \hat{\omega}$:

\[
(1 - \theta(\hat{\omega}))u^{i(1)}(\omega^{i(1)}) + \frac{\theta(\hat{\omega})}{|C| - 1} \sum_{i \neq (1)} u^{i(1)}(\omega^{i}) \leq u^{i(1)}(\hat{\omega}) \quad (2.28)
\]

Observing that if no concession policies are admissible $\omega^{i}$ always satisfies this admissibility condition by construction (2.22), it is also necessary to find the subset $\bar{\Omega}^* \subseteq \bar{\Omega}$ such that $\forall \omega', \omega'' \in \bar{\Omega}^*$ sequential rationality is ensured, i.e.:

\[
u(\omega') + \theta(\omega')u(\omega) = u(\omega'') + \theta(\omega'')u(\omega) \quad (2.29)
\]

Unlike the pure sanctioning case, every such game must have an RE since $\omega$ satisfies the sequential-rationality conditions when there are no other strategies that do: $\bar{\Omega}^* \neq \emptyset$ such that $\bar{\Omega}^* = \Omega$ or $\bar{\Omega}^* \subseteq \Omega \setminus \bar{\Omega}$. The non-compliance RE, where $\bar{\Omega}^* = \bar{\Omega}$, simply results in a special case of the pure selection model discussed in the previous subsection.

**Proposition 2.6.** The two-period game with strategic selection and control always has an RE.

Before delving deeper into the substantive implications of the characteristics of the RE set, some consideration should be given to the structure of the model. Introducing heuristic preferences in this framework would allow the
elimination of its main structural weakness – the assumption that there is a known conditional distribution of policy realizations \( f \). It is hard to construe a real-world scenario where principals would have anything even close to such a distribution at hand; and in a non-ergodic world it would be altogether inadmissible. A heuristic preference for punishing poor performance, however, would resolve the difficulty of operating in conditions of true uncertainty. Its impact on the results would not necessarily be in favor of improved policy responsiveness because it would induce more punishment, constraining the set of acceptable outcomes that would entice an incumbent to deviate from his or her ideal policy. Conversely, introducing office rents would increase the allure of getting reappointed, thereby relaxing the sequential rationality constraint (2.22)-(2.23) and potentially expanding the set of admissible policies \( \bar{\Omega} \), which would induce greater congruence of the agents’ equilibrium policies with the ideal policy of the principals. Rents that are not directly costly to the principals may include social status, on-the-job prestige or subsequent employment opportunities elsewhere. If office enjoys a high profile of this kind, the theory suggests that then agents are more likely to adhere to the interests of the principals. Other rents such as corruption and patronage for supporters already seem to be linked with higher policy responsiveness, at least anecdotally. Constituencies such as Illinois, New York and New Jersey are known for their political corruption and machine politics, especially at the municipal level, but also for their populist candidates, of which Franklin Delano Roosevelt is perhaps the best-known.

The value of office is important because incumbents’ strategies can be sequentially rational only if there are expected future benefits from a policy compromise (i.e., moving away from one’s own ideal policy) – in the form of an increase in their electability \( \theta \) and the value of future office \( \delta \). The constraints that determine the viability of compliance REs are affected by the nature of \( f \), the
outcome conditional distribution, which is object of so much attention in the literature, being interpreted as a representation of institutional transparency or clarity of responsibility. Model results in this substantive area would be driven almost entirely by the type of distribution assumed and its parameters. This is fundamentally a domain assumption and, absent empirical justification for assuming one way or another, no credible conclusions can be drawn about \( f \)'s effects. The normality assumption behind so much previous formal research is at best unjustified and misleading when applied to any complex and statistically “messy” formal setting.\(^{21}\)

Even without assuming a specific distribution, it is still possible to draw some conclusions about the nature of the possible equilibrium strategies. Keeping the distribution of agents’ types \( \Xi \) the same, the expected utility of the principals with strategic selection and control is always at least as good as the one they get with pure selection. If there is a non-compliance RE, they can expect the average utility of all the agents’ ideal policies \( |C|^{-1} \sum_{\omega^i \in \Xi} u^v(\omega^i) \) in period 1; and the expected policy as well as its realization is that same average. Observing the average would make them indifferent between removing or keeping the incumbent, so in the second period they get the average yet again, leading to a total expected utility

\[
U^v = \frac{2}{|C|} \sum_{\omega^i \in \Xi} u^v(\omega^i) \tag{2.30}
\]

\(^{21}\) This is a reference to the use of the normal distribution in formal models, not to its application in the statistical models used to test those formal models.
In a compliance RE, at least one of the agents will implement a compromise policy $\hat{\omega}$, which is better for the principals than just the agent’s ideal $\omega^i$. Additionally, the expected utility of the policy implemented in the first period is the average of all the equilibrium first-period policies, so again there is no signal as to whether to keep or replace the incumbent. Thus, the second-period expected utility is again just the average $|\mathcal{C}|^{-1} \sum_{\omega^i \in \Omega} u^v(\omega^i)$, so the principals’ entire expected utility gain is from the first-period compromise policy, not directly from acting upon the signal it sends about the type of the incumbent. Their compliance RE expected utility would then be

$$U^v = \frac{1}{|\mathcal{C}|} \left( \sum_{\omega^i \in \Omega} u^v(\hat{\omega}^i) + \sum_{\omega^i \in \Omega} u^v(\omega^i) \right)$$

(2.31)

where $\hat{\omega}^i \neq \omega^i$ at least for some $i \in \mathcal{C}$ and $u^v(\hat{\omega}^i) > u^v(\omega^i)$. Therefore, the expected utility in a compliance RE (2.31) is greater than that in the noncompliance RE (2.30) of Game 4 and in the pure selection model (2.18).

**Observation 3.** The expected utility of the principals with fully strategic agents is as good as or better than that with naive (non-strategic) agents (i.e., in pure selection).

The results of Game 4 and all the models taken together seem to lend fairly strong support to the preponderant belief that type selection dominates sanctioning as an enforcement mechanism. On one hand, the results of the mixed model closely resemble those of the selection model. On the other, the very mechanism whereby the principals’ strategy is derived is entirely focused on distilling a signal about the type of the agent in office during the first term. While these observations are not far from the truth, they present a somewhat lopsided view. The key takeaway regarding the dominant enforcement mechanism goes much deeper. Sanctioning is less effective because the principals cannot commit to
actually dispensing the punishment – or providing the reward (in the absence of heuristic preferences to punish underperformance). Nevertheless, the optimization mechanism of the agents is one entirely based on the logic of sanctioning because they simply have no other avenue to signal their type. Thus, contrary to what scholarship has long assumed, type selection works though the credible path of retrospective rather than the unreliable prospective signaling. This theoretical result is supported by recent experimental data showing retrospective performance concerns dominate voting behavior (Woon 2012) and empirical data demonstrating no behavioral impact from position-taking during election campaigns (Adams, Ezrow and Somer-Topcu 2011).

**Observation 4.** Type selection is the dominant enforcement mechanism and it produces more representative policy with strategic agents than with naïve ones.

What is truly significant, however, are the separating conditions which determine whether there is a compliance RE. Several factors can unequivocally improve at least some policy responsiveness from the agents. The sequential rationality conditions (2.28)-(2.29) suggest that, first and foremost, there needs to be a reasonable level of alignment between candidates’ and principals’ interests. If Ω is too far from the preferred set of the principals, no amount of transparency would be able to forestall a non-compliance RE.

The internal distribution of Ω itself is rather consequential as well. It would be particularly favorable if the ideal policies of the principals are “closer” in utility to those of the agents than the agents’ are to one another. The principals may achieve better compliance from the incumbents because being replaced in office carries a higher cost (of a more divergent policy being implemented instead of one’s own), yet compliance itself is cheaper than otherwise. As the dissimilarity between agents’ preferences (relative to their remoteness from the principals’ preferences) increases, incumbents become less willing to risk being replaced. A
diverse field of agents may function as an indirect way for the principals to divide and rule. Candidates, not the ballot box, are at the crux of political power and representation. And the rulers of Latin America’s nondemocratic regimes seem to have appreciated this fact:

preelection tools of manipulation have a strong reductive effect on [the effective number of legislative parties], whereas, perhaps surprisingly, ballot fraud does not. This implies that election day rigging is relatively ineffective at reducing party competition and may be used as a last resort by incumbents in an already weak position. [M]isconduct intimidates and deters opposition parties’ entry [and] is associated with fewer parties running in the election. […] A reduction in party system size below its expected level implies a mismatch between voters’ true preferences and the ensuing – biased – electoral outcome, while the deterrence of opposition party entry creates a de facto “representation gap”. (Donno and Roussias 2012, 577–578)

Sanctioning plays second fiddle at best. The nature of f is relevant to policy choices only when the field of candidates is already aligned somewhat favorably with the preferences of the principals. The effects of competitiveness and accountability are not readily separable, but mutually contingent; they become relevant and determinate only in particular configurations with one another, a conditional relationship with profound implications for the empirical evaluation of democratization, accountability and representation theories.

**Observation 5.** The lesser the preference divergence between agents and principals, the more likely is equilibrium policy to move towards the ideal of the principals.

**Observation 6.** The more diffuse the field of candidates in a delegation game, the more likely is equilibrium policy to move towards the ideal of the principals.
2.5. IMPLICATIONS AND EMPIRICAL EVIDENCE

Together, the results suggest that the decisive factor for the representativeness of a political system is not so much its transparency as the competitiveness of the field of candidates for office and their a priori alignment with the interests of the represented. One of the main implications of the theory is that political competition is a critical driver not only of policy responsiveness, but of systemic stability. Systems that can engender and channel political competition are the ones which must exhibit institutional resilience. Rational equilibria, an indicator of a stable institutional arrangement, can only be found in cases where divergent policy preferences can become manifest in the policy output, whether that divergence is among the candidates or between the incumbent and the principals.

The mixed-enforcement model, in particular, effectively pictures a microcosm of electoral representation that renders strikingly relevant Schumpeter’s (1942) vision of democracy as a system of competition between elites rather than one of direct programmatic representation of the masses in government. It is only when genuine elite competition is present that democracy can don its cloak of representativeness. This concept of democracy casts in a different light some widely accepted views about clarity of responsibility and the broader performance of democratic institutions. The transparency of policymaking itself appears to be of secondary importance and not necessarily conducive to normative goals; the system’s capacity to generate viable candidates, preferably somewhat congruent with the electorate, may be the leading determinant of representation and policy responsiveness. The impact of institutions on developing political capital, upgrading candidate quality and improving elites’ governing capacity may be of greater significance than their
direct effects through the delegation channels of elections, governing coalitions and bureaucracies.

There is substantial evidence of elite-competition mechanisms at work in one of the most ossified and gerrymandered representative systems in developed democracies. Investigating the agenda and voting records of members of the US House of Representatives after rounds of redistricting, Hayes, Hibbing and Sulkin (2010) discover “impressive”, consistent and, to them, puzzling levels of responsiveness to demographic and partisan shifts in the constituencies. The type of redistricting rules (partisan or nonpartisan) and (the changes in) the electoral margin appear to have no effect on the level of responsiveness. Nor do party, seniority or vulnerability. The authors cannot even identify a potential causal mechanism for their finding, attributing it to “risk aversion” (i.e., towards sudden and unexpected loss in the next election).

The clear and plausible explanation of this unexpected responsiveness is related to the formation of political capital. Incumbents may be preempting the mobilization of potential voting coalitions powerful enough to mount a consistent challenge, build a political organization and, over time, groom a viable contender for the seat from within or without the incumbent’s party. This preemption does not require that the member please everyone or merely his or her voting bloc. Rather, the legislator must seek to preserve that bloc while sowing division among potential voting coalitions outside of it by appealing to one group or another. The measure of success may not be an increased vote share but rather immobilizing a group that is a core component of the potential rival coalition that can field a viable challenger over time.

Rigby and Wright (2013) suggest such cross-cutting appeals by Democrats to the wealthy and by Republicans to the middle class are a routine part of American electoral politics. Meanwhile, the poorest are underrepresented and
responsiveness to the upper class increases where inequality is higher. The authors conjecture that this would be due to lower turnout by the lower class, but do not differentiate the mechanism in their empirical analysis. Even in theory, the turnout argument would likely only produce a slower movement towards the lower class, not that “in states with higher levels of income inequality, Democratic party positions were even more highly skewed toward the rich [but empirically] neither patterns of electoral success nor income bias in voting explains [sic] the differential responsiveness” (Rigby and Wright 2013, 562). The explanation may be that the lower class cannot field viable contenders, therefore is effectively excluded from the computation of the electoral median. Higher levels of inequality make it less likely that a Democrat will face a challenge from the left because the poor get poorer and even less capable of mobilizing, aligning with other income groups or developing candidates. Inequality might also make the middle class feel more threatened from below, thus less likely to form a coalition with the poor against the rich. Responsiveness does not require a change of the guard, just a change in the competitive dynamic and the alignments of different voting blocs.

In a reversion of this unanticipated responsiveness in US elections, but again through the mechanism of restricting credible competitive entry, tight partisan control of candidate selection overturns centrifugal institutional forces in Lithuania’s mixed-member system:

MPs representing single-member districts voted against their party less than proportional representation (PR) MPs from party lists […] due to the fact that SMD candidates were selected by central party leaders, while PR candidates had a broader selectorate. In a parallel way, dual-listed PR MPs whose preference votes came mostly from the SMD district in which they were nominated by their party behaved like “pseudo-SMD” candidates and defected from the party line less than PR MPs whose preference votes were
more geographically dispersed. Both of these results support the idea that selectoral incentives can dominate electoral incentives. (Preece 2014, 122)

Competitive dynamics trump expectations about institutional effects on responsiveness. Instead, institutions must have an indirect long-term effect on responsiveness by shaping the competitive dynamics through their potential effects on the development of political capital.

Competitiveness, at the nexus of political institutions and social cleavages and conceptualized as the availability of a diverse set of viable candidates, can be a powerful modifier not just of policy responsiveness and effectiveness, but also of other – intermediate – institutional phenomena such as regime stability, party realignments and government duration. It is related to the accumulation of political capital, which can be defined in three distinct dimensions of candidate quality: electioneering skills, experience in governance and specialized knowledge. A system with greater political capital would have more candidates with a record of electoral competition, proven abilities to manage people and create policy in some organizational setting, and a pool of candidates that encompasses a diverse set of issue-specific expertise. The remainder of this section outlines recent evidence for the impact of (often only implicit) competitiveness and sketches out its implications for further research.

2.5.1. Parties, Elections and Voting Behavior

The compliance RE conditions require some rethinking of rational-choice notions of strategic voting and already are finding support in empirical research. The rational-choice literature on strategic voting that started with the simplistic goal of maximizing seats (Cox 1997) has moved forward to a more sophisticated view including coalitional and policy concerns (Duch, May and Armstrong 2010; Indridason 2011). Scholars on both sides of the ideology-valence debate are
looking for ways to reconcile these viewpoints, which appear to be sides of the same coin (Duch and Stevenson 2011; Sanders et al. 2011). Some strands of the discipline are beginning to recognize and even finding evidence for competitive conditions’ central role in the calculus of voting, especially in a strategic context.

Some students of economic voting, perhaps the best-documented phenomenon in electoral behavior, are already arguing that much of the variation in its potency can be explained by the nature of the competitive landscape, not just by dilutive coalitions and veto players in government. Parties are less likely to lose votes if they are part of a minority or grand-coalition government, conditions suggesting lack of effective competition (Powell and Whitten 1993; Duch and Stevenson 2008). Likewise, “a fragmented opposition does not induce as much vote transfer even when the government is not popular” (Maeda 2010a, 433).

Economic voting is largest for opposition parties that are in competition to produce the next premier and is rather subdued for perennial cabinet parties and for incumbents that have no chance of becoming part of the next executive. Conversely, voters are willing to punish poor performance if there is clarity of responsibility and alternatives are available. Most of 16 Latin American presidents who used bait-and-switch tactics to impose neoliberal economic policies in the 1990s studied by Stokes (2002) did not win reelection afterwards. Some evidence even suggests voters see as electorally distinct presidents running for reelection, their anointed successors and intraparty rivals (Ferrari 2015).

The impact of competitive dynamics extends to the even more significant issue of turnout. Lack of competitiveness diminishes both heuristic (valence) and instrumental (spatial) incentives to turn out. A significant portion of the decline in turnout for US House elections can be attributed to the decline in their competitiveness precipitated by institutional factors (Engstrom 2012). Indeed, parties which engage in coalition politics may have an inkling of these facts as they
seek to distinguish themselves from their partners, especially before elections (Martin and Vanberg 2008).

One badly understudied and potentially game-changing aspect of electoral systems are campaign-finance rules, which may have profound influence on both selection and compliance dynamics. Fund parity, defined as limits on campaign donations and spending as well as access to free media time and public funds for smaller parties, has a positive relationship with party competition, increasing the effective number of parties (Potter and Tavits 2015). Parties play an important role in building and maintaining candidate quality (Snyder and Ting 2011). More parties, at least in a consolidated democracy, must therefore be conducive to more variety of policy choices and the accumulation of political capital, which must enhance overall policy responsiveness, according to the model. The unexplored portion of the causal path is whether in advanced democracies with long-standing professionalized bureaucracies parties can really affect outcomes as swiftly – do policy changes follow policy effort or circumstance (Blais, Blake and Dion 1993)? Further, is there a nonmonotonic relationship between democratic consolidation and policy responsiveness, the latter increasing with democratization and then declining as policymaking becomes more institutionalized or bureaucratized?

Given the dominance of selection mechanisms over sanctioning, the theory predicts that the personal vote would retain some significance even if ideological voting dissipates for institutional or societal reasons. Even in low-salience elections for the European Parliament, which voters habitually use just to punish their national governments, there is evidence that “parties choosing a ‘high-quality’ representative are indeed rewarded by voters. This effect is strongest in the middle of the national electoral cycle” (Hobolt and Høyland 2011, 497), when partisan-programmatic influence is weakest. As valence theory has been gaining ground on spatial models of voting, there are even suggestions that, to the extent
that it does, policy only matters because it has an impact on perceived competence (Sanders et al. 2011). The personal vote is a critical aspect of the competitiveness and effectiveness of the political system. In the near-perfect majoritarian institutions of Westminster, “big beasts of the jungle” – politicians endowed with the support of some sectoral interest and considerable personal influence and political aptitude – can make plenty of trouble for a presumably all-powerful executive (King and Allen 2010). Open primaries are a particularly powerful tool for improving candidate quality and ensuring competitiveness. “[T]he introduction of primaries would strengthen the voter's incentive to select good types, because a voter no longer needs to discipline a ‘bad’ incumbent from a favored party by electing a candidate from an unfavored party [and] reduce the ability of incumbent officeholders to shirk” (Snyder and Ting 2011, 794).

2.5.2. PARTY GOVERNMENT

Applying the model’s logic in the context of coalition formation in parliamentary government draws attention to a largely understudied aspect of bargaining, monitoring and survival dynamics. Looking at political parties or party leaders as the principals and at backbenchers and party grandees as the pool of candidates, it can be hypothesized that parties with deeper benches of qualified candidates and with some level of diversity around the “party line” would find it easier to form cabinet coalitions and keep them stable for an entire mandate. Parties with smaller or more homogenous executive capacity on their slate will be less likely to participate in cabinets directly and the systemic prevalence of such parties may make minority governments more likely. The rationale is straightforward – when political capital is low, it would be much more difficult to find agreeable appointees who inspire partner parties’ confidence that coalition agreements will be upheld. Again, the competitive dynamics should not be
overlooked in this context. If extra-coalitional parties have poor executive capacity, that would make the incumbent coalition even more stable. Coalitions rich in political capital would also be likely to engage in less extensive legislative (Martin and Vanberg 2004) or junior-ministerial (Martin and Vanberg 2011; Thies 2001) monitoring of cabinet members’ portfolios relative to coalitions without that many qualified operatives. This effect should be sustained even when controlling for the legislative size of the party.

2.5.3. MAJORITARIAN VERSUS CONSENSUAL VISIONS OF REPRESENTATION

In view of the importance of competitiveness for representation and of the recent empirical evidence on the development of political capital, it is also possible to venture a response to the perennial question of whether majoritarian or consensual government is most conducive to achieving the normative goals of democracy. From a competitiveness perspective, neither is a good option. Proponents of majoritarianism contend that it provides necessary clarity of responsibility for political accountability and policy responsiveness; advocates of consociational and other forms of consensus democracy argue that their vision allows the inclusion of a broader set of interests in policymaking and channels political conflict more effectively. In the extreme, however, both approaches suppress the competitiveness of the political system. A majoritarian electoral system with strong parties and unified government would exclude many qualified candidates for ideological reasons and suppress representativeness in the long-run because new ideas will have a hard time getting out onto the public arena. Meanwhile, the indecisiveness of a fragmented consensual system with grand coalitions and many veto players would disincentivize qualified candidates from even considering a career in government. Furthermore, the all-inclusive establishment working together would likely be able to block or deter political
entrepreneurs from entering the fray in an even more effective way than majoritarianism would.

Non-majoritarian institutions, albeit perhaps not full-blown consociationalism, may be a desirable precondition for maximizing democratic capacity. For example, there is mounting evidence that proportional representation increases the competitiveness of local elections (Eggers 2015). However, the system has to concentrate power just enough to make policy change possible and entry worthwhile. The fact that political systems reflective of Lijphart’s consensus-democracy model seem to have ended up in an electoral condemnation of it (e.g., Rose 2000) suggests that competition between distinct options is the glue that binds together the masses and the ruling elites. An institutional setting that would maximize competitiveness should on one hand combine consensual characteristics such as proportional representation, open primaries and/or preferential ballot lists, allowing voters to select the candidates they prefer without undermining generalist policy objectives. On the other hand, it would include majoritarian decisiveness characterized by parliamentary government, strong parties (i.e., campaign-finance restrictions) and fewer “independent” agencies, ensuring that the best candidates will enter political competition in the first place and that their efforts will affect policy through a clear line of control. These are the basic outlines of what could be termed a Schumpeterian ideal of robust elite competition.

2.5.4. Responsiveness in Presidential versus Parliamentary Systems

Strøm (2006) argues that presidential systems are less susceptible to moral hazard because the governmental institutions with competing powers watch over one another’s shoulder. But he concludes that from a principal-agent perspective parliamentary government still seems better because, despite its opaqueness and
the starker information blindness for both opposition and electorate, strong parliamentarism is well-equipped to handle agent selection. He seems to find these ex ante controls a better deal for constituents than the mostly ex post controls of presidentialism. The theory provides formal support for his intuition, certainly insofar as pure moral hazard does not appear controllable. Therefore, presidentialism can be representative (and stable) only with a robust balance of power so as not to inhibit the formation of political capital and the fielding of high-quality (rival) candidates.

In this line of reasoning, the theory also makes an important contribution to the quarter-century-old debate about the merits and demerits of parliamentarism and presidentialism. The model suggests a potential source of unresponsiveness and instability in certain types of presidential systems that inhibit competitiveness and the development and accumulation of political capital. The principals’ ability to affect policy is channeled through effective competition between candidates and is contingent on candidates’ ability to affect policy. Competition is more robust when there are viable candidates on as many sides as possible from the representative voter, which requires a robust party system.

In a presidential system, there are two critical channels for fielding such candidates – subnational governments and the parliamentary opposition. Thus, it is reasonable to expect that presidentialism will be more unstable (i.e., more predisposed to slipping into authoritarianism or civil unrest) if these channels are obstructed either constitutionally or by the party system (that would induce a situation similar to the pure moral hazard setting – but with a small, not just homogenous, field of candidates). Paradoxically, presidentialism seems to fail not because it encourages interbranch conflict and creates gridlock, but because it fails to implement the effective separation of powers that would engender the
competing centers of power that spur political-capital accumulation. Government instability under presidentialism is associated with strong presidents and weak legislatures and party systems, which make it less costly to engage in transactionalism (Martínez-Gallardo 2012), as opposed to programmatism, and to suspend democracy if needed.

Parliamentary parties would likely be inhibited in developing high-quality contenders for the executive in hybrid systems where the executive has legislative powers, particularly if there is line-item veto in budgeting. Competition for the executive would also be stifled if parliamentary parties simply are weak (regardless of their budgetary authority) for other reasons, which would change the cost-benefit balance between being co-opted by the executive and the potential to take it over. Weak parties mean legislative candidates will have small (possibly territorial – district-level) power bases, which would make attempts at gaining executive office less likely to succeed. A disproportional electoral system (e.g., first-past-the-post, majoritarian or at-large districts) with regional cleavages (so that national parties cannot cohere) would likely induce party weakness of this type.

Among other reasons, a strong party system (but with numerous parties) is important for building political capital because parties can play a significant role in reducing transaction costs when aggregating diverse sources of expertise. There is a tradeoff between being able to leverage different skills and viewpoints in large groups and getting good policy decisions (Krause and Douglas 2013), which can be managed by the hierarchical structures of political parties. High-quality experts would not be enticed to enter and politicians would not be encouraged to cultivate specialized expertise in a chaotic environment producing mediocre policy through the meat grinder of groupthink. Thus, one way that strong presidentialism may impair the development of political capital and representativeness is by a
propensity to allocate cabinet positions to “nonpartisan” experts who are more likely to be loyal to the president (Martínez-Gallardo and Schleiter 2015). This undermines legislative parties’ ability to develop and lay claim to executive capacity and governing expertise, which effectively weakens the competitiveness of the system. Weak parties simply cannot provide the career opportunities that would motivate investments in specialized knowledge and attract the most qualified political entrepreneurs. Where cooptation reigns, competition flounders.

Meanwhile, to be a significant source of political capital for national politics, competition at the subnational level would require more than token decentralization and delegation from the central government. At least three distinct features are necessary to ensure the subnational tiers’ ability to sway presidentialism towards greater stability and responsiveness. First, local and regional units’ executives should be directly elected, not appointed by their legislatures or by the national government. Second, subnational units should have independent fundraising authority, preferably through taxation, not merely fees and fines. Third, and this is an often underappreciated feature of grassroots competitiveness, local parties should be strong but independent from national parties, which means national parties should not have control over their nominations and campaign funds. The idea that the recruitment power of parties has an impact on institutions further up the power structure is far from novel (Swenson 1982), however it does not often appear front and center in institutionalist analysis. There is some evidence that recruitment power can even invalidate the effects of the personal vote (Preece 2014), thus it is all the more important that if national elites are coopted by a powerful president, they cannot stifle the accumulation of political capital at subnational levels.

Powerful presidents seeking to consolidate their regimes seem to be appreciative of these dynamics. One of the first major constitutional changes that
Vladimir Putin made after becoming president of Russia was to abolish the direct elections of provincial governors and make them presidential appointees. While governors never had the sort of authority that could not be overruled by the federal government if necessary, direct provincial elections were an effective way for potential presidential rivals at the national level to gain experience and credibility. This pattern of undemocratic-regime consolidation is far from unique to Russia, as becomes clear in the following section.

2.6. TOWARDS A POLITICAL-CAPITAL THEORY OF DEMOCRATIZATION

The theoretical implications and the empirical findings associated with the agency model coalesce around one of the most jarring puzzles in positive political science – what determines the success or failure of democratization. There are three sets of approaches\(^{22}\) to understanding the transitions between conditions of democracy and non-democracy. Perhaps the oldest one is the sociological modernization theory pioneered by Lipset (1959; 1960). In this view, as societies become industrialized and urbanized, they build the social capital necessary to mobilize publics and pressure elites into democratic reform; rising standards of living and more and more people moving up Maslow’s pyramid of needs generate the demand for such change. This theory’s empirical record is mixed at best because there are numerous examples of very rich consolidated autocracies and theocracies (e.g., most of the Persian Gulf states) as well as not so rich democracies (e.g., India after 1947, Ireland after 1922, Finland after 1917).

\(^{22}\) There are numerous other significant contributions on conflict-resolution and democratization, including those of Lijphart (1977; 1999), Horowitz (1985) and Laitin (1986), which are omitted from this brief typology as they are not expressly focused on identifying a non-interventionist approach to democratization.
The redistributive approach manifest in the work of Boix (2003) and Acemoğlu and Robinson (2006), among others, suggests that the timing and success of transitions are contingent on the distribution of wealth or income as well as their absolute level. In this view, democracy can succeed when societies have moved up the income ladder, but incomes and wealth are at a middling level of concentration, so that dictatorship cannot consolidate in a poverty or natural-resource trap. There are some disturbingly powerful counterexamples to these theories. The United Kingdom in the 1860s and the United States in the 1900s implemented – at a mindboggling pace – some of the most radical electoral and governance reforms in their history at times of record income inequality. Neither of those places descended into chaos or reverted to dictatorial rule in the following decades.

Finally, there is the elite-led transition approach proposed by Przeworski (1991), which, unlike the previous two, attempts to pinpoint a very specific causal mechanism but lacks a large empirical literature behind it. In this neoliberal reading of modernization theory, free markets and open economies as well as rising income levels bring societies to a tipping point of transition, but the outcome is contingent on elite conflict and bargaining. Elites and reformers bargain to redistribute power and benefits, with five different outcomes possible depending on their information and transaction costs. Przeworski does not map an empirical research agenda that could measure and disprove the outcomes and the variables that affects them in a convincing way.

What all three approaches are badly lacking is a logically compelling and empirically valid path leading from conditions for democracy to a functioning democracy much like biologists are still missing the bridge from the primordial soup of organic compounds to life itself. Thus far, institutions have been regarded as valuable and significant because of the particular ways in which they channel
conflict and translate interests into outcomes, but have been conspicuously absent from modernization theory and its refinements. Representativeness and the transparency that is perceived as necessary for accountability have long been held as the leading desirable features of democratic institutions. However, they may have a much more important long-term role in creating the supply of professional politicians and a functioning political marketplace that can become a more attractive venue for conflict resolution than violence or smoke-filled rooms. In that marketplace, the more sophisticated political demands of economically developed societies can meet the supply of skilled political operatives. This is the essence of a political-capital theory of democratization (PCT).

Stable institutions probably are not just the outcome of democratic transitions but an inherent part thereof. The critics of presidentialism have had a pretty strong inkling of this fact, but have focused on institutions as outcomes and as second-order conditions for reversion to dictatorship rather than on their role in democratization. What is common among societies that have transitioned to democracy without reverting back to dictatorship is that they have sustained through that process longstanding institutions of political competition. Transitions which have established such institutions abruptly, no matter how democratic, mostly seem to have failed. To be successful, transitions must not destroy but rather coopt the political capital – electioneering, legislative and administrative skills – accumulated in the old institutions (if there had been any) and even the established elites that can support or subvert a transition.

Building on the insights of prior democratization theories, and particularly the work of Lipset, this section locks onto three core sets of questions that the political capital theory of democratization based on Schumpeterian democracy aims to address:
1. What is the mechanism whereby non-democracies transition to democracy and consolidate within it?

2. What is the role of institutions, if any, in that process?

3. What practical prescriptions follow from the theory that could help the normative goals of advocates for democracy?

2.6.1. STATEMENT OF THE POLITICAL-CAPITAL THEORY

The democratization process goes through three general stages and can oscillate back and forth repeatedly before democracy becomes consolidated. The first key ingredient of that process is economic development, whose societal and transactional effects need no further elaboration given Lipset and others’ exhaustive treatment. This is, by and large, a proxy for technological advances and patterns of communication and coordination that grow exponentially in their complexity and require new skills and new types of social interaction to be managed effectively and taken advantage of. As economies move from agrarianism to industrialism, feudal tribalism is displaced by oligarchic clientelism as the predominant form of sociopolitical organization. Tribalism is hierarchical and mass obedience is motivated mostly by a struggle for survival; social bonds are at the village or guild level, whereas feudal lords frequently compete with one another by violence and coercion.

With industrialization and urbanization, tribalism can no longer perform its functions and significant parts of the population outside the elite have moved beyond survival and towards consumerism and climbing the social ladder. Increasingly sophisticated administrative organization is necessary to manage growing cities. Landed and oligarchic elites coopt numerous members of the lower classes to fill those roles. Appointed or newly elected public officials establish client networks both to get the job done (so as to keep it and/or profit from it
through graft) and to gain more power. The management of these networks and keeping one’s position requires considerably greater sophistication than tribal relations within the family, in the village/guild and with the seigneur. The oligarchic lords compete mostly through the markets, the courts and by peddling political influence – channels that, unlike violence, do not lead to major disruption of profit or client networks. Meanwhile, political institutionalization expands under oligarchic clientelism as capitalists seek to push the landed aristocracy aside and regulate commerce. The oligarchs expand the number of elected positions to coopt or buy off the middle class and appease the mobilizing workers with promises of a (marginally) better life. As incomes rise and technology advances, client networks proliferate and expand – growing in number, reach and complexity, they become most valuable assets, worth the skills needed to protect them. The growth of client relations itself triggers strong demand for and increases the value of political capital, which can subsequently be transferred to the next – programmatic stage of political organization. Non-democratic and corrupt clientelistic institutions such as the rotten boroughs of Georgian Britain and the political machines of the American Gilded Age are the highly competitive institutional instruments that produce that political capital. Without them, political capital is much harder to accumulate and restricted to a narrower segment of the population; if they are annihilated by a transition overnight, the capital account is itself set back significantly. In either case, when true democratic institutions are set up in their stead, there are too few powerful agents with a vested interest in them or with the skills to operate them. This makes it much easier to generate the demand and take advantage of the opportunity to overthrow a newfangled democracy.

Political capital is a necessary ingredient for democracy to consolidate and survive continually; the competitive non-democratic institutions that facilitate its
accumulation before and its preservation after the transition to democracy are the missing link in modernization theory.

2.6.2. PATRONAGE AND CLIENTELISM – BUILDING BLOCKS OF DEMOCRACY?

The non-disruption of clientelistic political capital during the transition characterizes (seemingly) successful transitions to democracy. Britain and France both had failed revolutions before taking a more gradual and successful path to democracy. Those two as well as the Scandinavian countries, Belgium, Nederland, Canada, the United States, Australia and New Zealand all democratized gradually and successfully in the late 19th century without destroying the institutions or elites that had built their oligarchic governments and their clientelist institutions. In building successful democracies, both Ireland and Finland largely preserved existing colonial institutions, which were characterized by non-democratic elections and administration by local client elites, as well as much of the elites that operated them. As a rule of thumb, all these states had institutionalized clientelism as well as some form of open elite competition for political power for some 50-100 years before undergoing a gradual transition to much greater democracy, conditional, of course, on economic development. Similar, processes seem to have been at work in post-Soviet Europe, some parts of Latin America in the early 21st century and in parts of Asia such as Japan and South Korea.

Svolik (2013) has already suggested that electoral accountability has to do with democratic consolidation, but on reputational grounds. If the polity experiences economic shocks before politicians have developed reputational barriers to entry by inferior types, the transition may fail. PCT suggests that during

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23 Female suffrage is excluded here to avoid clumping all cases to the 1920s-1940s period and highlight the minimally needed duration of the clientelist institutions.
the dictatorship period, electoral and other competitive institutions precipitate the accumulation of real political capital. Combined with continued development and a peaceful democracy, that political capital provides for democratic consolidation after reform. The key part of the mechanism is that institutions begin to function, albeit aberrantly, before democracy takes place; political and administrative elites develop around them. Others have already made arguments about the relative costs and benefits of institutionalized channels of conflict resolution versus alternative arenas such as street protests (Scartascini and Tommasi 2012) or violence. But such “explanations” are effectively begging the question. If stability is dependent on institutionalization, what is the difference between the two and what causes them? Rather, through competition for office and incentives to invest in relevant skills, institutionalized competition engenders over time powerful groups of people who have a stake in the survival of the institution. During this incubation period, institutionalization must be nursed in some form of dictatorship – whether foreign occupation or authoritarianism – that takes on the burden of building institutions for its own consolidation purposes. Then, even as nondemocratic institutions are gradually replaced, the residual political elite needs the new institutions to be able to benefit from its political capital and is more likely to support them rather than resist.

The political-capital hypothesis is supported by Kitschelt and Kselman’s (2012) finding that clientelism increases with economic development until a country reaches intermediate levels, as in the American case, while programmatic politics increases monotonically. Meanwhile, “[r]epeated rounds of electoral competition are associated with more credible and well-established organizational structures, which in turn facilitate the use of clientelistic electoral strategies” (Kitschelt and Kselman 2012, 1455) and over time provide the elite capacity to implement policy. However, democracy itself is not necessary for the elite
formation process to take place; party structures and elections can take place under nondemocratic regimes: “parties endowed with the organizational capacity to engage in clientelist targeting tend to be either (a) parties with roots in antecedent authoritarian regimes or (b) parties that have built their organizational reach over successive democratic elections” (Kitschelt and Kselman 2012, 1477).

Economic development and mobilization alone are not sufficient to ensure the success of a transition. Even though redistributive conflict may well trigger one, without the counterweight of clientelist political capital, a reversion to nondemocracy or institutional collapse is more likely. Political capital increases the cost of disrupting the institutionalized system and makes it easier to meet the cost of sustaining a democracy after the transition. In their meticulous qualitative analysis of third-wave transitions, Haggard and Kaufman (2012) distinguish between cases on the basis of the causes of political mobilization and the substantive motivation for regime change, identifying redistributive conflict as the probable cause in just over half the cases. There is considerable ambiguity in the data because in many cases transitions were initiated by the ruling elite rather than issue-specific mass mobilization, consistent with a political-capital mechanism of democratization rather than with distributive theory. Reversions to authoritarianism were even more often driven by non-distributive factors and were strongly associated with repeated prior experience of coups suspending the functioning of democratic institutions. It appears that

the weakness of the distributive conflict theory of regime change is not simply an artifact of the coding rules; the causal mechanisms stipulated in the theory do not appear to operate either. Electoral competition in Thailand, Nigeria, Pakistan, Honduras, Ecuador, Ghana and Guatemala was dominated by *patronage parties* with close ties to economic elites or the military establishment.

In none of these cases do we see a significant presence of *parties, interest groups,*
or social movements representing the interests of the poor that could serve as the basis for distributive conflict that would in turn trigger elite intervention.

[emphasis added] (Haggard and Kaufman 2012, 512)

In other words, rather than presumably redistributive programmatic democracies, the conflict was between reactionary elites and clientelist party systems, whose development and patronage efficiency had been stifled by prior coups. Political conflict of some sort appears necessary to trigger transitions, but it is also trivial. Democracy is fathered by clientelism in conditions where competitive (s)electoral politics can take a firm hold. If clientelism is disrupted by institutional instability, military juntas or judicial intervention, political capital fails to develop and (often violent) tribalism persists as the dominant form of sociopolitical organization.

In its infancy, American democracy seems to have gone through the same two-stage process from tribalism to clientelism and only then to democracy and mass enfranchisement. In the mid-19th century, the Civil War disrupted the feudal system in the South while industrialization and the political mobilization engendered by the abolitionist movement begot a system of bare-knuckle political contestation in the North. Out of the clientelism and machine politics that characterized the rampant poverty and social inequality of the Gilded Age grew incredibly strong – but corrupt and fundamentally undemocratic – national parties controlled by graft and patronage (Swenson 1982). In the early 20th century, however, first Progressivism interrupted the supply of patronage benefits by campaign reform (secret ballots and open primaries). Then, the New Deal provided a safety net and better income opportunities from the government rather than from local party bosses. Together with continuing economic development, this undermined the value of clientelism and weakened the machine politics of the preceding era. Party power began to wane rapidly and personal styles replaced
kickbacks in congressional contests. This multi-decade transition was supported the entire time by elevated political competitiveness. The critical ingredient was not the expansion of suffrage, but the process of political-capital formation and the dynamics of competitive entry:

A growing professional middle class, often aligned for the first time with labor and farmer groups […] provided the ideas, leadership and reforms that would shatter many carefully assembled party machines. […] Direct congressional primaries robbed the party of its direct control over the recruitment process, and turned it into a *mere source of personnel and expertise for more independent politicians*. [emphasis added] (Swenson 1982, 22–23)

This mechanism is distinct from Putnam’s social-capital theory of democracy, which does not specify the means whereby political mobilization can be channeled through the political process sustainably. The buildup of social capital associated with urbanization and industrialization creates the demand for transition to democracy, but does not supply the tools to make it stable, which are developed at the clientelism stage. Unsuccessful attempts to jump directly from tribalism to democracy – and the subsequent reversions to authoritarianism – have been characteristic of Latin America in the 20th century, where sporadic military coups and persistently low levels of economic development stifled clientelist politics. Only towards the end of the 20th century did stable clientelistic regimes emerge through much of the continent. At the vanguard of this process was Mexico, where the Institutional Revolutionary Party (PRI) ran a clientelistic regime with competitive elections for well over half a century and where democracy finally appears to be taking a firm hold. The key is the word “institutional” – the PRI ruled without being interrupted by military coups and developed extended client networks at all levels of government. Through clientelism, PRI operatives
competed with one another for power, appointments and elected offices for themselves or their cronies, which resulted in continual political-capital accumulation.

Municipal-level analysis of clientelism in Argentina indicates that it is strongly associated with electoral competitiveness but naturally peters out at higher income levels because pandering to or outright buying off the poor costs middle-class votes (Weitz-Shapiro 2012). These data indirectly support the conjecture that when competitiveness is present, clientelism is gradually replaced with programmatism as the economy and society develops. Similarly, economic voting appears to change from egotropic to sociotropic as income levels rise (Singer and Carlin 2013). The local-government effects of competitiveness are observable in their developed form in Britain, where councils with more competitive politics exhibit measurably better public-service performance (Boyne et al. 2012).

2.6.3. The Role of Competitive Political Institutions

Of course, an ossified clientelist system alone would not be fertile ground for democratic transition. While regimented clientelism provides incentives to accumulate the three component characteristics of political capital, institutionalized competition weeding out less apt contenders is what makes such accumulation possible. Combined with professional legislatures and subnational offices, parties can open attractive opportunities for career politicians, yet allow voters to weed out weak candidates through the personal vote. The American states provide direct evidence for the institutionalization process at work building political capital through enhanced competition: 
Three of the four states exhibiting the most competition – California, Michigan and Ohio – are among the states with the most professionalized legislatures. In addition, many of the states considered to have low levels of legislative professionalism, particularly those in the South, are characterized by high levels of uncontested races in both chambers (e.g., Arkansas, Georgia, Mississippi and Tennessee). (Konisky and Ueda 2011, 202)

Additionally, there is a strong negative relationship between districts which repeatedly go without effective contestation and the legislators’ levels of activity and success in the chamber. This effect is present within and across states despite the powerful hold of the incumbency advantage. “State house members on average skipped a higher percentage of roll-call votes when they were frequently unopposed in previous elections” (Konisky and Ueda 2011, 216), whereas the last election alone did not have a discernible impact. This result seems to provide differential support for the mechanism of the political-capital theory that the threat of an effective challenger (expansion of the pool of viable challengers) rather than the margin of victory (immediate sanctioning by voters) is the leading motivator of career politicians. And there is fairly good evidence that voters respond to candidate quality even when elections are dominated by party politics (Buttice and Stone 2012).

These results are also supported by party strategy in Italy’s parliamentary system. Galasso and Nannicini (2011) find that candidates of higher valence – measured as years of schooling, previous market income and past experience in local governments – are more likely to be allocated to contestable (non-safe) districts. Even more tellingly, parties of the left and the right have different valence patterns in safe districts, but converge on the same highly competitive type of candidate in the toughest races. Using a quasi-natural experiment, this research also demonstrates that legislators from competitive constituencies perform better
even after controlling for electoral incentives – i.e., because these delegates effectively are better *types* – so that the selection mechanism is yet again dominant over sanctioning not just in terms of voters’ behavior but in the tangible results of the process. This is not to say that sanctioning is not at work alongside selection: “when a safe district turns contestable, low-valence incumbent politicians tend to exert more effort” (Galasso and Nannicini 2011, 80). Ultimately, democracies also tend to have more educated leaders even after controlling for average levels for education and other factors (Besley and Reynal-Querol 2011).

But then one might conjecture that if representation and the quality of public policy are mostly driven by competition, institutions must be little more than a sideshow. This is simply not so. At the outset institutions provide an alternative to competition by graft, albeit not one that is oft entertained (Miller 2015). As society develops, expanding communications and rising wealth make machine politics less and less affordable (the amount of resources necessary to buy people off increases while resistance intensifies). Some skilled machine politicians begin exploiting the institutional channel’s policy pipeline, hedging between patronage and policy; junior members get to learn the ropes under the old guard eyeing those growing competitive opportunities rather than taking up arms to overthrow the (likely corrupt) regime. Not interrupting these processes of accumulation (through sudden reformist or military intervention) seems to be critical to bringing the democratization process to fruition.

### 2.6.4. PRESCRIPTIONS FOR DEMOCRATIZATION AND INSTITUTIONALIZED COMPETITION

Advocates have long promoted the obvious when it comes to ending oppressive regimes: democratic elections, market reforms, rule of law and the like. But these are outcomes rather than methods. A more indirect approach may yet
prove more effective. Instead of agitating for fair ballots and crackdowns on bribery, reformers’ energy may be better spent establishing the institutions and political capital that will one day make it possible to build resilient democracies and effective governance. Rather than promote power-sharing and government transparency, which are likely to engender instability if attempted too early, diplomats and activists may be well-advised to work with the regimes they are trying to topple. For example, foreign aid may be tied to creating elected local governments and functioning legislatures, even if the elections are rigged, the candidates are cherry-picked and the roll calls are mere rubber stamps – an institutional “fake it till you make it”.

Harstad and Svensson (2011) argue that firms will engage in bribery at low levels of economic development and in lobbying at higher levels. This is the demand side of the graft equation – the corporate sector. Bribery becomes less efficient than lobbying only when capital accumulation has reached a certain critical mass – i.e., when it is too expensive to dispense enough bribes to cover a firm’s entire footprint. Increasing bribery penalties early on in the process may deter investment by making bribes unaffordable too early and push the country into a poverty trap. “In early phases of development, tough penalties on corruption can prolong the period in which firms choose to bribe by reducing the incentives to invest. Thus, [the] model suggests that the penalty for corruption should be lower in poor countries” (Harstad and Svensson 2011, 58). A similar process may be at work in the development of political capital. Wherever institutions induce periodic political crises, they could destroy the already amassed capital, prevent it from reaching critical mass and probably also undermine the economic development that is the other necessary ingredient for a stable democracy. In short, it is critical to design transitional and pre-transitional
institutions in a manner that they do not lead to instability that interrupts the accumulation of economic and political capital.

Neglecting the role of political capital in the success of governing coalitions can be perilous. Broader coalitions require more monitoring of coalition partners by junior ministers (Carroll and Cox 2012; Martin and Vanberg 2011), which is costly (Martin 2004; Lipsmeyer and Pierce 2011) and may lead to instability or cabinet gridlock. Thus, the blind implementation of power-sharing agreements or consensus government institutions can lead to instability and then to reversions that set the democratization process back by decades. Dividing power so that rival groups have control over territorial or functional domains, which would allow them to build client networks, could be more conducive to long-term institutionalization, pacification and democratization than sharing power in a gridlocked consociational model, which could erode the value of clientelism and patronage, reducing incentives to accumulate political capital.

Transparency can also cause this kind of damage early in the process of political-capital accumulation in authoritarian institutions such as elected rubber-stamp legislatures or party congresses. Boix and Svolik contend that authoritarian regimes use such institutions to channel conflict among their supporters, gather information and help maintain the balance of power in their ruling alliances (2013). “The key [in non-democratic elections] is that voters are offered a tradeoff – voting against the regime triggers policy concessions at the national level, but reduced patronage at the individual or local level” (Miller 2015, 692). Perhaps the most telling litmus test is an experimental study conducted on some members of the Vietnamese National Assembly (Malesky, Schuler and Tran 2012). The experimenters created freely accessible websites with the parliamentary activities of about a third of assembly members and registered substantially reduced “corrective” activities vis-à-vis the regime among the treatment group,
particularly those coming from districts with higher Internet penetration rates. Central leadership tried to buy off treated delegates by placing them in districts with higher chances of reelection; those who would not be appeased were moved to localities where they would have a harder time returning to the VNA after the next election.

Patronage, a highly politicized form of clientelism, used to enhance US political parties’ ability to gain local and statewide offices. The competitive advantage associated with patronage increases with entrenchment; “the entrenched party is expected to win three out of four elections even when the elections are very close. Under civil service the entrenched parties have no advantage in winning very close elections” (Folke, Hirano and Snyder 2011, 582). One of the main arguments for the effectiveness of entrenchment is that in these conditions patronage appointees have a career to look forward to and an incentive to hone their electioneering and networking skills. Along with making the positions more attractive to better candidates for patronage appointments, these incentives improve the competitive political capacity of party machines, triggering a self-reinforcing loop of political capital accumulation in the respective constituencies. A similar role, although not as powerful because of central party control, is played by elections in Vietnam, where candidates compete for a clear shot at a more lasting political career.

From Russia to Vietnam, stable autocracies seem to have a strong preference for electioneering rather than ballot fraud; “preelection tools of manipulation have a strong reductive effect on [the effective number of legislative parties], whereas, perhaps surprisingly, ballot fraud does not” (Donno and Roussias 2012, 577–578). That is to say, fraud appears to be a measure of last resort for already weak incumbents. Cherry-picking the set of candidates is what makes a ruling regime truly strong.
Vietnam has allowed independent candidates and self-nominated candidates to compete, but these candidates should not be viewed as a de facto opposition party [...] they are also subjected to the same vetting procedures that the party-backed candidates have to go through. As such, the competition in the elections is not between organized parties, but between individuals selected or approved by the party. (Malesky and Schuler 2011, 503–504)

As Fearon (1999) remarks, the evidence that voters care more about the “personality” of their representatives than their political platforms is quite overwhelming; behavioral cues and the tone and subject of discussion seem to count for more than policy proposals as such (cf. Zaller 1992), which seems to allow valence-based competition to take place in an authoritarian state where policy arguments cannot be had. Even in advanced democracies, voters do not seem to pay attention to electoral grandstanding (Adams, Ezrow and Somer-Topcu 2011). Such empirical evidence implicitly lends support to the mechanism behind Fiorina’s (1981) original theory of retrospective voting.

This need for elite competition highlighted by Schumpeter is where presidentialism may prove a challenging institutional environment for a consolidating democracy, especially if it is not very advanced economically (as South Korea, Singapore and Taiwan were before transitioning to democracy) and suddenly faces economic headwinds. Presidentialism without a powerful legislature or regional authorities means that the president’s party is the only game in town for political entrepreneurs and careerists, which constrains the scale and scope of any competition and contestation, even at the lower rungs of power. This decreases the cost of and resistance to the president’s seizing power and ruling by decree because

the likelihood of institutionalized policymaking increases as the cost of alternative political actions increases, as the damage these alternatives can
cause decreases, and as the economy becomes wealthier. If the distribution of de jure political power is very asymmetric, the use of alternative political technologies and low degrees of institutionalization are likely to be observed. (Scartascini and Tommasi 2012, 798)

In a similar vein, Maeda (2010b) finds that military coups are more likely in economic weakness and political leaders are more likely to suspend democracy in presidential than in parliamentary systems. The fragility of presidential democracy in economically less developed countries can therefore have little to do with gridlock or dual “legitimacy” but the much more prosaic issue of lacking the political capital of a robust and skilled ruling elite with sufficiently diverse policy positions on a number of salient dimensions. Diversity ensures the promise that the democratic process is a viable conflict-resolution avenue across several different cleavages (so no prominent cleavage conflict has to be resolved by extra-institutional means). To wit, it is the promise, not the realization that is requisite. It is not institutions that make democracy strong but the sociopolitical elite they help create. Elite capacity is needed so that efforts and results be aligned meaningfully.

The bottom line is that much of democratization efforts in the late-20th century may have been misguided. PCT predicts that some of the most commonly advocated policies by the United Nations and international diplomats looking to cajole democratic reform out of clientelist and dictatorial regimes will not only prove ineffective, but may significantly delay a country’s journey to democracy. A more targeted approach, which likely will also be more palatable to the regimes in power, may produce gradual and sustainable results that both improve continuously life for ordinary citizens and help the polity democratize faster and irreversibly.
- *Fair elections* for the legislature or subnational units (or for the executive itself, as is often the case) may only push the regime to suspend the rule of law, thereby destroying institutional memory and the political capital that may have been accumulated. Advocates would be better served focusing on ensuring *free candidate entry into the process and fair campaign finance* to allow political entrepreneurs leeway to build political capital and find their way into the system without tipping over the institutional food cart.

- *Cracking down on bribery and corruption* reduces incentives to participate in the clientelist institutions of government and potentially slows down foreign investment and the capital accumulation that is necessary to reach income levels where democracy can be sustainable. A better approach may be to use international trade negotiations to push for reform in critical areas such as *education, public health and the environment*, leaving areas such as civil rights and rule of law for local reformers to handle organically.

- Rather than *isolating the worst dictatorships*, which undermines economic development and the accumulation of political capital, it may be more constructive to focus on promoting and nurturing *grassroots-level institutionalization*. PCT singles out military and theocratic regimes as the most perilous because they tend to wipe out civilian political structures, restrict competitive entry or make it unattractive for political entrepreneurs. Progress can be made by pressuring or bargaining for elected local government at the most basic level (e.g., village councils, city mayors), even if elections are not free, and promoting competitive entry into existing institutional arenas by, for example, low-level diplomatic visits, conference participations and exchanges.
• Power-sharing between ethnic or political groups in conflict does not seem viable without prior institutionalization and a high level of economic development. When violence has already broken out, intervention without a long-term peacekeeping commitment (20-30 years) may do more damage than good, misleading the civilian population and dragging out the bloodshed in fits and starts. Especially in those toughest cases, the critical task is to start rebuilding civil institutions from the bottom up rather than imposing top-down national constitutions and free elections (e.g., Bosnia, Iraq).

Every so often, there is an inevitable choice between practical results and what one sees as justice. The implications of political-capital theory are far from sanguine, but they may offer a more realistic view than the interventionism of the late 20th and early 21st centuries. Improved production and communication technology is essential to uplifting the poorest societies and helping marginalized groups mobilize and enter the political process. Investments in infrastructure and education may be a more powerful force for change than any intervention – through war or sanctions – or diplomatic pressure.

2.7. CONCLUSION

This chapter started by introducing a consistent definition of strategic rationality and a formal solution concept consistent with it. Those ideas were then applied in the general setting of a non-cooperative principal-agent interaction. The first, and perhaps strongest, theoretical finding is that, when applied to the class of delegation games with asymmetric information, uncertain outcomes and absence of third-party enforcement, post-electoral control on its own is revealed to be unfeasible without heuristic preferences. Pure moral hazard is not a workable
theoretical approach to the delegation problem because principals cannot commit credibly to rewards and punishments, not because of agents. Desirable equilibria do not materialize because there is no quantifiable guarantee that even the best performance will result in reappointment; the vagaries of nature and the whim of voters can waylay even the best-behaved agent. In the absence of objective commitment mechanisms based on measurable performance criteria, good behavior falls in the domain of the irrational. Type selection dominates the process and determines whether it will result in compliance or defiance.

The results broadly confirm and strengthen a generally accepted tenet of the literature on representation, which suggests that selection trumps sanctioning as a control mechanism when both are available. Thus, the second important finding is that a real diversity and choice among agents are essential to ensuring proper representation. That only a small fraction of US election candidates are women, for example, therefore speaks volumes about the representativeness of some democracies. Not without some irony, the politics of Hong Kong after its return to China highlight this point. Beijing did not mind free elections in the territory as long as it picked the candidates. Voters showed appreciation for this fact, as they took to the streets in their thousands and staged months-long protests in response.

There is, however, another much more important and very disturbing implication of these results: persistent public perceptions that in politics “everyone is the same” (it is not even necessary to go as far as “everyone is a crook”) can become self-fulfilling prophesies undermining accountability and resulting in systemic instability even in the most democratic society. The more pervasive such attitudes are, the more likely they are to become self-fulfilling prophesies.

The theory does leave room for much future development. Strategic competition between the principals and entry by the principals themselves as
candidates (i.e., mixing the sets $C$ and $V$) are important variations, which need to be explored. Much like the struggle for office or policy between the agents, a competitive dynamic among the principals can have substantial effects on the game, likely of undermining their ability to exercise control – or the ability of agents to read messages from the principals and respond to them effectively.

Perhaps the most significant implication of the theory is that ideas and strategies for modernization and democratization are due for a substantial reconsideration. The competitive model leads to a new political-capital theory of democracy, which suggests that the development of diverse pools of politically viable candidates is perhaps the most effective way to spur democracy and help it consolidate. Political-capital accumulation is where institutions come into play, as they provide arenas for political entrepreneurs to enter the process as well as incentives and opportunities to invest in political expertise. Consolidated dictatorships may be open to establishing, for informational and other purposes, the very institutions that will someday supersede them. Competitive elections are more important than fair elections because “[d]efying the regime at the ballot box [...] gains general policy concessions, but at a personal cost of lost patronage or increased repression” (Miller 2015, 697). Only when the economy is developed enough to trigger the former reaction from the regime, progress is made towards democracy as politics begins a transition to programmatism.

The vision of democracy encapsulated by the model is that of Schumpeter rather than that of Lipset or Lijphart. In Schumpeter’s political economy, democracy is about competition between elites and elite institutions, not about the masses’ sending their representatives to the halls of government (O’Toole 1977). The long-sideline art of studying the development and role of political elites (e.g., Putnam 1976) is due for an institutionalist revival. The final chapter of this work ventures an empirical step on this path.
Chapter 3

Competitive Political Institutions and Democratic Consolidation

Chapter 2 introduced a new theory of democratization that suggests transitions to democracy may be more lasting if polities have had prior experience with competitive political institutions and have accumulated political capital. Because panel data directly measuring these concepts are not available, this chapter conducts an empirical test of the theory by reconstructing data from the Polity IV dataset. The unit of analysis is the country-year. A detailed evaluation is conducted to validate the applicability of Polity IV data to measuring institutionalized political competitiveness and to ensure that the outcome of interest – sustained democracy – is distinct from explanatory variables. Institutional metrics on the competitiveness of the political system are converted into a uniform categorical measure of the system’s capitalization. The measure is then used as a basis for deriving sample probabilities over whether a country is likely to transition to democracy and consolidate in that condition. The results, which are robust to sampling and measurement checks provide support for political-capital theory. A new avenue of study opens for a longstanding research question within the discipline.

3.1. INTRODUCTION AND METHODOLOGICAL SUMMARY

The formal theory laid out in Chapter 2 suggested that the characteristics of the pool of candidates available within a framework of delegation, whether political or not, is likely the most critical determinant of its functioning. The
models show conclusively that favorable equilibrium outcomes are predicated on the composition of the set of agents available at the outset even more than on the clarity of responsibility in the political process. If potential agents are universally incompetent or ill-intended, no amount of accountability can make the system work for the goals of the principals. Competition between agents with diverse skills and objectives appears to be an essential prerequisite for the functioning of a representative system. Accordingly, in order to ensure a sustainable democracy, a set of political institutions must not only be democratic in their principles of functioning but also, first and foremost, must help engender a political elite with the appropriate characteristics.

In consequence, it must be the case that the very process of democratization itself is substantially predicated on the development of such elites, broadly termed the accumulation of political capital. This is the basic rationale for the political-capital theory of democratization developed in Chapter 2, which is based on Schumpeter’s competitive model of democracy. The theory suggests that transitions are conditional on economic development and the accumulation of political capital, which can be facilitated by a dictatorship’s establishment and sustenance of competitive political institutions. Thus, it is hypothesized that sustained democratization is they are preceded by consolidated regimes that have nonetheless allowed some level of institutionalized political competition to take place. This is the main relationship that is measured and evaluated in this chapter.

While PCT posits that democratization and consolidation are conditional on economic development as well, it is perfectly appropriate to begin the evaluation of the theory by looking at the effects of a sustained competitive environment alone. The main thrust of PCT is not concerned with the probability of transitions themselves because, as has been documented conclusively in the literature, there are many potential triggers for them. As stated earlier, instability
is trivial, especially in the context of economic insecurity. Stability is the unusual phenomenon and, therefore, likely the one that can reveal important information.

Even though there may be some validity issues, the Polity datasets are one of the most widely used measures of democracy in the discipline. They also provide the longest time series, beginning as early as 1800 for some states. It is advantageous that institutionalization as operationalized by Polity IV and institutionalized political competition are distinct concepts. Polity’s measurement aims to reflect the generally accepted view that democracy is characterized by political outcomes where institutions operate under the rule of law (i.e., can constrain one another) and officeholders are elected in free and fair elections. PCT looks at the competitiveness of the political system regardless of the rule of law or the fairness of elections as a precondition for the emergence and consolidation of the characteristics anticipated by the traditional view.

There are at least two sets of issues which make traditional methods of empirical testing suspect in this setting. The first is related to the reliability and validity of the categorical variables, as the authors of Polity IV themselves recognize expressly. Validity may be questioned on the grounds that what is really measures are events and (less frequently) institutions that tend to correlate with what is intuitively perceived as democracy or dictatorship, as the case may be, but hardly capture any specific definition of democracy (in contrast with Vanhanen’s democracy score, which has other problems). While what democracy is certainly is a topic open for normative debate (and therefore a matter of opinion rather than fact), this operationalization produces a corollary problem, which is rarely taken into account in empirical work: the measure not only may produce endogeneity when used in conjunction with outside data identical or close to the categorical variables underlying the Polity score, but also, much more significantly and much more fundamentally, may interfere with identifying causal mechanisms by
correlation or spurious causation with unobserved variables affecting both the outside data and the Polity data.

To avoid the measurement issues discussed above, the analysis is constrained as possible to the Polity dataset, which should help ensure measurement consistency, if not maximal validity. Economic development (whether in absolute or relative terms) is an important intervening variable that prior studies have shown to be empirically important and PCT itself recognizes as theoretically compelling. Since the specific purpose of this effort is to find a discernible effect from institutionalized competition rather to test the theory in its entirety, it is not absolutely indispensable to control for economic development (whether operationalized in absolute or distributional terms) for at least a couple of reasons.

One critique of this empirical approach may be that economic development “causes” both democracy and political capital/competitiveness. But the very essence – empirical as well as theoretical – of the distributional literature on democratization is that high levels of income (and other operationalizations) alone are less than a good correlate of successful transitions or consolidated democracy overall. Some of the most oppressive and anticompetitive regimes also have some of the highest levels of per capita income as well as other measures of advancement such as the human development index (HDI).

Additionally, PCT expressly stipulates that certain levels of socioeconomic and technological development are positively necessary before political capital-accumulation becomes an attractive proposition for political entrepreneurs, without whose participation institutionalized political competition is simply not viable (see Subsection 2.6.1). Hence even if economic conditions are a good predictor of the dependent variable, that does not contradict in any way the political-capital pathway. The critical test of much greater interest relates to the
ability of a state, whether advanced or not, to democratize successfully without having institutionalized competition. The mechanism of PCT would suggest that this is not just unlikely but probably close to impossible – the difference in probability of success between institutionalized and deinstitutionalized cases must be in orders of magnitude (an expectation substantiated by the data below). A detailed substantive analysis is included to examine this point further.

3.2. Overview of Primary Data

A critical missing piece in Polity IV’s operationalization of democracy and its components is that it does not cover essential aspects such as a freedom of speech and assembly, general rule of law and personal privacy. These are characteristics that the theory would certainly aim to apply in explaining democratization, but in the absence of effective measurements over extended periods, they have to be relegated to the theoretical backdrop of this study. The empirical work that follows is thus restricted to concepts which can be operationalized with reasonable validity using Polity IV data.

3.2.1. Observations

Each of the 16,727 observations in the 2013 Polity IV Annual Time-Series dataset is a country-year, where most variables of interest are coded as of the year’s end (an important exception to this rule are transition-specific data, which may provide some within-year characteristics). Longitudinally, the data span the period 1800-2013, with data available on most distinct state entities in existence during this period. Notably, the dataset does not include most of the smaller states of the German (and, later, North German) Confederation in the 19th century. This should not be a major cause of concern as these were by that time under the de facto control of Prussia, Austria or a non-German power such as Denmark. Also
absent are data on states in Sub-Saharan Africa, which were being overrun by neocolonialism and for which reliable data may be hard to obtain. Similarly absent are data on the Indian princely states, which, although de jure still in existence, were firmly under the control of the British East India Company and, after 1858, of the imperial government.

With a few manageable exceptions, there are no obvious coding issues with distinguishing between countries. The Russian monarchy and its successor states poses the greatest operationalization challenge on this front. Polity IV assigns to the USSR a different country code from Russia, but codes pre- and post-Soviet Russia as the same country. However, by the Polity IV Manual’s own coding standards for territorial and institutional transformations, this approach appears an arbitrary exception, particularly when considered in the context of transitions. Unlike the post-Soviet Baltic states and their prewar predecessors, the Russian Federation is substantially distinct from Imperial Russia, thus it was recoded as a separate country with its unique country code (376).

A less challenging special case is that of Germany, which is coded in Polity IV as one continuous entity from the Kingdom of Prussia in 1800 through the fall of the Third Reich in 1945 and then again as a reconstituted country from unification in 1990 onwards. Meanwhile, the Federal Republic of Germany and the German Democratic Republic are coded as separate entities (West and East Germany respectively). A more reasonable reading of the underlying historical events is that the Federal Republic simply expanded its territory upon unification, a view bolstered by the fact that there were no fundamental changes in its institutional organization or political system, which was simply replicated and expanded in the eastern provinces. Thus, West Germany and post-unification Germany were recoded as a single continuous country code, distinct from both
pre-1945 and East Germany, and the 1990 transition entry was eliminated along with the duplicate entry for that year.

Another similar case, but in reverse to the German one, is that of Yugoslavia. Polity IV recognizes two distinct state entities. One begins in 1921 after the expansion of the Serbian monarchy to the Balkan lands of the Habsburgs as the Kingdom of Serbs, Croats and Slovenes (not reflected in Polity IV), which was only later renamed Yugoslavia. This country unit continues through World War II to the dissolution of Tito’s Yugoslavia in 1991. A “Residual Yugoslavia” is coded from that year to the dissolution of the union of Serbia and Montenegro in 2006, whereafter the Republic of Serbia is coded as a continuation of the 19th-century Kingdom of Serbia. By analogy with Germany, the post-Yugoslav republican Serbia was recoded as separate, which results in four “Yugoslav” countries in total: pre-1921 Serbia, Yugoslavia (1921-1991), Residual Yugoslavia (1991-2006) and post-Yugoslav Serbia from 2006 onwards. Montenegro and the other former-Yugoslav republics are left unchanged.

Finally, Vietnam before and after its 20th-century wars of independence is coded by Polity IV as three distinct entities: North, South and post-unification Vietnam. As in the case of postwar Germany, the rationale for this approach is not obvious. Unification essentially consisted in the North Vietnamese government conquering and extending its authority to the south of the country, thus North Vietnam was recoded as a single state code and country “Vietnam”, beginning with the French withdrawal in 1954 and continuing through 2013. A resulting duplicate entry for the year 1976 was consequently eliminated from the dataset.

3.2.2. VARIABLES

Polity IV contains five distinct types of variables (Fig. 3.1). Country and case identifier codes include the COUNTRY, country code CCODE and YEAR, as well as
several other technical variables concerning coding reliability. Upon inspection of the data, the documented coding concerns did not appear pertinent to this empirical study.

The \textit{composite indicators} in the dataset are measures of the regime type and stability. DEMOC and AUTOC are 11-point scales of “institutionalized” democracy and autocracy respectively. Subtracting the AUTOC from the DEMOC score generally results in the composite POLITY and POLITY2 score for each country-year. POLITY2 is a normalization of the POLITY score to a range of $-10$ to $10$. According to the dataset’s authors, polity scores in the range $(-10, -6)$ should be interpreted as indicating an autocracy and scores in the range $(6,10)$ as a democracy, with the middle range attributed to intermediate regimes sharing features of both and termed “anocracy”. Alternatively, the authors suggest a POLITY score of $1$ to $6$ indicates a partial and a score from $7$ to $10$ a full democracy. The POLITY score itself may also include \textit{standardized authority scores} outside the typical range, which correspond to interregnum ($-77$), transition periods ($-88$) and interruptions ($-66$) such as foreign occupation. Note the distinction between a score signifying a \textit{transition period} for the country-year and the \textit{regime-transition variable} REGTRANS discussed below.

\begin{table}[h]
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**Composite indicators**

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<th>Variable Type</th>
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<th>Source</th>
</tr>
</thead>
<tbody>
<tr>
<td>democracy</td>
<td>DEMOC</td>
<td>interval</td>
<td>integer from 0 to 10 as well as standardized authority scores</td>
<td>component variables</td>
</tr>
<tr>
<td>autocracy</td>
<td>AUTOC</td>
<td>interval</td>
<td>integer from 0 to 10 as well as standardized authority scores</td>
<td>component variables</td>
</tr>
<tr>
<td>polity score</td>
<td>POLITY</td>
<td>interval</td>
<td>integer from −10 to 10 as well as standardized authority scores or DEMOC less AUTOC</td>
<td>standardized authority scores</td>
</tr>
<tr>
<td>Variable Name</td>
<td>Variable Notation</td>
<td>Variable Type</td>
<td>Data Type</td>
<td>Source</td>
</tr>
<tr>
<td>---------------</td>
<td>-------------------</td>
<td>---------------</td>
<td>-----------</td>
<td>-----------------------------</td>
</tr>
<tr>
<td>polity2 score</td>
<td>POLITY2</td>
<td>interval</td>
<td>integer from 1 to 10</td>
<td>POLITY smoothed for standardized authority scores</td>
</tr>
</tbody>
</table>

**Component variables**

<p>| regulation of chief executive recruitment | XRREG | categorical | integer from 1 to 3 | qualitative data |
| competiveness of chief executive recruitment | XRCOMP | categorical | integer from 1 to 3 | qualitative data |
| openness of chief executive recruitment | XROPEN | categorical | integer from 1 to 4 | qualitative data |
| executive constraints | XCONST | categorical | integer from 1 to 7 | qualitative data |
| regulation of participation | PARREG | categorical | integer from 1 to 5 | qualitative data |</p>
<table>
<thead>
<tr>
<th>Variable Name</th>
<th>Variable Notation</th>
<th>Variable Type</th>
<th>Data Type</th>
<th>Source</th>
</tr>
</thead>
<tbody>
<tr>
<td>competitiveness of participation</td>
<td>PARCOMP</td>
<td>categorical</td>
<td>integer from 0 to 5</td>
<td>qualitative data</td>
</tr>
</tbody>
</table>

**Concept variables**

| executive recruitment | EXREC | categorical | integer from 1 to 8 | XRREG, XRCOMP, XROPEN |
| executive constraints | EXCONST | categorical | integer from 1 to 5 | identical to XCONST |
| political competition | POLCOMP | categorical | integer from 1 to 10 | PARREG, PARCOMP |

**Regime transition variables**

<p>| regime transition | REGTRANS | categorical | 12 specific integer values | changes in POLITY score and qualitative data |
| regime transition completed | D4 | binary | 0 or 1 | REGTRANS |</p>
<table>
<thead>
<tr>
<th>Variable Name</th>
<th>Variable Notation</th>
<th>Variable Type</th>
<th>Data Type</th>
<th>Source</th>
</tr>
</thead>
<tbody>
<tr>
<td>prior polity code</td>
<td>PRIOR</td>
<td>interval</td>
<td>integer from −10 to 10 as well as “begin state” codes</td>
<td>prior POLITY score or qualitative data</td>
</tr>
<tr>
<td>post polity code</td>
<td>POST</td>
<td>interval</td>
<td>integer from −10 to 10 as well as “begin state” codes</td>
<td>prior POLITY score or qualitative data</td>
</tr>
<tr>
<td>total change in POLITY value</td>
<td>CHANGE</td>
<td>interval</td>
<td>integer from −20 to 20</td>
<td>POST less PRIOR</td>
</tr>
</tbody>
</table>

Like the standardized authority scores, component variables are the fundamental substantive data of Polity IV. They cover six different aspects of political organization and behavior, grouped in three categories: executive recruitment, executive constraint and political competition (outside the executive itself). The regulation of chief executive recruitment (XRREG) reflects the extent to which the country’s executive is selected in an established way, whereas competitiveness of chief executive recruitment (XRCOMP) specifies whether that process involves an election and the openness of chief executive recruitment (XROPEN) indicates if the process is restricted to a narrow set of candidates. Together, these three component variables are used to construct a concept variable of executive recruitment (XREC).
The *executive constraints* component variable (XCONST) measures whether the political power of the executive is checked by another power center, typically a legislature or privy council. Finally, there are the two component variables that measure *political competition and opposition*. The *regulation of participation* (PARREG) variable reflects the structure of political participation (e.g., sectarian, regulated or unregulated), whereas the *competitiveness of participation* (PARCOMP) indicates to what extent the process is open to members of the polity and does not involve coercion and other normative distortions. The *political competition* (POLCOMP) concept variable constructed from PARREG and PARCOMP integrates this information into a single score. The third concept variable – about executive constraint – is identical to the XCONST variable itself.

The other group of fundamental substantive variables are related to regime change and transition, including the critical REGTRANS variable, which categorically codes three distinct types of transitions, two types of smaller regime change, no change or state failure (the special score −77). The significance of these data is detailed at greater length in Section 3.3, where the core metrics are discussed.

Some missing values for the composite variables had to be imputed to make possible subsequent measurement of the variables of interest. Missing values for PARCOMP for Canada and Luxembourg for 1888-1920 and 1880-1919, respectively, were coded as PARCOMP = 9 if PARREG = 5 and PARCOMP = 4, a combination of component variables which is not covered by Polity IV’s own coding scheme. A similar underspecification issue was encountered with the EXREC variable. It was necessary to fill the gap in the coding specification, as this is a critical metric for the composite CAPIT variable. The observations affected and the coding scheme used to impute values for EXREC are disclosed in Fig. 3.2.
Table 3.2. EXREC Imputation for Underspecified Coding of Component Variables

<table>
<thead>
<tr>
<th>Country</th>
<th>Years</th>
<th>XRREG</th>
<th>XRCOMP</th>
<th>XROPEN</th>
<th>Concept Variable</th>
</tr>
</thead>
<tbody>
<tr>
<td>Costa Rica</td>
<td>1876-1881</td>
<td>3</td>
<td>2</td>
<td>4</td>
<td>7</td>
</tr>
<tr>
<td>Paraguay</td>
<td>1870-1935</td>
<td>1</td>
<td>1</td>
<td>4</td>
<td>0</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>1837-1900</td>
<td>3</td>
<td>2</td>
<td>4</td>
<td>7</td>
</tr>
<tr>
<td>Belgium</td>
<td>1919-1929</td>
<td>3</td>
<td>2</td>
<td>4</td>
<td>7</td>
</tr>
<tr>
<td>Luxemburg</td>
<td>1867-1889</td>
<td>3</td>
<td>1</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>Luxemburg</td>
<td>1890-1919</td>
<td>3</td>
<td>2</td>
<td>4</td>
<td>7</td>
</tr>
</tbody>
</table>

3.3. Measuring Transitions, Competitiveness and Democracy

The core insight of PCT is that transitions are successful when they rely on pre-existing competitive political institutions and the elites that have a stake in them. Political capital itself – conceptually the most straightforward explanatory variable – would be difficult to measure outside of surveys and such data can hardly be obtained for the 19th century or even for the not-so-distant past. However, the theory specifies that competitive political processes are the condition driving the accumulation of political capital and therefore it may be possible to use appropriate behavioral and institutional data on political competitiveness as a proxy for political capital itself.

A basic formulation of this approach would consist of constructing a variable capturing the level of competitiveness at a particular point in time. To make the measurement more robust, i.e., to maximize its validity as a proxy for
political capital in the system, it may further be necessary that the level of competitiveness be sustained over an extended period.

Conceptually, the issues surrounding the measurement approach to capturing “democracy” are quite similar. An interval metric such as the POLITY or POLITY2 score or a categorical variable constructed from the underlying component variables observed in a single year is just a part of the story. There are too many instances of polities briefly adopting not just pro-forma democratic institutions but also the fair elections and other behaviors that go with them only to descend into utter havoc shortly thereafter. Observing the requisite institutions and desirable behaviors over extended periods would certainly make for a more credible empirical result.

In addition to these two dimensions (structure and duration), transitions involve a third level of complexity, as they can be segmented in at least three conceptually distinct stages: initiation, process and conclusion. Respectively, these stages are related to core theoretical questions:

i. What are the necessary conditions and attendant triggers of transitions? Which, if any, of those factors are conducive to a “successful” transition? How does the type of initiation (e.g., from the elite, through guerilla activity, by external intervention) affect the nature of the transition process and its outcomes?

ii. To what extent is the transition process itself orderly and institutionalized? Does it have clear goals in terms of the institutions and social order of the subsequent regime or is it merely a repudiation of the previous one? How much does it rely on the established institutional channels of the prior regime? Are certain segments of society excluded from participating in the transition
process? Is widespread coercion used to establish a new political order or demolish the old one?

iii. Is the end of the transition process determined by design (of its initiators or participants), external intervention or unforeseen circumstance? Are any large groups of society disaffected with its conclusion? Does it leave any major transition issues unresolved?

Are the new regime’s institutions equipped to handle them?

This is but a smattering of each stage’s qualitative characteristics that could potentially affect its “outcome”, particularly as it relates to the superseding polity’s level of democracy, its further improvement and its sustainability. While Polity IV includes some level of detail on the characteristics of each regime transition, the data are by no means sufficiently detailed or of the level of validity that would allow for a granular stage-by-stage analysis. Thus, it is necessary to constrain the empirical evaluation to the core question of whether there is a strong correlation between institutionalized competition (measured as a durable availability of competitive conditions) and democratic consolidation (measured as remaining above some threshold democracy score over an extended period).

3.3.1. DEMOCRACY AND ITS CATEGORIZATION

Polity IV provides at least two empirically valid ways to measure the attainment of a democratic political system. The obvious one is the POLITY score itself or a categorical variable for the level of democracy DEML based on it and distinguishing a partial (POLITY = 1 ... 6) and a full democracy (POLITY = 7 ... 10) as well as nondemocracy (Fig. 3.3), as discussed in Subsection 3.2.2. An even more compelling option is suggested by the dataset’s creators through the conceptual definition of the DEMOC variable:
A mature and internally coherent democracy [could] be operationally defined as one in which (a) political participation is unrestricted, open and fully competitive; (b) executive recruitment is elective; and (c) constraints on the chief executive are substantial. (Marshall, Gurr and Jaggers 2014, 15)

Respectively, this suggested definition of a *mature democracy* variable (denoted by DEMM) implies a combination of POLCOMP = 10, EXREC = 8 and EXCONST (or, equally, XCONST) = 5 … 7, which are the top values for the first two concept variables and the top range for the latter one. This is about as rigorous as a country-year-based measure can be within the Polity IV framework.

**Figure 3.3. Higher-Order Measures of Democratization**

<table>
<thead>
<tr>
<th>Variable Name</th>
<th>Variable Notation</th>
<th>Variable Type</th>
<th>Coding Scheme</th>
</tr>
</thead>
<tbody>
<tr>
<td>level of democracy</td>
<td>DEML</td>
<td>categorical</td>
<td>2 if POLITY = 7 … 10 (“full democracy”); 1 if POLITY = 1 … 6 (“partial democracy”); 0 otherwise (“non-democracy”)</td>
</tr>
<tr>
<td>mature democracy</td>
<td>DEMM</td>
<td>binary</td>
<td>1 if all of POLCOMP = 10, EXREC = 8 and EXCONST = 5 … 7 are satisfied; 0 otherwise</td>
</tr>
<tr>
<td>Variable Name</td>
<td>Variable Notation</td>
<td>Variable Type</td>
<td>Coding Scheme</td>
</tr>
<tr>
<td>---------------</td>
<td>-------------------</td>
<td>---------------</td>
<td>---------------</td>
</tr>
<tr>
<td>duration of partial democracy</td>
<td>DDEML1</td>
<td>nonnegative integer</td>
<td>prior-year DDEML1 value plus 1 if current- and prior-year DEML = 1; 0 otherwise</td>
</tr>
<tr>
<td>duration of full democracy</td>
<td>DDEML2</td>
<td>nonnegative integer</td>
<td>prior-year DDEML2 value plus 1 if current- and prior-year DEML = 2; 0 otherwise</td>
</tr>
<tr>
<td>duration of mature democracy</td>
<td>DDEMM</td>
<td>nonnegative integer</td>
<td>prior-year DDEMM value plus 1 if current- and prior-year DEMM = 1; 0 otherwise</td>
</tr>
</tbody>
</table>

These two variables can be easily translated into annual-duration measures. Following the duration coding scheme of Polity IV, each of the duration variables is incremented if the regime level was achieved in the previous year and is sustained in the current one; otherwise the value resets to zero. For example, if Cuba becomes a full democracy in 2020 and remains so in 2021, its DEML2 will be 0 for 2020 and 1 for 2021. It will increment to 2 for 2022 if the full-democracy status is maintained and reset to zero otherwise.

### 3.3.2. Institutionalized Competition

In designing the operational metrics for political competition, it is necessary to keep in mind that the larger objective is to create measures that are good proxies for political capital rather than the most valid measure of institutionalized competition itself. From a rational-choice perspective, political entrepreneurs
must be motivated by the combination of incentives to accumulate political capital and the opportunities to do so afforded by the extant political regime. In economic terms, the incentives can be viewed as the actors’ demand for political capital and the opportunities as their ability to meet that demand. Much like in a market model, these factors are not substitutable but complementary – one is not much help in increasing political capital without the other. On the supply side would be institutional channels to compete and acquire expertise in the three dimensions outlined in Chapter 2: electioneering, policymaking skill and specialized knowledge of salient issues. On the demand side must be found the overall value of becoming a career politician (or using a high political position as a launching pad for lateral advancement up the social ladder in other power domains). System instability or clear lack of opportunities for advancement beyond the lower levels of the political power structure would likely disincentivize investment of time and effort in acquiring political capital even if opportunities to do so exist.

The relevant information in Polity IV for grasping these supply-demand dynamics are most conveniently coded in the concept variables POLCOMP, EXCONST and EXREC. Both the incentives and opportunities are affected to the greatest extent by the nature of political competition as operationalized in the dataset. For example, in a despotism opportunities both to accumulate political capital and to take advantage of it are likely concentrated within a narrow and regimented hierarchy and there hardly are institutionalized channels of competition. Rather, competition would take the form of behind-the-scenes power struggle, where political capital of the variety useful in the context of open institutionalized competition (even if not free and fair) is not particularly valuable. In a sham democracy, on the other hand, there may be a much broader range of channels for the acquisition of political power and its deployment to productive ends.
Therefore, the deinstitutionalization of political competition would be a hindrance to political-capital accumulation on both the demand and the supply side. This effect can be expected to be worst in failed states (POLCOMP = −77) followed by foreign-occupied or otherwise institutionally destabilized polities (POLCOMP = −66). The tribal warfare that characterizes failed states ought to be more destructive to political capital than a foreign occupying force, which in many cases may try to coopt existing elites and institutions in order to pacify or colonize the territory, but still erode any pre-existing political capital and remove incentives to accumulate any. At the next level would be polities where competition is either restricted to a rigid hierarchy or uninstitutionalized (POLCOMP = 1 ... 5), e.g., totalitarian regimes would score in this range (Fig. 3.4).

Figure 3.4. Coding Institutional Effects on Political-Capital Accumulation

<table>
<thead>
<tr>
<th>Variable Name</th>
<th>Variable Notation</th>
<th>Variable Type</th>
<th>Coding Scheme</th>
</tr>
</thead>
<tbody>
<tr>
<td>deinstitutionalization of competition</td>
<td>DINST</td>
<td>categorical</td>
<td>3 if POLCOMP = −77;</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>2 if POLCOMP = −66;</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>1 if POLCOMP = 1 ... 5, −88;</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>0 if POLCOMP &gt; 5</td>
</tr>
<tr>
<td>executive rule by fiat</td>
<td>XRF</td>
<td>categorical</td>
<td>2 if EXCONST &lt; 5;</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>1 if EXCONST = 5;</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>0 if EXCONST = 6, 7</td>
</tr>
<tr>
<td>executive appointment by fiat</td>
<td>XAF</td>
<td>binary</td>
<td>1 if EXREC &lt; 6;</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>0 otherwise</td>
</tr>
</tbody>
</table>
The other two Polity IV concept variables, concerning the executive, are relevant for the effect they might have on the incentives to invest in political capital. Executive appointment is the less important of the two as it presents a fairly narrow channel for advancement and very few political entrepreneurs can realistically have a shot at reaching the chief-executive level even in an open system. While this potential opportunity may have a discernible (positive) effect on the incentives, it is far from decisive relative to other institutional channels for acquiring political power. Thus, it makes sense to code the executive recruitment concept variable as a dichotomous *executive appointment by fiat* institutionalization variable XAF, which takes a value of zero only when there is an elected chief executive as coded via EXREC.

The mode of executive rule and the sway of the executive over other political institutions is much more important because it poses a potential threat to those alternative channels. On one hand, an unconstrained executive may invade the formal sphere of policy influence of other authorities – territorial such as regions and municipalities or functional such as legislatures, courts and militaries. Such intrusions could diminish the value of holding a high position in these power structures and thus the incentives to strive for such positions through an institutionalized competitive process even if one exists. Effectively, in such conditions all paths for advancement would collapse into one – a much narrower informal power structure commanded by the executive. On the other hand, if the executive could at any time abolish competitive institutions and wipe out the accumulated political capital, the attendant shadow of uncertainty can also discourage political entrepreneurs from entering those arenas. This sort of dynamic seems to have characterized much of South America in the 20th century and was not ameliorated, to put it mildly, by *formally* powerful presidentialism.
These considerations are reflected in a three-level institutionalization variable XRF capturing *executive rule by fiat*, taking a value of 0 only if the executive is significantly constrained (EXCONST = 6, 7), a value of 1 if the chief executive is somewhat constrained by other institutions (EXCONST = 5) and 2 if there are weak or no constraints.

From these intermediate institutionalization variables, it is possible to construct the categorical proxy variable CAPIT for the *political capitalization* of the system by gaging the territory’s friendliness to the accumulation of political capital (Fig. 3.5). As the clichéd Anna Karenina principle goes, there are multiple ways in which institutionalized political competition can be impaired, while there is a very specific set of conditions that make it possible, insofar as the operationalization is constrained to the Polity IV data. Among the three institutionalization concepts, the deinstitutionalization of competition is the most damaging factor, thus it is coded as dominating the other two; political capital is relevant only as long as the institutions within which it can be deployed exist. The negative values are chosen to emphasize that in the respective political capital has been or is being actively destroyed, not merely that it cannot accumulate to levels whereat a democratic transition can occur or consolidate.

**Figure 3.5. Conceptualization and Coding Scheme for Political Capitalization**

<table>
<thead>
<tr>
<th>Indicative Regime</th>
<th>Indicative Capitalization</th>
<th>Variable Values</th>
</tr>
</thead>
<tbody>
<tr>
<td>state collapse/failure</td>
<td>fully depleted; no foreseeable recovery</td>
<td>DINST 3, XRF NA, XAF NA, CAPIT −3</td>
</tr>
<tr>
<td>interruption/foreign control</td>
<td>depleted; recovery remote, unlikely</td>
<td>DINST 2, XRF NA, XAF NA, CAPIT −2</td>
</tr>
<tr>
<td>Indicative Regime</td>
<td>Indicative Capitalization</td>
<td>Variable Values</td>
</tr>
<tr>
<td>---------------------------</td>
<td>--------------------------</td>
<td>-----------------</td>
</tr>
<tr>
<td>totalitarianism, despotism, transition</td>
<td>depleted; openly and covertly vitiated</td>
<td>1 any any −1</td>
</tr>
<tr>
<td>authoritarianism</td>
<td>frozen; marginal; covertly vitiated</td>
<td>0 2 any 0</td>
</tr>
<tr>
<td>semi-authoritarianism</td>
<td>stifled; not insignificant</td>
<td>0 1 any 1</td>
</tr>
<tr>
<td>sham democracy</td>
<td>dynamic; significant</td>
<td>0 0 1 2</td>
</tr>
<tr>
<td>political pluralism</td>
<td>dynamic; abundant</td>
<td>0 0 0 3</td>
</tr>
</tbody>
</table>

The important distinction between the authoritarian systems and consolidated dictatorships in the collective category associated with \( \text{CAPIT} = -1 \) is that those systems develop monopolistic hierarchies; they actively suppress any forms of social organization or status beyond a party, a religion, a tribe or an similar structure established by the dear leader. In the early 21st century, for example, authoritarian Russia has opposition parties and other organizations independent of the regime, albeit ones that are frozen out of the system and therefore gradually losing their political capital, unlike totalitarian North Korea or despotic Saudi Arabia, where the very *thought* or *word* of criticism or opposition can in itself be a criminal – and even capital – offense.
3.3.3. RECORDING TRANSITIONS

The REGTRANS variable within Polity IV and the auxiliary variables in its group provide a convenient and fairly detailed overview of transitions. The CHANGE variable indicates the POLITY change during each transition, but also includes special codes for entry and exit. These values are easily recoded into binaries for pre-existing (PSTATE), beginning (BSTATE) and ending (ESTATE) polities (Fig. 3.6), which provide within-sample identifiers for data truncation (see next section). There are 22 states in the sample which pre-existed 1800, the first year of record.

<table>
<thead>
<tr>
<th>Special Value</th>
<th>Interpretation</th>
<th>Coding Scheme</th>
</tr>
</thead>
<tbody>
<tr>
<td>88</td>
<td>pre-existing polity</td>
<td>PSTATE = 1</td>
</tr>
<tr>
<td>96</td>
<td>state disintegration</td>
<td>ESTATE = 1</td>
</tr>
<tr>
<td>97</td>
<td>state transformation</td>
<td>BSTATE = 1</td>
</tr>
<tr>
<td>98</td>
<td>state demise</td>
<td>ESTATE = 1</td>
</tr>
<tr>
<td>99</td>
<td>state creation</td>
<td>BSTATE = 1</td>
</tr>
</tbody>
</table>

In addition to these special codes, REGTRANS provides regular transition values based on directional changes in the POLITY score. To facilitate the analysis, these values are normalized to a REGTRANS2 variable (Fig. 3.7). Given the data available in Polity IV, transitions can be conceptualized in three different ways, depending on the unit of analysis. The most obvious one is the country-year, which is the dataset’s “observation”. At this level, it is possible to derive sample probabilities for democratization occurring and consolidating successfully. Since
the focus is not on predicting transitions themselves but their propensity to engender long-term democratic consolidation, it makes sense to eliminate lower-level variation and focus on the strongest effects.

**Figure 3.7. Regularizing REGTRANS to REGTRANS2**

<table>
<thead>
<tr>
<th>REGTRANS Value</th>
<th>REGTRANS2 Value</th>
<th>Polity IV Interpretation</th>
</tr>
</thead>
<tbody>
<tr>
<td>3</td>
<td>2</td>
<td>major democratic transition: more than five points increase in POLITY over no more than three years and a shift from partial to full democracy or from autocracy to partial democracy</td>
</tr>
<tr>
<td>2</td>
<td>1</td>
<td>minor democratic transition: three to five points increase in POLITY over no more than three years and a shift from partial to full democracy or from autocracy to any form of democracy</td>
</tr>
<tr>
<td>1</td>
<td>0</td>
<td>positive regime change</td>
</tr>
<tr>
<td>0</td>
<td>0</td>
<td>no significant change</td>
</tr>
<tr>
<td>−1</td>
<td>−1</td>
<td>negative regime change: three to five points decrease in POLITY</td>
</tr>
<tr>
<td>−2</td>
<td>−2</td>
<td>adverse transition: more than five points decrease in POLITY score</td>
</tr>
<tr>
<td>−66</td>
<td>−66</td>
<td>interruption</td>
</tr>
<tr>
<td>−77</td>
<td>−2</td>
<td>state failure</td>
</tr>
<tr>
<td>REGTRANS Value</td>
<td>REGTRANS2 Value</td>
<td>Polity IV Interpretation</td>
</tr>
<tr>
<td>----------------</td>
<td>----------------</td>
<td>--------------------------</td>
</tr>
<tr>
<td>96</td>
<td>−2</td>
<td>state disintegration</td>
</tr>
<tr>
<td>97</td>
<td>0</td>
<td>state transformation</td>
</tr>
<tr>
<td>98</td>
<td>−2</td>
<td>state demise</td>
</tr>
<tr>
<td>99</td>
<td>0</td>
<td>state creation</td>
</tr>
</tbody>
</table>

### 3.3.4. Descriptive Statistics

Descriptive statistics are particularly important in this case because they both help ensure the validity of the empirical approach and provide a comparison baseline for the empirical results. There are 195 countries in the modified dataset with 1,118 country-years of transition or interruption as coded by the REGTRANS2 variable (i.e., exclusive of creation and transformation codes 97 and 99). These amounted to 445 unique periods of transition, or over two episodes per country (Fig. 3.8). (The statistics on the country-year level of analysis are similar to those at the episode level, so they are not presented here.) Interceding interruptions or state failures are counted as part of the transition period and not as separate episodes. For example, if a transition starts in Year 1, there is foreign intervention in Years 5-10 (special code −66), Years 11-12 are coded as transition or state failure, and a non-transitional regime is established only in Year 13, all of these events are counted as a single 13-year transition episode.

---

**Figure 3.8. Transition Episodes by POLITY Change**

<table>
<thead>
<tr>
<th>REGTRANS2</th>
<th>Episodes</th>
<th>Interpretation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
The 402 episodes that resulted in substantial changes in POLITY (445 less 43 interruptions that ended with POLITY classification very close to that at the outset of the transition) exhibit a bimodal clustering in the extreme categories; most episodes produce large moves in the POLITY score and minor democratic transitions are particularly rare, accounting for less than 10% of the sample.\textsuperscript{24} Nearly 58% of episodes are negative: 258, inclusive of interruptions, versus 187 positive ones. More than half of the episodes are single-year (Fig. 3.9). Durations over 10 years typically correspond to state failure and/or continuous war, with the notable exception of the Meiji Restoration in Japan.

\textsuperscript{24} The bimodal distribution of transition outcomes is maintained even if the minimum restrictions on the POLITY score change are removed.
As of 2013, there were 10 ongoing transitions, among them four failed states (Haiti, the Central African Republic, Libya and South Sudan) and two foreign interventions (Bosnia and Afghanistan). The dataset does not indicate any ongoing transitions as of 1800, only records the time-of-entry POLITY score for the 22 pre-existing states. Roughly a quarter of the countries each had experienced no episodes at all or just one episode (Fig. 3.10). Another quarter had two to four episodes. Thus, there is a satisfactory amount of variation in the REGTRANS2 variable across various levels of analysis.

The number and percentage of ongoing episodes varies with the yearly sample size (Fig. 3.11). The spikes in the chart correspond to major military conflicts – the Napoleonic Wars, World War I and World War II, when many countries are under foreign control (−66), and the period in the immediate aftermath of the collapse of the Soviet bloc. With or without those interruption observations, however, the annual propensity to transition appears strongly correlated with the number of states in the world system, as the transition total
and its percentage of the global system membership overlap closely. Unsurprisingly, as empires collapse, so does stability. What is more interesting is that the number of countries in transition appears to remain a fairly constant proportion of the number of states in the world system for the time span of the series. In other words, there does not seem to be a discernible trend in transitions.

Figure 3.10. Country Cases by Number of Episodes
There is also substantial variation in regime types, even after the POLITY scores and component variables are aggregated into larger categories. (POLITY2
scores are nearly uniformly distributed when considered at the basic country-year level of analysis.) The number of mature democracies shows an almost uninterrupted upward trend since they first appeared on the scene in 1845, which is punctured only by World War II (Fig. 3.12). Their share of the overall number of countries in the dataset appears to have subsided in the second half of the 20th century largely because of decolonization; too many of the newly independent states quickly slipped into various forms of non-democracy.

Figure 3.13. Regime Types as Percentage of All States (DEML) 1800-2013

When plotted as a percentage of the total number of states (Fig. 3.13), it is evident that democratic regimes surpassed the 50% mark about the mid-1990s, a proportion of democracies unseen since the immediate aftermath of World War I. There is a clearly identifiable upward trend both in the number and proportion of full democracies. From the perspective of modernization theory in its original variant, the time trend can be interpreted as a reflection of rising income levels. These data are not inconsistent with the redistributive theories either, as they deal
primarily with when and what triggers transitions and not so much with their success. Regardless of the focus, a qualitative look at the data reveals that in relative terms most states that have democratized successfully by either measure typically do not exhibit a “natural-resource curse” or other types of extreme inequality where both most of income and the factors of production are controlled by a tightly knit elite.

A similar picture emerges from the data on level of democracy (Fig. 3.14) appear to be tightly correlated with capitalization (Fig. 3.15). As can be expected from its construction, the capitalization score CAPIT appears closely correlated with the POLITY score, at least in the aggregate. Using the distance correlation as a robust measure of independence (Szekely, Rizzo, and Bakirov 2007), the picture looks a lot more nuanced (Fig. 3.16).
For example, since the fall of the USSR, the correlation of the mature democracy variable with capitalization has dropped almost to 19th century levels, diverging broadly from the capitalization correlation of level of democracy, which is near-perfect. The average correlation between CAPIT and DEMM was 0.51 with mean deviation\textsuperscript{25} of just under 0.23, which suggests a wide variation in the correlation between the two variables. This makes sense theoretically at least because CAPIT is categorical and somewhat more nuanced, whereas DEMM is dichotomous and very restrictive relative to the component variables. This story is consistent with the higher 0.79 average correlation of DEML with CAPIT and its much lower mean deviation of 0.12. The divergence can thus indicate the presence of a growing number of capitalized or capitalizing countries, which have not yet crossed the threshold to be counted as mature democracies. Of course, a disaster scenario where a group of mature democracies are becoming decapitalized is also a possible explanation. To adjudicate which one is more likely, it is necessary to look into the data at a more detailed level (see Section 3.4).

\textsuperscript{25} Several different metrics showed that the correlation coefficients are not normally distributed, thus the mean deviation is reported to avoid bias (see Gorard 2005).
As evident from Fig. 3.15, the yearly distribution of CAPIT is bimodal – first between despotic and authoritarian conditions and, after a transitional period, between despotic/totalitarian and democratic conditions. Failed states seem to be a distinguishing feature of colonial decline. What stands out is the disappearance of semi-competitive states, where a constrained unelected executive cohabitates with a constraining legislature or regional authorities. As of 2013, almost 2/3 of all states had some form of competitive political environment. A reversion to the mean trend of declining proportion of totalitarian, despotic and tribal states can be observed. Sham democracies fade away. A second-order bimodality of sorts seems to have collapsed this transitional species into either fully competitive pluralist status or semi-authoritarianism. As a validity check, all state values of CAPIT for 2013 are included in Appendix II.

3.4. ASSESSMENT STRATEGY AND EMPirical METHODOLOGY

From a methodological perspective, there are three main areas of special attention suggested by particular characteristics of the Polity IV dataset. The first object of special concern is implied by the exploratory analysis in the previous subsection. There is strong correlation between the dependent variables – measures of democracy and its durability – and the explanatory variables – the measures of capitalization of the political system in each country. It should be noted that this high correlation is not necessarily problematic because much of it is due to the “bad” cases where the states are coded as undemocratic and typically they do not have good competitive conditions. The testing ground for the theory are the cases with persistently good competitive conditions, which, if coupled with economic development, should result in democratization and its subsequent consolidation. The empirical assessment of the theory must aim to control for the
correlations between the variables created by the way they are constructed from the component variables in Polity IV.

Second, control data for the main competitive explanations for democratization are not available for the time span of the Polity IV data. Modernization theory and distributive theory require data on income levels and income distribution within each polity. Income data going back to the 19th century are only available through the Maddison Project dataset, but it does not cover many of the countries in the Polity IV dataset and there certainly are reliability concerns with data derived for such a remote period in the past. Comparable data on income distribution simply are not available prior to the mid-20th century. Thus, it is necessary to define and evaluate the alternative causal paths of those theories in conjunction with PCT and disentangle their potential confounding effects insofar as the available data permit or qualify the results accordingly. This is done in particular detail in the substantive evaluation of 20th-century transition waves in Section 3.6.

Finally, the nature of the dataset presents a more technical challenge. The time span of the data truncates the time series in ways which may lead to mismeasurement of the effects and therefore bias the results. Thus, depending on the nature of each test, some data may need to be excluded or adjusted in a reasonable way. For example, in comparing the effects of state survival and PCT, it may be necessary to implement robustness checks by conducting an alternate test on the sample exclusive of any states that predate the inception date of the Polity IV time series. Additionally, sampling accuracy and omitted data (both countries and potential control variables) may also confound the results. As noted earlier, despite its unmatched comprehensiveness, Polity IV does not cover all state entities since 1800 and the lack of comparably extensive economic data does not make the task at hand any easier. If the confounding effects cannot be
identified or extracted, the only remaining approach is to randomize them in order to make their effects as uniform as possible within the units of analysis. Within the comparative method, in an analogous situation it would be necessary to compare between cases at perceptibly similar levels of income and income distribution. In a large-dataset test such as the present one, the same methodological goal of negating the confounding effects can be achieved in the opposite way – by expanding the analysis to latent “unobserved” configurations of the data. This can be done by could be done at each level of analysis (country-year, transition episode and country) whenever such techniques can be implemented.

In the absence of control data, the use of regression methods would be suspect at best. In such circumstances, the empirical work is limited to using sample probabilities and correlations, simulated data, and close qualitative and theoretical examination of any relationships uncovered. Of course, the primary concern is to avoid confusing correlation with causation or misidentifying spurious causation as supportive of the theory. Four groups of conceptual variables are relevant to understanding these considerations and some simplifying notation is presented in Fig. 3.17.

Figure 3.17. Notation of Relevant Variables/Empirical Variation

<table>
<thead>
<tr>
<th>Notation</th>
<th>Definition and Relevance</th>
<th>Examples</th>
</tr>
</thead>
<tbody>
<tr>
<td>$P$</td>
<td>probability measures that can be used to compare effects on outcomes</td>
<td>probabilities derived from sample frequencies</td>
</tr>
<tr>
<td>Notation</td>
<td>Definition and Relevance</td>
<td>Examples</td>
</tr>
<tr>
<td>----------</td>
<td>--------------------------</td>
<td>----------</td>
</tr>
<tr>
<td>$D$</td>
<td>dependent variables regarding levels of democracy and its resilience</td>
<td>DEMM, DEML, DDEMM, DDEML1, DDEML2, POLITY</td>
</tr>
<tr>
<td>$S$</td>
<td>within-model explanatory variables related to capitalization of the polity</td>
<td>CAPIT, DCAPIT</td>
</tr>
<tr>
<td>$T$</td>
<td>within-model transition-related variables that may be dependent or explanatory according to the context</td>
<td>REGTRANS, REGTRANS2, DT</td>
</tr>
<tr>
<td>$C$</td>
<td>confounding omitted or latent variables</td>
<td>income and its distribution, cultural and political institutions not measured by POLITY, dynamic effects of the interstate system</td>
</tr>
</tbody>
</table>

The situations where causation can be misidentified can be divided into three general categories (Fig. 3.18, interrupted lines indicate spurious relationships or data):

i. *spurious causation* introducing bias due to omitted variables, which have an independent effect on the dependent variable, cause the variation in both the dependent and the independent variable, or are correlated with the explanatory variable due to mismeasurement or misspecification;
ii. *reverse causation* where the dependent variable is correlated with the explanatory variable but the causal path specified by the model is in reverse of the one actually producing the correlation;

iii. *sampling error* in which the relationship is an artefact of statistical sampling or availability bias (the propensity to use methods and data which are readily available or serve non-research goals).

Figure 3.18. Schematic Examples of Misidentification of Causal Relationships

The capacity to minimize the probability and potential impact of spurious causation is constrained by the sample data. Subsampling and designing critical or quasi-critical tests will be used to address this problem. To account for the second set of issues, it is necessary to conduct robustness checks using subsamples where democracy is at sufficiently low levels so as not to be a concern. Addressing
the first two issues in such a multifaceted way will also help mitigate the possibility of sampling error.

3.5. EMPIRICAL ASSESSMENT

There are three levels of analysis available for falsification of the theory within the Polity IV data. The country-year unit of analysis would provide the largest sample with the most variation in both dependent and explanatory variables, but it is also the most severely affected by sampling issues. A few long-lasting polities such as the US and UK which had both substantial political and economic capital account for a disproportionately large proportion of the observations. This is not to say that the theory could not be falsified using these data, but the results can be suspect due to the potential sampling bias and spurious causation.

This makes necessary to also to conduct tests at the transition level of analysis. This approach would help introduce some controls for oversampling from democratizing cases as democracies also appear to be more resilient states overall (their proportion in the sample grows over time). The distinct focus on the intermediate transition level is justified beyond these methodological considerations because much of the support for democratizations in the real world is concentrated particularly on those most promising cases. However, given the limited amount of data such may not be feasible.

The evaluation begins with finding the sample probabilities $P(D|S)$ for the dependent variables, given certain conditions on the explanatory variables are met. This is done using a simple algorithm. First, outcome dummies for the desired duration and value of the dependent variables are attached to each country-year observation. For example, for country-year AAA1801 the value of the hypothetical
outcome dummy DEMM_5 takes a value of 1 if the value of DEMM in country-year AAA1806 is 1. In other words, DEMM_5 shows whether the country is a mature democracy five years down the line. Taking the outcome dummy as the new dependent variable D, it is possible to compute sample probabilities $P(D|S)$ using Bayes’ rule:

$$P(D|S) = \frac{P(S|D)P(D)}{P(S)}$$

Taking this indirect approach – rather than using sample frequencies to arrive at the conditional $P(D|S)$ – builds into the process a technical bulwark against selecting on the dependent variable.

In computing the component probabilities on the right side of the equation, it is necessary to control for sample truncation – i.e., that outcomes after the year 2013 are not available. Thus, the sample priors $P(D)$ and $P(S)$ are calculated using a subsample exclusive of the observations whose outcome values are unobservable due to the truncation. In this example, if the explanatory variable $S$ is the country-year value of CAPIT, then for the five-year forward horizon of a hypothetical outcome variable such as DEMM_5, observations after 2009 will be counted towards neither the numerator (occurrences of the desired value of CAPIT) nor the denominator (the total number of potential observations) of the sample prior $P(S)$.

Additionally, the computation of the posterior requires nonzero values in the explanatory prior that appears in the denominator. Because the dataset does not contain all possible combinations of explanatory and outcome variables, it is necessary to agglomerate the values of the explanatory variables into “thicker” category so as to induce a positive value for the denominator $P(S)$ within each
data cell. Thus, for example, instead of looking at the posterior probability of a country attaining a mature democracy given a sustained value of CAPIT of 1 and comparing that to probabilities for other values, it is necessary to compare probabilities between connected ranges of CAPIT (e.g., \( \text{CAPIT} > 0 \) versus \( \text{CAPIT} > 1 \)). This approach is also necessary because minor fluctuations in CAPIT would quickly eliminate duration observations if those are restricted to specific values.

Fig. 3.19 displays posterior probabilities for having achieved mature-democracy status (\( \text{DEMM} = 1 \)) for at least five consecutive years (i.e., \( \text{DDEMM} > 4 \)) after a given period of minimum capitalization. The horizontal axis shows the number of years of maintaining a minimum level of capitalization before the reading of \( \text{DDEMM} \) is taken. For example, a country which has had \( \text{CAPIT} = 3 \) for the past 10 years has about 5% probability of having had a five-year streak (or longer) of mature democracy (the grey line in the graph). The black curve at the bottom of the graph captures probabilities of democratization for having been in the sample a number of years, which are represented on the horizontal axis. This is the baseline average reading for the entire sample available without controlling for capitalization levels – i.e., without restriction on the minimum level of political competitiveness. The almost constant probability of about 1% suggests no obvious correlation between the length of a state’s presence in the sample and its developing a mature democracy of a five-year duration. If anything, the probability seems to peak at about 12 years of existence and then declines to about half a percentage point by year 30. This dynamic likely reflects the self-reinforcing nature of persistent deinstitutionalization in failed states; when failed and occupied states are excluded – the dotted line corresponding to states with \( \text{CAPIT} \) values above \(-2\), – the far end of the curve levels off somewhat, approximately doubling the probability at those durations.
As expected by the theory, the probability of maturing democracy increases substantially as capitalization persists. The advantage of states with $\text{CAPIT} > -1$, which excludes not only failed and occupied states but also totalitarian, despotic and other anticompetitive systems, increases from double the baseline in year 10 to quadruple in year 20 of maintaining their level of competitiveness. In other words, just by maintaining a minimum of an authoritarian government, the probability of a sustained period of democratization must increase substantially. Accordingly, this suggests that adverse institutional settings – the deinstitutionalization which characterizes failed states and the institutionalized anti-competitiveness of totalitarian regimes – must have a substantial deleterious effect on the odds of democratization. Just staying above the totalitarian/tribal level of capitalization (i.e., by maintaining $\text{CAPIT} > -1$) results in an enormous improvement in the probability of becoming a mature democracy: more than six times the baseline at longer capitalization durations. That probability itself is doubled if the minimum level is raised another notch to $\text{CAPIT} > 0$. In other words, the probability of becoming a mature democracy lost from dipping below
semi-authoritarian levels of competition (CAPIT = 1) is the same as dipping from an authoritarian minimum into totalitarianism, tribalism or other anti-competitive (de)institutionalized settings.

In drawing these conclusions, it is important to note that the with every increase in the CAPIT minimum, there is a corresponding increase in the number of sample observations excluded from the computation of the posterior, thus the potential for bias in the computation relative to the underlying theoretical population is greater. However, the large margin of differentiation even at the lower thresholds of capitalization somewhat alleviates these concerns. Furthermore, subsampling does not alter the relative values substantially even if absolute probabilities decline across the board. For example, the relationships are maintained even when the US and the UK are excluded from the sample (Fig. 3.20), and when DDEM values of 10 and 20 as minimum levels of consolidation.

Figure 3.20. Sample Probability of Having Maintained a Mature Democracy for at Least Five Years (US, UK Excluded)
As the graph suggests, the exclusion of the US and UK removes a lot of positive observations from the posterior of the sample and a disproportionately smaller part of the total number of observations, which leads to overall decreases in the estimated probabilities. Nevertheless, the large differentials between the lower and medium levels of capitalization are maintained, remaining in the range of orders of magnitude, which is still substantial support. In addition, the duration lines are much better behaved than in the general sample, with monotonic increases in the probability of sustained mature democracy both in absolute and in relative terms as the threshold capitalization is maintained over longer periods.

Another robustness check involves subsampling over time – by excluding the 19th century, when there is a clear dichotomy between the UK, the US and a handful of other longtime democracies and a large number of authoritarian states. This has the effect of eliminating from the sample observations attributable to states that never democratized such as Bavaria, which were overrun by the German and the Italian unification, as well as some defunct states in Latin America. There are a couple of differential observations to be made relative to the complete sample. As expected from the data exploration, there is a compression at the top of the graph perhaps corresponding to the near-disappearance of sham democracies in the 20th century. But surprisingly, in absolute and relative terms the bottom three lines in Fig. 3.21 are close to identical to those in Fig. 3.19. This seems to strengthen support for the conjecture made in coding the CAPIT metric that conditions of deinstitutionalization or active suppression of political competition will likely have disproportionate and more sustained effects on the territory’s long-term prospects of democratization.
Within the subsample beginning in the year 1901, the relative differences remain discernible between the categories, with the exception of the distinction between pluralist and sham-democratic societies, which seems to disappear as the top two series almost perfectly overlap. The difference between the authoritarian floor (CAPIT > 0) and the totalitarian floor (CAPIT > −1) is again the most pronounced, but other margins have shrunk, especially in relation to the baseline. The increase in the baseline can be due to several factors. First, the exclusion of the 19th century eliminates from the sample a large number of observations with strictly nondemocratic values on the dependent variables. Second, there is a possible income effect, where the global increase in incomes is lifting all boats in terms of probability of democratization, in line with the predictions of modernization theory. If indeed present, such an impact would be highlighted by the exclusion of the poorer 19th-century subsample.
The use of floors as identifiers rather than strict categorization on the explanatory variable CAPIT is necessary because of two empirical facts. First, the CAPIT prior $P(S)$ on singleton levels of capitalization (e.g., $\text{CAPIT} = 0$ for $n$ consecutive years) is zero for durations of more than 5-10 years at the lower levels simply because they are too unstable to generate such durable sequences in the first place. This precludes finding the posterior on the dependent variable $P(D|S)$ because division by zero is not feasible. Second, the likelihood $P(S|D)$ cannot be calculated from frequencies for the same reason because mature democracy, for example, does not overlap at all with lower levels of CAPIT, particularly over longer periods. This result in effect lends support to the theory, as it can be interpreted as persistent deinstitutionalization of competition undermining long-term prospects for democratization. These findings are generally resilient to different operationalizations of democratization – i.e., using durations on DEML instead of DDEM as the dependent variable.

The core empirical prediction of PCT – about the effect of institutionalized competition on democratization and its consolidation relative to other potential focal points of pro-democratic reform. This is even more strongly consistent with the 20th-century subsample, where sham democracies and true plural societies ($\text{CAPIT} = 2$ and $3$, respectively) are almost identical in their prospects for democratization as long as non-chief-executive channels for competition are maintained open over sustained periods. This is the case because, by the very coding scheme, the distinction between these two top levels of participation is entirely based on the unfree selection of the chief executive in a sham democracy. Over longer durations of maintaining a minimum of semi-authoritarian level of competition ($\text{CAPIT} > 0$) even their probability converges to that of the top two competitive levels and diverges from the lower, authoritarian floor (right edge of Fig. 3.20).
The maintained strong effect of slipping even briefly into totalitarianism, tribalism or other forms of political organization that are destructive to institutionalized political competition and inimical to the preservation of political capital, let alone its further accumulation, also lends some credence to the main proposed mechanisms of PCT. If these results are true, the bottom line is that from a policy perspective it may be more appropriate or valuable for the long-term good of the population to encourage despotic regimes and totalitarian states to allow some level of institutionalized competition and “upgrade” to an authoritarian mode of government, rather than trying to fix semi-authoritarian or sham-democratic polities.

3.6. **Substantive Analysis**

Of course, this large-sample analysis is far from conclusive in light of the limited data available which do not allow for good controls and may further be of suspect validity as they produce some rather “thick” categories of institutionalized competition. The latter is itself only one component of the overall theory – a necessary but by no means sufficient condition. Beyond the undoubtedly gradual experience of the Great Britain and the United States, there are a wide spectrum of transitions that depart widely from this “managed” mode of expansion of suffrage and political competition. It is important to note that the political-capital theory of democratization does not necessarily imply that the gradual transitions would be the norm or even more successful (faster and stabler) than others. The critical driver in the theory (beyond economic development) is the accumulation of political capital among a society’s elites. Indeed, economic factors themselves are just a proxy for the social and technological characteristics that underlie a complex society where political capital is more valuable and the opportunity costs of
violence are so disruptive as to make it highly unattractive as a tool of conflict
resolution, if not altogether unthinkable.

In large-scale studies, almost by definition political capital’s effects have to
be incorporated by means of proxies and instruments because of its multifaceted
and intangible nature. Time alone is not a good proxy for political-capital
accumulation even though this approximation had to be used in the preceding
subsection due to the operationalization constraints posed by the Polity IV data.
One strategy to falsify the theory is to take a more qualitative look at a wide range
of successful and not-so-successful transitions around the globe, which are fairly
well-documented. This subsection reviews and compares a number of cases of
transitions from Latin America, post-Soviet Eurasia and East Asia, which
encompass a diverse range of initial conditions and “final” outcomes. Indeed, even
in a qualitative context, when a transition ends and another regime begins is itself
an exigent question.

3.6.1. EAST ASIA

In terms of its experience with democracy since World War II, East Asia
offers perhaps the most diverse set of experiences ranging from quickly
consolidated democracies to gradual to frequently reverting regime changes. The
success stories of the region – Japan, Taiwan, South Korea and Singapore – share
a lot with, but also differ a lot from, the history of postwar West Europe. Japan had
had parliamentary elections and some level of legislative control for more than
half a century before the American occupation and the defeated emperor,
worshipped by much of the populace, remained and supported the democratic
changes imposed by the occupiers. Foreign aid and military presence, as well as
the complete lack of resistance due to the imperial sanction, acted as the
authoritarian incubator in which democracy could take hold. The authoritarian
regimes supported by the United States in the other three countries in this group established quickly sham democratic institutions or continued preexisting ones. All of them developed bustling economies and only slowly liberalized their societies, gradually introducing multiparty elections before allowing even their presidents to be elected freely. In none of those cases were there any purges of the ruling classes during the transition, with the exception of legitimate corruption charges. There can hardly be better examples of the political-capital theory at work than these three authoritarian states. Left to their own devices and encouraged economically, they transitioned successfully without missing a heartbeat.

Meanwhile, the region abounds in failures. The Philippines, Indonesia and Burma were all slated to be democracies at their time of independence and established democratic or semi-democratic governments as their foreign overlords rushed to leave. They were at the time all undeveloped extractive economies without much of a history of independent statehood or well-preserved colonial institutions with lasting local government. Thus, democracy could not survive for long without foreign military support and they all reverted to military dictatorship. The Philippines, which emerged first from the darkness, also had the fastest economic development among the three and maintained the full swathe of sham-democratic institutions throughout the decades of authoritarian rule, which is consistent with theoretical expectations. Indonesia started off much worse economically and with virtually no democratic institutionalization or well-functioning elites, so its democracy is much younger and more fragile. Burma, a long-lasting totalitarian state, with its rock-bottom incomes and essentially abolished electoral institutions, is where dictatorship has survived the strongest.
3.6.2. East Europe and Central Asia

Post-Soviet transitions pose a particularly stark challenge for the theory because of their ostensible inconsistency with its core tenets and because of the transitions’ widely differentiated outcomes. The decline of the Soviet Union and particularly glasnost unleashed several competing alternatives to the dominant ideology of state communism-Leninism: democracy, nationalism and militarism. The communist bloc states involved in this group of transitions started in 1988 can themselves be divided in three broad groups: success stories in Europe, most of which have joined the EU; authoritarian and semi-authoritarian regimes in Russia, the Caucasus and Central Asia; and conflict or failed states – Moldova, Georgia and Ukraine.26

The conflict states present no difficulty for PCT. Although these countries shared very similar fate with the rest of the Soviet bloc, their economic development after the fall of the Soviet Union was severely impaired by Russian military intervention making it impossible to sustain institutional stability. The frozen conflicts in Transnistria (Moldova), South Ossetia and Abkhazia (Georgia), and the south and east of Ukraine have had a pronounced impact on the respective countries. Ironically, these were among the regions with the highest economic potential within each of these formerly Soviet states. That conflict has affected their economic development is quite clear from a simple juxtaposition of conflict duration and income levels. Moldova, with its conflict nearly a quarter-century

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26 It is hard to determine whether Armenia should be counted towards the second or the third group, as it is a semi-authoritarian polity with a frozen conflict in reverse – while Armenia has occupied foreign territory rather than the opposite, its frozen occupation and national security create a similarly powerful draw with Russia.
old, is the poorest country in Europe with a per capita GDP of less than $4,000 in 2015, followed by Georgia with $7,200 and Ukraine at about $8,300.

Perhaps the only significant query within this group is why Ukraine did not manage to build a sustained democracy before the Western and Russian intervention in 2014, given that it was among the most developed and resource-rich regions of the former Soviet bloc. Perhaps the explanation for the country’s fate is not only the lack of commitment from the EU over the previous couple of decades to help it develop economically and integrate, but also its longer-term lack of institutional and even government traditions. The Russian-imperial and early Soviet legacy is what it shares with Belarus, Russia and the authoritarian states of Central Asia. Although elections were held for a few years in the late imperial period and before Lenin’s death in 1924, almost without exception these countries never had a sustained experience of electoral democracy and even independent statehood before the dissolution of the Soviet Union.

This history is in sharp contrast to the Baltic states and the other Soviet satellites which had had electoral institutions for decades if not centuries before World War II. Democratic practices and institutional features throughout the region existed in a way that was completely foreign in the Russian Empire and the Soviet Union that superseded it. Despite that authoritarianism was the norm from Poland to Greece before World War II, all of these countries had established government and democratic aspirations and institutionalized methods of political competition, even if those were often rigged and/or suppressed. Although only Czechoslovakia had sustained a democratic government throughout the interwar period, the Baltic states were the only other ones to remain democratic until well into the Great Depression, despite just having regained their independence in the aftermath of World War I. Hungary had a parliamentary tradition going back about half a millennium almost without interruption. Bulgaria had one of the most
liberal constitutions in the world, with universal male suffrage at age 21 as early as 1879.

Surely, the 45 years of totalitarian rule cannot be discounted just on the basis of these ancient legacies. Few of the people alive in the early 1990s had any memory of when those institutions, let alone democratic aspirations, had last been at work. And where such memory would have existed it was of the unhappy days of the Great Depression. It therefore appears that PCT fails to account for the region’s successful transitions, many of which have sustained democracy for over a quarter-century. The quantitative analysis showed that such anti-competitive regimes would have a much lower chance of successful transition than the authoritarian states that preceded most of them and failed to democratize.

The totalitarian experience – and the transitions to democracy – of post-Soviet Europe is distinct from other regions in several important aspects. First, in establishing the people’s republics after 1946, the Soviets generally sought to restore or maintain the pre-existing elected institutions such as legislatures and courts, even of those were purged and elections were merely a sham for the next 45 years. To the extent that it did have any, communism brought to the region several favourable developments – secularism, women’s social equality and enfranchisement (at least on paper), free higher education and industrialization. Second, on their way out of communism, only Romania, Slovenia and Croatia experienced any violence, but even they did maintain their communist-era institutions and, as in most of the remaining countries in the region, it was communist party elites that supported and often even initiated their transitions. Throughout the region, these elites were never excluded from political life despite the lustration laws and new constitutions that were adopted throughout the region in the following decade – in other words, political capital was effectively transferred to the new regimes. Third, the transitions were triggered internally and
for the most part there was a consensus between elites and masses that democracy (and not strongman regimes, for example) would be the destination. Except for some more conservative elements of the party elite, there was no real resistance that could mobilize against the changes and no foreign enemy to use as rallying point for such resistance (with the notable exception of the Yugoslav republics). If anything, clever foreign intervention reinforced the process by the enormous flows of accession funds from the EU that soon started flowing east and were conditional on sustained democratization. These are all characteristics consistent and even integral to the core mechanism of political-capital theory.

Thus, it appears that this set of transitions fail to falsify the theory in a conclusive way and perhaps even lend substantial qualitative support to its main claims. The within-region differentiation in outcomes between the more economically advanced and institutionalized states on one hand and the anti-competitive and militarily disrupted transitions on the other is largely in concert with theoretical expectations.

### 3.6.3. Latin America

The most interesting longitudinal and cross-sectional comparisons can perhaps be made in Latin America. Among many tumultuous national histories, perhaps those of Mexico and Argentina stand out as the most telling and diametrically contrasting. By 1912, Argentina had world-beating literacy rates, was among the dozen or so richest countries in the world, implementing an industrialization program to diversify its economy away from the primary sector, and introduced universal male suffrage. Even though it had essentially been ruled by the agricultural oligarchy, the country had never had a government deposed by a coup. Despite that it was far from a full-fledged democracy, parties of the left and the center were a normal part of political life just as much as the conservatives
supported by the landowners. This peaceful record was sustained after the
election of its first socialist president in 1916 and despite intermittent strife among
workers in some of the provinces, which was associated with the increased
immigration from Europe bringing proletarian ideas to Argentina. Despite the
serious bite of the Great Depression, Argentina’s vast agricultural wealth
positioned the country to weather the crisis better than most of the developed
world until a fascist coup in 1930 deflated its prospects of democratizing further.
After a brief return to elected government, over the next dozen years its military
became increasingly radicalized by fascist commanders and other conservative
elements. The generation of officers coming of age in the 1930s and 1940s would
turn military government into ordinary practice for almost half a century. Between
the 1930 coup and the end of the Falklands’ War, Argentina had 23 presidents, of
whom 13 were military dictators and most of the rest were installed either by a
junta or a rigged election. Particularly damaging in the Argentine case were the
intermittent campaigns of “disappearance” of thousands of political activists and
members of civil society opposed to the fascist elements in the military. This
practice normalized violence and disconnected political entrepreneurs from
institutionalized competition, which has made the return to democracy since the
early 1980s rather insecure.

Meanwhile, Mexico had had a diametrically opposite experience, with
some dozen coups in about half a century of independence as well as the French
and American military interventions that essentially bankrupted the country and
stripped it of half of its territory. Mexico was by that time massively
underdeveloped and struggled to feed its own population, the vast majority of
which lived in poverty and ignorance. This tumultuous history was topped off by
the unabated despotism of the Porfiriato that lasted from 1876 to 1911 and collapsed
into a quarter-century of almost unrelenting civil war. The country was not
substantially pacified until the creation of the Institutional Revolutionary Party (Partido Revolucionario Institucional or PRI) in 1929, whose main goal was to protect the 1917 constitution that decentralized governmental institutions and to defang permanently the conservative establishment and the church that had supported or condoned the Porfiriato. The constitutional restrictions on the church in particular would remain in place for some 80 years while PRI would monopolize elected offices, including the provincial governorships, until 1989. However, PRI rule in Mexico was specifically aimed at maintaining institutional continuity even if elections were rigged and opposition candidates suppressed or coopted. After the end of the civil wars, PRI did not engage in the type of terror purges that became the staple of the Argentine juntas. Elected local, provincial and federal offices remained a draw for people who wanted to pursue a career in politics – and the spoils of the graft that accompanied it. It was in local and gubernatorial elections that PRI rule began to show cracks and culminated in the end of one-party control of the presidency in 2000. Despite the Mexican peso crisis in the 1980s and the Asian crisis in the 1990s that both brought the economy to its knees, the transition was handled without large-scale concerted political violence. The country’s gross domestic product is more than twice that of Argentina and has nearly caught up with the southern country even on per-capita terms by 2014.

Overall, only few Latin American countries slipped away from dictatorship in the 19th and 20th centuries before the wave of transitions that started in the 1980s. Sometimes democratically elected governments such as that of Chile in 1973 and intermittently in Central America were toppled by US interventions, while other times they collapsed on their own. Until the 1980s, it appears that the fundamental problem was the economic underdevelopment of the region, coupled with the revolutions and coups that interfered with competitive institutionalization to the extent that it existed. Argentina between the 1860s and
1930 was the exception to the region’s pariah economic status, whereas Costa Rica, with its full democracy sustained since 1890, is perhaps the most puzzling case from the perspective of political-capital theory. The only interruption in Costa Rica’s resilient democracy was due to a brief civil war, whereby a military junta intervened to prevent an attempted coup and then oversaw constitutional changes to abolish the military altogether and grant the vote to women and blacks before handing power over to the newly elected president. It is impossible to explain away this confounding case convincingly.

Much of Latin America’s recent wave of democratizations, however, appears consistent with political-capital theory. Countries such as Brazil, Chile, Peru and Ecuador consolidated military and authoritarian regimes with sham-democratic institutions beginning in the late 1970s before transitioning in the 1990s and early 2000s to democratic rule. This period has also been characterized by rapidly improving socioeconomic conditions. The observed wave of democratizations should by no means be considered irreversible, as much of the region is yet to modernize as of 2015.

3.7. CONCLUSION

This chapter constructed and conducted an empirical test of the political-capital theory of democracy proposed in Chapter 2. Given the dearth of economic data for extended periods in the past, it was necessary to rely exclusively on data from the Polity IV dataset. The sample posteriors point in the direction suggested by the theory but further testing is needed to subject it to more rigorous scrutiny. Overall, countries which do not fall below certain thresholds of political competitiveness appear more likely to progress towards democracy and consolidate in that state. What is particularly telling is that, consistent with
theoretical expectations, beachheads of competitiveness established in transitions from polities which overtly suppress nearly all forms of dissent and competition towards less oppressive authoritarian and semi-authoritarian regimes induce the greatest marginal changes in the probability of improvement. The effects are contingent on sustaining stable competitive institutions, as limited as they may be, over time.

The exploratory analysis and the likelihoods of different observed levels of competitiveness suggest a lot of fluctuation between nondemocratic regime types as defined by Polity IV. While autocracies appear more likely to be unstable, polities towards the top of the POLITY scale show more consistent levels of democracy as measured by this metric. Regimes at the frontier of stability have nearly disappeared from the data probably by passing into the firm democratic zone of no return or descending deeper into the more volatile ranges of autocratic rule.

The differences between varied levels of competitiveness in the probability of progress and stabilization in a democratic context are robust to manipulations with the sample range, but more testing is necessary to address concerns about potential spurious causation by other variables. One such confounding factor could be the level of economic development. As indicated in Chapter 2, from the beginnings of modernization theory to more recent evidence on the subject, the relationship between income levels and measures of democracy is one of the strongest empirical findings in the literature. However, from a theoretical perspective, this effect is expected to be complementary rather than necessarily an alternative to political capital theory.

The common conception of representativeness is one of voters as principals delegating authority to their agents – government officials. In the context of the evidence presented here, Schumpeter’s less sanguine conception of democracy as
voters’ right to have elites compete for their votes resonate stronger. In the stark case of the European Parliament, there may be plenty of accountability but it may not be to the voters. Rather, MEPs are much more dependent on their domestic governments and, particularly, on national parties than on the direct support of their impasive electorate. Instead of addressing the supposed “deficit of democracy” in the EU, the world’s unique supranational assembly may mostly be a counterweight for the national governments in their struggle to keep some level of control over the bureaucracies of the Commission and the lobbyists that permeate them.

The theoretical analysis presented in Chapter 2 sought to extrapolate and refine a more general set of ideas about principal-agent relationships beyond the stark reality of EU lawmaking. The formal theory points in the direction of moving at least some of the focus of research and public attention from issues of accountability to those of developing and selecting adequately prepared and voter-friendly candidates for office. To be sure, accountability is indispensable in the quest for more effective representation. But the selection of the initial pool of candidates is even more impactful.

Political-capital theory adds three important contributions that are not controverted by the Polity IV data to the existing body of knowledge about transitions to democratic government. While previous work has focused mostly on the top levels of institutionalization – e.g., getting from an electoral democracy to a mature one or from an authoritarian regime to nonviolent elections, – the theory and empirical work includes every level of political competition. Indeed, the results are strongest at the lower levels, where it appears that helping states transition from totalitarian and theocratic systems to authoritarian and semi-authoritarian ones may add more long-term value to their overall prospects to democratize sustainably. The differential between the anti-competitive (e.g., tribal,
despotic, totalitarian) and authoritarian regime threshold is the largest and the one that remains nearly identical across different subsamples and robustness checks.

From the qualitative analysis, it also becomes obvious that foreign intervention – regardless of the specific intentions – acts as a disruptor, not as a promoter of the capitalization process and ultimately of democratization unless it is in the form of a complete and determined occupation of the target country with appropriate economic aid. The frozen conflicts in the Russian periphery and the US meddling in Latin America for almost a century now, which often aimed to support democracy (or at least purported to), have surely set back the democratization progress of those regions. Japan and Germany succeeded only after being reduced to rubble and with the absolute commitment – military and economic – of the foreign powers that subjugated them.

Finally, it is important to recognize that there is no single path to democracy nor perfect correspondence between competitive political institutions and resilient mature democracy. The process of democratization seems to be strongly contingent not merely on economic development, but on general socioeconomic modernization, as the Argentine reversal and the success stories in the former Soviet bloc seem to suggest. The single most invariant feature among all the successful cases – as well as many unsuccessful ones – is perhaps that competitive elections had become part of political life long before democracy could take hold. After all, the 13 British colonies had had some 150-200 years of elected local government behind them before founding the republic that is now the United States. Like the party elites of post-Soviet Europe and East Asia, the colonial oligarchies had the good sense of preserving and strengthening the existing institutionalized channels of political conflict and competition.

The effects of elite capacity span far beyond democratization. The stability they seem to help engender in pluralist competitive political systems alongside
economic development is suggestive of their being at the very core of the functioning of democratic government. There are broad implications for the expansion of the body of knowledge of diverse aspects of political institutions: the control of bureaucracies; legislative organization; debates over valence versus spatial voting; pre- and post-electoral coalition politics; presidentialism and parliamentarism and their representativeness and stability. Wherever political agency comes into play, competition is essential to ensuring that votes matter and matter in the right way.
Appendix I. Formal Proofs

PROPOSITIONS 1.1 AND 1.2. The constituents believe that the government is maximizing expected constituent support \( q = \sum_k \eta_k \pi_k \), therefore they envision its first-order condition (FOC) for maximization to be of the type:

\[
\frac{d q}{d x} = \sum_{i \in K} \frac{d q}{d \pi_i} \frac{\partial \pi_i}{\partial x} = \sum_{i \in K} \eta_i \frac{\partial \pi_i}{\partial x} = 0
\]  

(1.1)

The partial differential of the support function relative to policy \( x \) is

\[
\frac{\partial \pi}{\partial x} = \sum_{i \in K} \frac{\partial P(u_i(x, \cdot))}{\partial x} =
\]

\[
= \sum_{i \in K} \frac{\partial (1 - \Phi_i(M_i - \alpha_i(x - x_i)^2 - \beta_i(y - y_i)^2))}{\partial x}
\]

(1.2)

Substituting (1.15) in (1.14) and expanding the sum yields the equivalent FOC:

\[
\eta_k \alpha_k (x - x_k) \varphi_k(M_k - \alpha_k(x - x_k)^2 - \beta_k(y - y_k)^2) =
\]

\[-\eta_k \alpha_k (x - x_k) \varphi_k(M_k - \alpha_k(x - x_k)^2 - \beta_k(y - y_k)^2) =
\]

(1.3)

After rearranging, (1.16) is equivalent to:

\[
\varphi_k(M_k - \alpha_k(x - x_k)^2 - \beta_k(y - y_k)^2) =
\]

\[-\frac{\eta_k \alpha_k (x - x_k)}{\eta_k \alpha_k (x - x_k)} \varphi_k(M_k - \alpha_k(x - x_k)^2 - \beta_k(y - y_k)^2)
\]

(1.4)
Assuming provisionally that \( x_k < x^* < x_{-k} \), group \( k \)'s utility-maximizing strategy is to act so as to induce the lowest possible supply of \( x \). In order to do that, group \( k \) must choose

\[
M_k^* \in \arg \max \varphi_k(M_k - \alpha_k(x - x_k)^2 - \beta_k(y - y_k)^2) \tag{1.5}
\]

Because by assumption the distribution of the random errors is with zero mode and mean, the choice of \( M_k^* \) must be such that \( \varphi_k(M_k - \alpha_k(x - x_k)^2 - \beta_k(y - y_k)^2) = \varphi_k^\max = \varphi_k(0) \). Therefore, the best response of the group in question is implied by the equation

\[
M_k^* - \alpha_k(x^*(M_k^*, M_{-k}^*) - x_k)^2 - \beta_k(y^*(M_k^*, M_{-k}^*) - y_k)^2 = 0 \tag{1.6}
\]

Analogically, it can be shown that for the other group

\[
M_{-k}^* - \alpha_{-k}(x^*(M_k^*, M_{-k}^*) - x_{-k})^2 - \beta_{-k}(y^*(M_k^*, M_{-k}^*) - y_{-k})^2 = 0 \tag{1.7}
\]

However, the government actually maximizes (1.3), therefore its FOC is

\[
\begin{align*}
\frac{\partial q}{\partial x} + \frac{\partial \omega}{\partial x} &= 0 \\
\frac{\partial q}{\partial y} + \frac{\partial \omega}{\partial y} &= 0 
\end{align*} \tag{1.8}
\]

Bearing in mind the constituents' equilibrium values (1.19) and (1.20), the part of condition (1.21) relative to \( \partial x \) is equivalent to:
\[
\sum_i 2\alpha_i(x - x_i) + \sum_i 2\eta_i\alpha_i(x - x_i) \varphi_i(0) = \\
= \sum_i 2\alpha_i(x - x_i)(1 + \eta_i\varphi_i(0)) = 0
\] (1.9)

Noting that the normal density \(\varphi(0) = (\sigma\sqrt{2\pi})^{-1}\) for \(\mu = 0\), the FOCs of the government then become

\[
\begin{align*}
\sum_i \alpha_i(x - x_i) \left(1 + \eta_i\left(\sigma_i\sqrt{2\pi}\right)^{-1}\right) &= 0 \\
\sum_i \beta_i(y - y_i) \left(1 + \eta_i\left(\sigma_i\sqrt{2\pi}\right)^{-1}\right) &= 0
\end{align*}
\]

(1.10)

The FOCs are a maximum because the second-order conditions are negative \((\alpha, \beta \ll 0\) by construction):

\[
\begin{align*}
\left| \frac{\partial}{\partial x} \sum_i 2\alpha_i(x - x_i) \left(1 + \eta_i\left(\sigma_i\sqrt{2\pi}\right)^{-1}\right) \right| &= \sum_i 2\alpha_i \left(1 + \eta_i\left(\sigma_i\sqrt{2\pi}\right)^{-1}\right) < 0 \\
\left| \frac{\partial}{\partial y} \sum_i 2\beta_i(y - y_i) \left(1 + \eta_i\left(\sigma_i\sqrt{2\pi}\right)^{-1}\right) \right| &= \sum_i 2\beta_i \left(1 + \eta_i\left(\sigma_i\sqrt{2\pi}\right)^{-1}\right) < 0
\end{align*}
\]

(1.11)

From (1.23), the equilibrium solution for the government’s strategy is then given by

\[
\begin{align*}
x^* &= \frac{\sum_i x_i\alpha_i \left(1 + \eta_i\left(\sigma_i\sqrt{2\pi}\right)^{-1}\right)}{\sum_i \alpha_i \left(1 + \eta_i\left(\sigma_i\sqrt{2\pi}\right)^{-1}\right)} \\
y^* &= \frac{\sum_i y_i\beta_i \left(1 + \eta_i\left(\sigma_i\sqrt{2\pi}\right)^{-1}\right)}{\sum_i \beta_i \left(1 + \eta_i\left(\sigma_i\sqrt{2\pi}\right)^{-1}\right)}
\end{align*}
\]

(1.12)
Thus, the optimal supply of each policy is just a weighted average of the ideal points of the two interest groups, which is consistent with the heuristic assumption \( x_k < x^* < x_{-k} \).

Substituting the equilibrium values from (1.25) into (1.19) and denoting \( \psi_i = 1 + \eta_i / \sigma_i \sqrt{2\pi} \) yields constituent \( k \)'s equilibrium performance criterion:

\[
M_k^* = \alpha_k \left( \frac{\sum_i x_i \alpha_i \psi_i}{\sum_i \alpha_i \psi_i} - x_k \right)^2 + \beta_k \left( \frac{\sum_i y_i \beta_i \psi_i}{\sum_i \beta_i \psi_i} - y_k \right)^2
\]  

(1.13)

Since the utility functions of all actors are quadratic, preferences are strictly convex and therefore the subgame-perfect equilibrium is unique so there is no need to check for corner solutions. This completes the partial optimization with respect to the policy utility of the constituents, but they also have to choose an optimal quantity of information to consume.

Dropping the subscripts whenever possible, the FOC for the constituents' equilibrium information acquisition is

\[
\frac{\partial U}{\partial c} = \frac{\partial u}{\partial h} \frac{\partial h}{\partial c} - \frac{\partial c}{\partial c} = 0
\]

(1.15)

If \( c > \tau, \partial h / \partial c = 0 \), therefore condition (1.27) cannot be met. Then, in every equilibrium it must be the case that \( c^* \leq \tau \), in which region \( \partial h / \partial c = 1 \). Therefore, it makes sense to define equilibrium information cost \( c^*(h) = h \) with domain \( h \in [0, \min\{\tau, \lambda\}] \) and rewrite (1.27) as the equivalent FOC

\[
\frac{\partial U}{\partial h} = \frac{\partial u}{\partial h} - \frac{\partial c}{\partial c} = 0 \iff \frac{\partial u}{\partial h} = \frac{\partial c}{\partial h} = 1
\]

(1.15)
Whenever \( \partial u / \partial h \leq \partial c / \partial h \) the constituent will choose to consume the maximum available and affordable amount of information \( h^* = \min\{\tau, \lambda\} \), i.e., there will be a corner solution. Otherwise, \( h^* = 0 \). Therefore:

\[
c^* = h^* = \int \left( \frac{\partial u}{\partial h} \leq \frac{\partial c}{\partial h} \right) \min\{\tau, \lambda\}
\]

(1.16)

This concludes the proofs of Propositions 1.1 and 1.2.

**Proposition 1.3.** This follows directly from inspecting the equilibrium policy divergence \( D_k := |x_k - x^*| \). Substituting \( x^* \) with the equilibrium value given in (1.25) and rearranging yields

\[
D_k = \left| x_k - \frac{\sum_i x_i \alpha_i \left( 1 + \eta_i \left( \sigma_i \sqrt{2\pi} \right)^{-1} \right)}{\sum_i \alpha_i \left( 1 + \eta_i \left( \sigma_i \sqrt{2\pi} \right)^{-1} \right)} \right| = \\
= \left| \frac{x_k \sum_i \alpha_i \left( 1 + \eta_i \left( \sigma_i \sqrt{2\pi} \right)^{-1} \right) - \sum_i x_i \alpha_i \left( 1 + \eta_i \left( \sigma_i \sqrt{2\pi} \right)^{-1} \right)}{\sum_i \alpha_i \left( 1 + \eta_i \left( \sigma_i \sqrt{2\pi} \right)^{-1} \right)} \right| = \\
= |x_k - x_k| \left| \frac{\alpha_{-k} \left( 1 + \eta_{-k} \left( \sigma_{-k} \sqrt{2\pi} \right)^{-1} \right)}{\sum_i \alpha_i \left( 1 + \eta_i \left( \sigma_i \sqrt{2\pi} \right)^{-1} \right)} \right|
\]

The last expression is strictly positive and decreasing in the denominator, therefore

\[
\frac{\partial D_k}{\partial \eta_k}, \frac{\partial D_k}{\sigma_k}, \frac{\partial D_k}{\alpha_k} < 0
\]
Meanwhile, since the preference divergence $|x_k - x_{-k}|$ is only present in the numerator,

$$\frac{\partial D_k}{\partial |x_k - x_{-k}|} > 0. \blacksquare$$

**PROPOSITION 1.4.** Taking the first and second partial derivatives of $\omega$ to the two policies respectively yields the FOCs and SOCs

$$\begin{align*}
\frac{\partial \omega}{\partial x} &= \sum_i 2\alpha_i(x - x_i) = 0 \\
\frac{\partial \omega}{\partial y} &= \sum_i 2\beta_i(y - y_i) = 0
\end{align*}$$

The FOCs resolve precisely in the proposed solution for $x^*, y^*$ and the SOCs satisfy the (negativity) conditions for maximum. Again by quasi-concavity of the utility functions, the maxima must be unique. $\blacksquare$

**PROPOSITION 1.5.** To demonstrate the first part of this proposition, it is easiest to work backwards. If $\alpha_k(x - x_k) = \alpha_{-k}(x - x_{-k})$ and $\beta_k(y - y_k) = \beta_{-k}(y - y_{-k})$, then obviously Definition 1.2 is satisfied. Solving these two equations yields exactly

$$\begin{align*}
x &= \frac{\sum_i x_i \alpha_i}{\sum_i \alpha_i} = \bar{x}^* \\
y &= \frac{\sum_i y_i \beta_i}{\sum_i \beta_i} = \bar{y}^*
\end{align*}$$
The proof of the second part is by contradiction. For the rest of the argument, assume without loss of generality\(^{27}\) that \((x, y)_k < (x, y)_{-k}\). Suppose that for vectors \((x, y)\) and \((x', y')\) both conditions \(\Theta(x, y) > \Theta(x', y')\) and \(\omega(x, y) < \omega(x', y')\) are satisfied. If there is to be an improvement in social welfare, then at least one of the policies in \((x, y)\) must be suboptimal. Suppose again without loss of generality that the suboptimal policy is \(x\) so that \(x_k < x < \bar{x}^*\). Then, by the domestic equilibrum solution, \(y_k < y < \bar{y}^*\) must also be true – i.e., \(y\) is also suboptimal. Adding the assumed inequalities for social welfare and social equity together yields
\[
\omega(x', y') + \Theta(x, y) < \omega(x, y) + \Theta(x', y') \iff
\]
\[
\begin{align*}
&u_k(x', y') + u_{-k}(x', y') - |u_k(x, y) - u_{-k}(x, y)| < \\
&< u_k(x, y) + u_{-k}(x, y) - |u_k(x', y') - u_{-k}(x', y')| \tag{1.17}
\end{align*}
\]

Since \(x_k < x < \bar{x}^*\) and \(y_k < y < \bar{y}^*\), by equation (1.5) and Definition 1.2 \(u_k(x, y) > u_{-k}(x, y)\) and thus \(|E[u_k(x, y)] - E[u_{-k}(x, y)]| = u_k(x, y) - u_{-k}(x, y) = -\Theta(x, y)\) so that the condition becomes
\[
\begin{align*}
&u_{-k}(x, y) - u_k(x, y) + u_k(x', y') + u_{-k}(x', y') < \\
&< -|u_k(x', y') - u_{-k}(x', y')| + u_k(x, y) + u_{-k}(x, y) \tag{1.18}
\end{align*}
\]

From this point on, there are two possible configurations that must be considered:

**Scenario 1.** Suppose that \(u_k(x', y') - u_{-k}(x', y') > 0\). Then, inequality (1.31) yields further
\[
\begin{align*}
&-u_k(x, y) + u_k(x', y') + u_{-k}(x', y') < -u_k(x', y') + u_{-k}(x', y') + u_k(x, y) \iff
\end{align*}
\]

\(^{27}\) The proof can be replicated analogically for any combination of ideal points.
\[ u_k(x', y') < u_k(x, y) \quad (1.19) \]

Then \( \omega(x, y) < \omega(x', y') \) requires that \( u_{-k}(x', y') > u_{-k}(x, y) \), but subtracting this inequality from (1.29) leads to:

\[ u_{-k}(x', y') - u_k(x', y') > u_{-k}(x, y) - u_k(x, y) \quad (1.20) \]

Because \( u_k(x', y') - u_{-k}(x', y') > 0 \), \( u_{-k}(x', y') - u_k(x', y') = \Theta(x', y') \), but as was shown earlier \( u_k(x, y) - u_{-k}(x, y) = -\Theta(x, y) \). Substituting these two equalities in (2.33) implies that \( \Theta(x, y) < \Theta(x', y') \Rightarrow ! <. \)

**Scenario 2.** Suppose that \( u_k(x', y') - u_{-k}(x', y') < 0 \). Substitution in inequality (1.31) results in the condition

\[ u_{k}(x', y') - u_{-k}(x', y') - u_k(x, y) < u_{k}(x', y') - u_{-k}(x, y) \iff u_{-k}(x', y') < u_k(x, y) \quad (1.21) \]

But \( \omega(x, y) < \omega(x', y') \iff u_k(x, y) + u_{-k}(x, y) < u_k(x', y') + u_{-k}(x', y') \), which then leads to \( u_{-k}(x, y) < u_k(x', y') \iff u_{-k}(x, y) + u_{-k}(x', y') < u_k(x', y') + u_{-k}(x', y') \) when added to (1.34). Adding (1.34) yet again results in the condition

\[ u_{-k}(x, y) + u_{-k}(x', y') + u_{-k}(x', y') < u_k(x', y') + u_{-k}(x', y') + u_k(x, y) \iff u_{-k}(x, y) - u_k(x, y) < u_k(x', y') - u_{-k}(x', y') \quad (1.22) \]

QED \( u_{-k}(x, y) - u_k(x, y) = \Theta(x, y) \). Since in this case \( u_k(x', y') - u_{-k}(x', y') < 0 \), it equals exactly \( \Theta(x', y') \). Thus, (1.31) must be equivalent to \( \Theta(x', y') > \Theta(x, y) \Rightarrow ! <. \)
**Proposition 1.7.** This proof takes three steps. The first step shows the general relationship between two equilibrium policies and the corresponding distributions of political clout among the constituents. The second one derives the clout distribution necessary to achieve a social optimum in equilibrium. The final step puts the first two together to show how the equilibrium changes as the distribution of clout changes.

Consider the difference $x - x'$ of any two equilibrium policies

$$x = \frac{\sum x_i \alpha_i \psi_i}{\sum \alpha_i \psi_i}, x' = \frac{\sum x_i' \alpha_i \psi_i'}{\sum \alpha_i \psi_i'}.$$  

Some preparatory work is necessary to make them comparable:

$$x - x' = \frac{\sum x_i \alpha_i \psi_i}{\sum \alpha_i \psi_i} - \frac{\sum x_i' \alpha_i \psi_i'}{\sum \alpha_i \psi_i'} = \frac{\sum x_i \alpha_i \psi_i \sum \alpha_i \psi_i' - \sum x_i' \alpha_i \psi_i'}{\sum \alpha_i \psi_i \sum \alpha_i \psi_i'} = (1.23)$$

$$\sum x_i \alpha_i \psi_i \sum \alpha_i \psi_i' = (x_k \alpha_k \psi_k + x_{-k} \alpha_{-k} \psi_{-k})(a_k \psi_k' + a_{-k} \psi_{-k}') =$$

$$= x_k \alpha_k^2 \psi_k \psi_k' + x_k \alpha_k \psi_k a_{-k} \psi_{-k}' + a_k \psi_k' x_{-k} \alpha_{-k} \psi_{-k} + x_{-k} \alpha_{-k}^2 \psi_{-k} \psi_{-k}'$$

$$\sum x_i \alpha_i \psi_i' \sum \alpha_i \psi_i = (x_k \alpha_k \psi_k' + x_{-k} \alpha_{-k} \psi_{-k}')(a_k \psi_k + a_{-k} \psi_{-k}) =$$

$$= x_k \alpha_k^2 \psi_k \psi_k' + x_k \alpha_k \psi_k a_{-k} \psi_{-k}' + a_k \psi_k' x_{-k} \alpha_{-k} \psi_{-k} + x_{-k} \alpha_{-k}^2 \psi_{-k}' \psi_{-k}$$

Further denote the common denominator of the expansion of $x - x'$ (1.36) to be

$$A = \sum \alpha_i \psi_i \sum \alpha_i \psi_i' = (a_k \psi_k + a_{-k} \psi_{-k})(a_k \psi_k' + a_{-k} \psi_{-k}')$$
Substituting the expanded numerator and denominator sums into expression (1.36) for $x - x'$ leads to the equivalent:

$$(x - x') A = x_k \alpha_k^2 \psi_k \psi'_k + x_k \alpha_k \psi_k a_{-k} \psi'_k + a_k \psi'_k x_{-k} \alpha_{-k} \psi_{-k}$$

$$+ x_{-k} \alpha^2_{-k} \psi_{-k} \psi'_{-k}$$

$$- x_k \alpha_k^2 \psi_k \psi'_k - x_k \alpha_k \psi_k a_{-k} \psi_{-k} - a_k \psi_k x_{-k} \alpha_{-k} \psi'_{-k} - x_{-k} \alpha_{-k}^2 \psi_{-k} \psi'_{-k} =$$

$$= x_k \alpha_k \psi_k a_{-k} \psi'_{-k} + a_k \psi'_k x_{-k} \alpha_{-k} \psi_{-k} - x_k \alpha_k \psi'_k a_{-k} \psi_{-k} - a_k \psi_k x_{-k} \alpha_{-k} \psi'_{-k}$$

$$= x_k \alpha_k \alpha_{-k} (\psi_k \psi'_{-k} - \psi'_k \psi_{-k}) - x_{-k} \alpha_k \alpha_{-k} (\psi'_k \psi'_{-k} - \psi_k \psi_{-k})$$

$$= \alpha_k \alpha_{-k} (x_k - x_{-k}) (\psi_k \psi'_{-k} - \psi'_k \psi_{-k})$$

Using that by construction $\alpha_i < 0$ and by assumption $x_k > x_{-k}$, the sign of the difference can be found by taking the sign of each side of the above result:

$$\text{sgn}(x - x') \text{sgn} A = \text{sgn}(\alpha_k \alpha_{-k}) \text{sgn}(x_k - x_{-k}) \text{sgn}(\psi_k \psi'_{-k} - \psi'_k \psi_{-k}) \Rightarrow$$

$$\text{sgn}(x - x') = \text{sgn}(\psi_k \psi'_{-k} - \psi'_k \psi_{-k})$$

Therefore, whenever $x_k > x_{-k}$,

$$x > x' \iff \frac{\psi_k}{\psi_{-k}} > \frac{\psi'_k}{\psi'_{-k}} \quad (1.24)$$

In words, as the advantage in political clout of constituent $k$ increases, equilibrium policy $x$ moves towards that constituent. The proof works analogically for dimension $y$.

For the second step of the proof, suppose that the optimum is also an equilibrium, i.e., that $\bar{x}^* = x^*$, which implies:
\[ \frac{\sum x_i \alpha_i}{\sum \alpha_i} = \frac{\sum x_i \alpha_i \psi_i}{\sum \alpha_i \psi_i} \iff \sum x_i \alpha_i \sum \alpha_i \psi_i = \sum x_i \alpha_i \psi_i \sum \alpha_i \iff \]

\[
(x_k \alpha_k + x_{-k} \alpha_{-k})(a_k \psi_k + a_{-k} \psi_{-k}) = (x_k \alpha_k \psi_k + x_{-k} \alpha_{-k} \psi_{-k})(a_k + a_{-k}) \iff
\]

\[
x_k a_k \psi_k + x_{-k} \alpha_{-k} \psi_{-k} + a_k \psi_k x_{-k} \alpha_{-k} + x_{-k} \alpha_{-k} \psi_{-k} =
\]

\[
= x_k a_k^2 \psi_k + x_k \alpha_k \psi_k a_{-k} + a_k x_{-k} \alpha_{-k} \psi_{-k} + x_{-k} \alpha_{-k} \psi_{-k} \iff
\]

\[
x_k (\psi_k - \psi_{-k}) + x_{-k} (\psi_k - \psi_{-k}) = 0 \iff
\]

\[
(x_k - x_{-k})(\psi_k - \psi_{-k}) = 0
\]

Therefore, in the nontrivial case (i.e., whenever \( x_k \neq x_{-k} \)):

\[
\bar{x}^* = x^* \iff \psi_k = \psi_{-k}
\] (1.25)

That is, to achieve the social optimum in equilibrium, the constituents must have equal clout, which is consistent with Proposition 1.6.

For the final step, setting \( x = x^* \) and \( x' = \bar{x}^* \) in equivalence (1.38), (1.37) implies that whenever \( x_k > x_{-k} \)

\[
x^* > \bar{x}^* \iff \psi_k > \psi_{-k}
\] (1.26)

Finally, it is necessary to check that \( x_k > x^* \):

\[
x_k - x^* = \frac{\sum x_i \alpha_i \psi_i}{\sum \alpha_i \psi_i} = \frac{x_k \sum \alpha_i \psi_i - \sum x_i \alpha_i \psi_i}{\sum \alpha_i \psi_i} =
\]

\[
= \frac{x_k \alpha_k \psi_k + x_{-k} \alpha_{-k} \psi_{-k} - x_{-k} \alpha_{-k} \psi_k}{\sum \alpha_i \psi_i} = \frac{(x_k - x_{-k}) \alpha_{-k} \psi_k}{\sum \alpha_i \psi_i} > 0
\]
since \( \alpha_i < 0 \), \( \psi_i > 0 \) and \( x_k > x_{-k} \). Thus, \( x^* \in (\bar{x}^*, x_k) \). Analogically, it can be shown that \( y^* \in (\bar{y}^*, y_k) \). ■

**PROPOSITION 1.8.** First, it is necessary to expand the ratio down to \( \overline{\sigma} \):

\[
\frac{\psi_k}{\psi_{-k}} = \left( 1 + \frac{\eta_k}{\overline{\sigma}(1 - h_k)\sqrt{2\pi}} \right) = \frac{(\overline{\sigma}(1 - h_k)\sqrt{2\pi} + \eta_k)(\overline{\sigma}(1 - h_{-k})\sqrt{2\pi})}{(\overline{\sigma}(1 - h_{-k})\sqrt{2\pi} + \eta_{-k})}
\]

Denoting \( r \) for the numerator and \( s \) for the denominator of the expanded ratio, the impact of \( \overline{\sigma} \) on the ratio can be shown by taking the partial derivative in order to determine its sign:

\[
\frac{\partial}{\partial \overline{\sigma}} \left( \frac{\psi_k}{\psi_{-k}} \right) = \frac{r's - rs'}{s^2} \iff \frac{s^2}{\sqrt{2\pi}} \frac{\partial}{\partial \overline{\sigma}} \left( \frac{\psi_k}{\psi_{-k}} \right) =
\]

\[
= \left( (\overline{\sigma}(1 - h_{-k})\sqrt{2\pi} + \eta_{-k})(1 - h_{-k})(1 - h_k)^2 - (\overline{\sigma}(1 - h_k)\sqrt{2\pi} + \eta_k)(1 - h_k)(1 - h_{-k})^2 \right)
\]

It is obvious that since \( s^2/\sqrt{2\pi} > 0 \), the sign of the derivative is the same as that of the last expression, which can be divided further by \( (1 - h_{-k})(1 - h_k) > 0 \), yielding:

\[
(\overline{\sigma}(1 - h_{-k})\sqrt{2\pi} + \eta_{-k})(1 - h_k) - (\overline{\sigma}(1 - h_k)\sqrt{2\pi} + \eta_k)(1 - h_{-k}) =
\]

\[
= \sqrt{2\pi} \eta_k(1 - h_{-k}) + \eta_{-k}(1 - h_k) - \sqrt{2\pi} \eta_k(1 - h_{-k}) - \eta_k(1 - h_{-k})
\]

\[
= \eta_{-k}(1 - h_k) - \eta_k(1 - h_{-k})
\]
If $k$ is the group with the greater clout, $\eta_k > \eta_{-k}$ and $1 - h_{-k} \geq 1 - h_k$, therefore the derivative is negative and the ratio decreases in $\bar{\sigma}$.

Now it is necessary to show that as the ratio decreases, it does not overshoot the optimum. This is evident by evaluating the clout ratio in the limit:

$$\lim_{\bar{\sigma}\to\infty} \frac{\psi_k}{\psi_{-k}} = \lim_{\bar{\sigma}\to\infty} \frac{1 + \eta_k \varphi_k}{1 + \eta_{-k} \varphi_{-k}} = \frac{1 + \eta_k \lim_{\bar{\sigma}\to\infty} \varphi_k}{1 + \eta_{-k} \lim_{\bar{\sigma}\to\infty} \varphi_{-k}} = 1$$

But then by (1.35) in the limit $x^* = \bar{x}^*$. ■

**PROPOSITION 1.9.** The solution follows the approach of Proposition 1.8. There are two interesting cases: one in which $\tau'$ is binding on the information consumption of $k$ and another in which it is binding on both. If $\tau > \tau' > h_k$, then there is not change in the ratio and, therefore, in the equilibrium policy. First, suppose that $h_{-k} < \tau' < h_k$. Working from the expanded clout ratio and taking the denominator to equal $s$, it is straightforward to obtain the partial derivative with respect to $\tau'$:

$$\frac{\psi_k}{\psi_{-k}} = \frac{(1 - h_{-k})(\bar{\sigma}(1 - \tau')\sqrt{2\pi} + \eta_k)}{(1 - \tau')(\bar{\sigma}(1 - h_{-k})\sqrt{2\pi} + \eta_{-k})}$$

$$s^2 \frac{\partial}{\partial \tau'} \left( \frac{\psi_k}{\psi_{-k}} \right) = -\sqrt{2\pi}(1 - h_{-k})\bar{\sigma}(1 - \tau')(\bar{\sigma}(1 - h_{-k})\sqrt{2\pi} + \eta_{-k})$$

$$+ (1 - h_{-k})(\bar{\sigma}(1 - \tau')\sqrt{2\pi} + \eta_k)(\bar{\sigma}(1 - h_{-k})\sqrt{2\pi} + \eta_{-k}) =$$

$$= (\bar{\sigma}(1 - h_{-k})\sqrt{2\pi} + \eta_{-k})(1 - h_{-k})\left(\bar{\sigma}(1 - \tau')\sqrt{2\pi} + \eta_k - \sqrt{2\pi}\bar{\sigma}(1 - \tau')\right)$$
The signs of all multiples in the last expression are positive, therefore the partial is positive and a decrease in $\tau'$ in this region would decrease the ratio and cause the equilibrium policy to move towards the optimum (by Proposition 1.7). To show that there will be no overshooting of $\bar{x}^*$, it is needed to take the limit to the lower bound of the region $h_{-k}$:

$$\lim_{\tau' \to h_{-k}} \frac{\psi_k}{\psi_{-k}} = \frac{(1 - h_{-k})(\bar{\sigma}(1 - h_{-k})\sqrt{2\pi} + \eta_k)}{(1 - h_{-k})(\bar{\sigma}(1 - h_{-k})\sqrt{2\pi} + \eta_{-k})} = \frac{\bar{\sigma}(1 - h_{-k})\sqrt{2\pi} + \eta_k}{\bar{\sigma}(1 - h_{-k})\sqrt{2\pi} + \eta_{-k}} > 1$$

Therefore, by Proposition 1.7, $x^* \in (\bar{x}^*, x_k)$ even as $\tau' \to h_{-k}$.

Next suppose $\tau' < h_{-k} < h_k$. Again working from the expanded ratio and substituting $\tau' = h'_{-k} = h'_k$:

$$\frac{\psi_k}{\psi_{-k}} = \frac{(1-\tau'')(\bar{\sigma}(1-\tau'')\sqrt{2\pi} + \eta_k)}{(1-\tau'')(\bar{\sigma}(1-\tau'')\sqrt{2\pi} + \eta_{-k})}$$

$$s^2 \frac{\partial}{\partial \tau'} \left( \frac{\psi_k}{\psi_{-k}} \right) = -\bar{\sigma}\sqrt{2\pi}(\bar{\sigma}(1-\tau'')\sqrt{2\pi} + \eta_{-k}) + (\bar{\sigma}(1-\tau'')\sqrt{2\pi} + \eta_k)\bar{\sigma}\sqrt{2\pi} = \bar{\sigma}\sqrt{2\pi}(\bar{\sigma}(1-\tau'')\sqrt{2\pi} + \eta_k - (\bar{\sigma}(1-\tau'')\sqrt{2\pi} + \eta_{-k})) = \bar{\sigma}\sqrt{2\pi}(\eta_k - \eta_{-k}) > 0$$

Therefore, the ratio is again increasing in $\tau'$ and thus decreasing $\tau'$ leads to a shift in the equilibrium toward the optimum as in the prior case. Checking the limit yields

$$\lim_{\tau' \to 0} \frac{\psi_k}{\psi_{-k}} = \frac{(1 - 0)(\bar{\sigma}(1 - 0)\sqrt{2\pi} + \eta_k)}{(1 - 0)(\bar{\sigma}(1 - 0)\sqrt{2\pi} + \eta_{-k})} = \frac{\bar{\sigma}\sqrt{2\pi} + \eta_k}{\bar{\sigma}\sqrt{2\pi} + \eta_{-k}} > 1$$

Therefore, by Proposition 1.7, $x^* \in (\bar{x}^*, x_k)$ even as $\tau' \to 0$. $\blacksquare$
**PROPOSITION 1.10.** The first step is to set $h_{-k} = \underline{h}$ to get the clout ratio

\[
\frac{\psi_k}{\psi_{-k}} = \frac{(1 - h_k)\bar{\sigma}(1 - h_k)\sqrt{2\pi} + \eta_k}{(1 - h_k)\bar{\sigma}(1 - h_k)\sqrt{2\pi} + \eta_{-k}}
\]

Using the approach from the proof of Proposition 1.8, then obtain the partial derivative, denoting $s^2$ for its denominator:

\[
s^2 \frac{\partial}{\partial \underline{h}} \left( \frac{\psi_k}{\psi_{-k}} \right) = -\left( \bar{\sigma}(1 - h_k)\sqrt{2\pi} + \eta_k \right) \left( 1 - h_k \right) \left( \bar{\sigma}(1 - h_k)\sqrt{2\pi} + \eta_{-k} \right)
\]

\[
+ \left( 1 - h_k \right) \left( \bar{\sigma}(1 - h_k)\sqrt{2\pi} + \eta_k \right) \left( 1 - h_k \right) \bar{\sigma}\sqrt{2\pi} = 
\]

\[
= \left( 1 - h_k \right) \left( 1 - h_k \right) \sqrt{2\pi}\bar{\sigma}^2 + \eta_k \left( 1 - h_k \right) \left( 1 - h_k \right) \bar{\sigma}\sqrt{2\pi} - \bar{\sigma}\sqrt{2\pi} \left( 1 - h_k \right)^2 \eta_{-k}
\]

\[
- \eta_k \eta_{-k} \left( 1 - h_k \right) - \eta_k \left( 1 - h_k \right) \left( 1 - h_k \right) \bar{\sigma}\sqrt{2\pi} - \left( 1 - h_k \right) \left( 1 - h_k \right) \sqrt{2\pi}\bar{\sigma}
\]

\[
< 0
\]

Because the partial is negative, the clout advantage of the special interest group $k$ is decreasing as the floor $\underline{h}$ rises in this interval, hence by Proposition 1.7 the equilibrium is moving towards the optimum. Checking the limit yields

\[
\lim_{h \to h_k} \frac{\psi_k}{\psi_{-k}} = \frac{\left( 1 - h_k \right) \left( \bar{\sigma}(1 - h_k)\sqrt{2\pi} + \eta_k \right)}{\left( 1 - h_k \right) \left( \bar{\sigma}(1 - h_k)\sqrt{2\pi} + \eta_{-k} \right)} = \frac{\bar{\sigma}(1 - h_k)\sqrt{2\pi} + \eta_k}{\bar{\sigma}(1 - h_k)\sqrt{2\pi} + \eta_{-k}} > 1
\]

Therefore, by Proposition 1.7, $x^* \in (\bar{x}^*, x_k)$ even as $\underline{h} \to h_k$. ■

**PROPOSITION 1.11.** This proof follows closely that for Propositions 1.1 and

1.2. ■
PROPOSITION 1.13. Since the choice whether to shift policy to a supranational body is binary, the government will simply compare its expected utility from the domestic to that from the supranational equilibrium. Because constituents shift their performance criteria \( M_i \) with the noisiness of the outcome signal (see the proof of Propositions 1.1 and 1.2), their political support is the same in both cases, thus the expected total wealth \( \omega \) would determine which arrangement is better in terms of its expected utility. Therefore, the supranational game is the equilibrium institutional choice of the government if \( \omega(x^*, y^*) - \omega(x^{**}, \bar{y}) < 0 \). To unpack this condition, some preliminary work is necessary first:

\[
\omega(x, y) - \omega(x', y') = \sum_i (u_i(x, y) - u_i(x', y')) = \\
= \sum_i (\alpha_i((x - x_i)^2 - (x' - x_i)^2) + \beta_i((y - y_i)^2 - (y' - y_i)^2)) = \\
= \sum_i (\alpha_i(x + x' - 2x_i)(x - x') + \beta_i(y + y' - 2y_i)(y - y')) = \\
= (x - x') \sum_i \alpha_i(x + x' - 2x_i) + (y - y') \sum_i \beta_i(y + y' - 2y_i)
\]

After appropriate substitution, the supranationalization condition becomes:

\[
(x^* - x^{**}) \sum_i \alpha_i(x^* + x^{**} - 2x_i) < (\bar{y} - y^*) \sum_i \beta_i(y^* + \bar{y} - 2y_i) \Leftrightarrow \\
(x^* - x^{**}) \sum_i \alpha_i(x^* + x^{**} - 2x_i) < (\bar{y} - y^*) \sum_i \beta_i(y^* - 2y_i) + \bar{y}(\bar{y} - y^*) \sum_i \beta_i \Leftrightarrow \\
(x^* - x^{**}) \sum_i \alpha_i(x^* + x^{**} - 2x_i) + y^* \sum_i \beta_i(y^* - 2y_i) < \bar{y} \sum_i \beta_i(\bar{y} - 2y_i)
\]

The left side of this condition is contingent on \( \bar{\sigma} \) and \( \bar{\sigma}' \), whereas the right side is dependent on the value of \( \bar{y} \). \( \blacksquare \)
## Appendix II. Capitalization CAPIT as of 2013

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