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Direct Democracy and the Stability of State Policy

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Governments change policies. One reason is that the preferences of voters or of leaders change. But policy may also change because democratic institutions make for instability: even with unchanged preferences, different winning coalitions will form, causing instability of policy. Intuitively, it would seem that the initiative, which lets the electorate bypass their elected representatives, would increase responsiveness to public opinion, and thus reduce stability. However, some social choice theoretic reasons (to be outlined below), predict that the initiatives would increase stability. That is, initiatives may act as “veto points” disrupting logrolling coalitions, and thus leading to stability of policy. This chapter empirically tests these two competing hypotheses, using expenditure data from US States from 1980 through 2002.

How the initiative may generate instability

The initiative process allows the public to bypass unresponsive politicians. If the initiative increases responsiveness to changes in public opinion, then we would expect its presence to make policy less stable. For example, in Italy in the 1970s divorce and abortion laws were liberalized by substantial majorities in initiative, at a time when these measures would have certainly been filibustered to death by Christian Democratic representatives in the regular parliamentary process (or even kept off the agenda altogether).

The initiative may overcome another source of stability--- incumbents want it. A special characteristic of an incumbent is that he won. The conditions that got him elected in the previous elections are therefore also likely to help him in the next election. A change in policy, say one that redistributes income, or that changes the major concerns of the public, may therefore lead to a loss of political support. Voters on an initiative need not share the incumbent’s preference for the status quo.

The initiative may especially reduce stability when the legislature has features which make it prone to gridlock. Among these factors are

supermajoritarian decision rules; rules which allow filibusters; the regulation of behavior by party leaders (Kiewiet and McCubbins (1991); the executive veto and the presence of two legislative houses, which requires agreement among all to change policy (Hammond and Miller (1987)); and expectations by the current majority that by not reversing policy it could induce a future majority to maintain policy (Bernholz (1978)).

How the initiative may generate stability

Some features of politics may, however, lead to instability when policy is set by the legislature. In particular, theoretical work shows that in the presence of multiple issues, an agenda setter can package a set of policies that a majority of legislators will prefer over any given status quo. The generality of the problem was discovered by McKelvey (1976), and named "chaos." Other important works include Black 1948, Black and Newing 1951, Plott 1967, McKelvey 1976, and Schofield 1978, who show that, except under extremely restrictive conditions, whatever is the status quo, a politician can find another bundle of policies that the majority prefers to the current bundle. Riker (1982) goes so far as to argue that politicians strategically exploiting this instability is the primary driving force of politics. Though Riker exaggerates the degree of instability inherent in majority rule (see Miller (1980) among others), it is clear that change in public opinion is not a necessary condition for policy instability.

The problem does not, however, generally arise if the alternatives that voters consider lie along a single dimension. Direct democracy often requires voters to vote on a proposal that would change the status quo on only one issue, and may therefore lead to greater stability of policy than would occur when legislatures alone determine policy: when initiatives force each policy dimension to be treated as a separate decision, policy is pulled to the median voter's position on each dimension, frustrating the manipulative ambitions of political élites. Thus, Tsebelis (2002) argues that initiatives form an extra veto point, and therefore increase policy stability.

This, of course holds if initiatives and referenda address only one issue. This is a constitutional requirement in some jurisdictions, such as California. But the restriction to one issue can arise for additional reasons. Voters may get confused by a complicated referendum, fearing that what they don't understand will hurt them. So for a referendum to succeed at the polls, it may need to focus on one issue. Moreover, it may be more difficult for organizers of a referendum to logroll and adopt a complicated policy than it is for legislators (who do

see each other all the time). Furthermore, the preference of a majority of the population may change infrequently, compared to more frequent change in the preferences of a majority of the legislature: in the legislature, the majority can change if the majority of voters in one district changes while the majority in the state does not. Direct democracy will then generate the stability of policy.

We note that if different voters or representatives put different weights on different issue dimensions, then the initiative can have strongly counter-majoritarian effects (Anscombe 1976, Lacy and Peterson 2001, Saari and Sieberg 2001): the potential for using the initiative can disrupt the construction of logrolling coalitions. It may be possible for various groups to trade their support on an issue they care little about for support on the issue that is most important to them, and for the resulting trades to produce an outcome preferable to all. The ability to use the initiative, however, undermines such deals, as an initiative will pull the outcome back to the position of the median voter *on each issue*. The initiative then frustrates the ability to construct multidimensional coalitions to change the status quo, and so increases stability. Linder (1998) argues that this indeed holds in Switzerland, and that the initiative has typically reinforced the stability of policy. Indeed he explains the long (until 1972) Swiss denial of suffrage to women in terms of direct democracy: in other countries, female suffrage could be introduced as part of a broader political deal, whereas in Switzerland it needed to win approval from a majority of (male) voters on its own.

We thus have two plausible stories about the effect of direct democracy on political stability, producing opposite predictions. After reviewing literature, we turn to testing these theories.

Literature

A starting point for "chaos" theorems is McKelvey (1976) who showed that, in general, any set of positions can be defeated by a majority vote, and, furthermore, that any set of positions can be reached by a sequence of majority votes starting from any other position.

An important implication of the chaos theorems is that some institutions can force political issues into a one-dimensional space (Riker (1982), Shepsle (1979), Shepsle and Weingast (1981)). Thus, in the U.S. Congress, germaneness rules reduce the policy space to a single dimension, thereby limiting post-committee cycling between different policy packages and generating a structure-induced stable equilibrium.

Several papers argue that policy will be more stable under proportional representation than under plurality voting (where a small shift in the preferences in a few districts can drastically change the majority in the legislature); see in particular Morelli and Tertilt (2000). Houser and Freeman (1988) indeed find that the variability of labor taxes is higher in the United Kingdom (which has plurality voting) than in Germany (which has proportional voting). Grilli et al. (1991) find that the countries with the most stable governments use proportional representation.

A different approach to studying the stability of policy considers veto players: individuals or institutions whose agreement is required for a change of the status quo. The basic prediction of the veto-player theory is that when the number of veto players increases and their ideological distances increase, policy stability also increases (Tsebelis 1995, 1999, 2002).

Though both policy stability and government budgets have been analyzed in the literature, few papers discuss both. Bawn (1999) studies specific items in the budget of the Federal Republic of Germany from 1961 to 1989, finding that budget allocations varied with the identity of the parties in the coalition government. König and Troger (2001) essentially replicate Bawn's findings over a longer period, and use the estimated preferences of the different parties.

Our paper builds on Tsebelis and Chang (2004). They consider the change in budget allocations in 19 OECD countries in the years 1973-1995, finding support for two hypotheses: parties located farther from each other in a multidimensional space cannot modify the status quo as significantly as a coalition with less diversified parties, and that the farther is the status quo from the preferences of the veto players, the greater the possible departure from the status quo.

Method

Our study will examine budget allocations across different states in the United States. Like Tsebelis and Chang (2004), we view a budget allocation as a vector in an n -dimensional Euclidean issue space. (Unlike Tsebelis and Chang we use the absolute value of spending on each item as a proportion of state personal income, rather than the proportion of state spending allocated to each item.) It consists of a set of expenditures allocated to different budget categories: (a_1, a_2, \dots, a_n) . Each year has a different budget allocation, so the above sequence should be indexed by the time it was selected. The difference between two budgets can be represented by the distance between the points that represent them in the n -dimensional

Euclidean space. The dependent variable, the change in the budget allocations, is $[(a_{1,t}-a_{1,t+1})^2 + (a_{2,t}-a_{2,t+1})^2 + \dots]^{1/2}$.

We also calculated the mean deviation of the spending vector. This summarizes the typical variation of the vector from a central tendency, as opposed to year by year variation. This is given by $[(a_{1,t}-\mu_1)^2 + (a_{2,t}-\mu_2)^2 + \dots]^{1/2}$, where μ_i is the mean spending by the state on policy category i .

For budget allocations we look at the fifty states over the years 1980-2002. The budget items we consider are those listed in the *Statistical Abstract of the United States*, namely spending on education, highways, public welfare, and health (including hospitals), and other expenditure. We divided all values by state personal income in that year and state. Spending in these five categories defines a vector. The dependent variable is the change in each state from year to year in this vector, as defined by the Euclidean distance between the vectors in each state for each pair of years.

We regress our measure of policy instability against variables measuring institutional features of state government as well as other control variables. We use a dummy variable for the presence of a popular initiative process (whether statutory or constitutional). We also include several dummy variables to capture the effects of other institutional features that may affect stability; these are drawn from Grooters and Eckl (1998). One institutional feature is a supermajoritarian legislative process, which may increase stability by making it harder to pass legislation. The presence of a line-item veto would also be expected to increase stability, by increasing the veto power of the governor, and making it possible for the governor to undermine logrolling deals. Lastly, the presence of a biennial budget process would be expected to reduce instability.

Patterns of state expenditure, however, are not simply the result of processes with the states. The states are, after all, part of the United States of America, and their spending is likely to be conditioned by the federal government. Therefore we include the per capita intergovernmental income 2002 of each state as a control variable. We also included state population as a control variable. We would expect small states to be more liable to exhibit policy instability, because small demographic changes may change median policy preferences.

Our independent variables are:

Fed. Transfers: Per capita intergovernmental revenue of state in 2002 (in thousands of dollars)

Population: State population in 2002

Super Majority: Dummy variable equal to 1 (and 0 otherwise) for a states with a super majority requirement for passing the budget (Alabama, Arkansas, California and Rhode Island, plus Alaska, Connecticut, Hawaii, Maine, Massachusetts and Nebraska, which have super majoritarian requirement in some circumstances)

Line Item Veto: Dummy variable for a state which grants the governor a line item veto

Biennial Budget: Dummy variable for a state which has a biennial budget process

Initiative: Dummy variable for a state which has a popular initiative process

Results

Table 1 lists the results of the regression of Euclidean distance of the annual change in spending.

Table 1:

Dependent variable: Euclidean distance of change in spending (all states)

	Estimate	Std. Error	t-value	Pr(> t)
(Intercept)	-7.18e-04	1.29e-03	-0.56	0.58
Fed. Transfers	3.70e-03	7.91e-04	4.67	2.92e-05***
Population	-8.56e-08	4.54e-08	-1.88	0.07
SuperMajority	-1.49e-04	7.10e-04	-0.21	0.83
Line Item Veto	8.16e-04	7.91e-04	1.03	0.31
Biennial Budget	7.63e-04	5.80e-04	1.32	0.20
Initiative	2.84e-04	5.73e-04	0.50	0.62

Residual standard error: 0.001935 on 43 degrees of freedom

Multiple R-Squared: 0.4405, Adjusted R-squared: 0.3625

F-statistic: 5.643 on 6 and 43 DF, p-value: 0.0002168

We see that the only highly significant variable is Federal Transfers: states which receive more federal money show greater volatility in their spending patterns than do states which receive little aid. This is

consistent with the hypothesis that much of the instability we observe arises not from processes within the state, but from national policy. Population is significant at the 6 percent level: small states show higher volatility than do larger states. None of the institutional factors, such as the initiative, has any statistically significant effect.

We can see from the raw data that Alaska is an outlier: it receives far more federal money per capita than other states. Since federal grants are so important, Alaska might be driving the results. We therefore repeat the analysis, but without Alaska. Table 2 shows the results.

Table 2:

Dependent variable: Euclidean distance of change in spending (excluding Alaska)

	Estimate	Std. Error	t-value	Pr(> t)
(Intercept)	5.25e-04	1.26e-03	0.42	0.68
Fed. Transfers	2.62e-03	8.11e-04	3.23	0.00**
Population	-7.97e-08	4.18e-08	-1.91	0.06
SuperMajority	-6.76e-04	6.76e-04	-1.00	0.32
Line Item Veto	8.48e-04	7.27e-04	1.17	0.25
Biennial	1.00e-03	5.38e-04	1.86	0.07
Initiative	1.17e-04	5.29e-04	0.22	0.83

Residual standard error: 0.001778 on 42 degrees of freedom
 Multiple R-Squared: 0.3501, Adjusted R-squared: 0.2572
 F-statistic: 3.77 on 6 and 42 DF, p-value: 0.00431

The pattern of results is the same: Federal Transfers continues to be significant, and small states show more volatility. None of the institutional variables is significant at the 5 percent level, but the data show that at the 6 percent significance level, states with biennial budgets are more volatile.

To check for robustness, we ran the same regression with mean deviation as the dependent variable. The results are similar to those reported above. Here again, Federal Transfers is the most significant explanatory variable, followed by population. The supermajority variable is significant to the 10% level, but this appears to result from the outlying case of Alaska. When Alaska is excluded, supermajoritarianism is no longer significant.

Table 3: Mean deviation of spending vector

Coefficients:

	Estimate	Std. Error	t value	Pr(> t)
(Intercept)	-2.280e-04	1.514e-03	-0.151	0.8810
Fed. transfers	7.014e-03	9.271e-04	7.566	1.97e-09 ***
Population	-9.968e-08	5.327e-08	-1.871	0.0681 .
SuperMajority	-1.408e-03	8.328e-04	1.691	0.0981 .
Line Item Veto	8.014e-04	9.275e-04	0.864	0.3924
Biennial	4.328e-04	6.796e-04	0.637	0.5276
Initiative	1.211e-05	6.713e-04	0.018	0.9857

Significance codes: 0 '***' 0.001 '**' 0.01 '*' 0.05 '.' 0.1 ' ' 1

Residual standard error: 0.002268 on 43 degrees of freedom
 Multiple R-Squared: 0.6474, Adjusted R-squared: 0.5982
 F-statistic: 13.16 on 6 and 43 DF, p-value: 2.144e-08

Table 4: Mean deviation of spending vector (Alaska excluded)

Coefficients:

	Estimate	Std. Error	t value	Pr(> t)
(Intercept)	2.011e-03	1.243e-03	1.618	0.1131
Fed. Transfers	5.077e-03	8.013e-04	6.336	1.30e-07 ***
Population	-8.901e-08	4.131e-08	-2.155	0.0370 *
SuperMajority	4.603e-04	6.681e-04	0.689	0.4947
Line Item Veto	8.608e-04	7.186e-04	1.198	0.2376
Biennial	8.627e-04	5.323e-04	1.621	0.1126
Initiative	-2.893e-04	5.229e-04	-0.553	0.5831

Significance codes: 0 '***' 0.001 '**' 0.01 '*' 0.05 '.' 0.1 ' ' 1

Residual standard error: 0.001757 on 42 degrees of freedom
 Multiple R-Squared: 0.5745, Adjusted R-squared: 0.5138
 F-statistic: 9.453 on 6 and 42 DF, p-value: 1.435e-06

Thus we find evidence for neither theory about the effect of the initiative on stability. The presence of the initiative does not appear to be significantly associated with either increased or decreased policy stability. Instead policy stability seems to depend far more on intergovernmental transfers from the federal government, and to a lesser degree, state population.

Tax and Expenditure Levels

So far we discussed changes in spending, finding few effects. As a test of robustness, we ask whether our variables can explain any important features of government. We first look at the level of taxes. We are particularly interested to see whether the introduction of Federal Transfers as a control variable has any effect. Table 5 gives the results for all states; Table 6 gives results with Alaska excluded. Federal transfers do not significantly affect tax levels. The effects of the initiative and of supermajoritarianism are of similar magnitude but work in opposite directions: the initiative is associated with lower levels of taxation, and supermajoritarianism with higher levels. Both supermajoritarianism and the initiative are significant to the 10% level when Alaska is excluded, but supermajoritarianism just fails to make the 10% level with the entire sample. We note, however, that the R^2 statistic for both these regressions is low, and the magnitude of the effect of supermajoritarianism and the initiative is modest (about \$200 per head). These variables explain little of the variation in tax levels.

Table 5

Dependent variable: Taxes per capita in 2002

	Estimate	Std. Error	t-value	Pr(> t)
(Intercept)	1774	239	7.39	3.46e-09***
Fed. Transfers	78	146	0.54	0.59
Population	1.63e-03	0.01	0.19	0.85
SuperMajority	207	131	1.57	0.12
Line item veto	-2.32	147	-0.02	0.98
Biennial	101	107	0.94	0.35
Initiative	-201	106	-1.89	0.07

Residual standard error: 359.3 on 43 degrees of freedom

Multiple R-Squared: 0.1337, Adjusted R-squared: 0.01283

F-statistic: 1.106 on 6 and 43 DF, p-value: 0.3746

Table 6

Dependent variable: Taxes per capita in 2002 (Alaska excluded)

Coefficients:

	Estimate	Std. Error	t value	Pr(> t)	
(Intercept)	1.697e+03	2.547e+02	6.664	4.41e-08	***
Fed. transfers	1.451e+02	1.642e+02	0.884	0.3818	
Population	1.270e-03	8.465e-03	0.150	0.8815	
SuperMajority	2.397e+02	1.369e+02	1.751	0.0872	.
Line item veto	-4.353e+00	1.473e+02	-0.030	0.9766	
Biennial	8.626e+01	1.091e+02	0.791	0.4335	
Initiative	-1.906e+02	1.072e+02	-1.779	0.0825	.

Significance codes: 0 '***' 0.001 '**' 0.01 '*' 0.05 '.'
0.1 ' ' 1

Residual standard error: 360.1 on 42 degrees of freedom
Multiple R-Squared: 0.1467, Adjusted R-squared: 0.02478
F-statistic: 1.203 on 6 and 42 DF, p-value: 0.3236

When we consider the level of state expenditure, we find supermajoritarianism associated with somewhat greater expenditure and the initiative with somewhat lower levels. However, Federal Transfers is by far the strongest predictor. Tables 7 and 8 report these results with and without the case of Alaska. With Alaska included, the effect of the initiative is insignificant, whereas supermajoritarianism is significant at the 2% level. However, when Alaska is excluded, the initiative is significant at the 10% level, whereas supermajoritarianism only makes the 13% level. The coefficient on SuperMajority is still slightly higher than that of the initiative (supermajoritarianism is associated with an increase in spending per head of \$390, whereas the initiative is associated with a decrease of \$340). Both effects, however, are much smaller than the effect of federal transfers. Increasing transfers by \$1,000 increases spending by \$1450. It is notable that this effect is greater than one-to-one. That is, federal transfers lead states to spend more money from other sources. This may be the result of federal matching funds, which reduce the marginal cost of state spending.

Table 7:
Dependent variable: Spending per capita

	Estimate	Std. Error	t-value	Pr(> t)
(Intercept)	1565	622	2.52	0.01*
Fed. transfers	2317	318	6.09	2.71e-07***
Population	0	0	-0.11	0.92
SuperMajority	816	342	2.39	0.02*
Line item veto	191	381	0.50	0.62
Biennial	-75	279	-0.27	-0.79
Initiative	-205	276	-0.74	0.46

Significance codes: 0 '***' 0.001 '**' 0.01 '*' 0.05 '.'
0.1 ' ' 1

Residual standard error: 931.1 on 43 degrees of freedom
Multiple R-Squared: 0.5364, Adjusted R-squared: 0.4718
F-statistic: 8.294 on 6 and 43 DF, p-value: 5.441e-06

Table 8:
Dependent variable: Spending per capita (Alaska excluded)

Coefficients:

	Estimate	Std. Error	t-value	Pr(> t)
(Intercept)	2.571e+03	4.735e+02	5.430	2.61e-06 ***
Fed. Transfers	1.448e+03	3.053e+02	4.742	2.45e-05 ***
Population	2.468e-03	1.574e-02	0.157	0.8761
SuperMajority	3.901e+02	2.546e+02	1.532	0.1329
Line item veto	2.175e+02	2.738e+02	0.794	0.4315
Biennial	1.185e+02	2.028e+02	0.584	0.5623
Initiative	-3.401e+02	1.992e+02	-1.707	0.0952 .

Significance codes: 0 '***' 0.001 '**' 0.01 '*' 0.05 '.'
0.1 ' ' 1

Residual standard error: 669.4 on 42 degrees of freedom
Multiple R-Squared: 0.4075, Adjusted R-squared: 0.3228
F-statistic: 4.814 on 6 and 42 DF, p-value: 0.0008075

It is interesting that a supermajoritarian budget process is associated with higher taxation and spending. The argument often made for a super majority rule is that it makes it harder for legislators to raise taxes and spending. At least when it is applied to the entire budget process, this effect is absent. This should not be surprising. If it is necessary to get a 2/3 vote to pass a budget, a broader logroll is required than with a simple majority vote. A supermajoritarian rule empowers veto-players who hold out for concessions, which may often come in the form of costly side-payment projects.

Conclusion

We considered two alternative theories concerning the effects of the initiative process on policy stability, as measured by state spending patterns. The first theory suggests that states with the initiative will be less stable than states without, because the initiative makes policy more responsive to public opinion, and thus changes in public opinion get directly translated into changes in policy, bypassing (possibly obstructionist) party élites. The other theory suggests that states with the initiative will be more stable in terms of policy. The initiative works as a form of veto point, forcing policy to the position of the median voter on each dimension, and preventing the construction of logrolling coalitions that can challenge the status quo. We find support for neither of these theories. States with the initiative do not seem to have either more or less policy stability than states without it. Interestingly, other institutional features, such as a supermajoritarian budget process and the line-item veto, also appear to have no effect on policy stability. The variable with the strongest explanatory power is the per capita transfer from the federal government.

The importance of federal transfers indicates that state governments are not sovereign nations; their behavior cannot be explained only by factors internal to the state. This leads to a degree of skepticism when using the states as a natural experiment to assess the effect of institutional variables. Many programs are mandated at the national level. It appears that the effect of the federal government on policy stability is far greater than that of state level institutions.

We do, however, find that state level institutions do affect the aggregate level of taxes and expenditure. The presence of the initiative leads to lower taxes and expenditure (replicating Matsusaka 2004) whereas a supermajoritarian budget process leads to higher taxes and spending. These effects, however, are relatively modest, amounting to a couple of hundred dollars per head per year. We find that the strongest predictor of state expenditure is once again the level of federal transfers.

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