Chapter 1
Introduction to Part I

1.1 A Metaphor?

One might reason that political offices function like a private labor market and that a political office-holder is the voters' employee. Every applicant for an open position advertises his ability to fill this position successfully. The prospective employer chooses the applicant that seems the most able and the best match, and after a predefined period, he assesses his employee's performance and either keeps him or has him fired. The details of employee's and employer's rights and duties are put on record in a contract.

Quite similarly, a political candidate proposes a work agenda, advertises his ability to implement it and if elected, is appointed office-holder for a certain period. During his term in office, he receives a "salary", i.e. a reward package consisting of money, perks, and honor, and is given the authority and resources to put the promised agenda into effect. Towards the end of his term, his performance is assessed, and like any employee who will be kept for good work and fired for poor performance, the office-holder will be reelected if he has performed well and deselected if he fails to do so—theoretically.

The relationship between voters and members of the legislature or of executive boards, however, differs from the relationship between employer and employee in some fundamental aspects. First of all, "equal voting rights" suggests that voting has to be the sole device used to appoint office-holders. Second, voters disagree about many policy issues, rendering it difficult to determine what a good performance is, i.e. which policy measures will improve social welfare. Different answers can be optimal when it comes to the question how much a society should redistribute, for example.

Another important issue is that several aspects, such as separation of powers in the state, parliamentary procedures and referenda, as well as the state's monopoly of power, the protection of basic rights and elementary functions of the state, determine and constrain an office-holder's activities: Performance does not solely depend on ability and effort.

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In addition, elections and reelections seem to be a rather crude device to select and to motivate office-holders, and they encounter several difficulties. Reelection, for instance, does not seem to be linked as directly to the office-holders' performance as one might think. An office-holder could be reelected simply because he is better-known than his challengers thanks to his first office-term, or he might benefit from favorable shocks that affect his jurisdiction. He might also be reelected because the voters do not expect his challengers to perform better and prefer to retain the office-holder, possibly hoping for a certain "learn-by-doing"-effect. Furthermore, an office-holder might pursue policies that are favorable to particular interest groups, which, in turn, might provide stronger support for his reelection bid.

Up to now, deselection seems to be the voters' sole weapon against lack of effort and ability, and this weapon cannot warrant optimal effort, let alone good performance—even if applied consistently.

The length of the office-term is another problem. One full term being much longer than an employee's trial period, a bad performer is costly, even if he is deselected after his first term. On the other hand, this office period can prove too short as well: Despite the fact that during his electoral campaign, the candidate promised to implement long-term projects, an office-holder might give priority to short-time results that will foster his reelection, and neglect those projects that take longer than one term.

Such complications might suggest that new incentive and selection devices cannot be used in democracy to mitigate performance problems. One might even argue that they are not necessary: Good performance and farsighted policy are among the candidates' campaign promises. Yet, many office-holders' actual performance denotes a shift in priorities after election—towards less socially desirable. The other way around, candidates make promises to pander to the public's opinion, whose fulfillment is not socially desirable in the long run. We still end up with the same basic question: How can we foster good performance in democracy?

1.2 Political Contract: Definition

What we need is a device that can complement elections and can be integrated in a democracy. One of our major ideas is that office-holders should be rewarded for promises kept and punished for promises broken. Then, the candidates should promise more realistically and, once elected, invest more effort into keeping their word. But how to link such promises to rewards and punishment? This is where the employee metaphor is helpful: Through a contract.

Yet, the employee metaphor can only start reflection, and our notion of contract must be adapted if we want to use it for political office-holders: Democracy requires new ways of contracting. In particular, a "political" contract would not be a contract of the usual type signed by two parties, but a declaration signed by the candidate and certified by an independent authority. We call these certified declarations "Political

Contracts".[1] They contain the performance a candidate will have to deliver if elected, together with the reward due if he fulfills these promises, and/or the corresponding punishment if he fails to do so. To certify the contract, to evaluate performance, and to award rewards and punishments, an "Independent Authority" is needed. One could imagine a newly-created institution or an already-existing authority being entrusted with this new set of tasks.[2]

Thus, Political Contracts differ from a contract of employment signed in every-day life.[3] A judicious combination of Political Contracts and elections is characterized by the following chronology:

1. Candidacy
   Campaign promises are tied into a Political Contract
   (Performance – Reward – Punishment)
   Certification – Publication
2. Election
3. First office-period
   (a) Implementation of campaign promises
   (b) Assessment of performance
   (c) Independent Authority declares whether the Political Contract was kept or not
   (d) Reward/punishment is declared due
   (e) Reward/punishment is implemented
4. Second Candidacy
5. Reelection/deselection

Note: *While both reward and punishment could take place at any given time after performance assessment, they have to be put on record at Stage (1). Stage (3d) only consists of a declaration by the Independent Authority, stating which of the two is due and will be awarded. The implementation date itself depends on the type of reward or punishment that was chosen for the Political Contract, as we will see in what follows.*

The candidates would not be forced to sign Political Contracts, but as such a contract enhances credibility, competing candidates are likely to resort to such contracts during electoral campaigns. Of course, Political Contracts only become effective if the candidate is elected.

[1] A more detailed survey of the current state of affairs on Political Contracts can be found in Gersbach (2012).

[2] In Germany, it could be the Federal President (see Gersbach and Schneider 2012b).

[3] As they are certifiable and enforceable, they cannot be compared to the theoretical "social contract" that free men contract with each other to establish civil society, as analyzed in Hobbes' *Leviathan*, for instance. A social contract can be implemented by a set of constitutional rules (see Aghion and Bolton 2003 and Gersbach 2009a, b).

Let us now address the main issues arising from this setting, and start with a crucial point: Whatever is settled in a Political Contract must comply with the fundamental rules of democracy.[4]

1.3 Does Any Campaign Promise Qualify as Contract Matter?

To qualify for inclusion in a Political Contract, a performance has to be definable and measurable with a sufficient degree of precision. Ideally, it consists of a single figure such as the GDP, the unemployment rate, a particular crime index, the level of CO_2 emissions or a debt level to be reached. If the outcome of a particular policy is measurable by social, macroeconomic or environmental indicators, it can be tied into a Political Contract. The contract must contain a precise description of the performance indicator to be used for evaluation. A neutral third party to be entrusted with the collection and verification of the relevant data is also necessary. This third party could either be appointed to verify all contracts that are offered in a particular election, or appointed from contract to contract, depending of the type of assessment needed, in which case its name and duties should be specified in the corresponding Political Contract.

There are cases in which a simple yes/no answer is possible when asking whether the performance was achieved. The building of a bridge, the abolishment of a law, or the raising of retirement age, for instance, do not require a specific performance index, as the completion of the task is evident.

Greater, more complex projects such as the reform of health care, for instance, might not qualify so easily for a Political Contract, or might require the implementation of alternative measuring procedures for performance assessment. One way to assess performance might be to divide the project into stages (sub-projects), and define in the Political Contract which sub-project is to be reached by a certain deadline. One could imagine a series of deadlines by which each stage of the project has to be completed. One might also restrict the measuring of a project outcome to those parts of the project that are precisely measurable, leaving the non-measurable parts out of the Political Contract.

Such necessary precision precludes certain parts of a candidate's agenda from being inserted into a Political Contract, namely rather "ideological" performances that escape every precise assessment, such as "more social justice". Hence, a number of vague, not-verifiable or even demagogic promises would not qualify for being put into a Political Contract—and would, as a rule, have less credibility. It would be a beneficial side-effect of Political Contracts that their introduction would separate campaign promises into verifiable, credible promises—the ones that can be included

[4] See Gersbach (2012).

in Political Contracts—and those vague, not measurable promises that cannot be part of a Political Contract, and thus tend to be less credible.[5]

Extension – Contracts Offered by Parties

Our main suggestion is to allow every candidate for executive or legislative office to sign Political Contracts, but the signatory does not necessarily have to be a person. A party could also offer a contract, such as a tax contract specifying a range of tax rates to which it will be committed if in government (see Gersbach and Schneider 2012a, b). One can also imagine that parties offer Political Contracts in which they define a list of partners with whom they are willing—or unwilling—to enter a government coalition. If one party has excluded another from its list, it cannot form a government coalition with it after elections. A more detailed assessment of the use of Political Contracts by parties is given in Gersbach (2012), and the particular variant of a Political Contract in which a party precludes another, or others, from any government coalition is analyzed in Gersbach et al. (2014).

1.4 Punishment and Rewards

To perform efficiently as incentives, rewards should please and punishments should hurt. Let us focus on wages, pensions, perks, and immaterial benefits that an office-holder is awarded in exchange for his work.

Punishment

- **Money, perks, and honor**

  Our first idea to foster performance is to tie it to the material goods the office-holder receives, be it money or perks. If an office-holder performs badly, one could reduce his wages, for instance. Gersbach (2003, 2004) outline how such a material punishment might be designed and whether Political Contracts really are offered by candidates during their campaigns. The Political Contract could tie the office-holder's salary to his performance, so that this salary could vary during the office-period. If the office-holder does not achieve the performance defined in his Political Contract, he will earn less. Depending on the kind of performance to be achieved—budget goals, debt levels, growth of GDP or project implementation, for example—, the wages can be adapted yearly. But also an adaption over several office-terms is imaginable, as well as wages divided into a basic, regularly-paid part and a performance-dependent part that is to be paid or refused after performance evaluation.

  One might also link the office-holder's performance to the pension he will receive after his term in office. This would allow to judge performance over a longer time

[5] See Gersbach (2012).

span, which, in turn, would foster the implementation of long-term projects. Ideally, one could take the entire time in office as a basis for performance-assessment (see Gersbach and Müller 2010 and Gersbach and Ponta 2017).

As for the perks and honor that are part of an office-holder's salary, it is not easy to draw the line between material and immaterial rewards. The right to use an official car driven by a chauffeur and fixed allowances are examples of material perks. If the car is of first-grade type, its use could be perceived as an honor or as a manifestation of power, a so-called "ego rent". This might be the case for all advantages an office-holder can make use of, from state airplanes to priority seating at sports events.

All these benefits might be used as punishment tools. By reducing the material reward, a simultaneous reduction of the immaterial reward is achieved automatically.

- **No second term – Term limitation – Higher bar for incumbents**

  An alternative way to punish office-holders is to make it more difficult to obtain all of the material and immaterial benefits of holding-office in future terms. This could be particularly powerful as in a variety of cases, money might not be very efficient as an incentive for good performance. The punishment for bad performance could be very simple:

  No right to second candidacy. One sanction for bad performance could be to repeal the right to candidacy for reelection. If a politician promises to renounce candidacy for a second term if he fails to reach a certain performance threshold, he has a powerful incentive to reach this same threshold. And as he would be the one who *offers* such a sanction, this renouncement would be voluntary and would not challenge every citizen's democratic right to candidacy.[6] This incentive is bound to be inefficient during a last term in office—be it because the constitution limits the number office-terms or because the office-holder knows he will not be a candidate anymore. Thus, one should find a replacement incentive for such particular last-term situations, by which office-holders would be more motivated to excel or even undertake socially desirable long-term projects that might be unpopular in the short-term.[7]

  Premature term ending. One might also imagine a premature ending of the office-term in case of bad performance. Yet, the legal implications are intricate, and such punishments are only imaginable for office-holders behaving like criminals or evidently neglecting the state's core interests.

  Higher bars for incumbents. A particular way to assess performance might be to use the vote-share that an office-holder receives on reelection day as an indicator. This vote-share can be used for a Political Contract, in much the same way one would use a pre-defined performance level. Instead of promising a certain performance,

[6]The chances and drawbacks of contracts tying reelection to a certain performance threshold are analyzed thoroughly in Gersbach and Liessem (2008a, b).

[7]For incentive schemes that can overcome this difficulty, see Gersbach and Müller (2010) and Gersbach and Ponta (2017).

the candidate can promise to work so well during his first term in office that his reelection vote-share will reach a certain percentage. In a traditional two-candidate race, the candidate who obtains 50% of the votes or more is elected. The reelection percentage should be above the one needed for first-term election. If the office-holder fails to work well enough and does not reach this pre-defined reelection threshold,[8] he will not take office for a second term, although his vote-share would have been sufficient in a first-term election. Such a threshold is offered by a candidate during his election campaign, and would be tied into a Political Contract.[9]

Such a higher vote-percentage—possibly making the incumbent's reelection more difficult than a candidate's first-term election—counterbalances the incumbency advantage of the office-holder. Be it because he is better known than his challenger, has access to more campaign funds and support of interest groups, or because he is simply perceived as a "safer bet" by the public, it is usually less difficult for an office-holder to be reelected than for his challenger to obtain office. Knowing this, the office-holder might be tempted to put less than the socially optimal amount of effort into his first-term policy and might be reelected even if his ability is below his challengers'. If a Political Contract stipulates that he has to obtain a higher vote-share for reelection than for election, the office-holder will have to invest more effort during his first term in office to earn the extra votes he needs, and the average effort of office-holders would improve. However, higher bars for incumbents may also cause the deselection of candidates having only average ability. Our latest research on this idea and an analysis of its social desirability are presented in Part I, Chaps. 3 and 4.

- **Loss of public funding or of parties' perks**

  Finally, any kind of benefit an office-holder or his party receives from the public treasury can be reduced—which makes it a tool suitable for Political Contract purposes. One could link the office-holder's performance to the public funds his party receives, and pause the payments for a certain time in case of bad performance. This may be particularly useful if Political Contracts are offered by an entire party.

Rewards

Let us now turn to rewards—the flip-side of punishments. We must emphasize that the importance of a particular reward may vary among candidates: A wealthy candidate might not desire higher wages nor suffer much from a salary cut. And candidates typically differ with regard to their intrinsically-desired mix of monetary and non-monetary benefits. This has to be kept in mind if such schemes are introduced.[10]

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[8] The terms "reelection vote-share" and "reelection threshold" are used synonymously for this scheme, the result being the same. A Political Contract that stipulates a certain pre-defined vote-share for reelection is called a "Vote-share Contract".

[9] Alternatively, the public could set higher reelection thresholds.

[10] See Gersbach (2012) for a detailed discussion on who should set the boundaries for material and immaterial rewards and punishments for office-holders.

- **Money, perks, and honor**

  A raise in salary or suitably-designed rewards—material or immaterial—may be used as incentives for good performance. One could make the payment of a certain percentage of the office-holder's salary dependent on the reaching of particular performance levels. If immaterial rewards are preferred, those politicians who have done particularly well in office could be awarded an honorific title such as "Father of the State", or they could be granted a seat in a particular "State Advisory Board" (see Gersbach 2012).

- **Longer term granted**

  One can imagine that the current office-term is prolonged in case of good performance. If the office-holder has fulfilled his Political Contract by the end of his term, he could remain in office for one more year, for example (see Gersbach 2012).

- **Rewards from the future – RSRs**

  Up to now, our examples dealt with candidates acting on behalf of current voters who are the beneficiaries of "their" office-holder's performance. If they are satisfied with these benefits, they will reelect him. Yet, this might prevent candidates from suggesting long-term policies that will only be beneficial to *future generations*, as they might not win elections with such an agenda. As they do want to be elected, they might only suggest policies beneficial to the *current* electorate.[11]
  To foster the implementation of policies that will benefit younger generations, special types of Political Contracts are needed, as an office-holder undertaking such policies will endanger his reelection. For such a case, a possible Political Contract would define a "Rejection-Support-Reward" (RSR), which would be awarded to this office-holder if he is deselected, but has received the majority of votes from the younger generation.
  As most office-holders want to be reelected, few are likely to implement policies that will threaten their reelection, so that they are unlikely to offer this particular type of Political Contract voluntarily. Thus, Political Contracts that should foster the implementation of projects detrimental to reelection would have to be designed by the public.[12] However, as the public itself may have little interest in introducing RSRs, special procedures allowing their delayed introduction might prove necessary.

Alternative Performance Assessment

As we have seen, performance is easily gauged if there exists some kind of measuring tool for it. A figure such as the percentage of unemployed workers cannot be manipulated easily at short-term notice—at least not if it has been defined precisely and applied consistently—, which makes it suitable for our purpose. If an office-holder has managed to achieve a pre-defined figure, he has fulfilled his Political Contract.

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[11] Of course, this does not apply to all circumstances. In particular, statesmen may be willing to undertake policies that are unpopular in the current electorate (see Gersbach 1999).

[12] See Gersbach and Kleinschmidt (2009) for details.

Yet, things might prove complex in many cases. Thus, to evaluate an office-holder's achievements, one might also use an information market to produce a "price"—a figure that can be incorporated into a Political Contract. A first analysis of this idea is outlined in Gersbach and Müller (2010), and our latest research findings on that subject are presented in Part I, Chap. 5.

1.5 Renegotiation – Negative Effects

Should Political Contracts Be Renegotiable?

Of course, circumstances can change in the course of an office-term, so that the enforcement of a contract can become unreasonable, illogical or even damaging to society. A goal that was within reach when the corresponding Political Contract was signed can become impossible to achieve due to unforeseen events. Changing circumstances might also render a goal undesirable, despite the fact that it was considered to be socially beneficial at contracting time. If national security is threatened, for instance, balancing the budget might lose priority.

In such cases, it is necessary to include the possibility to cancel, renegotiate or replace a Political Contract in the contract itself. All three amendments should be subject to a particular form a parliamentary approval such as a super-majority (see Gersbach 2012).

Can Political Contracts Be Counterproductive?

As is the case for most institutional devices, there might be circumstances under which particular Political Contracts may not improve welfare, or might even reduce it. If candidates can offer Political Contracts containing fixed salaries that compete with each other, it could happen that large ability differences allow high-ability candidates to obtain large rents, because the voters might prefer an able candidate, even if he will cost substantially more. As a consequence, competitive wage offers made by candidates can yield lower welfare than remunerations set by the public. Competition with wages may lead to higher costs for the voters, or to the election of less able candidates, if the voters prefer a "cheaper", less able office-holder. Our findings on competition for wages and office are presented in Part I, Chap. 6.

Competition with Political Contracts may also invite candidates to make binding promises just to be elected for one term. Such promises might be attractive for the electorate, but could prove difficult to fulfil, once in office. The office-holder might give up the realization of such promises and settle on one term in office.

1.6 Retrospect and New Developments

Despite possible drawbacks in particular circumstances, Political Contracts have the potential to mitigate some of the problems inherent to democracy. Beside a fresh look at democratic institutions and the willingness to allow for a certain experimentation period, the implementation of Political Contracts would require changes at the constitutional and legislative level, a careful assessment in which areas they might be implemented, and a thorough planning and monitoring of all processes connected. This was addressed in more detail in Gersbach (2012). Yet, our latest research shows that such a challenge is worth accepting. Using the basic structure of Political Contracts outlined above, we want to present our most recent research on that subject, after a brief look backwards, to where it all began.

The Start: Competition of Politicians for Incentive Contracts and Elections

In the late 1990s, we developed our basic ideas on Political Contracts. A first publication on the subject, was the chapter "Incentive contracts and elections for politicians and the down-up problem". Edited by Murat R. Sertel and Semih Koray (see Gersbach 2003), it was a contribution to *Advances in Economic Design* and included as Chap. 2 in *Designing Democracy*. Our early research on competition through incentive contracts followed. It was first published in *Public Choice* and included with minor amendments as Chap. 3 in *Designing Democracy* under the title "Short-termism and competition for incentive contracts" (see Gersbach 2004, 2005).

As this particular contribution sets the basis for all our research on democracy issues, we include the original article in this volume. The insights gained such a long time ago are still crucial for our current work: They fructified into a world of insights and we are still harvesting!

Vote-share Contracts Without Knowledge About Ability

Chapters 3 and 4 in Part I of this book were originally developed as companion papers. Both deal with higher vote-thresholds for incumbents, yet with a slight, but important, difference: The knowledge an office-holder has, or doesn't have, about his own ability when he offers a Political Contract containing a higher vote-share for reelection.

In Chap. 3, we will examine a setting in which a candidate has *no knowledge about his ability* at the time of his candidacy for office, and analyze a Political Contract that uses an incumbent's reelection vote-share to assess performance. We will use the terms *Vote-share Contract* and *vote-share thresholds* indiscriminately to denominate a contract that stipulates a certain vote-share to be attained for reelection.

Vote-share Thresholds with Some Knowledge About Ability

In the companion paper presented in Part I, Chap. 4, we will examine the same setting, yet with the candidates having *some knowledge about their own ability* before they offer a Political Contract containing a vote-threshold. As this private information is crucial for the candidate's accuracy when setting the reelection vote-threshold that is optimal for him—i.e., which ensures his reelection—, the comparison of our findings with those from the previous chapter will yield significant new results, which we present in Part I, Chap. 4.

Information Markets and Political Contracts

One of the most important issues with regard to Political Contracts is the assessment of performance. This assessment may be very simple if performance can be summarized in one figure or in a single event. If it cannot be measured and/or described with a certain degree of precision, alternative ways to assess output have to be found, sometimes tailored to the needs of a specific project or policy. An interesting new way to generate performance measures is the use of information markets. We will illustrate performance assessment methods in the context of long-term projects, where it might prove particularly difficult to measure performance, as these projects will be completed only long after the office-term in which they were started.

An information market that predicts the long-term performance of a policy might be used to produce information for a Political Contract. On such a market, an office-holder should reach a certain "price" to be reelected, which is serving as a performance indicator. The price he has to reach could be tied into a Political Contract, and an office-holder that fails to reach "his" pre-defined price—on average, over a certain time-span during his office-term—would lose the right to stand for reelection. We will examine the chances and drawbacks of Political Contracts that are based on such information market prices in Part I, Chap. 5.

Competition of Politicians for Wages and Office: Limits of Political Contracts

In electoral competition, the candidates might offer a Political Contract on their remuneration. At first sight, this seems a good way to save tax money. We will analyze a model in which two politicians compete for office and for wages, and show that surprisingly, competitive wage offers from the candidates can yield lower welfare than remunerations determined by the public. Part I, Chap. 6 will present our latest finding on these limitations and close the first part of this book.

1.7 Background

Our suggestion to establish a "Contractual Democracy" via Political Contracts originates from the firm conviction that better democracies are possible, and that scientists should play a key role in their development. Our current work stems from the observation that Political Contracts are not permitted in democracies.[13] Of course, government officials in the executive and legislative branch are accountable to the

[13]There is an important body of literature on incentive contracts for non-elected public authorities like central bankers, initiated by Walsh (1995a). The government imposes a penalty if it can verify that the central bank has not attempted to meet its target level. For the theory of the enforcement of such arrangements and the nature of penalties, see further Persson and Tabellini (1993), Walsh (1995b), Lockwood (1997), Svensson (1997), and Jensen (1997).

general public. The central manifestation is accountability of officials via elections or accountability to elected intermediaries.[14] Political Contracts would significantly enlarge the menu of manifestations how accountability of government officials can work. It is thus unclear why the exclusion of Political Contracts should be carved in stone—both from a scientific perspective and from the citizen's point of view.[15] We combine democratic decision-making with Political Contracts.

The perspective on democracy put forward in this book significantly differs from traditional political-economic, public-choice, and social-choice approaches. Nevertheless, the knowledge embodied in these areas was instrumental for the development of our ideas and models. The pioneer work of Arrow (1951), Black (1958), Downs (1957), Buchanan and Tullock (1962), Sen (1970), Olson (1965), and Niskanen (1971), together with a large body of literature surveyed in leading textbooks such as Müller (1989), Bernholz and Breyer (1993/94), Drazen (2000), and Persson and Tabellini (2000) is the groundwork on which our research was built. Furthermore, the work of Fleurbaey and Maniquet (2011), as well as the theory of private complete and incomplete contracts[16] (see Hart 1995 and Bolton and Dewatripont 2005) have helped to look beyond utilitarian considerations and to incorporate fairness, equity, and power in the discussion on Political Contracts.

Finally, the suggestions put forward in the first part of this book aim at improving the functioning of democracy. We do not address the appropriate boundaries of collective decision-making and their relation with individual liberties. This set of issues is an enduring theme of democracy research (see Buchanan 1975, Hayek 2002, Samet and Schmeidler 2003 and the assessments by Plattner 1998, for instance). Political Contracts may well help craft new and more efficient boundaries between individual liberties and democracy.

[14]There is a voluminous conceptual (and even larger empirical) literature on the role of electoral accountability that can be traced back to Downs (1957) and the classic work of Barro (1973) and Ferejohn (1986) on how elections may punish poor performance of officials. Theoretical work that identifies the role of elections as a screening device for officials has been triggered by Banks and Sundaram (1993), Samuelson and Fearon (1999). A survey on the potential and limits of electoral accountability can be found in Asworth (2012). The role of finite versus infinite horizons for accountability is surveyed in Duggan and Martinelli (2015). Accountability through elected intermediaries is developed in Vlaicu and Whalley (2015).

[15]Historically, contracts were used to limit the power of rulers. In the Middle Ages, specific contracts for rulers were a step for the development of constitutions or a mean to commit them to pursuing certain policies (see, e.g. Kleinheyer 1968, Vierhaus 1977, Pozza 1997 and Lottes 2000). Moreover, in ancient Athens, the officials were liable with their personal funds. In some cases, officials were even executed if the citizens' assembly was not satisfied with their performance (see, e.g., Bleicken 1991).

[16]With incomplete contracts, allocation of residual control rights—i.e. power—is central. This was examined, e.g., by Persson et al. (1997) and Persson and Tabellini (2000) to rationalize the separation of powers and of the checks and balances of various branches of government. We take an allocation of power as given and examine how Political Contracts can help mitigate abuse of power, and can foster the alignment of the politicians' incentives with the voters' interests.

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