

# The trade-off between governance and checks and balances

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June, 2017

## Abstract

Strong checks and balances aimed at protecting citizens from government abuse of power are key features of well performing democracies. Nevertheless, some presidents have enjoyed strong and often explicit popular support when they undermined these controls. We present a formal model of the trade-off between control on the executive and delegation to analyze voters' decision on the strength of checks and balances. We argue that voters may support their loosening, even when this allows rent extraction, if they are convinced that checks on the executive are blocking necessary reforms. We discuss several cases of strong presidents in Latin America who, alleging that radical reforms were necessary, obtained popular support that allowed them to loosen checks on the executive. Some of these presidents had a pro- and some an anti-market reform agenda so, as our model suggests, voters' willingness to remove checks and balances can emerge under both right- and left-wing executives.

**Keywords:** Political agency, Separation of powers, checks and balances.

**JEL Codes:** H11, P16, P48

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‡We are grateful to Gani Aldashev, Laurent Bouton, Micael Castanheira, Antonio Estache, Mónica Martínez-Bravo, Clemens Puppe, and Guido Tabellini for their insightful comments and suggestions, as well as seminar participants at the 25th anniversary of ECARES workshop, the 6th Christmas Meeting of Belgian economists, the Department of Economics at the University of Gothenburg and the dECON-FCS-UdelaR seminars. The usual disclaimer applies.

# 1 Introduction

The tension between governance and checks and balances is at the core of modern theories of democracy. Governance entails the capacity of the executive to implement its policy agenda. Under checks and balances, “separate branches are empowered to prevent actions by other branches and are induced to share power.”<sup>1</sup> Strong checks and balances are an effective way to control politicians but, at the same time, they can impede the government from undertaking new initiatives. The way citizens manage the trade-off between governance and protection from the abuse of power depends on multiple dimensions as the expected benefits of reforms and the characteristics of the politicians in power. The analysis of how these dimensions shape voters’ decision on the strength of checks and balances is the main goal of this paper.

The need of checks and balances arises most clearly in presidential systems. The separation of powers is in the essence of presidentialism, and checks and balances are crucial to limit the power of the executive in these systems. However, some critics argue that checks on the executive can cause political gridlocks that generate the temptation to undermine those checks moving in the direction of hyper-presidentialism (Arato 2000; Linz 1990; Rose-Ackerman et al. 2011). In a similar vein, Fukuyama (2017), commenting on the last election in the US, argues that “the American political system in fact has too many checks and balances (...) and the rise of an American strongman is actually a response to the earlier paralysis of the political system.”

Empirical evidence suggests that an increase in checks on the executive has been the general trend in recent decades (Besley and Persson 2011). However, the move has not always been smooth, and there have been reversals in many developing democracies (Besley and Persson 2011; Karakas 2016). This was the case of several Latin American countries during the nineties, as they reformed their constitutions by introducing or reinforcing urgency bills that increased the legislative power of the executive. Also strong leaders like presidents Fujimori in Peru and Menem in Argentina manipulated the integration of the supreme court to increase their control over the judiciary (Finkel 2004, 2008). In Venezuela in 1999, president Hugo Chávez received the support of 72 per cent of the electorate in a plebiscite that introduced a unicameral legislature and reallocated legislative powers to the executive. In Ecuador in 2008 and in Bolivia in 2009, presidents Rafael Correa and Evo Morales obtained 64 and 61 per cent of votes, respectively, in plebiscites that reformed the constitutions on similar lines. We investigate *which were the common elements in these cases that led voters to support the weakening of checks on the executive.*

The main hypothesis of the present paper is that loosening the constraints on the executive facilitates reforms that citizens consider necessary. Controls on the executive are useful to limit rent extraction or,

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<sup>1</sup>Encyclopædia Britannica: <https://www.britannica.com/topic/checks-and-balances>. Accessed 08.02.2017

more generally, to ameliorate agency problems, but they also make more difficult the implementation of radical or profound policy changes. When the executive claims that a reform is needed, and citizens are convinced, they face the dilemma between loosening the controls to facilitate the reform proposed by the executive, but at the cost of more corruption or policies that are not totally representative of their own views, and keeping the controls that put a break on corruption but at the cost of no reform.

We present a formal model of the trade-off between governance and checks and balances (CB), and three main results. *First*, citizens support the weakening of checks and balances if and only if their expected gains from reform are sufficiently high compared to the expected losses from rent extraction. Citizens must be convinced that the country needs key reforms that cannot be implemented with the existing system of checks and balances. Even if this opens the window for more corruption, citizens should see this as a “small” price to pay for the much needed reforms. *Second*, citizens expected gains from reform depend on the importance of the policy agenda and the president standing and credibility regarding the benefits of reform. Expected gains cannot be high unless citizens are convinced that (i) key reforms are at stake, (ii) it is highly likely that these reforms are beneficial and (iii) the president is committed to the reform program. *Third*, when voters and the executive preferences are not very different, the executive proposes a reform only when it is needed, in which case voters accept less checks and balances. However, an executive with a strong pro-reform bias or sufficiently high valuation of rents might always claim that a reform is needed, even when it is not beneficial for citizens. Aware of this bias, citizens will not believe in the announcement, but they might still grant special powers. In particular, weak checks and balances emerge in this case if both voters disutility from rent extraction is not too large and their own conjecture about the probability that the reform is required is sufficiently high. In this latter case, there will be too much reform and rent extraction in the sense that special powers and reform will occur not only when the reform is beneficial for citizens, but also when it is not.

Our model generates interesting results, capable of replicating episodes of weakening of CB, only if the agency different from the executive favors the status-quo. Indeed, in our model it is the political gridlock stemming from CB and disagreement what prompts citizens support for the loosening of CB. We think the assumption makes sense conceptually and reflects the cases analyzed in the paper.<sup>2</sup> In our view, supporters of highly popular leaders who weakened the legislature and the judiciary simply thought that the parliament and the judiciary were blocking the reforms and, in many cases, they were right. First, by their very nature, while the executive typically represents one view (one party, or a coalition) the parliament represents different views and interests. Parliaments are naturally more plural than executives.<sup>3</sup> Therefore, the parliament tends to water down the proposals of reform of the

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<sup>2</sup>In addition, we present an extension of our basic model where we introduce elections, and we show under which conditions citizens vote for a conservative legislature and a reformist executive.

<sup>3</sup>This is less so however in the case of unified governments, something that has been common in Latin America. See more on this below.

executive. Giving more power to the executive vis-à-vis the congress increases the ability of the party in the executive office —and particularly of strong leaders— to move their agenda forward. Second, the judiciary is naturally conservative (both *stricto sensu* and often also in ideological terms). It seems more difficult to push sweeping reforms with a strong than with a weak judiciary. Reformist leaders, who often proclaimed themselves as little less than founding fathers of their nations, claimed that the judiciary was a stumbling block in the reform process. Supporters of these leaders also often claimed that the judiciary was partial and that the prosecution of corruption was an excuse (a claim that could have solid grounds in some weak judicial systems).<sup>4</sup>

The story our model tells is akin to the political science literature that discusses the relationship between governance and democratization (O’Donnell 1994). Carrión (2006) explains the involved tensions very clearly: “Governance, defined broadly as the capacity to formulate and implement policies in an effective manner, can sometimes clash with the demands of democratization. (...) Situations of extreme crisis, such as that experienced by Peru in the late 1980s and early 1990s, may exacerbate this uneasy relationship by persuading many to accept the claims of aspiring dictators that the country “cannot afford” democracy.” Similarly, Rose-Ackerman et al. (2011) analyze episodes in which strong presidents undermined the checks on the executive arguing the need of administrative efficiency in times of crisis. Kenney (2000) also emphasizes the risk that checks and balances lead to ineffective government that may even threaten the stability of democracy. Our main contribution to this literature is the formal modeling of this tradeoff, and the analysis of the determinants of citizens’ support for the weakening of checks and balances.

The theme in the present paper has been addressed before in the political economy literature, most notably in Acemoglu et al. (2013). They argue that the poor majority supports the dismantling of checks and balances because politicians are less tempted to accept bribes from the rich elites if they can extract rents than if they cannot. In other words, the dismantling of checks and balances makes politicians “expensive” to bribe. Therefore, according to their story, rent extraction may be conducive to the success of reformist policies that favor the poor.

Acemoglu et al. (2013) story explains recent episodes in Latin America in which voters support the dismantling of checks and balances under left-wing executives. But, in our view, it does not explain so well why in the nineties equally popular politicians holding a pro-market agenda got the support of citizens to undermine these controls when the reform agenda was firmly supported by the elites. The elite lobbies would not bribe politicians to derail many pro-market reforms, like the privatization of state owned enterprises or financial reforms aimed at deepening financial development, and yet several

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<sup>4</sup>Nassif (2016), for example, published a newspaper article in which he said, in reference to judicial procedures for government corruption during the government of Lula da Silva in Brazil, that “Corruption was the alibi to erase the recent history of the country, even the fight for democracy”. (Own translation from a Spanish version: “La corrupción fue la coartada para borrar la historia reciente del país, hasta la lucha por la democracia.”)

of these politicians got citizens support for special powers to further reform. Our model can explain the dismantling of checks and balances that took place during both the nineties pro-market reforms and the two-thousands anti-market reforms.<sup>5</sup>

Also related to our study is the paper of Aghion et al. (2004). The authors analyze the trade-off between delegation of power and control of politicians, and show how the optimal amount of delegation varies with some political-economic features. However, their focus differs from ours, as they investigate the optimal design of political institutions in order to protect citizens from the tyranny of the majority.

Unlike in Acemoglu et al. (2013) and Aghion et al. (2004) models, the executive in our basic model plays an active role in promoting the loosening of CB, which we think is a distinctive feature in all the cases we analyze in this paper. Presidents actively campaigned to convince citizens to grant them special powers to advance reforms. In order to capture these facts, we assume that voters are uncertain about the state of nature. The executive is better informed and can announce and, in our basic model, can also commit to policies. Voters use these announcements to update their beliefs about the state of the world and then decide whether or not to grant special powers. We then discuss an extension of our model where politicians cannot commit to their platforms, so we can study the impact of commitment on the occurrence of special powers.

The trade-off between delegation and control that is at the center of our paper has been analyzed before by Maskin and Tirole (2004), but their focus is different from ours. They study the allocation of decision-making powers between direct democracy, representative democracy and judges. In the case of representative democracy, they focus on electoral accountability. We rather focus on non-electoral accountability through checks and balances.<sup>6</sup> Electoral incentives are crucial in their environment. We analyze a complementary issue: to what extent will citizens be willing to grant special powers to a politician that is already in the executive? Their analysis regarding politicians is in the realm of pre-electoral politics; ours is in the realm of post-electoral politics.

In our basic model, we borrow from Persson et al. (1997, 2000) the modeling of checks and balances as a specific procedure to assign decision powers that, creating a conflict of interests between the executive and another branch of the government and forcing them to agree on a common policy, blocks rent extraction.<sup>7</sup> We model the absence of checks and balances as a procedure in which the executive rules, both in terms of policies and rent extraction.<sup>8</sup>

In the next section we present and solve our basic model in which the two government agencies are

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<sup>5</sup>This is the “paradox” Manzetti (2014) highlights in his analysis of the Argentinean case.

<sup>6</sup>Of course, we would expect that these two forms of accountability interact with each other, as Stephenson and Nzelibe (2010) have convincingly argued. In a separate paper, still in progress, we analyze this challenging issue.

<sup>7</sup>Notice that in this setting there is a conflict of interests, but there is no institutional instability and conflict of powers, as for example in Taylor-Robinson and Ura (2012).

<sup>8</sup>See however Robinson and Torvik (2016), who argue that US-like checks and balances do not work in developing presidential countries and hence, in their analysis of the choice between presidential and parliamentary systems, they model presidential systems without checks and balances.

the executive and the legislature. In the basic model the identity of the politicians in office is given and we assume the executive is able to commit its referendum campaign promises. We then present two extensions of the model, one in which we drop the commitment assumption and another one in which we introduce elections. In section 3, we present an extension in which the judiciary substitutes the legislature. In section 4 we discuss some empirical evidence, analyzing five cases of Latin American presidents who managed to loosen checks and balances with public support. Section 5 ends the paper with some concluding remarks. The proofs of the formal propositions are presented in the appendix.

## 2 The executive and the legislature

In this section, we introduce the basic model where the executive and the legislature decide on a policy issue and rent extraction. Citizens vote on the rules that determine how these two agencies proposals map into actual policies. Policy preferences of voters and the two agencies may not be aligned. Voters prefer the policy that matches the state of nature, and each agency may have a policy bias. Agencies like their own rents but dislike the rents extracted by the other agency. Voters dislike rent extraction.

After observing the state of nature, both agencies announce and commit to a policy: status quo or reform.<sup>9</sup> Without observing the state of nature, citizens vote in a referendum to choose the policy rule: checks and balances (*CB*) or special powers (*SP*). With *CB* a reform is implemented only if both government agencies agree on the reform. The executive defines first the total amount of rents and the legislature decides later how to distribute it between the executive and the legislature. When voters choose *SP*, the executive decides everything, i.e. the policy and the rents of the two agencies.

We assume a conservative legislature that always supports the status quo and hence there is no reform with *CB*. Also, because of the opposition of interests it creates between the two government agencies, *CB* impede rent extraction. If voters choose *SP* after the executive proposed a reform, the reform takes place and the executive extracts rents. Thus, reform is only possible when it is proposed by the executive, and voters grant *SP*. As we show in this section, the former occurs only when the executive is **not** strongly pro-status quo biased, and the latter when voters' expected gains from reform are larger than the costs of rent extraction.

Finally, we present two extensions of the basic model. In one of them, we drop the assumption that the executive can commit its policy before the referendum. We then compare the equilibrium outcomes with and without commitment. In a second extension, we introduce elections at the beginning of the

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<sup>9</sup>There is no consensus in the literature about whether policies can be committed in political campaigns. Furthermore, some leading contributors in the field have alternatively assumed, depending on the specific application, that politicians can commit to policies (Alesina and Rosenthal 2000) and cannot do it (Alesina and Rosenthal 1995, 1996). The ability to commit probably varies depending on institutional contexts and policy arenas and, as Alesina and Rosenthal (2000) suggest, does not need to be a binary variable. We do not adopt a strong stance regarding the ability to commit. We present an extension of the basic model in which politicians cannot commit to policies. This extension allows us to analyze the impact of commitment on the occurrence of special powers and reform.

game. This version of the model is meant to explain why citizens might vote for a conservative legislature and a reformist executive and then grant the executive the special powers it needs to advance reform. While the specific results do depend on these alternative assumptions, the main qualitative message remains.

## 2.1 The setting

Two government agencies, the executive ( $X$ ) and the legislature ( $L$ ), participate in policy making. There are two policy dimensions: a policy issue  $p \in \{0, 1\}$  and rent extraction  $r_X \in [0, \bar{r}]$  and  $r_L \in [0, \bar{r}]$ ,  $r_X + r_L \in [0, \bar{r}]$ , where  $r_X$  and  $r_L$  are the rents extracted by the executive and the legislature, respectively. Both the executive and the legislature make policy proposals and there is a policy rule that maps the agencies proposals and the status quo policy, denoted by  $p_0$ , into the two dimensions of policy.

We consider two types of policy rules:

1) *CB*, (standing for checks and balances), determines that:

1.  $p = \begin{cases} p_X & \text{if } p_X = p_L \\ p_0 & \text{if } p_X \neq p_L \end{cases}$
2. *Executive chooses*  $r \in [0, \bar{r}]$
3. *Legislature chooses*  $r_L \in [0, r]; r_X \in [0, r - r_L]$

where  $p_X$  and  $p_L$  are the executive and legislature proposals regarding the policy issue, respectively.

2) *SP*, (standing for special powers), determines that:

1.  $p = p_X$
2. *Executive chooses*  $r_X \in [0, \bar{r}]; r_L \in [0, \bar{r} - r_X]$

Voters prefer the policy that matches the state of nature and dislike the rents extracted by politicians. More specifically, we assume that voters preferences are given by:

$$v = -E_s [(p - s)^2] - c(r_X + r_L),$$

where  $c > 0$  and  $E_s[\cdot]$  is the expected value across the states of nature. Note that the parameter  $c$  represents voters' marginal disutility from rent extraction *relative* to the disutility of the policy mismatch. Thus, a smaller value of  $c$  implies a higher weight of the policy mismatch relative to the rent component in voters utility function.

Politicians also care about the policy matching, but unlike voters who want to match exactly the policy and the state of nature, politicians may have a policy bias that could be either positive or

negative.<sup>10</sup> Additionally, they value their own rents and dislike the rents extracted by the other power. More precisely, politicians preferences are given by:

$$u_j = -(p - s - \delta_j)^2 + a_j r_j - b r_{-j},$$

where  $\delta_j \in \mathbb{R}$  is the bias of politician in office,  $a_j > 0$ ,  $j \in \{L, X\}$ ,  $b > 0$ , and  $r_{-j}$  is the amount of rents extracted by the politician in the other branch of government.

All the parameters are common knowledge.

The timing is as follows:

1. At the beginning of the game, Nature chooses:
  - (a) the status quo policy  $p_0 \in \{0, 1\}$ ;
  - (b) the state of nature, using a random mechanism by which  $s = 1$  with probability  $q$  ;
  - (c) a politician to run the legislature; and
  - (d) a politician to run the executive.
2. Politicians make a policy proposal  $p_j$ ,  $j \in \{L, X\}$ , knowing previous Nature's moves, including the state of nature.
3. Referendum: voters choose the policy rule  $CB$  or  $SP$ , knowing  $p_0$ ,  $p_X$  and  $p_L$ , but not  $s$ .
4. If in step 3 voters choose  $CB$ , then
  - (a)  $p = \begin{cases} p_X & \text{if } p_X = p_L \\ p_0 & \text{if } p_X \neq p_L \end{cases}$
  - (b) the executive first proposes  $r \in [0, \bar{r}]$ , and later
  - (c) the legislature chooses  $r_L \in [0, r]$ ;  $r_X \in [0, r - r_L]$ .
5. If in step 3 voters choose  $SP$ , then  $p = p_X$ , and the executive chooses  $r_X \in [0, \bar{r}]$  and  $r_L \in [0, \bar{r} - r_X]$ .
6. The game ends and payoffs are computed.

Notice that this timing embeds the assumption that politicians can commit to policies in the referendum campaign. Also notice the informational advantage of politicians over citizens in the sense that, at the time they move, politicians but not citizens observe the state of nature.<sup>11</sup>

The following timeline describes how events unfold.

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<sup>10</sup>This is what Maskin and Tirole (2004) call the legacy motive. A politician with a non-zero bias in our model corresponds to what they call *noncongruent*.

<sup>11</sup>Our basic model is similar to Cukierman and Tommasi (1998) in these two assumptions.

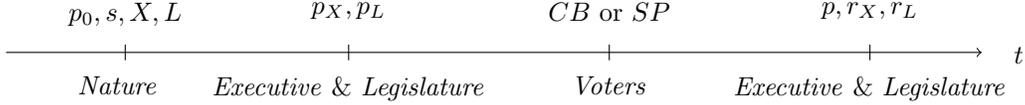


Figure 1: The timing of the game

## 2.2 Equilibrium

We look for Bayesian perfect equilibria. For concreteness, we will assume that the status quo policy is zero:  $p_0 = 0$ . More importantly, we assume that the legislature favors the status quo policy no matter which is the state of nature:  $p_L = 0$ .<sup>12</sup> For this to be true, the legislature bias must be sufficiently negative.<sup>13</sup>

Notice that the executive and the legislature interaction after the referendum can be treated as separate perfect information games. We solve these games first and then use the outcomes to analyze the extensive form of the imperfect information referendum game played by the executive and voters.

### 2.2.1 The continuation games after the referendum

*The continuation game after voters chose CB in step 3.* Using backward induction, we consider first the legislature choice of rents. At this stage (4c), the executive has already chosen  $r$  (the maximum amount of total rents to be extracted by both politicians together). The legislature chooses  $r_X = 0$ , and  $r_L = r$ . In the previous stage (4b), the executive chooses  $r = 0$ , despite of  $a_X > 0$ , because it knows that the legislature will choose  $r_X = 0$ , irrespective of  $r$ , and its utility is decreasing in the rents the legislature extracts. The policy rule determines  $p = p_0 = 0$ , since the legislature favors the status quo and, with *CB*, the executive cannot impulse a reform alone. Therefore, the equilibrium policies if voters chose *CB* are

$$p = p_0 = 0, \text{ and } r_L = r_X = 0. \quad (1)$$

*The continuation game after voters chose SP in step 3.* The executive is the last player to move and chooses  $r_X = \bar{r}$  and  $r_L = 0$ . It is already committed to the announced policy  $p = p_X$ , and hence the equilibrium policies are

$$p = p_X, r_L = 0, \text{ and } r_X = \bar{r}. \quad (2)$$

### 2.2.2 The extensive form referendum game

The executive has four pure strategies: (i)  $p_X = 0$  irrespective of  $s$ ; (ii)  $p_X = 1$  irrespective of  $s$ ; (iii)  $p_X = 0$  if  $s = 0$ , and  $p_X = 1$  if  $s = 1$ ; and (iv)  $p_X = 1$  if  $s = 0$ , and  $p_X = 0$  if  $s = 1$ . We identify these

<sup>12</sup>The model can be solved with the alternative assumption of a reformist legislature, but the issue we want to analyze does not arise in this case.

<sup>13</sup>The condition for this to be true is  $\delta_L \leq -0.5$ . Indeed,  $u_L(p = 0 | s) - u_L(p = 1 | s) = -(s + \delta_L)^2 + (1 - s - \delta_L)^2 \geq 0 \iff \frac{1-2s}{2} \geq \delta_L$ . This condition holds for  $\delta_L \leq 0.5$  if  $s = 0$  and for  $\delta_L \leq -0.5$  if  $s = 1$ .

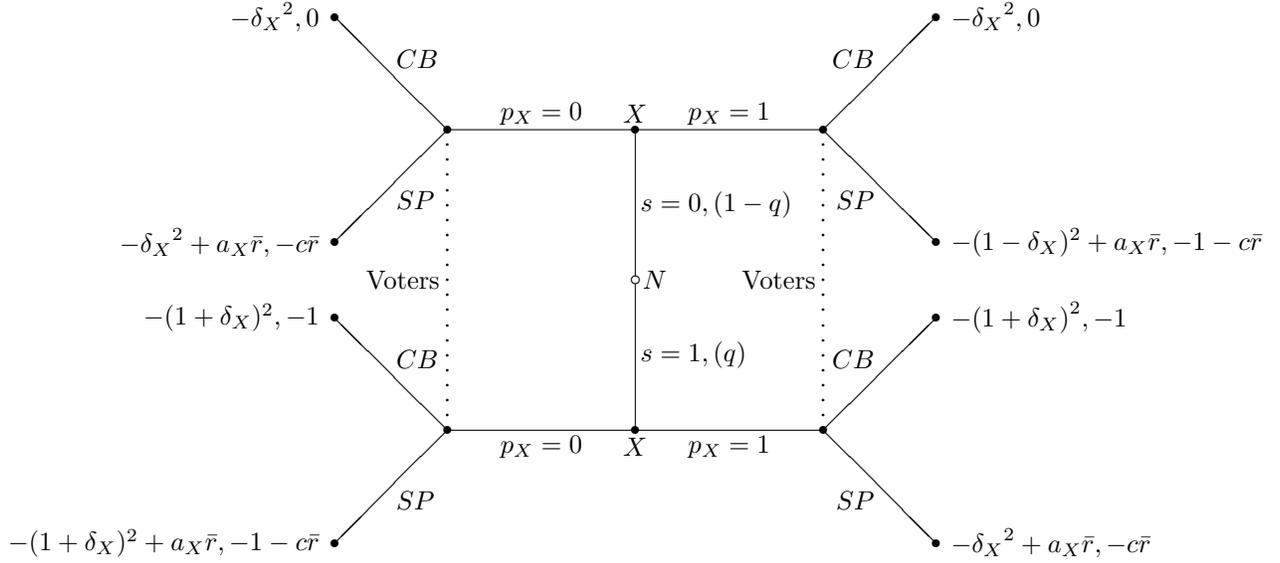


Figure 2: The extensive form referendum game

four strategies as  $(0, 0)$ ,  $(1, 1)$ ,  $(0, 1)$  and  $(1, 0)$ , respectively.

Voters also have four pure strategies: (i)  $CB$  irrespective of  $p_X$ ; (ii)  $SP$  irrespective of  $p_X$ ; (iii)  $CB$  if  $p_X = 0$ , and  $SP$  if  $p_X = 1$ ; and (iv)  $SP$  if  $p_X = 0$ , and  $CB$  if  $p_X = 1$ . We will identify these strategies as  $(CB, CB)$ ,  $(SP, SP)$ ,  $(CB, SP)$  and  $(SP, CB)$ , respectively. Figure 2 presents the extensive form of the referendum game.

There are in principle 16 strategy profiles that could be considered as candidates for PBE. But we can immediately rule out half of them after observing that when voters receive the announcement  $p_X = 0$ , they know that the implemented policy will be  $p = 0$  independently of their decision in the referendum. Therefore, special powers do not modify the implemented policy and open the opportunity for rent extraction, implying that after observing  $p_X = 0$  voters choose  $CB$ . We summarize this result in the following remark:

**Remark 1.** *After observing  $p_X = 0$ ,  $CB$  dominates  $SP$  for voters. Thus, only voters strategies  $(CB, CB)$  and  $(CB, SP)$  can belong to a PBE.*

When deciding their optimal responses, both the executive and voters take rent extraction and the matching of policies into account. Consider first the problem from the executive's perspective. Conditional on what voters do, the executive policy proposal may impact on its ability to extract rents and the policy outcome. As we have noted, voters always choose  $CB$  after  $p_X = 0$ . If they also vote for  $CB$  when  $p_X = 1$ , then the executive has no real choice, and both possible actions,  $p_X = 0$  and  $p_X = 1$ , have the same consequences:  $p = 0$  and no rent extraction.

If voters choose  $SP$  when the executive chose  $p_X = 1$ , then the executive's utility gains from this

choice are:

$$-(1 - s - \delta_X)^2 + (0 - s - \delta_X)^2 + a_X r = -1 + 2s + 2\delta_X + a_X \bar{r}, \quad (3)$$

The executive proposes  $p_X = 0$  if the expression (3) is negative, and hence an executive with a sufficiently strong preference for the status quo — $\delta_X$  sufficiently negative— never proposes the reform. Conversely, the executive proposes  $p_X = 1$  if the expression (3) is positive, and hence an executive with a sufficiently strong preference for reform always proposes  $p_X = 1$ .<sup>14</sup> Because the utility gains from choosing  $p_X = 1$  are larger when  $s = 1$  than when  $s = 0$ , there will be an intermediate range of values of the executive bias  $\delta_X$  such that the executive chooses  $p_X = 1$  if and only if  $s = 1$ .

Consider now the problem voters face. At the referendum time, voters ignore the state of nature but they know the policy proposal of the executive, so expectations over the state of nature are conditional on the announcement. When they observe  $p_X = 1$ , their expected utility from *SP* is

$$Pr(s = 0|p_X = 1)(-1) + Pr(s = 1|p_X = 1)0 - c\bar{r}, \quad (4)$$

whereas their expected utility from *CB* is

$$Pr(s = 0|p_X = 1)0 + Pr(s = 1|p_X = 1)(-1). \quad (5)$$

Therefore, voters expected utility gains from special powers (as of the referendum time), are:

$$[Pr(s = 1|p_X = 1) - Pr(s = 0|p_X = 1)] - c\bar{r}. \quad (6)$$

This expression has a simple interpretation. The term between square brackets includes voters gains from reform: voters gain one “util” if  $s = 1$ , and lose one “util” if  $s = 0$ . At the referendum time, voters believe that the reform raises welfare with probability  $Pr(s = 1|p_X = 1)$  and that it reduces welfare with probability  $Pr(s = 0|p_X = 1)$ . The second term in expression 6,  $c\bar{r}$ , represents voters utility losses from rent extraction. When, conditional on the executive announcement, the expected utility gains from the reform are higher than the utility losses associated with rent extraction, so expression (6) is positive, voters grant the executive special powers.

For future use, we summarize these observations in the following remarks:

**Remark 2.** *The executive’s utility gains from rent extraction are  $a_X \bar{r}$ .*

**Remark 3.** *The executive’s utility gains from reform are  $-1 + 2s + 2\delta_X$ .*

**Remark 4.** *Voters utility losses from rent extraction are  $c\bar{r}$ .*

**Remark 5.** *Voters expected utility gains from reform are  $Pr(s = 1|p_X) - Pr(s = 0|p_X)$ .*

<sup>14</sup>Notice however that even an executive with a status quo bias may propose  $p_X = 1$  if the utility gains from rent extraction are sufficiently high, provided its bias against reform is not too strong.

### 2.2.3 Equilibria with special powers

The following proposition studies the equilibria in which voters grant special powers on the equilibrium path.

**Proposition 1.** *The model exhibits two, and only two, PBE in pure strategies in which the equilibrium outcome includes special powers. The strategy profiles and the configuration of parameters that are necessary and sufficient for these equilibria to arise are as follows:*

1.  $(0, 1, CB, SP)$  is a PBE iff  $c\bar{r} \leq 1$  and  $-\frac{1+a_X\bar{r}}{2} \leq \delta_X \leq \frac{1-a_X\bar{r}}{2}$
2.  $(1, 1, CB, SP)$  is a PBE iff  $c\bar{r} \leq 2q - 1 \leq 1$  and  $\delta_X \geq \frac{1-a_X\bar{r}}{2}$

*Proof.* See the appendix. □

In the equilibrium  $(0, 1, CB, SP)$ , the executive chooses  $p_X = 1$  only when the state of nature is  $s_1 = 1$ , i.e. it proposes a reform only when the reform is beneficial for citizens. As the politician tells the truth about the state of nature and citizens vote for  $SP$ , we call this equilibrium the *truth-telling equilibrium with special powers*. In this equilibrium voters believe in the executive's implicit announcement about the state of nature and they are not fooled.

For this strategy profile to be a PBE, the executive must not be “too” biased in either direction. Also the rents the executive will extract cannot be “too” large, or voters will not vote for special powers.

The interpretation of these conditions can also be clarified using remarks 2 and 3. In this equilibrium the executive tells the truth because the utility gains from rents and reform it obtains claiming that a reform is needed are not positive when the state of nature is 0 and not negative when it is 1. When  $s = 0$ , the executive utility gains from reform are  $-1 + 2\delta_X$ , and from rent extraction are  $a_X\bar{r}$ . As  $0 \geq a_X\bar{r} - 1 + 2\delta_X$ , the utility from rent extraction does not compensate the implementation of an unnecessary reform. Equivalently, when  $s = 1$ , the executive utility gains from reform are  $1 + 2\delta_X$ , and from rent extraction are  $a_X\bar{r}$ . Given that  $0 \leq a_X\bar{r} + 1 + 2\delta_X$ , the executive has no negative gains from  $p_X = 1$ .

In this equilibrium voters learn the true state of nature. Because of learning, voters grant special powers only when they are needed, and the executive can extract rents only in this state of nature. Voters have no incentives to grant special powers after the executive announced  $p_X = 0$ , but the decision is a bit more complicated if the executive announced  $p_X = 1$ . If voters do not deviate and grant special powers, the policy will be  $p = p_X = 1$  and the executive will extract rents. The expected utility of voters is then  $-c\bar{r}$ . If they deviate and choose checks and balances despite of the executive claim  $p_X = 1$ , then  $p = 0$  and there is no rent extraction. Voters expected utility is then  $-(0 - 1)^2$ . Therefore, voters do not deviate iff  $c\bar{r} \leq 1$ . In summary, in this equilibrium voters grant special powers after the incumbent

announces  $p_X = 1$  because the losses due to rent extraction  $c\bar{r}$  are not larger than the expected utility gains from reform  $Pr(s = 1|p_X = 1) - Pr(s = 0|p_X = 1) = 1$ .

In the equilibrium  $(1, 1, CB, SP)$ , the executive chooses  $p_X = 1$  no matter which is the true state of nature, and voters grant special powers. So there will be special powers, reform and rent extraction both when the reform is beneficial for voters and when it is not.

For this strategy profile to be a PBE, the executive must have a “sufficiently” large bias for policy 1 and/or a “sufficiently” high valuation of the rents it can extract choosing  $p_X = 1$ .

In this strategy profile, voters learn nothing from the executive’s announcement because the executive always reports that the state of nature is 1. Hence, the probability voters ascribe to the state being 1 is the same before and after receiving the announcement:  $Pr(s = 1|p_X = 1) = q$ . Therefore, voters expected net gains from granting special powers are  $[q - (1 - q)] - c\bar{r}$  and voters do not deviate if, and only if,  $c\bar{r} \leq 2q - 1$ .

#### 2.2.4 Equilibria without special powers

The model also exhibits several equilibria in which only checks and balances arise on the equilibrium path. The following proposition characterizes these equilibria.<sup>15</sup>

**Proposition 2.** *The model exhibits five, and only five, PBE in pure strategies in which the equilibrium outcome always includes CB (SP is never part of the equilibrium outcome). The strategy profiles and the configuration of parameters that are necessary and sufficient for these equilibria to arise are as follows:*

1.  $(0, 0, CB, CB)$  is a PBE iff  $c\bar{r} \geq 2Pr(s = 1|p_X = 1) - 1$ ;
2.  $(0, 0, CB, SP)$  is a PBE iff  $c\bar{r} \leq 2Pr(s = 1|p_X = 1) - 1$  and  $\delta_X \leq -\frac{1+a_X\bar{r}}{2}$ ;
3.  $(1, 1, CB, CB)$  is a PBE iff  $c\bar{r} \geq 2q - 1$ ;
4.  $(0, 1, CB, CB)$  is a PBE iff  $c\bar{r} \geq 1$ ;
5.  $(1, 0, CB, CB)$  is a PBE.

*Proof.* See the appendix. □

In the equilibrium  $(0, 0, CB, CB)$ , the executive always chooses the status quo policy and voters never grant special powers. Given that the executive in step 2 announces no reform and, accordingly, commits to policy  $p_X = p_0 = 0$ , voters have no real choice: the policy will be  $p = 0$  no matter what they

<sup>15</sup>As we show in the Appendix, the profile  $(1, 0, CB, SP)$  is not a PBE for any configuration of parameters.

do. In this scenario, there is no reason to grant special powers *on the equilibrium path*, for that would imply rent extraction with nothing in return. Hence, voters choose  $CB$ , after observing  $p_X = 0$ .<sup>16</sup>

But the executive must also consider whether voters' threat of choosing  $CB$  if it chooses  $p_X = 1$  is credible. For this to be the case, the (out-of-equilibrium) probability that voters ascribe to  $s = 1$  after observing  $p_X = 1$ , i.e.  $Pr(s = 1|p_X = 1)$ , cannot be "too" large. Otherwise voters would prefer to choose  $SP$  after observing  $p_X = 1$  and hence the strategy  $(CB, CB)$  would contain an empty threat. In other words, with these parameter values and beliefs, voters utility losses from rent extraction (Remark 4) are no smaller than their expected utility gains from reform (Remark 5) and hence they do not grant special powers. Note that the threat is necessarily credible if  $c\bar{r} \geq 1$ . If the utility cost of rents is "sufficiently" large, there is no belief that makes voters grant the executive special powers.

The equilibrium  $(0, 0, CB, SP)$  produces exactly the same outcome as the previous equilibrium: the executive always chooses  $p_X = 0$  and voters do not grant special powers. The fact that voters would be willing to do it had the executive announced a reform policy makes no difference in terms of equilibrium outcomes because the executive never chooses this policy. For this reason, these two equilibria are empirically indistinguishable.

The set of parameter values for which these two equilibria arise are different. A necessary condition for the profile  $(0, 0, CB, SP)$  to be a PBE is that the executive has a "sufficiently" strong status-quo bias:  $\delta_X \leq -\frac{1+a\bar{x}\bar{r}}{2}$ . This is because voters are now willing to grant special powers if the executive proposes a reform and this opens the window for rent extraction. These rents might convince the executive to push the reform, unless its status-quo bias is "sufficiently" strong.

As in the previous equilibrium, voters have no reasons to provide special powers after the executive announced a no reform policy. But unlike in that equilibrium, in this one voters would be willing to grant special powers if the executive announced a reform policy. This is because voters utility losses from rent extraction are compensated by sufficiently large expected gains from reform:  $c\bar{r} \leq Pr(s = 1|p_X = 1) - Pr(s = 0|p_X = 1) = 2Pr(s = 1|p_X = 1) - 1$ . Notice that this implies that the out-of-equilibrium probability  $Pr(s = 1|p_X = 1)$  must be "sufficiently" large for this equilibrium to arise.

In the equilibrium  $(1, 1, CB, CB)$ , the executive always claims the reform is needed, but voters do not concede. The incumbent has no prospects of rent extraction or of having a material impact on policies since voters never grant special powers.

Voters do not grant the special powers the executive claims because the probability they ascribe to the state of nature in which the reform is needed is not "sufficiently" high and/or the utility cost of rents is "too" high:  $c\bar{r} \geq 2q - 1$ . The executive always claims that the reform is needed in this equilibrium, and hence policies are totally uninformative. Voters cannot update their beliefs and the posterior is

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<sup>16</sup>Notice that this decision does not depend on the probability that voters ascribe to the state being 1 after the executive claimed 0. Even if this probability is 1, voters do not grant special powers since the reform is not implemented if the executive is already committed to  $p_X = 0$ .

equal to the prior belief  $q$ . Voters strategy includes the threat of  $CB$  if the executive announces  $p^X = 0$ . This is not an empty threat for, as already mentioned, they have no incentives to grant special powers when the reform is not announced by the executive.

In the equilibrium  $(0, 1, CB, CB)$  the executive proposes the reform only when it is needed and yet voters do not concede. The opportunity of a beneficial reform is lost in this equilibrium, even when voters learn which is the true state of nature, because the utility cost of rents is too high:  $c\bar{r} \geq 1$ .

Finally, the strategy profile  $(1, 0, CB, CB)$  is a PBE for any configuration of parameter values. In this equilibrium, there is no reform since voters always vote for  $CB$ . The executive reports exactly the opposite of the true state of nature, and hence voters learn which the state of nature is. Nevertheless, they have no incentives to provide special powers after they learn that a reform would be desirable because this occurs after the executive committed to the status quo policy. Conversely, when the executive claims that a reform is needed, voters learn it is not. The executive has no incentives to depart from this strategy either, because the outcome does not depend on its decision once voters have decided to vote for  $CB$  irrespective of the executive's actions.

### 2.2.5 A summary of the equilibria

Notice that in none of the equilibria discussed above voters grant special powers unless the expected utility gains from reform outweigh the utility losses from rent extraction, i.e. unless  $Pr(s = 1|p_X = 1) - Pr(s = 0|p_X = 1) \geq c\bar{r}$ . But  $Pr(s = 1|p_X = 1) - Pr(s = 0|p_X = 1) \leq 1$  and hence voters will not grant special powers unless  $c\bar{r} \leq 1$ . Thus, we have the following corollary.

**Corollary 1.** *Voters do not grant special powers in equilibrium if the utility cost of rents is larger than 1.*

As shown in Proposition 2, the profile  $(1, 0, CB, CB)$  is a PBE for any possible configuration of parameter values, and propositions 1 and 2 show that other equilibria arise for some configurations of parameter values. Thus, the model exhibits multiple equilibria. In the following proposition, we show that equilibria in which voters grant special powers weakly Pareto dominate the  $(1, 0, CB, CB)$  equilibrium.

**Proposition 3.** *Whenever two equilibria exist, one in which special powers are granted with positive probability and another one in which they are never granted, the first equilibrium weakly Pareto dominates the second.*

*Proof.* See the appendix. □

The following corollary establishes when special powers arise as an equilibrium outcome.

**Corollary 2.** *Special powers are part of the equilibrium outcome only if*

1. voters expected gains from reform are larger than their utility cost from rent extraction:  $Pr(s = 1|p_X = 1) - Pr(s = 0|p_X = 1) \geq c\bar{r}$ , and
2. the incumbent is **not** strongly pro-status-quo biased:  $\delta_X \geq -\frac{1+a_X\bar{r}}{2}$ .

Furthermore, special powers are part of the equilibrium outcome of any PBE that is not weakly dominated in the Pareto sense if, and only if, conditions 1 and 2 hold.

Corollary 2 follows immediately from propositions 1 to 3.

In Figure 3, we present the equilibrium outcomes for different configurations of the parameters.<sup>17</sup> As the figure shows, there are some parameter values such that voters grant special powers and the reform is passed if and only if  $s = 1$ . With these parameter values, the executive reports the state of nature truthfully.

Notice that, for some parameter values, our model predicts a “Nixon-going-to-China” type of result (Cukierman and Tommasi 1998). A decisive reformist incumbent is less able to convince citizens that a reform is necessary than a moderate conservative if  $q \leq 1/2$  and  $\bar{r} \leq 1/c$  or if  $q > 1/2$  and  $\frac{2q-1}{c} \leq \bar{r} \leq 1/c$ . As a result, if these conditions are fulfilled, voters grant *SP* and the reform is implemented if the incumbent is moderate, but not if he is a stubborn reformist.

But there is also a set of parameter values for which the executive always claims that a reform is needed and voters concede. For this outcome to occur in equilibrium, the unconditional probability that a reform is necessary must be larger than  $\frac{1}{2}$ . If the state of nature is actually 0, voters lose because of the passing of an inadequate reform and because of rent extraction. With these parameter values, the executive may pander to citizens beliefs in order to win the referendum. Indeed, if the reform is “popular” ( $q > \frac{1}{2}$ ), even an executive with a pro-status-quo bias might always report that a reform is needed to woo the electorate and win the referendum. The executive chooses the popular policy  $p_X = 1$ , even when the state of nature is  $s = 0$ , to obtain citizens support. In our model, the executive wants political support to win the referendum and get the special powers that make it possible to extract rents. In traditional models of pandering, the executive wants political support to be reelected (Besley 2005; Maskin and Tirole 2004; Smart and Sturm 2013).

### 2.3 Assumptions: interpretation and rationale

Before presenting the extensions of our basic model, we make a few remarks regarding some of our assumptions. First, we assumed that checks and balances are highly effective: rents are zero with checks and balances. This is of course an extreme assumption, useful to illustrate the mechanism in a simple form. In the real world, the mechanism is likely to be less effective. But our point is that even

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<sup>17</sup>In building this figure, we ruled out the equilibrium profile (1,0,CB,CB) even when this profile is an equilibrium for any parameter values because, as we have shown in Proposition 3, this equilibrium is weakly Pareto dominated by the equilibria with special powers.

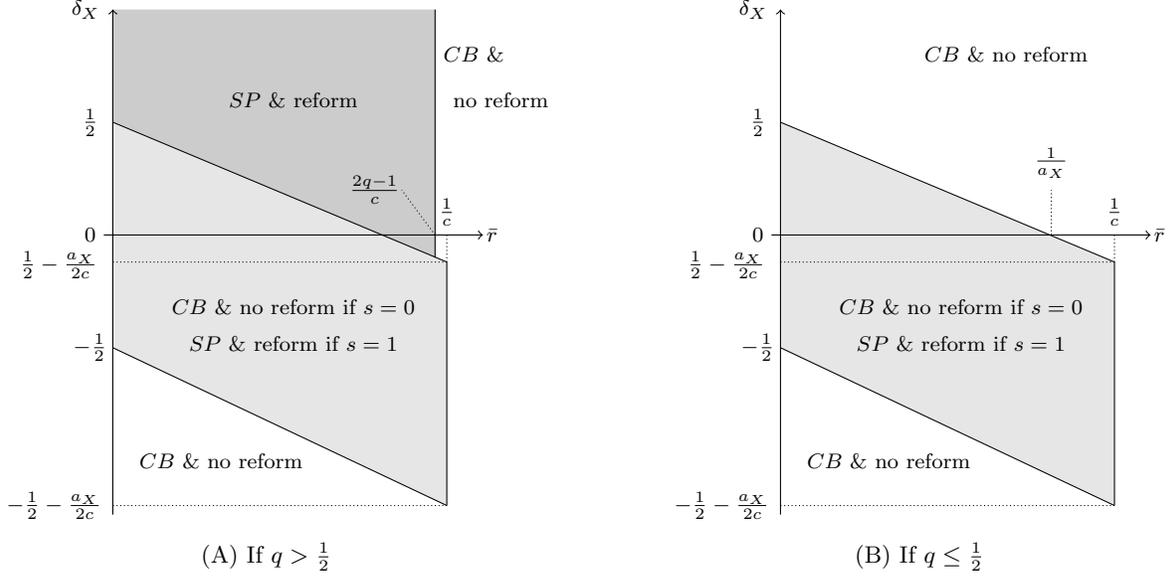


Figure 3: Equilibrium outcomes

with this highly effective mechanism, voters sometimes prefer special powers. It would be more so with less effective checks and balances.

Second, we have considered the costs associated with special powers, rent extraction and policies nonaligned with voters' preferences, concerning one period only. However, in many cases (as we describe in Section 4), the weakening of checks and balances was implemented through a constitutional reform which may have long-term consequences. We are certainly not modeling these effects. However, we can think about the costs associated with rent extraction ( $c\bar{r}$ ) as a reduced form of the discounted expected costs of special powers. Future analysis should include voters' and politicians' decisions in a dynamic model where special powers have costs spanning multiple periods.

Third, citizens support for special powers is key in our story as it is necessary for special powers to arise. We are not explaining cases in which unpopular dictators ruled without checks and balances based on military force. We are interested in the same type of phenomenon analyzed in Acemoglu et al. (2013). For simplicity and concreteness, we model this support as an explicit vote in a referendum, but this should not be taken literally. Our model is meant to encompass cases in which public opinion support was instrumental for the executive to obtain special powers, even if the specific procedure was not always a referendum (see Aghion et al. 2004, for a similar point).

Indeed, several observers of the Latin American experience have argued that citizens support was crucial for the weakening of checks on the executive in several cases in which the executive did not call for a referendum. Some analysts stress the impact that the spread of polls in the nineties in Latin America had to facilitate or hinder reform. Finkel (2008) and Weyland (2003), for example, argue that

high popularity was instrumental for Fujimori and Menem to take actions that undermined the checks on the executive. Some of these actions did not require an explicit referendum, but they would not have been possible had the president not been highly popular. And conversely, Weyland (2003) argues that Collor de Melo in Brazil could not advance reforms and was eventually ousted from office, among other reasons, because of the erosion of his popularity in polls. Also, there are other forms of political action citizens can use to impact on the ability of the executive to impose its will, like demonstrations. In Latin America, this type of political action has been important in many cases both to strengthen some popular leaders and to weaken unpopular ones. Aydin (2013), for example, describes how in 2004 Ecuadorian parliament ousted President Gutiérrez after popular riots in response to Gutiérrez takeover of the supreme court.

Fourth, in our basic model a gridlock occurs when the legislature and the executive have different preferences regarding reform. This is reminiscent of the conventional wisdom that asserts that divided government—the control of the executive and the legislature by different parties—leads to gridlock, an hypothesis that has been challenged in some studies of American politics (see Alesina and Rosenthal 1995; Bernecker 2016; Fiorina 1990, 1991, 1992; Frymer 1994; Kelly 1993; Krause 2000; Krutz and Peake 2009; Mayhew 1991; Saeki 2009, among many others). In our model we assume that the executive and the legislature have different ideological preferences, rather than they are controlled by different parties. More importantly, what is key for our results is that CB reduce the capacity of the executive to advance reform (or at least citizens think this is the case). It is less important whether this is because different parties control the executive and the legislature or the legislators and the executive hold different ideologies (as, for example, Frymer (1994) finds). Furthermore, as we discuss in Section 3, the model can be easily adapted to consider the scenario in which the key agency controlling the executive is the judiciary rather than the legislature. In this case, CB may slow down reform simply because the judiciary controls the strict application of procedures.

Finally, a key assumption of our model is that CB hinder reform. While this is a common view in the literature (Aghion et al. 2004; Carrión 2006; Kenney 2000; O'Donnell 1994; Rose-Ackerman et al. 2011; Tsebelis 1995, among many others), Stephenson and Nzalibe (2010) warn us that rational voters would adjust their voting strategies in response to tighter control of the executive so that the net effect of CB on policies is in principle ambiguous. In their words, “internal checks and balances reduce the voters’ need to rely on asymmetric electoral punishments or rewards.” As a result of these countervailing effects, adding a veto player does not necessarily reduce the probability that a new policy is enacted. We do not tackle this important point in our stylized framework that abstracts from electoral accountability. We simply assume that the direct effect prevails and hence CB hinder reform. This is what leaders claiming for special powers argued in all the cases we discuss below, and it seems sensible to assume that voters who supported them accepted this claim.

## 2.4 Extensions

In this section we study two extensions of the basic model. First we consider the case where politicians cannot commit their policy proposals at the referendum time. The second extension includes elections at the beginning of the game where voters choose a politician for the executive and another for the legislature. In both cases, we discuss the main results, and relegate the definitions and propositions to the Appendix.

### 2.4.1 The model without commitment

In the basic model, we assumed that politicians can commit the policy they announce in the referendum campaign. In this section, we discuss a variation of the model where politicians cannot commit their referendum platforms, and we study the impact of commitment on the occurrence of special powers.

The model without commitment also has a practical interest for at least some of the episodes analyzed in this paper: Fujimori in Peru and Menem in Argentina promised policies in the electoral campaign that they did not follow once in office (O'Donnell 1994; Stokes 2001). So the assumption that the executive commits its policies may not be granted.

In the absence of commitment, the executive with *SP* implements its preferred policy and extracts rents. Thus, an executive with a pro-reform bias ( $\delta_X \geq \frac{1}{2}$ ), a small bias ( $-\frac{1}{2} \leq \delta_X \leq \frac{1}{2}$ ) or a pro-status quo bias ( $\delta_X \leq -\frac{1}{2}$ ), implements  $p = 1$ ,  $p = s$ , or  $p = 0$ , respectively. As we show in the Appendix (Proposition 5) and discuss below, the ability of the executive to commit its campaign promises may have very different effects on the occurrence of special powers depending on the parameter values.

Consider first the case of an executive with a pro-reform bias:  $\delta_X \geq \frac{1}{2} - \frac{ax\bar{r}}{2}$ , so it always proposes the reform in the model with commitment. If rents are sufficiently large ( $\bar{r} \geq \frac{q}{c}$ ), voters do not grant *SP*, no matter the commitment ability of the executive. Conversely, if rents are small enough ( $\bar{r} \leq \frac{2q-1}{c}$ ), voters grant *SP* with and without commitment. However, there is a range of rents ( $\frac{2q-1}{c} \leq \bar{r} \leq \frac{q}{c}$ ) such that voters are willing to grant *SP* only when there is no commitment. Indeed, if the executive bias is such that ( $\frac{1}{2} - \frac{ax\bar{r}}{2} \leq \delta_X \leq \frac{1}{2}$ ), commitment implies a policy distortion as there is reform in both states of nature, even when voters and the executive prefer the status quo policy when  $s = 0$  after *SP*. This distortion increases the cost of *SP* with commitment. Without commitment, there is no distortion of policies, which makes *SP* more attractive for voters. Thus, with a pro-reform executive, voters are more willing to grant *SP* without commitment than with commitment. Moreover, the absence of the policy distortion makes voters and the executive weakly better off without commitment than with commitment.

Second, with a small policy bias ( $-\frac{1}{2} \leq \delta_X \leq \frac{1}{2} - \frac{ax\bar{r}}{2}$ ), the executive in the model with commitment reveals truthfully the state of nature, and so voters grant *SP* only when the reform is needed and rents are such that  $\bar{r} \leq \frac{1}{c}$ . Without commitment, the executive cannot credibly inform citizens. Nevertheless,

if rents are small enough ( $\bar{r} \leq \frac{q}{c}$ ), they grant *SP* as the executive will choose the “right” policy, even when it will extract rents in both states of nature. Hence, when the executive has a small policy bias and rents are small enough, the absence of commitment increases the events of *SP*, and makes voters weakly worse off, and the executive weakly better off. For intermediate rents ( $\frac{q}{c} \leq \bar{r} \leq \frac{1}{c}$ ), voters are willing to allow rent extraction if the reform is implemented, but not when the implemented policy is the status quo. However, this is only possible when there is policy commitment. Thus, without commitment, voters never grant *SP*, and they do it with commitment only when  $s = 1$ . In this case, both voters and the executive are weakly worse off without commitment.

Finally, with sufficiently strong pro-status quo bias, the absence of commitment has either no effect or tends to discourage voters to grant special powers. If the status quo bias is very strong ( $\delta_X \leq -\frac{1}{2} - \frac{ax\bar{r}}{2}$ ), no matter the commitment ability, voters do not grant special powers because the executive will not implement the reform. If the status quo bias is not so extreme but it is still negative enough ( $-\frac{1}{2} - \frac{ax\bar{r}}{2} \leq \delta_X \leq -\frac{1}{2}$ ), the executive will never implement reform if there is no commitment. However, with commitment the executive is willing to propose and to implement a reform in order to capture rents. Knowing this, voters are willing to grant *SP* if rents are not so painful ( $\bar{r} \leq \frac{1}{c}$ ). Thus, in the absence of commitment voters never grant *SP*, while in the basic model they do it only when the reform is needed. Note that this is the counterpart of the first case, as the executive would prefer to commit its policy in order to capture rents, and voters will also be better off. As a result, the inability to commit increases the distortion of policies in this case, and makes voters and the executive weakly worse off.

### 2.4.2 Introducing elections

In our basic model, we do not analyze how the government is elected. We take it as given that the legislature is pro status quo so a gridlock may arise under CB. The electorate may then grant the executive special powers to break the gridlock. However, when we think of the identities of the politicians in the two agencies, one may wonder why would the electorate choose a conservative legislature and then grant the executive *SP* to further reform. Would it not be better to prevent the political stalemate at the election time? Doing so, voters would avoid gridlock without dismantling controls on the executive.

In this section we introduce elections. Following the lead of the political science literature on divided government, we explore two different lines of argument.<sup>18</sup> The first explanation is that divided government is just an unintended outcome, resulting from voters ignorance and lack of coordination. The only difference of this framework with the basic model is that now voters rather than Nature choose

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<sup>18</sup>The fact that in the US voters often choose candidates of different parties for the executive and the legislature generating a divided government has spanned considerable academic attention (see Alesina and Rosenthal 1995, 1996, 2000; Fiorina 1990, 1991; Howitt and Wintrobe 1995; Krutz and Peake 2009; Mayhew 1991, among others). While this literature is to some extent specific to the US political system, we think that its basic insights are useful to think of other presidential systems.

politicians. But since they have no information about the candidates, the election is trivial: there are no strategic considerations or even simple utility maximization at this stage. While voters would like to choose unbiased politicians for both offices, they have no basis to judge. Having a biased pro status quo legislature, as we assumed in our basic model, is thus one possible outcome.

The second explanation follows the argument of Alesina and Rosenthal (1995, 1996, 2000) by which voters consciously choose divided government to moderate policies. A simple way of obtaining this result in our framework is to assume that there are only two types of politicians, a conservative one with a strong pro status quo bias ( $\delta_C < -1/2$ ) and a reformist one with a strong pro reform bias ( $\delta_R > 1/2$ ). Voters observe the candidate type and may choose different types for the two agencies to hedge against the risk of extreme policies. In this model, when the legislature is conservative and the executive reformist, CB bring moderation of policies in the sense that the implemented policy is  $\alpha \in [0, 1]$ , rather than the status quo policy as in the basic model. Furthermore, after choosing a divided government, voters can grant the executive special powers to facilitate reform if they receive information that suggests that a reform might be beneficial. In this sense, in our model divided government can also produce policy moderation across states of nature.

As we show in the Appendix (Proposition 8), there is an equilibrium of the model for intermediate values of  $q$ , where voters choose a divided government with a reformist executive and a conservative legislature. This equilibrium produces the paradoxical result that voters do not give the president the legislative majority that would allow him to implement his agenda, and later vote for SP to advance the same agenda with the added cost of rent extraction. The reason is that while at the election time voters only know that  $s = 1$  with probability  $q$ , at the referendum time they observe the realized state of nature.

### 3 The executive and the judiciary

Our basic model lacks a judiciary, but we show in this section that with only minor modifications, the model can be adapted to the case in which the two public agencies are the executive and the judiciary, rather than the legislature. Albeit quite straightforward, we think this extension is important for the analysis of the Latin American experience. In several of the cases we discuss below, the high popularity of the president and the concomitant control of the legislature left the judiciary as the last and only check on the executive. Not surprisingly, the judiciary became an institution in dispute.

The judiciary is meant to play a key role in the system of checks and balances: it has a mandate to exert constitutional control, ensuring that the executive and the legislature remain within their constitutional limits. The role of the judiciary in controlling the executive is particularly important in the case of strong presidentialism and unified government (Chavez 2004). For this mandate to be

fulfilled, the judiciary must be independent, something that is not warranted in general, and particularly not so in less developed democracies. Finkel (2008) argues that it must also wield authority, and uses the term “judicial power (...) to best capture the idea of a court whose actions demonstrate that it enjoys independence as well as authority.” There is a growing and lively literature on judicial independence and the role of the judiciary in political accountability (Almendares and Le Bihan 2015; Aydin 2013; Finkel 2004, 2008; Inclán Oseguera 2009; Rios-Figueroa 2014; Stephenson 2003, among others).

As Finkel (2008) observes, the constitutional mandate to exert control on the other powers generates the possibility that the judiciary interferes with the ability of a ruling party to implement its preferred policies. In our model, this interference is the reason why citizens sometimes grant the executive special powers to advance a reform they consider necessary.

### 3.1 The setting

As before, there are two policy dimensions: a policy issue  $p \in \{0, 1\}$  and rent extraction, but in this case only the executive may extract rents  $r_X \in [0, \bar{r}]$ . If allowed to act independently, the judiciary can veto some policies and ban rent extraction.<sup>19</sup>

As before, there are two policy regimes, but CB are simpler now:

1. *CB* determines that:

1.  $p = p_0$
2.  $r = 0$

2. *SP* determines that:

1.  $p = p_X$
2. *Executive chooses*  $r_X \in [0, \bar{r}]$

Notice that we are assuming a “conservative” judiciary that chooses  $p = p_0$ , irrespective of the state of nature. This is a simple form of representing the idea that the judiciary is the custodian of the law and so is naturally bent towards the status quo.

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<sup>19</sup>The judiciary in this model is honest and efficient by assumption, and yet citizens will sometimes vote against it. Our goal is to explain why citizens may not support the judiciary, **even if** it is efficient and honest. To this end, we put ourselves in the most difficult situation of a completely honest judiciary. Of course, this assumption would not be appropriate to analyze why some decisions should be handed to the judiciary as in Maskin and Tirole (2004) or Almendares and Le Bihan (2015).

The preferences of voters and the executive look very much like in the basic model:

$$v = -E_s [(p - s)^2] - c r_X,$$

$$u_X = -(p - s - \delta_X)^2 + a_X r_X,$$

the only difference is that the terms related to the legislature have been dropped.

The timing is as follows:

1. Nature chooses:
  - (a) the status quo policy  $p_0 \in \{0, 1\}$ ,
  - (b) the state of nature  $s \in \{0, 1\}$ , using a random mechanism by which  $s = 1$  with probability  $q$ ;
  - (c) a politician to run the executive.
2. The executive makes an announcement regarding the state of nature and commits to the matching policy proposal  $p_X$ . The executive observes previous Nature's moves, including the state of nature.
3. Referendum: voters choose the policy rule  $CB$  or  $SP$ , knowing  $p_0$  and  $p_X$ , but not  $s$ .
4. If in step 3 voters choose  $CB$ , then the judiciary imposes  $p = p_0$  and  $r = 0$ .
5. If in step 3 voters choose  $SP$ , then  $p = p_X$ , and the executive chooses  $r_X \in [0, \bar{r}]$ .
6. The game ends and payoffs are computed.

As before, we assume that the status quo policy is zero:  $p_0 = 0$ .

### 3.2 Solution

If voters choose  $CB$ , the equilibrium policies are:  $p = r_X = 0$ . If voters choose  $SP$ , the rents are  $r_X = \bar{r}$ . The executive rules but it is already committed to the policy announced in step 2:  $p = p_X$ . Hence, the policy outcomes of the games that begin after the referendum took place are exactly the same as in the basic model (equations 1 and 2).

The referendum game that the executive and voters play is also the same as in the basic model. Therefore, the solutions are the same.

## 4 Case studies

In this section, we discuss some stylized facts and some historical episodes that illustrate the mechanisms in our formal model.<sup>20</sup> We consider case studies from several Latin American countries in the nineties,

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<sup>20</sup>We think this discussion is "illustrative" but we make no claim that we are empirically testing our model. Readers should be aware that we have been selective in the cases we discuss.

during the reign of the market-friendly paradigm baptized as the Washington Consensus, and in the two thousands, under the “progressive” paradigm.<sup>21</sup> These reforms were very different —arguably, the “progressive” were opposite to the “neoliberal” reforms—, but in all cases there were strong leaders who asked for special powers arguing that they could not advance the much needed reforms without them. A simple explanation of why many citizens voted for the dismantling of checks and balances is that they supported these leaders with their reform agenda, and accepted the argument that checks and balances blocked reform. This is in a nutshell what our model says.

## 4.1 The nineties: special powers to advance the pro-market reforms

### 4.1.1 Peru under Fujimori

In 1990, Alberto Fujimori was elected president of Peru with the largest majority ever obtained by a presidential candidate in the country. Peru was suffering a severe economic and political crisis. Inflation had reached peaks of about 50 percent per month in 1989 and a bloody guerrilla was killing not only the military but also many civilians. The situation looked totally out of control and the general feeling was that something had to be done. Early in his mandate, Fujimori’s popularity was boosted by the progress he could exhibit in the fight against inflation and the guerrilla (Carrión 2006; Weyland 2003).

On April 5, 1992, Fujimori led an auto-coup, suspending the congress, and overriding the judiciary. In the speech in which he announced the closing of the legislature, Fujimori argued that “the lack of identification of some fundamental institutions with the national interests, like the legislature and the judiciary, blocks the actions of the government oriented to national reconstruction and development”. And he continued: “We cannot wait three more years until citizens identified with the real interests of the people reach the legislature. We cannot either wait one more day to carry on the total reorganization of the judiciary.” (Fujimori 1992b, our translation from Spanish). In a speech he gave in July 1992, the second anniversary of his taking office, he insisted on that he needed extraordinary powers as a justification of the auto-coup: “the issue of the forms remained to be solved, because there was a Constitution that impeded solving the problems out of its ways and courses of action. The dilemma again: doing or not doing.” (Fujimori 1992a, our translation from Spanish).

In a public opinion poll conducted two days after the closing of the legislature, 71 percent of the respondents agreed with the closing of the legislature and 89 percent approved the restructuring of the judiciary (*Caretas* magazine, April 4, 2002).<sup>22</sup>

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<sup>21</sup>We analyze the nineties in more detail than the two thousands because the main point in this narratives —the paradox of the dismantling of checks and balances with citizens support— has already been made for the two thousands very clearly by Acemoglu et al. (2013).

<sup>22</sup>[www.caretas.com.pe/2002/1715/articulos/golpe.phtml](http://www.caretas.com.pe/2002/1715/articulos/golpe.phtml). The poll was conducted by a firm called *Apoyo*. Some opposition politicians, like Mario Vargas Llosa, denounced that these polls were rigged. We have no direct evidence to judge this claim, but the facts that Fujimori won by wide margins the 1990 presidential elections and, more telling, the November 1992 elections for the constitutional congress and the 1995 legislature and presidential elections lend some credibility to these figures. Also some other analysts of Peruvian politics do not seem to question these polls (Carrión 2006).

After the closing of the legislature, Fujimori called special elections to settle a constitutional convention. The election took place on November 22, 1992, and Fujimori's coalition obtained a strong majority. The convention drafted and passed a reform of the constitution that, among other things, substituted a unicameral for the previous bicameral legislature, introduced the reelection of the president and strengthened presidential powers with the introduction of the decrees of necessity and urgency. The new constitution also created a National Judicial Council. The Constitutional Court was maintained. In the view of Finkel (2008), these latter rules that apparently strengthened the judiciary were concessions in exchange for the right to seek a second term. More importantly, in her view these were only temporary concessions as after the 1995 elections, in which Fujimori was reelected and gained a strong majority in the legislature, he "used his congressional majority to enact legislation systematically eviscerating all judicial autonomy and power."

The very high popularity Fujimori enjoyed during his decade in office seems to have been crucial to advance his policies and get the special powers he sought. The importance of public support is particularly obvious in the case of political reforms that were submitted to public consultation. But Fujimori's exceptional powers went well beyond what the new legislation explicitly stated. At least since Vladimiro Montesino's files became public, it has been widely accepted that his administration systematically performed operations to corrupt the media, manipulate the judiciary, subordinate the legislature and harass political opponents. This type of "special powers" were of course not submitted to public voting but, in the view of several analysts, the popularity that the regime held by that time greatly facilitated these practices. As Carrión (2006) puts it, "Fujimori's efforts to establish an authoritarian regime could have been unsuccessful if not for the substantial support he elicited from wide swaths of Peruvian society" (see also Weyland 2003, for a similar point). Therefore, even when not all of the "special powers" that Fujimori obtained in this period emerged from formal referendums, it seems safe to argue that strong public support was crucial in building his political power.

#### **4.1.2 Argentina under Menem**

After winning the 1989 elections, Carlos Menem took office for the first time in July 1989, six months in advance of the constitutional inauguration date and after the former president Raúl Alfonsín had to resign, unable to control a devastating economic crisis. Ferreira Rubio and Goretti (1996) convincingly argue that the crisis generated in the public opinion a demand for government efficacy, something that only a strong executive could provide. After a short failed attempt, Menem had a resounding success in fighting inflation thanks to a stabilization program that pegged the currency to the American dollar. According to Weyland (2003), the success in fighting inflation reinforced the already extended opinion that a strong effective executive was needed.

Early in his first term, Menem expanded the Supreme Court from five to nine justices. This reform,

compounded with the resignation of two of the existing judges and opaque appointing procedures, allowed Menem to have an “automatic majority” in the Court (Chavez 2004; Finkel 2004). Chavez (2004) cites striking declarations by some of the newly appointed members who did not even bother to simulate independence. Rodolfo Barra publicly declared that “*My only bosses are Perón and Menem*” and also that “*I cannot dictate a ruling that is against the government. I only issue rulings that are favorable to administration officials.*”<sup>23</sup> Menem’s minister of justice, Raúl Granillo Ocampo, also publicly argued that the executive needed a subservient judiciary to advance its policy agenda : “*An administration ... cannot govern with a judiciary whose views are antagonistic to those of the government. If the Court were to have a vision completely different from ours and to declare our laws unconstitutional, we could not implement our political and economic plans.*” (cited in Chavez 2004).

A distinctive feature of Menem’s government was the intensive use of decrees of necessity and urgency. The instrument was not new but the number of decrees in his administration rose dramatically compared to historical records. While only 35 decrees had been passed between 1853 and July of 1989, Menem issued 336 decrees of necessity and urgency between July 1989 and August 1994 (Ferreira Rubio and Goretti 1996). The ministry of finance, Domingo Cavallo, declared that, without the decrees, “it would not have been possible to implement more than twenty percent of the economic reform” (newspaper *La Nación*, 08/31/93).

The Argentinean constitution did not allow for the reelection of the president. Despite of high popularity, Menem did not have the special majorities needed in the house of representatives to pass a constitutional reform that gave him the opportunity for a second term in office. But in 1994, he negotiated an agreement with the main opposition party to promote a constitutional reform that included this provision.

The 1994 constitutional reform did not unambiguously increase the executive’s powers. Menem obtained the reelection for a second term, but in exchange he had to accept several measures geared at the strengthening of the checks on the executive. The new constitution introduced the figure of Chief of Cabinet, who would respond to the executive and the legislature. The rules for the selection of Supreme Court judges were modified to require two thirds of the senate vote instead of the simple majority required before, and a national judicial council was settled to select lower level judges and operate as a discipline tribunal.

Several analysts have argued that the attempt at strengthening the checks on the executive was to a large extent ineffective (Chavez 2004). After being reelected in 1995 with strong popular support, Menem maneuvered to delay the actual implementation of the judicial reform (Finkel 2004; Manzetti 2014). Also Rose-Ackerman et al. (2011) argue that the judicial council did not curtail the influence of

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<sup>23</sup>Similarly, in 1997 the Supreme Court justice Vázquez publicly declared that “*When there is a case against the government, I do not rule against the administration.*”

the president in appointing judges because council's candidates who lacked political connections would not be selected by the president or confirmed by the senate.

Finkel (2004) argues that the 1997 mid-term elections changed the incentives of the government regarding the judiciary. In these elections, an opposition coalition called the *Alianza* got a sounding victory. Hence the perspectives for Menem's party to gain the national elections in 1999 began to fade. The Alianza candidates had actively campaigned for the establishment of an independent national judicial council and immediately after the newly elected congressmen took office, a bill to set an independent council was presented and passed. Menem still delayed the selection of the Council members postponing the installation of the Council for one more year.

Like Fujimori in Peru, Menem embraced a pro-market reform agenda soon after he took office. This agenda came as a surprise because it departed from the traditional position of the Peronist party and even from Menem's own rhetoric during the electoral campaign (Stokes 2001). Menem was indeed an unlikely reformist in the environment of the early nineties with a reform agenda totally dominated by privatization, free trade, financial liberalization and macroeconomic discipline. Paradoxically, as our model suggests, his belonging to the Peronist party may have given him a leverage to convince fellow citizens that a reform was needed in the new critical juncture (the "Nixon going to China" effect described by Cukierman and Tommasi 1998).

Levitsky (2003) proposes an "organizational approach" to understand the progress Menem could make in advancing pro-market reforms in a labor-based party. In his view, the lack of "institutionalized routines" and formal structures facilitated the adaptation of this labor-based mass movement to a challenging new environment in which policies traditionally supported by the movement looked completely outdated. Unlike other labor based political parties with more rigid organizational structures, the Peronist party could rapidly and successfully process a change in its political platform. According to Levitsky, patronage also played an important role in this transformation. This analysis contributes to explain why Menem could obtain wide support for the new agenda. Our point is complementary to Levitsky's: Menem convinced citizens not only that pro-market reforms were needed, but also that a weakening of the checks on the executive was necessary to advance this much needed reforms.

In summary, during most of his mandate, Menem enjoyed a strong popular support that allowed him to increase his discretionary powers and advance his reform agenda. He enjoyed a strong disciplined majority in the legislature, so the issue was not the legislature but the judiciary control. And in fact, the legislature contributed with the executive to submit the judiciary. There were no referendums to grant the executive special powers, but the executive used the majority it had obtained in the legislature to subordinate the judiciary. He could then rule and advance his policy agenda with little control.

## 4.2 The two-thousands: special powers to advance the anti-market reforms

### 4.2.1 Venezuela under Chávez

Hugo Chávez won the 1998 Venezuelan presidential elections with more than 56 percent of the ballot (the second largest in four decades). He presented himself as an outsider of a very unpopular political class. Pursuing an unconditional support from collaborators and the people, he cultivated a confrontational political style and a radical left-wing rhetoric, that deliberately polarized the citizenry. With a strong use of symbols, Chávez left no doubt of his re-foundational goals when in 1999 changed the name of the country from *República de Venezuela* (Republic of Venezuela) to *República Bolivariana de Venezuela*, named after the country hero Simon Bolivar. His agenda was one of radical anti-market reform.

Immediately after taking power, and honoring a much publicized campaign promise, Chávez embarked in a process of reform of the constitution. In April 1999 almost 88 percent of the electorate voted in favor of calling the constitutional assembly. The text of the consult left no doubts regarding the re-foundational goals of the president: “Do you call a national Constitution assembly with the purpose of transforming the state and creating a new legal order that allows the working of a social and participatory democracy?” (our translation from Spanish). A new constitutional text was drafted in the following months and voted for in December 1999. It got 72 percent of the votes. The reform was clearly geared at strengthening the executive vis-à-vis the legislature and the judiciary. Very much like in the other cases, Chávez forcefully argued that he needed the reform of the constitution to advance his substantive reform agenda.

In the following years, Chávez continued strengthening the executive always with strong support from the population. In 2000 he obtained the right to rule by decree for a year. This right was renewed in 2007 and 2010 (in these opportunities by 18 months each time). In 2000, Chávez called again for presidential elections under the new constitution. He was reelected with almost 60 percent of the ballot. With the exception of a constitutional referendum held in 2007, which Chávez did not win by a relatively small margin, he won all other elections by wide margins.

### 4.2.2 Ecuador under Correa

Rafael Correa won the 2006 elections in Ecuador. In early 2007 he called for a referendum to hold a constitutional convention, which he won with 82 percent support from voters. The elections for the convention took place in September and his party won 80 of the 130 seats in the convention. The new constitution strengthened the executive. It granted the president ample rights to convoke referenda, dissolve the legislature and call for elections once in each term, reduced the incidence of the legislature in justice appointments, and allowed for reelection. The constitution was approved in 2008 with 64 percent of the votes (Acemoglu et al. 2013).

In the referendum campaign, Correa alleged that the strengthening of the executive powers was needed to advance reforms. He argued that the elites held significant *de facto* power and would derail the popular reforms unless strong political action with active popular participation took place (Correa 2008). In the campaign, Correa refused the criticism of the opposition that the constitutional reform would lead to hyper-presidentialism. However, in March 2009, soon after the reform was approved, he left no doubt that he did not believe in the separation of powers when he publicly declared that: “the President of the Republic, listen to me well, the President of the Republic is not only the head of the executive power, he is the head of the whole Ecuadorian state, and the Ecuadorian state is the executive power, the legislative power, the judicial power, the electoral power, the transparency and social control power, the superintendencies, the attorney general’s office, the government accountability office. All that is the Ecuadorian state.” (from Correa’s speech on March 7, 2009, quoted in Pásara 2014, our translation).

#### **4.2.3 Bolivia under Morales**

Evo Morales was elected president of Bolivia in 2005. He called a constitutional assembly, of which he could control a majority, but not the two thirds required to pass all the reforms he wanted. In 2009, the new constitution was ratified in a plebiscite and received 61 percent of the votes.

The reform significantly increased the executive’s powers. Although Morales could not obtain perpetual reelection rights, the one-term limit was removed. He also failed to substitute the unicameral for the existing bicameral legislature. But he succeeded in getting rid of supermajorities previously needed to confirm several president appointees. In 2010, he passed a law authorizing the executive to appoint new members in the supreme court, the constitutional tribunal and the judicial council (Acemoglu et al. 2013).

As in the previous cases, President Morales strengthening of the executive powers was justified on the grounds that the country needed radical policy reform. In his view, the reform was not possible unless he held more powers.

### **4.3 Common themes**

In all these episodes, there was some combination of the extension of the term limits or the introduction of reelection rights, the loosening of the checks by the parliament, the decrees of necessity and urgency and the reduction of the judiciary independence. The exact mix varies from case to case, but the strengthening of the executive vis-à-vis the rest is the common characteristic.

Also common was the fact that these measures were promoted by very popular presidents who received strong support from voters. Special powers were not always explicitly voted for, though. There are examples in which strong leaders *de facto* weakened checks on the executive without appealing to

popular vote, but the popularity of the presidents seems to have been crucial to make these reforms feasible in all these cases.

Like Fujimori and Menem had done in the nineties, Chávez, Correa and Morales in the two-thousands sought citizens support to strengthen the executive capacity, alleging that such instrument was needed to overcome political stalemate and advance sweeping reforms. The substantive content of the policy reforms was very different in the nineties and two-thousands, but the allegation that the country needed radical reforms that could not be done without strong executive is very much the same.

We are of course not claiming that citizens who supported these strong leaders were equally happy with the whole package. Carrión (2006), for example, based on polls conducted in Peru in the early nineties, argues that the population was much more supportive of the fiscal adjustment at the beginning of Fujimori’s administration, the control of inflation and the fight against the guerrilla than of other market-oriented reforms. In his view: “citizens rejected some of his economic policies regardless of their support for his overall performance in office”. It could be argued that citizens had to make a take it or leave it decision without being able to unbundle the package.<sup>24</sup>

Arguably, because of crisis the probability that a reform was needed rose short before all these episodes, or at least that was what many citizens thought. In terms of our model this means a rise in  $q$ .<sup>25</sup> The failure of traditional recipes during the eighties (“the lost decade”) paved the way for the pro-market reforms in the nineties. Also, the drawbacks of pro-market reforms in the nineties gave way to the leftist policies in the two thousands.

With moderate leaders (small  $\delta_X$ ) and limited opportunities for corruption (small  $\bar{r}$ ), the increase in  $q$  would have had a direct linear impact on the probability of reform. In terms of our basic model, this would be the case of an increase in  $q$  in a truth-telling equilibrium. Not only would the increase in the likelihood of reform been moderate, but also, and more importantly, it would have simply matched the increased need for reform. Even when these policy reforms implied some weakening of checks and balances creating the opportunity for rent extraction, it could be argued that this was the unavoidable cost of much needed reforms.

But if the executive was dominated by a president with a pro-reform bias and/or the opportunities for corruption were not so low, then the increase in  $q$  could have had a significant positive discrete impact on the probability of reform. In terms of our model, the increase in  $q$  may have completely changed the equilibrium, moving from checks and balances and no reform to an always reform equilibrium.<sup>26</sup> This disproportionate shift in policies —with the loosening of checks and balances and increased corruption— would have occurred with the blessing of public opinion.

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<sup>24</sup>In terms of our formal model, these unpopular ingredients in Fujimori’s package would raise the value of the parameter  $c$  that measures the relative weight of rents and reform in citizens utility.

<sup>25</sup>This is our formal representation of the “sense of urgency” generated by crisis that, in the view of O’Donnell (1994) “provides a fertile terrain for unleashing the delegative propensities”, i.e. for the loosening of checks and balances.

<sup>26</sup>This could happen if  $\bar{r} \leq 1/c$  and  $\delta_X \geq 1/2 - a_X \bar{r}/2$ .

Notice that if this was the case, the situation of these countries prior to the increase in  $q$  would have been characterized by too little reform and political stalemate (the checks and balances no reform equilibrium), and the situation after the increase in  $q$  would have been characterized by too much reform and insufficient checks on the executive (the always reform equilibrium). In the first case, the opportunity of good reforms would have been lost and inaction would have dominated the political scene. In the second case, too much action would have taken place with the associated abuse of power and corruption, and with some harmful reforms being enacted.

In all the case studies we considered, citizens provided strong support to reform and this allowed presidents to strengthen their powers weakening checks and balances with limited resistance from other branches of government. Taylor-Robinson and Ura (2012) analyze the case of Honduras during the presidency of Zelaya and convincingly argue that the uncertainty about citizens standing regarding his agenda prompted an escalation of conflict between the president and the judiciary. They present a model of conflict between branches of government in which public support is uncertain and is revealed only at the end of the game. This uncertainty paves the way for conflict of powers and political instability.

Special powers with citizens support seem to have been more prevalent in the recently re-democratized Latin American countries than in developed countries with old well established democracies. And this is so despite of the comparatively high levels of corruption in the region. One possible explanation is that citizens are highly unsatisfied with the current state of affairs and are willing to concede strong presidents much leeway so they can “do what it needs to be done”. In terms of our formal model, the larger the importance of the reform (the smaller is  $c$ ) the larger are the rents citizens will be willing to tolerate in order to “have things done”. If this is so, citizens in these countries will be more willing to grant special powers and tolerate corruption than citizens in countries that face comparatively less challenging policy options. A common saying in some Latin American countries summarizes this feeling quite neatly: “he steals but he delivers” (*roba pero hace*, in Spanish, and *rouba, mas faz*, in Portuguese).

## 5 Concluding Remarks

In this paper, we present a simple model and provide some case studies geared to understanding episodes in which citizens supported the loosening of the checks on the executive. Our main argument is that checks and balances may hinder reform. If citizens are convinced that the reform raises welfare but it cannot be implemented because of a political stalemate, they may explicitly or implicitly support the president’s efforts to untie his hands.

We discuss five cases that occurred in Latin America and that seem to present all the ingredients that are key for our formal results. In all of them, strong presidents undermined the checks on the executive with the support of large swaths of the population. Two of these cases took place in the nineties and

the other three in the two thousands. In the former, Fujimori in Peru and Menem in Argentina used the increased powers to further pro-market reforms. In the latter, Chavez in Venezuela, Correa in Ecuador and Morales in Bolivia used these powers to advance anti-market reforms. The specific content of the reform was very different in the nineties and the two thousands, but the extended feeling that these re-foundational reforms had to be implemented at any cost was the same.<sup>27</sup>

Our model suggests that episodes of strong presidents who obtain popular support for the loosening of checks and balances are more likely to occur in circumstances of extended citizens discontent. In these circumstances, citizens are more likely to believe that sweeping reforms are necessary and are thus more willing to support strong men that promise to further reform. Checks and balances are then seen as stumbling blocks that have to be removed.

The dynamics described in this paper is likely to lead to the emergence of “illiberal” or “delegative” democracies and “hyper-presidentialism”. In these regimes, electoral outcomes and the popularity of the leaders prevail over the separation of powers and checks and balances.

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<sup>27</sup>Although the historical episodes we have discussed involve only Latin American countries, other recent experiences seem to fit the narrative of the paper. This might be the case of Recep Erdoğan in Turkey, Viktor Orbán in Hungary, and Vladimir Putin in Russia. However, further research is required to identify which elements of our story may apply also to these cases.

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## 6 Appendix

In this appendix, in order to shorten notation, we denote voters’ beliefs as  $q_0 = Pr(s = 1 | p_X = 0)$ , and  $q_1 = Pr(s = 1 | p_X = 1)$ . Also, throughout the proofs in this appendix, whenever a deviation of the executive consists in extracting rents, we consider its most profitable deviation, that is  $r_X = \bar{r}$ .

### 6.1 The basic model: Proofs.

*Proof of Proposition 1.*

1. Consider the profile:  $(0, 1, CB, SP)$ .

This is a truth-telling profile, so  $q_0 = 0$  and  $q_1 = 1$ . Voters expected gains from deviating are:  $-c\bar{r} < 0$  and  $c\bar{r} - 1$ , after receiving  $p_X = 0$  and  $p_X = 1$ , respectively. So voters do not deviate iff  $\bar{r} \leq \frac{1}{c}$ .

The executive’s gains from deviating are  $a_X\bar{r} - 1 + 2\delta_X$  and  $-a_X\bar{r} - 1 - 2\delta_X$ , after observing  $s = 0$  and  $s = 1$ , respectively. Therefore, the executive does not deviate iff  $-\frac{1+a_X\bar{r}}{2} \leq \delta_X \leq \frac{1-a_X\bar{r}}{2}$ .

In summary,  $[(0, 1); (CB, SP, q_0 = 0, q_1 = 1)]$  is a PBE iff  $\bar{r} \leq \frac{1}{c}$  and  $-\frac{1+a_X\bar{r}}{2} \leq \delta_X \leq \frac{1-a_X\bar{r}}{2}$ .

2. Consider the profile:  $(1, 1, CB, SP)$

The signal is not informative so:  $q_1 = q$ . Voters expected payoffs from following the strategy on the equilibrium path are  $(1 - q)(-1 - c\bar{r}) + q(-c\bar{r})$ , and from deviating:  $q(-1)$ . So voters do not deviate from the equilibrium path if  $q \geq \frac{1+c\bar{r}}{2}$ . Also voters have no incentives to deviate from this strategy profile out of the equilibrium path. Indeed, as we mentioned before, after observing  $p_X = 0$ , it is a dominant strategy for voters to play  $CB$ . This also implies that there are no restrictions on voters beliefs out of the equilibrium path.

Payoffs of the executive after abiding by this strategy are  $-(1 - \delta_X)^2 + a_X\bar{r}$  and  $-\delta_X^2 + a_X\bar{r}$ , when  $s = 0$  and  $s = 1$ , respectively. When the executive deviates it gets:  $-(1 + \delta_X)^2$  in the first case, and  $-\delta_X^2$  in the second case. Thus, the executive does not deviate iff  $\delta_X \geq \frac{-1-a_X\bar{r}}{2}$ , and  $\delta_X \geq \frac{1-a_X\bar{r}}{2}$ , which is equivalent to  $\delta_X \geq \frac{1-a_X\bar{r}}{2}$ .

In summary,  $[(1, 1); (CB, SP, q_0, q_1 = q)]$  is a PBE iff  $c\bar{r} \leq 2q - 1$  and  $\delta_X \geq \frac{1-a_X\bar{r}}{2}$ .

□

*Proof of Proposition 2.*

1. Consider the profile:  $(0, 0, CB, CB)$ .

The signal is not informative so:  $q_0 = q$ . Voters have no incentives to deviate on the equilibrium path, as  $CB$  is a dominant strategy after observing  $p_X = 0$ . Out of the equilibrium path, payoffs after abiding the strategy are:  $(1 - q_1)0 + q_1(-1) = -q_1$  and from deviating:  $q_1(-c\bar{r}) + (1 - q_1)(-1 - c\bar{r}) = -1 - c\bar{r} + q_1$ . Thus, voters do not deviate out of the equilibrium path if:  $q_1 \leq \frac{c\bar{r}+1}{2}$ .

Given that voters never grant special powers to the executive, its payoffs do not depend on its strategy (the policy outcome is  $p_1 = 0$  with no rent extraction), so it will not gain from a deviation.

In summary,  $[(0, 0); (CB, CB, q_0 = q, q_1)]$  is a PBE iff  $c\bar{r} \geq 2q_1 - 1 = 2Pr(s = 1|p_X = 1)$ .

2. Consider the profile:  $(0, 0, CB, SP)$ .

The executive choice is not informative, so  $q_0 = q$ . Voters have no incentives to deviate from  $CB$  after the executive chooses  $p_X = 0$ , since  $CB$  is a dominant strategy. Voters gains from deviating from  $SP$  after the executive chooses  $p_X = 1$  are  $-2q_1 + c\bar{r} + 1$ . Therefore, voters do not deviate from  $SP$  if  $c\bar{r} \leq 2q_1 - 1 = 2Pr(s = 1|p_X = 1) - 1$ .

The executive gains from deviating are  $-(1 - \delta_X)^2 + a_X\bar{r} + \delta_X^2$  and  $-\delta_X^2 + a_X\bar{r} + (1 + \delta_X)^2$ , after  $s = 0$  and  $s = 1$ , respectively. Therefore, the executive does not deviate after observing  $s = 0$

if  $\delta_X \leq \frac{1-a_X\bar{r}}{2}$ , and after observing  $s = 1$  if  $\delta_X \leq \frac{-1-a_X\bar{r}}{2}$ . These two conditions are fulfilled simultaneously if  $\delta_X \leq -\frac{1}{2}(1 + a_X\bar{r})$ .

In summary,  $[(0, 0); (CB, SP, q_0 = q, q_1)]$  is a PBE if  $c\bar{r} \leq 2Pr(s = 1|p_X = 1) - 1$  and  $\delta_X \leq -\frac{1}{2}(1 + a_X\bar{r})$ .

3. Consider the profile:  $(1, 1, CB, CB)$ .

The executive choice is not informative for voters, so  $q_1 = q$ . Voters' gains from deviating on the equilibrium path are  $-1 - c\bar{r} + 2q$ . Then, they do not deviate if  $q \leq \frac{1+c\bar{r}}{2}$ . Out of the equilibrium path, voters do not deviate as  $CB$  is a dominant strategy after observing  $p_X = 0$ .

Given that voters never grant special powers to the executive, its payoffs do not depend on its strategy (the policy outcome is  $p_1 = 0$  with no rent extraction), so it will not gain from a deviation.

In summary,  $[(1, 1); (CB, CB, q_0, q_1 = q)]$  is a PBE if  $c\bar{r} \geq 2q - 1$ .

4. Consider the profile:  $(0, 1, CB, CB)$ .

The executive tells the truth in this case, so voters update their beliefs as follows:  $q_1 = 1$  and  $q_0 = 0$ . Voters expected gains from deviating to  $SP$  after observing  $p_X = 1$  are  $-c\bar{r} + 1$ . Thus, they will not deviate if  $\bar{r} \geq \frac{1}{c}$  (when  $p_X = 0$  they will not deviate as  $CB$  is a dominant strategy).

The executive has no incentives to deviate. Indeed, the gains the executive obtain from deviating are zero both when  $s = 0$  and  $s = 1$ .

In summary,  $[(0, 1); (CB, CB, q_0 = 0, q_1 = 1)]$  is a PBE if  $c\bar{r} \geq 1$ .

5. Consider the profile:  $(1, 0, CB, CB)$ .

Voters update their beliefs as follows:  $q_0 = 1$  and  $q_1 = 0$ . After observing  $p_X = 1$ , voters expected gains from deviating are  $-1 - c\bar{r} < 0$ , so voters do not deviate (when  $p_X = 0$  they will not deviate as  $CB$  is a dominant strategy).

The executive gains from deviating are zero as voters never grant special powers.

In summary,  $[(1, 0); (CB, CB, q_0 = 1, q_1 = 0)]$  is a PBE.

6.  $(1, 0; CB, SP)$  is not a PBE.

Voters would never grant  $SP$  if the executive's strategy is  $(1, 0)$ . With this executive's strategy, voters update their beliefs as follows:  $q_0 = 1$  and  $q_1 = 0$  (they learn which is the true state of nature). When the executive proposes  $p_X = 0$ , voters learn that  $s = 1$  so a reform might be desirable if rents were not too large, but the executive has already tied its hands to no reform. Therefore, voters will choose  $CB$ . When the executive proposes  $p_X = 1$ , voters learn that  $s = 0$  so there is no need of reform and voters prefer  $CB$ .

□

*Proof of Proposition 3.*

The expected utility in the PBE  $(1, 0, CB, CB)$  is  $-q$  and  $-q - 2q\delta_X - \delta_X^2$ , for voters and the executive, respectively.

Suppose the equilibrium  $(1, 1, CB, SP)$  exists, so  $q \geq \frac{1+c\bar{r}}{2}$  and  $\delta_X \geq \frac{1-a_X\bar{r}}{2}$ . The expected utility is  $q - 1 - c\bar{r}$  and  $-1 + 2\delta_X - \delta_X^2 + a_X\bar{r} + q - 2q\delta_X$ , for voters and the executive, respectively. This equilibrium Pareto dominates the PBE  $(1, 0, CB, CB)$  if:

$$2q \geq 1 + c\bar{r}$$

and

$$\delta_X \geq \frac{1 - a_X\bar{r} - 2q}{2}.$$

The first inequality holds given that  $q \geq \frac{1+c\bar{r}}{2}$ , and the second holds as  $\frac{1-a_X\bar{r}}{2} > \frac{1-a_X\bar{r}-2q}{2}$ .

Suppose that the equilibrium  $(0, 1, CB, SP)$  exists, so  $\bar{r} \leq \frac{1}{c}$ , and  $-\frac{1+a_X\bar{r}}{2} \leq \delta_X \leq \frac{1-a_X\bar{r}}{2}$ . The expected utility is  $-qc\bar{r}$  and  $qa_X\bar{r} - \delta_X^2$ , for voters and the executive, respectively. This equilibrium weakly Pareto dominates the PBE  $(1, 0, CB, CB)$  as:

$$1 - c\bar{r} \geq 0$$

and

$$\delta_X \geq \frac{-1 - a_X\bar{r}}{2}.$$

□

## 6.2 The model without commitment.

In this Appendix, we present and solve the model without commitment. The game we study is the same as in the basic model, with the only difference that the executive cannot commit its policy. Note that without commitment and after  $SP$ , the executive implements its preferred policy and captures rents. Therefore, if voters choose  $SP$  or  $CB$  based on the announcement, the executive always claims that the state of nature is the one after which voters give  $SP$ . This implies that the announcement of politician is not informative about the state of nature. We include this observation in the following remark.

**Remark 6.** *There is no information transmission between politicians and voters in the model without policy commitment.*

We summarize the equilibrium results of the model without commitment in the next proposition.

**Proposition 4.** *Assume that there is no policy commitment. Then:*

1. The executive prefers the reform in both states of nature if, and only if,  $\delta_X \geq \frac{1}{2}$ . In this case, voters choose *SP* if, and only if,  $\bar{r} \leq \frac{2q-1}{c}$ .
2. The executive prefers the policy that matches the state of nature if, and only if,  $-\frac{1}{2} \leq \delta_X \leq \frac{1}{2}$ . In this case, voters choose *SP* if, and only if,  $\bar{r} \leq \frac{q}{c}$ .
3. The executive prefers the status quo in both states of nature if, and only if,  $\delta_X \leq -\frac{1}{2}$ . In this case, voters always choose *CB*.

*Proof.*

When  $s = 0$  the executive's payoffs from the implemented policy are:

$$-(p - \delta_X)^2 = -p^2 + 2p\delta_X - \delta_X^2.$$

Then, when  $s = 0$ , the executive prefers to set  $p = 1$  over  $p = 0$  if and only if  $\delta_X \geq \frac{1}{2}$ .

When  $s = 1$  the executive's payoffs from the implemented policy are:

$$-(p - 1 - \delta_X)^2 = -1 + 2p - 2\delta_X + 2p\delta_X - p^2 - \delta_X^2.$$

Then, when  $s = 1$ , the executive prefers to set  $p = 1$  over  $p = 0$  if and only if  $\delta_X \geq -\frac{1}{2}$ .

Suppose the executive's bias is such that  $\delta_X \geq \frac{1}{2}$ , so it implements the reform no matter the state of nature. Knowing this, voters expected payoffs are  $(1 - q)(-1) - c\bar{r}$ , and  $-q$ , when they choose *SP* and *CB*, respectively. In this case, voters choose *SP* if and only if  $\bar{r} \leq \frac{2q-1}{c}$ .

If the executive's bias is sufficiently low so the executive never implements the reform, that is,  $\delta_X \leq -\frac{1}{2}$ , voters know that *CB* and *SP* give the same policy outcome, so they never grant *SP*.

For intermediate cases, the executive implements the policy preferred by voters, so the expected payoffs from *SP* and *CB* are  $-c\bar{r}$  and  $-q$ , respectively. Hence, voters grant *SP* if and only if  $\bar{r} \leq \frac{q}{c}$ .  $\square$

Figure 4 represents the equilibrium outcomes of the model without commitment.

### 6.2.1 The effects of commitment

In order to understand the effects of the ability to commit the campaign promises, we compare the equilibrium outcomes and welfare with and without commitment. In the next proposition we focus on the effects of commitment on the occurrence of special powers.

**Proposition 5.** *The effects of commitment on the occurrence of special powers.*

1. Irrespective of the ability of the executive to commit its policy, voters always grant *SP*, if and only if  $\delta_X \geq \frac{1}{2} - \frac{a_X \bar{r}}{2}$  and  $\bar{r} \leq \frac{2q-1}{c}$ .

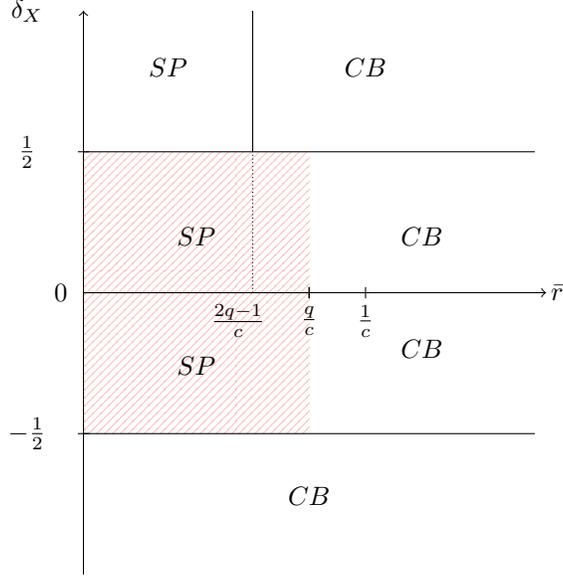


Figure 4: Equilibrium outcomes with no commitment ( $q > \frac{1}{2}$ )

2. Voters never grant SP to an executive that is committed to its policy, and do it always to an executive that is not committed, if and only if  $\frac{1}{2} - \frac{\alpha_X \bar{r}}{2} \leq \delta_X \leq \frac{1}{2}$  and  $\frac{2q-1}{c} \leq \bar{r} \leq \frac{q}{c}$ .
3. Voters grant SP to an executive that is committed to its policy only when  $s = 1$ , and does it always to an executive that cannot commit its policy, if and only if  $-\frac{1}{2} \leq \delta_X \leq \frac{1}{2} - \frac{\alpha_X \bar{r}}{2}$  and  $\bar{r} \leq \frac{q}{c}$ .
4. Voters grant SP to an executive that is committed to its policy only when  $s = 1$ , and never grant SP to an executive that cannot commit its policy, if and only if  $-\frac{1}{2} \leq \delta_X \leq \frac{1}{2} - \frac{\alpha_X \bar{r}}{2}$  and  $\frac{q}{c} \leq \bar{r} \leq \frac{1}{c}$ , or  $-\frac{1}{2} - \frac{\alpha_X \bar{r}}{2} \leq \delta_X \leq -\frac{1}{2}$  and  $\bar{r} \leq \frac{1}{c}$ .
5. In all other cases, voters never grant SP, irrespective of the executive's ability to commit its policy.

*Proof.* The proof follows directly from Figure 3 and Figure 4.  $\square$

The following proposition characterizes the welfare implications of commitment.

**Proposition 6.** *The effects of the executive commitment ability on welfare.*

1. Both voters and the executive are weakly better off without than with commitment if and only if  $\delta_X \geq \frac{1}{2} - \frac{\alpha_X \bar{r}}{2}$ .
2. Voters are weakly better off, while the executive is weakly worse off, with than without commitment if and only if  $\delta_X \leq \frac{1}{2} - \frac{\alpha_X \bar{r}}{2}$  and  $\bar{r} \leq \frac{q}{c}$ .
3. Both voters and the executive are weakly better off with than without commitment if and only if  $\delta_X \leq \frac{1}{2} - \frac{\alpha_X \bar{r}}{2}$  and  $\frac{q}{c} \leq \bar{r} \leq \frac{1}{c}$ .

4. *With other parameter values, commitment has no impact on welfare.*

### 6.3 The model with elections

In this Appendix, we introduce a model with elections at the beginning. We maintain the assumption made in the basic model that the status quo policy is zero:  $p_0 = 0$ .

#### 6.3.1 Divided government as an unintended result

We now assume that citizens choose politicians for the executive and the legislative office at the beginning of the game. As before, and for the sake of simplicity, we assume that the legislature is composed of only one politician. The pool of candidates is composed of politicians with different policy biases:  $\delta_j \in \mathbb{R}, j \in \{X, L\}$ . At the election time, voters do not know the type of the candidates, so they have no basis to choose. This is of course a key assumption, since otherwise voters would choose unbiased politicians and would be able to avoid both political gridlock and the need of special powers. After elections and before the referendum, voters learn the type of the elected politicians.

The timing of the model is the same as in the basic model, save for the first stage which is substituted by the following three stages:

1. At the beginning of the game, Nature chooses:
  - (a) the status quo policy  $p_0 \in \{0, 1\}$ ; and
  - (b) the state of nature, using a random mechanism by which  $s = 1$  with probability  $q$ ;
2. Elections take place and voters choose two politicians, one to run the executive and the other one to run the legislature. At this time, voters ignore politicians type.
3. Nature plays again and reveals the type of the elected politicians.

In this framework, voters rather than Nature choose politicians. But as they have no basis to judge, there are no strategic considerations, and the election is totally random. Having a biased pro status quo legislature is thus one possible outcome.

#### 6.3.2 Divided government as a moderating device

We redefine the policy rule under CB as follows:

1.  $p = \alpha p_X + (1 - \alpha)p_X p_L; \quad \alpha \in [0, 1]$
2. *Executive chooses*  $r \in [0, \bar{r}]$  (7)
3. *Legislature chooses*  $r_L \in [0, r]; r_X \in [0, r - r_L]$

For the sake of simplicity, we continue assuming that politicians only have a discrete choice—to favor or to oppose reform—but we now allow for a continuous policy. The parameter  $\alpha$  captures the “moderating” effect of divided government under CB. If the legislature is conservative and the executive reformist, the policy outcome is a weighted average of these two conflicting positions. This is a stylized representation of the capacity of the legislature to negotiate some moderation of the reform. With this policy rule, CB can moderate policies only if the legislature is conservative and the executive is reformist. If both agencies take the same standing regarding reform, then the policy outcome is consensual and there is no moderation. Notice also that we have introduced an asymmetry in the sense that there is no moderation when there is discrepancy and it is the executive the agency that adopts the conservative standing. Our hypothesis is that the executive cannot be forced to implement a reform it does not like.

With  $\alpha = 1$ , there is no moderation and the executive rules. With  $\alpha = 0$ , there is no moderation either and, as in our basic model, the reform can only be implemented if both the executive and the legislature agree. Divided government can bring moderation of policies under CB only if  $\alpha \in (0, 1)$ .

We now assume that citizens receive information after the elections and before the referendum that allows them to refine their beliefs about the state of nature. This is a key assumption that makes it possible that citizens choose a conservative legislature before they receive this information and vote for SP afterward. Without this updating, SP are dominated by a strategy of choosing reformist politicians for both offices. For the sake of simplicity, we suppose that the information citizens receive is so good that they learn the true state of nature before the referendum.<sup>28</sup>

In this model politicians cannot commit to policies, and hence policies are defined after the referendum.

The timing is as follows:

1. At the beginning of the game, Nature chooses:
  - (a) the status quo policy  $p_0 \in \{0, 1\}$ ;
  - (b) the state of nature, using a random mechanism by which  $s = 1$  with probability  $q$  ;
2. Citizens vote a politician for the executive and another one for the legislature. At this time, they observe politicians type but not the state of nature.
3. Nature reveals the state of nature.
4. Referendum: voters choose the policy rule  $CB$  or  $SP$ , knowing  $s$  and  $p_0$ .
5. Politicians make a policy proposal  $p_j$ ,  $j \in \{X, L\}$ , knowing previous Nature’s moves, including the state of nature.

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<sup>28</sup>The essential assumption is that there is some refinement of beliefs. The extreme assumption that the state of nature is fully revealed is just a particularly simple example.

6. If in step 4 voters choose  $CB$ , then

(a)  $p = \alpha p_X + (1 - \alpha)p_X p_L$

(b) the executive first proposes  $r \in [0, \bar{r}]$ , and later

(c) the legislature chooses  $r_L \in [0, r]; r_X \in [0, r - r_L]$ .

7. If in step 4 voters choose  $SP$ , then  $p = p_X$ , and the executive chooses  $r_X \in [0, \bar{r}]$  and  $r_L \in [0, \bar{r} - r_X]$ .

8. The game ends and payoffs are computed.

We consider subgame perfect equilibria (SPE). We first present the propositions and their main intuitions, and relegate the proofs to the end of the Appendix. We present first equilibria in which the utility cost of rents is too high for voters to grant SP. One of these equilibria involves the choice of a divided government with a conservative legislature and a reformist executive. As in Alesina and Rosenthal (1996, 2000), citizens value divided government in this environment because of its moderating effect on policies: rather than having only the two extreme policies  $p = 0$  and  $p = 1$ , divided government generates an intermediate policy  $p = \alpha$ . We then analyze the equilibria in which the utility cost of rents is lower. There is an equilibrium with a conservative legislature and a reformist executive in which voters are now willing to grant SP. In this case, there is policy moderation also across states of nature. Let  $(R, C)$  stand for a government integrated by a reformist executive and a conservative legislature, and  $(C, C)$ ,  $(C, R)$  and  $(R, R)$  stand for governments integrated by two conservative politicians, a conservative executive and a reformist legislature and two reformist politicians, respectively.

**Proposition 7.** *Suppose  $(1 - \alpha)^2 \leq c\bar{r}$ . The following strategy profiles are subgame perfect equilibria of the model with moderating CB:*

1. *In the elections, voters choose*

(a)  $(C, R)$  or  $(C, C)$  if  $q \in [0, \frac{\alpha}{2}]$ ,

(b)  $(R, C)$  if  $q \in [\frac{\alpha}{2}, \frac{\alpha+1}{2}]$ , and

(c)  $(R, R)$  if  $q \in [\frac{\alpha+1}{2}, 1]$ .

*In the referendum, voters choose CB.*

2. *The executive always plays  $p_X = 1$  if it is reformist, and  $p_X = 0$  if it is conservative. It proposes  $r = 0$  if voters choose CB, and  $r_X = \bar{r}$  and  $r_L = 0$  if voters choose SP.*

3. *The legislature always plays  $p_X = 1$  if it is reformist, and  $p_X = 0$  if it is conservative. It proposes  $r_X = 0$  and  $r_L = r$  if voters choose CB.*

In the equilibrium that arises for intermediate values of  $q$ , citizens choose a conservative legislature and a reformist executive. Voters choose a divided government because their expected utility associated to the intermediate policy  $p = \alpha$  produced by this government is higher than the expected utility associated to the more extreme policies that would arise with any other government choice. Notice that not only the government is divided, but it is so in a specific way: the conservative politician is chosen for the legislature and the reformist one for the executive. This specific choice induces policy moderation in “normal times” —i.e. when CB are in place—. Because of high disutility of rents, SP are not used in this equilibrium.

For this voters strategy to be part of a SPE, the probability that  $s = 1$  has to be neither too high nor too low, i.e.  $q \in [\frac{\alpha}{2}, \frac{\alpha+1}{2}]$ . If the probability is lower, then voters prefer to have  $p = 0$  rather than  $p = \alpha$ , since they expect that  $s = 0$  most of the time. They obtain this result choosing a conservative executive. The converse is true if the probability of  $s = 1$  is sufficiently high. In this case, voters obtain  $p = 1$  choosing a unified reformist government.

**Proposition 8.** *Suppose  $(1 - \alpha)^2 > c\bar{r}$ . The following strategy profiles are subgame perfect equilibria of the model with moderating CB:*

1. *In the elections, voters choose*

- (a)  $(C, R)$  or  $(C, C)$  if  $q \in [0, \frac{\alpha^2}{1+\alpha^2-c\bar{r}}]$ ,
- (b)  $(R, C)$  if  $q \in [\frac{\alpha^2}{1+\alpha^2-c\bar{r}}, \frac{1-\alpha^2}{1-\alpha^2+c\bar{r}}]$ , and
- (c)  $(R, R)$  if  $q \in [\frac{1-\alpha^2}{1-\alpha^2+c\bar{r}}, 1]$ .

*In the referendum, voters choose SP after  $(R, C)$  if  $s = 1$ . In all other circumstances, voters choose CB.*

- 2. *The executive always plays  $p_X = 1$  if it is reformist, and  $p_X = 0$  if it is conservative. It proposes  $r = 0$  if voters choose CB, and  $r_X = \bar{r}$  and  $r_L = 0$  if voters choose SP.*
- 3. *The legislature always plays  $p_X = 1$  if it is reformist, and  $p_X = 0$  if it is conservative. It proposes  $r_X = 0$  and  $r_L = r$  if voters choose CB.*

As in Proposition 7, Proposition 8 identifies an equilibrium with a conservative legislature and a reformist executive if  $q$  is neither too high or too low, but now voters grant SP if  $s = 1$ .

The moderating effect of divided government is present in the equilibria identified in propositions 7 and 8, but the equilibrium in proposition 8 has an additional form of moderation in which SP play a key role. In order to highlight this second mechanism we “shut down” the mechanism highlighted in proposition 7 considering the special case in which  $\alpha = 0$ . In this case there is no moderation of policies in the sense of that proposition. Nevertheless, there is still policy moderation in that different policies

are chosen in different states of nature. In “normal times” —i.e. when no reform is needed and CB are in place—, the status quo policy is implemented. Only when “special times” arrive in which the reform is beneficial voters facilitate reform through SP.

Thanks to SP, divided government has an option value. Only if the legislature is conservative and the executive is reformist, can voters keep open the option of facilitating reform through SP until new information about the state of nature arrives. The cost of executing this option is the utility cost of rents.

*Proof of Propositions 7 and 8 .*

As in the basic model, we first solve the subgames that the executive and the legislature play after the referendum. Using this solution, we prove propositions 7 and 8.

*The continuation game after voters chose CB in the referendum.* Using backward induction we conclude, as in section 2.2.1, that the legislature in stage 6c chooses  $r_X = 0$  and  $r_L = r$ . Anticipating this outcome, in the stage 6b the executive chooses  $r = 0$ . Finally, in stage 5, a conservative politician proposes  $p_i = 0$  and a reformist one proposes  $p_i = 1$ , irrespective of whether he occupies the executive or the legislative office,  $i \in \{X, L\}$ . Policies are then determined according to the policy rule in equation 7.

*The continuation game after voters chose SP in the referendum.* The executive is now the last player to move and chooses  $r_X = \bar{r}$  and  $r_L = 0$ . In stage 5, the executive chooses  $p_i = 0$  if he is conservative and  $p_i = 1$  if he is reformist.

Table 1 presents the equilibrium outcomes of these subgames.

	CB	SP
(C,C)	$p = 0$ and $r_X = r_L = 0$	$p = 0$ and $r_X = \bar{r}, r_L = 0$
(C,R)	$p = 0$ and $r_X = r_L = 0$	$p = 0$ and $r_X = \bar{r}, r_L = 0$
(R,C)	$p = \alpha$ and $r_X = r_L = 0$	$p = 1$ and $r_X = \bar{r}, r_L = 0$
(R,R)	$p = 1$ and $r_X = r_L = 0$	$p = 1$ and $r_X = \bar{r}, r_L = 0$

Table 1: Outcomes of the subgames that begin after the referendum.

We now compute the expected utility of voters at the election time associated with each choice of government. Voters prefer CB over SP in the referendum if they chose (C,C), (C,R) or (R,R) in the elections. As table 1 shows, with these government configurations, the policy outcomes are the same under CB and SP, and SP involve rent extraction so voters obtain higher utility with CB than SP in

these branches of the game. Considering this choice, we compute voters expected utility at the election time as  $-q$  if they choose (C,C) or (C,R), and  $-(1-q)$  if they choose (R,R).

Consider now the case in which voters choose a conservative politician for the legislature and a reformist one for the executive (R,C). At the referendum time, voters prefer CB over SP if  $s = 0$ , as the policy will be closer to their bliss point and there will be no rent extraction with this choice. If instead  $s = 1$ , then voters choose CB if, and only if,  $(1-\alpha)^2 \leq c\bar{r}$ . Considering these choices, we compute voters expected utility at the election time if they choose (R,C) as  $-(1-q)\alpha^2 - q(1-\alpha)^2$  if  $(1-\alpha)^2 \leq c\bar{r}$ , and  $-(1-q)\alpha^2 - qc\bar{r}$  if  $(1-\alpha)^2 > c\bar{r}$ .

Having computed voters expected utilities at the election time, we now determine voters choice under all possible parameter values. To this end, we divide the parameter space in four regions:

1.  $q \leq \frac{1}{2}$  and  $(1-\alpha)^2 \leq c\bar{r}$ . The expected utility of (C,C) and (C,R) is  $-q$  and of (R,R) is  $-(1-q)$ . Thus (C,C) and (C,R) are preferred over (R,R) if  $q \leq \frac{1}{2}$ . In turn, voters choose (R,C) over (C,C) or (C,R) if:

$$-(1-q)\alpha^2 - q(1-\alpha)^2 \geq -q,$$

or equivalently if  $q \geq \frac{\alpha}{2}$ .

2.  $q \geq \frac{1}{2}$  and  $(1-\alpha)^2 \leq c\bar{r}$ . (R,R) is preferred over (C,C) and (C,R) if  $q \geq \frac{1}{2}$ , and voters prefer (R,C) over (R,R) if:

$$-(1-q)\alpha^2 - q(1-\alpha)^2 \geq -(1-q),$$

or equivalently if  $q \leq \frac{1+\alpha}{2}$ .

3.  $q \leq \frac{1}{2}$  and  $(1-\alpha)^2 \geq c\bar{r}$ . Voters prefer (R,C) over (C,C) or (C,R) (which are in turn preferred over (R,R)) if:

$$-(1-q)\alpha^2 - qc\bar{r} \geq -q,$$

or equivalently, if:

$$q \geq \frac{\alpha^2}{1 + \alpha^2 - c\bar{r}}.$$

Note that  $(1-\alpha)^2 \geq c\bar{r}$  implies that  $1 + \alpha^2 - c\bar{r} \geq 2\alpha \geq 0$ . In turn, this implies that

$$0 \leq \frac{\alpha^2}{1 + \alpha^2 - c\bar{r}} \leq \frac{\alpha}{2} \leq 1/2.$$

4.  $q \geq \frac{1}{2}$  and  $(1-\alpha)^2 \geq c\bar{r}$ . Voters prefer (R,C) over (R,R) (which is in turn preferred over (C,C) and (C,R)) if:

$$-(1-q)\alpha^2 - qc\bar{r} \geq -(1-q),$$

or equivalently, if:

$$q \leq \frac{1 - \alpha^2}{1 - \alpha^2 + c\bar{r}}.$$

□