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Abstract

We initiate examination of the *political* boundaries of the firm by exploring the phenomenon of "businessman candidates": business owners and managers who bypass conventional means of political influence to run for public office themselves. We argue that in-house production of political influence will be more likely in institutional environments where candidates find it difficult to make binding campaign promises. When campaign promises are binding, then a businessman may always pay a professional politician to run on the platform that political competition would otherwise compel the businessman to adopt. In contrast, when commitment to a campaign platform is impossible, then candidate identity matters for the policies that will be adopted *ex post*, implying that a businessman may choose to run for office if the stakes are sufficiently large. We illustrate our arguments through discussion of gubernatorial elections in postcommunist Russia, where businessmen frequently run for public office, institutions to encourage elected officials to keep their campaign promises are weak, and competition for rents is intense.

Keywords: Businessman candidates, elections, citizen candidates, institutions, political economy

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1 Introduction

In politics as in commerce, firms face a "make or buy" decision. Influence can be "bought" through the provision of campaign finance to favored candidates during election campaigns, or the application of lobbying power when dealing with elected politicians.[1] Alternatively, businessmen may "make" their own influence by running for public office themselves.[2] This paper focuses on the latter phenomenon.

"Businessman candidates" first caught our eye in postcommunist Russia, where owners or managers of large businesses have in recent years frequently run for public office. We present some evidence below of the prevalence of this influence strategy in Russia. However, there are numerous examples of similar candidacies in other political-economic contexts. Various authors (e.g., Dahl, 1961; Bradley and Zald, 1965; Pessen, 1972; Kipp III, 1977) have noted that 19th-century urban mayors and aldermen in the U.S. were disproportionately drawn from the business elite, while Crandall (1950) discusses the frequent direct involvement of 19th-century U.S. railroad presidents in politics. (On the latter point, recall that Leland Stanford served as governor of California and U.S. Senator contemporaneously with his tenure as president of Central Pacific Railroad.) Sheehan (1968) reports that during the 1870s and 1880s businessmen were increasingly drawn into German politics. In Thailand, "tycoons" dominated party politics in the 1980s (Laothamatas, 1988), while in various societies estate owners have populated more-or-less democratically elected parliaments (see, e.g., Zeitlin, Neuman and Ratcliff (1976) on early 20th-century Chile). Finally, in Ukraine (a country which shares a number of institutional characteristics with Russia), large business owners and managers have been elected to parliament and mayoral office.[3]

[1] For a review and synthesis of the literature on special-interest politics in established democracies, see Grossman and Helpman (2001).

[2] In this paper, we use the non-gender-neutral term "businessman" to refer to businessmen and businesswomen. We do so a) because we find the more neutral term "businessperson" cumbersome, and b) because in our judgement the phenomenon we describe in this paper has historically involved businessmen rather than businesswomen. On the latter point, this judgement is certainly correct for contemporary Russia, a case we examine in detail, and seems to be so for the other political contexts we survey below. We personally look forward to increased participation by women in business and politics in Russia and elsewhere, if not necessarily to increased participation by businessmen and businesswomen in politics.

[3] See, e.g., "Banker Wins Ukrainian By-Election," Ukrainian Television First Channel (BBC Monitoring), June 9, 2003; "Ukrainian Paper Profiles New Lviv Mayor," *Ukrayina Moloda* (BBC Monitoring), April 4, 2003; or "Kyiv Developer Eyes Rada, Council Seats," *Kyiv Post*, March 28, 2002. The last story profiles an attempt by a Kyiv real estate developer to capture not only a parliamentary seat through his own candidacy, but up to 30 seats in the Kyiv city council through the candidacies of employees of his real estate firm.

What many of these examples share is an environment that can be thought of as "weakly institutionalized" in the following respect: Politicians in immature democracies may be especially tempted to renege on campaign promises, as institutional mechanisms such as political parties which would otherwise discourage opportunistic behavior by their members (Alesina and Spear, 1988; Cox and McCubbins, 1994; Aldrich, 1995) are underdeveloped.[4] Consequently, elections do not serve the disciplining role that they do in established democracies, where politicians are motivated to appeal to the center by making binding campaign promises. Instead, politics is a battle of personalities, where voters anticipate post-electoral behavior based on *who* a candidate is rather than *what* he has promised.

As a consequence, businessmen may be more inclined to enter the electoral arena when commitment power is lacking. Conditional on being able to win, businessmen can implement more favorable policies and save lobbying costs by obtaining political power directly. In contrast, when campaign promises are binding, policy will more or less reflect the preferences of the median voter regardless of who is running. In such an environment, it will often be cheaper for a businessman to finance the campaign of a professional politician than to run himself. (Implicit in this discussion is the assumption that businessmen will still have an incentive to favor their businesses once in office. While this may not hold where laws exist and are enforced requiring divestiture of assets by office holders, it seems to be true in many of the weakly institutionalized environments where businessman candidates are most common.)

Our theory bears a strong resemblance to the literature on "boundaries of the firm," where the choice between in-house production and purchase from an outside supplier has efficiency consequences when contracts are incomplete (e.g., Coase, 1937; Williamson, 1975, 1985; Klein, Crawford and Alchian, 1978; Grossman and Hart, 1986; Hart and Moore, 1990). But in our case it is a contract with an *outside* party – the voters – that matters. One consequence of this difference is that the outcome when commitment is possible is not necessarily jointly efficient from the point of view of the businessman and professional politicians. Candidates may prefer the outcome where no one has committed to any policy, as not committing preserves the opportunity to reap gains from trade when policy is made after the election. Nonetheless, when a contract with the electorate

[4]Our paper follows Acemoglu, Robinson and Verdier (2003) in exploring the political economics of environments with very weak institutions.

is binding, candidates have no choice but to appeal to the median voter.

In modeling the endogenous participation of candidates, our paper builds on the "citizen-candidate" literature of Osborne and Slivinski (1996) and Besley and Coate (1997). As in that literature, citizens (here, businessmen) may run for public office because of the inability of professional politicians to make binding campaign promises. Our paper expands upon this work by showing how the entry decision depends on the commitment technology available to political candidates; in contrast, other papers in the citizen-candidate literature take the inability to commit as given. Further, as in Besley and Coate (2001), we enrichen the basic citizen-candidate environment by considering the possibility that the winning candidate may be lobbied *ex post*, relying on the now-standard menu-auction model of Bernheim and Whinston (1986), first fully exploited in a political context by Grossman and Helpman (1994).

More generally, our work complements the political-economy literature on the role of institutions as commitment mechanisms (e.g., Shepsle and Weingast, 1979; North and Weingast, 1989; North, 1993; Acemoglu and Robinson, 2000, 2001). In our story, the phenomenon of businessman candidates rests on the weakness of institutions such as political parties which in other environments serve as commitment devices for political candidates. While we take the presence or absence of such institutions as exogenous, future work might consider the consequences of businessman candidacy for the development of parties and other institutions which serve to constrain the behavior of state officials.

The paper proceeds as follows. In section 2 we present the basic model, showing that strong forces exist to discourage businessmen from running for public office themselves when electoral commitment is possible, while "businessman candidacies" may emerge in equilibrium when commitment is lacking. Section 3 extends the model to a setting in which businesses compete with each other for rents. As we demonstrate, such competition increases the incentives for businessmen to run for public office when commitment is impossible, as an elected politician can otherwise play one business off of another and capture a large portion of the rents for himself. Section 4 discusses our results in the context of electoral politics in contemporary Russia, where businessmen frequently run for public office, institutions to encourage elected officials to keep their campaign promises are weak, and competition for rents is intense. Section 5 discusses our results. Technical proofs are relegated to the appendix.

2 Basic Model

2.1 Environment

Consider a model with three strategic players – a "left" politician (L), a "right" politician (R), and a businessman (B) – who contest policy along a single dimension, where the policy space is the real number line $\mathbf{R}$. Any of the three players is potentially a candidate for office, where voters with preferences over policy choose among the players who have entered the electoral campaign.

The professional politicians $P \in \{L, R\}$ have preferences represented by the following (von Neumann-Morgenstern) utility function:

$$u_P = -\gamma_P (x - x_P)^2 + C - \mathbf{1}(\text{enter}) \cdot q + \mathbf{1}(\text{win}) \cdot v \tag{1}$$

where $\gamma_P \in \{\gamma_L, \gamma_R\}$ captures the degree to which professional politicians value policy relative to other concerns; x is the policy implemented while x_P is the politician's ideal point; C is any compensation paid *ex post* by the businessman to the politician in return for implementing a particular policy; $\mathbf{1}(.)$ is an indicator variable, taking on a value of one if the politician has entered and won, and zero otherwise; q is a vanishingly small cost of entry; and v is a vanishingly small rent from holding office (separate from any compensation C that might be earned while holding office). For simplicity, we assume that $\gamma_L = \gamma_R$. Note that our assumption that policy preferences are quadratic captures the idea that a politician need be compensated more for a given change in policy, the farther is policy from his ideal point.

Similarly, the businessman has preferences represented by:

$$u_B = -\gamma_B (x - x_B)^2 - C - \mathbf{1}(\text{enter}) \cdot k + \mathbf{1}(\text{win}) \cdot v \tag{2}$$

where γ_B captures the importance of policy relative to other concerns for the businessman, x_B is the businessman's ideal point, and $k > q, v$ is some non-trivial cost of entry. Note that $k > q$ is the key assumption of the model: the opportunity cost of running for public office is assumed to be greater for the businessman than for professional politicians. The most obvious way to rationalize this is to note that the businessman must necessarily divert effort from business activities to manage a political campaign, while a professional politician may have few attractive options outside of politics. Alternatively, we can think of $(k - q)$ as the additional time and money that a businessman

must spend to make himself known to the general public.

We assume that voters have Euclidean preferences – they always prefer a policy closer to their "ideal point" (most preferred policy) to one further away, whether that policy is to the left or right of their ideal point – and that they vote "sincerely," i.e. vote for the candidate who they expect to implement the policy closest to their ideal point, regardless of how other voters are expected to cast their ballot.[5] If indifferent among all candidates, a voter randomly chooses one candidate for whom to vote.[6]

Voters have ideal points distributed on **R**, with the median ideal point x_m unique.[7] We assume that the politicians and businessman must decide whether or not to enter the campaign before this distribution is known with certainty. Formally, let $\{F_w(\cdot)\}_w$ be a family of distribution functions indexed by w, with G the measure of w and $x_m = x_m(w) = F_w^{-1}\left(\frac{1}{2}\right)$. Then we may define the distribution of x_m as $H(x) = \int \mathbf{1}(x_m \leq x)\, dG$, where $\mathbf{1}(.)$ is the indicator function, which takes a value of one if the statement is true and zero otherwise. We assume that $H(x) = 0$ for $x < \mu - \delta$, and $H(x) = 1$ for $x \geq \mu + \delta$, where $\mu = E(x_m)$ and $\delta = (x_B - \mu)$. Thus, the businessman has "extreme" preferences, in the sense that the median voter will always prefer a policy (weakly) to the left of the businessman's ideal point. Further, we order the players' ideal points such that:

$$\mu - \delta < x_L < \mu < x_R < x_B = \mu + \delta \tag{3}$$

so that x_L is located to the left of the expected position of the median voter, x_R to the right, and x_B further from the expected position of the median voter than is either professional politician. Implicitly, we are assuming the existence of "real" political competition, so that politics is potentially contested by candidates at both ends of the political spectrum who are (*ex ante*) more moderate than is the businessman.

The following sequence of play is observed, where brackets indicate a stage that exists only in the version of the game where commitment is possible. All elements of the game are common knowledge.

1. Entry: Simultaneously and independently, the businessman and two politicians decide whether

[5] In the citizen-candidate literature, Osborne and Slivinski (1996) consider sincere voting, while Besley and Coate (1997) assume strategic voting.

[6] Alternatively, we could assume that indifferent voters abstain.

[7] A sufficient (but not necessary) condition for existence of a unique median ideal point is that the distribution of ideal points be continuous and increasing on some interval of **R**.

or not to enter the race.

2. Resolution of uncertainty: The random variable w is realized, so that the distribution of voters' ideal points (and in particular, the median ideal point x_m) is now known with certainty.

3. [Commitment]: Any candidate i who has entered may commit to a policy $\hat{x}_i$ to be pursued after the election, with commitment decisions made simultaneously and independently.

4. Election: Voters cast their ballot for the candidate who they expect will pursue a policy closest to their own ideal point after the election. We assume that the election operates by a "runoff" rule, so that if no candidate wins an absolute majority in the first round, voters vote again, choosing among the two top vote getters in the first round. Ties are broken using an equal-probability rule.

5. Policy choice/lobbying: If the winning candidate has committed to a policy to be pursued after the election, that policy is chosen. If no commitment has been made and the winning candidate is one of the politicians (L or R), the businessman offers a compensation schedule $C(x)$, which for all $x \in \Re$ gives the amount of compensation the businessman will pay to the politician in return for implementing policy x. Following receipt of the schedule, the winning candidate chooses some policy x. If no commitment has been made and the winning candidate is the businessman, the businessman simply chooses some policy x, since there is no one to lobby the politician. Finally, we assume that if no candidate has entered, some status quo policy x_0 will be implemented.[8]

Two features of our formalization deserve further comment. First, note that we assume that uncertainty about the position of the median voter is resolved prior to the making of any policy commitments (when commitment is possible), in contrast to "probabilistic voting" models of political competition. This should be understood as follows: in principle there may be uncertainty that is resolved both between entry and commitment, and between commitment and the election. As with variants on the standard Downsian model, we assume away the latter type of uncertainty for simplicity, since we are merely interested in general convergence towards the median voter,

[8]With negligible entry costs for the two professional politicians, some politician will always prefer to enter rather than accept the status quo.

which one gets (completely) with deterministic models and (mostly) with probabilistic models. However, our interest in entry demands consideration of the former type of uncertainty, a factor ignored in those models that take entry as given.

Second, in assuming that elections operate according to a runoff rule, we model the elections involving businessman candidates that we know best: gubernatorial elections in contemporary Russia.[9] As a practical matter, runoff elections produce clean predictions about platform choice when there are three candidates who have the ability to make binding campaign promises, a feature not shared by plurality rule (see, e.g., Osborne, 1995). Our general results will hold to the extent that other electoral systems encourage convergence to *some* policy when campaign promises are credible, a point we address at greater length in Section 5 below.

2.2 Equilibrium When Commitment Possible

We begin our analysis by focusing on political environments where reputational mechanisms such as political parties allow politicians to make binding campaign promises, i.e. we examine the version of the model in which it is possible to commit to some policy to be pursued after the election. However, since commitment is merely an option, and not imposed, we must first determine the policy pursued after the election by a player who is elected without having committed to any particular policy.

Clearly, if the businessman is elected without having made any binding campaign promise, he will implement x_B after the election: there is no one else to lobby him. In contrast, if a professional politician is elected, then as discussed above the businessman lobbies by providing a compensation schedule $C(x)$ giving the amount of compensation $C \geq 0$ to be paid when policy x is implemented.

With one businessman, the outcome of this lobbying game is straightforward: the elected politician implements the policy that maximizes his and the businessman's joint payoff, and the businessman provides just enough compensation so that the politician is no worse off than if he had implemented his most preferred policy. (For discussion, see Bernheim and Whinston (1986) and

[9] Callander (2003) discusses use of the runoff rule in other political contexts. Our results for a position-taking game with runoff elections in which candidates are primarily policy-seeking expand on previous theoretical work on the runoff rule. Earlier contributions include Osborne and Slivinski (1996), who analyze runoff elections when candidates cannot commit to policy platforms, and Haan and Volkerink (2001) and Callander (2003), who assume that candidates are office-seeking.

Grossman and Helpman (1994).)

Proposition 1. *(Lobbying) If the winning candidate is a professional politician $P \in \{L,R\}$ who has not committed to some policy to be pursued after the election, that politician chooses:*

$$\bar{x}(P) = \alpha x_P + (1-\alpha)x_B \tag{4}$$

where $\alpha = \frac{\gamma_P}{\gamma_P+\gamma_B}$, in return for which the businessman provides the following compensation:

$$\bar{C}(P) = \gamma_P(\bar{x}(P) - x_P)^2 \tag{5}$$

Proof. Omitted. □

As Proposition 1 indicates, the policy implemented by the winning politician is a weighted average of his and the businessman's ideal points, where the weighting depends on the relative importance each of the two parties places on policy vs. other considerations.

With the outcome of the policy-choice stage in hand, we can proceed to consideration of the policy chosen by any candidate who has entered the race. When there is *one candidate*, by Proposition 1 that candidate (who will win whatever position he chooses) will be indifferent between committing to his most preferred policy (i.e. choosing $\hat{x}_i = x_i$) and not committing. In contrast, when there are *two candidates*, both candidates commit to x_m. To see this, note that a two-candidate runoff election is equivalent to a two-candidate plurality-rule election. Since both candidates receive some small exogenous rent v from holding office, the election essentially reduces to the standard Downsian model, though the logic is slightly complicated by the fact that each politician P may choose not to commit and thus retain the option of implementing $\bar{x}(P)$ in return for $\bar{C}(P)$ *ex post*.

Proposition 2. *(Policy choice with two candidates) When it is possible to commit to a policy to be pursued after the election and two players have entered the race, both candidates will choose to commit to the policy preferred by the median voter, x_m.*

Proof. See appendix. □

The proof of Proposition 2 relies on the fact that for any configuration of positions (either committed to or implied) other than (x_m, x_m), at least one candidate always has an incentive to adopt a position no more than some infinitesimal ε away from the expected winning policy, thus

gaining at least a share of the exogenous rent v while sacrificing essentially nothing in terms of policy utility. (When the two candidates adopt positions some equal distance to each side of x_m, then by deviating to x_m a candidate can not only win for sure and thus gain $\frac{v}{2}$, but can actually *increase* his policy utility since x_m is now implemented with certainty: recall that players are risk-averse with respect to policy.) The same basic logic applies to the case when *three candidates* have entered:

Proposition 3. *(Policy choice with three candidates) When it is possible to commit to a policy to be pursued after the election and all three players have entered the race, all candidates will choose to commit to the policy preferred by the median voter, x_m.*

Proof. See appendix. □

Thus, whether two or three candidates have entered, the policy outcome is the same: x_m will be implemented *ex post*. This immediately implies that there would never be an equilibrium in which all three candidates enter, since the businessman with his non-trivial entry cost k would prefer not to have entered, since by not entering he can receive the same policy payoff at a savings of k (less his share of the infinitesimal exogenous rent v from holding office).

Slightly less obvious is that the businessman would always prefer not to enter if he expects only R to enter. By the logic of Proposition 2, if the businessman stays in the race he must accept x_m, whatever the realization of that random variable turns out to be. In contrast, by not entering he will receive either x_R or $\overline{x}(R)$, the policy implemented by R *ex post* when R runs unopposed. Since $x_R > \mu = E(x_m)$, this is preferable for the businessman (though verifying this takes a bit of work, since x_m is a random variable and the businessman is risk-averse – see the proof to Proposition 4 for details). By a similar logic, the businessman would never enter alone, since L would always prefer to enter and move policy to some $x_m < x_B$.

Indeed, the only possible equilibrium in which the businessman enters when campaign promises are binding has B entering together with L. The fact that the businessman prefers entering to not in this equilibrium (when it exists) is due solely to the fact that R has not entered, since by Proposition 2 the same policy outcome can be achieved if R had entered instead of B, and the businessman's cost of entry k outweighs his share of the exogenous rent from holding office. Whether or not this equilibrium exists depends in particular on k (intuitively, the businessman will be more likely to

enter when his opportunity cost of running is low) and $(x_B - x_L)$ (the businessman will be more likely to enter when he has more to lose from leaving the election to L).

These observations are summarized in the following proposition:

Proposition 4. *(Businessman candidates) When it is possible to commit to a policy to be pursued after the election, the only possible equilibrium involving entry of the businessman has the businessman and the "left" candidate entering, while the "right" candidate stays out of the race.*

Proof. See appendix. □

Thus, there is at most one equilibrium involving entry by the businessman when campaign promises are credible. Moreover, that equilibrium is inefficient: the same policy outcome could be achieved if R entered rather than B, at a savings of $(k-q)$, the difference between the businessman's and R's opportunity cost of running. This implies that there are potentially gains from trade, with the businessman paying R to run in his stead. Note that such a contract will be self-enforcing when the policy that L would pursue if unopposed during the election (either x_L or $\overline{x}(L)$) is sufficiently far to the left: R will prefer to enter rather than leave policy to L, correctly anticipating that the businessman will not enter, while by the logic of Proposition 4 the businessman will not enter, knowing that R will. Further, even when not self-enforcing, it seems reasonable to believe that the same reputational mechanisms that make campaign promises credible will encourage the politician to hold up his end of the bargain.

Proposition 5. *(Pre-entry contracting) In an expanded game, where in a pre-entry contracting stage the businessman can propose to a politician that the politician enter the race in exchange for some compensation by the businessman, there is no equilibrium where the businessman enters.*

Proof. Omitted. □

2.3 Equilibrium When Commitment Impossible

In political environments where politicians may make binding campaign promises because of the presence of reputational mechanisms such as strong political parties, potential candidates decide not only whether to enter the race, but also what position to take upon entering. With platform choice dictated by the logic of political competition, candidate identity becomes largely irrelevant.

A businessmen therefore has little incentive to enter the race when commitment is possible, since the same outcome can typically be achieved without his direct participation.

In contrast, when campaign promises are meaningless, candidate identity matters for the policies that will be adopted *ex post*, implying two reasons why a businessman might choose to enter the race:

1. By winning, the businessman can implement a policy better than that which would be implemented by another candidate.

2. By winning, the businessman can save the cost of lobbying the winning candidate after the election.

Whether or not a businessman chooses to enter depends not only on his expectation of what will happen if he does not (i.e. on his beliefs about who will enter and his understanding of what will happen *ex post* if they do), but on the likelihood that the businessman will win against those other players who have entered. As the following example demonstrates, the expected gain from entering may be sufficiently great to support outcomes impossible when campaign promises are binding.

Example 1. *(Three-candidate equilibria) To study runoff elections when candidates cannot make binding campaign promises, we must make assumptions not only the distribution of the median ideal point x_m, but also about distribution of other ideal points. Recalling that $\{F_w(\cdot)\}_w$ is a family of distribution functions indexed by w, assume for simplicity that w is distributed uniformly on $[0,1]$, with each $F_w(\cdot)$ a normal distribution with mean w and variance close to* 0*. We may then derive the probability that a candidate wins, conditional on the set of players who have entered the race, as the probability that w is closer to the candidate's* implied *position (i.e. the position that*

will be implemented by the candidate ex post*) than it is to any other candidate's implied position:*[10]

$$\Pr(L \text{ wins} \mid L,R,B) = \frac{\bar{x}(L)+\bar{x}(R)}{2} \tag{6}$$

$$\Pr(R \text{ wins} \mid L,R,B) = \frac{x_B-\bar{x}(L)}{2} \tag{7}$$

$$\Pr(B \text{ wins} \mid L,R,B) = 1-\frac{\bar{x}(R)+x_B}{2} \tag{8}$$

$$\Pr(L \text{ wins} \mid L,R) = \frac{\bar{x}(L)+\bar{x}(R)}{2} \tag{9}$$

$$\Pr(L \text{ wins} \mid L,B) = \frac{\bar{x}(L)+x_B}{2} \tag{10}$$

$$\Pr(R \text{ wins} \mid R,B) = \frac{\bar{x}(R)+x_B}{2} \tag{11}$$

Let L, R, and B have ideal points $x_L = \left(\frac{1}{2}-a\right)$, $x_R = \left(\frac{1}{2}+b\right)$, *and* $x_B = \left(\frac{1}{2}+b+c\right)$, *where a, b, and c are positive numbers with* $a < b+c < \frac{1}{2}$. *Observe that this meets our assumption about the ordering of ideal points given in (3). Then if* $\gamma_L = \gamma_R = \gamma_B$, *there is a three-candidate equilibrium for q and k are sufficiently low.*[11] *Intuitively, when each player places equal weight on policy relative to money, the implied positions for each of the professional politicians fall halfway between their ideal points and the politician's. Then each candidate has both a non-trivial probability of winning and a strong incentive to stay in the race.*

In particular, given our distributional assumptions, the probability that L wins remains the same whether B stays in the race or withdraws. Thus, the businessman's decision to remain in the race reduces to whether the possibility of implementing his own ideal point and avoiding the expense of lobbying outweighs the opportunity cost of being a candidate.

Beyond showing the existence of equilibria (for certain parameter values and distributional assumptions) in which the businessman enters against L and R, Example 1 demonstrates that the

[10] *This is derived for three-candidate elections as follows: For notational simplicity, let the three candidates' positions be x, y, and z, with* $x \le y \le z$, *and refer to the candidates by their positions. Then in the first round the share of votes received by the three candidates is* $F_w(\frac{x+y}{2})$, $F_w(\frac{y+z}{2}) - F_w(\frac{x+y}{2})$, *and* $1-F_w(\frac{y+z}{2})$, *respectively. The candidates that have the two highest shares advance to the second round. (Note that there is no need to separately consider the case of a candidate who wins a majority in the first round, as any such candidate would always win a second round.) In the second round, x beats y if and only if* $F_w(\frac{x+y}{2}) > \frac{1}{2}$, *y beats z if and only if* $F_w(\frac{y+z}{2}) > \frac{1}{2}$, *and x beats z if and only if* $F_w(\frac{x+z}{2}) > \frac{1}{2}$. *Letting the variance of* $F_w(\cdot)$ *go to zero and recalling that w is distributed uniformly on* $[0,1]$ *gives the expressions in (6) to (11).*

[11] *Showing this is straightforward but a bit tedious, requiring substitution of* $\bar{x}(L)$, $\bar{x}(R)$, $\bar{C}(L)$, *and* $\bar{C}(R)$ *from Proposition 1 into the conditions for each player to want to remain in the race rather than withdraw. Details are available from the authors upon request.*

businessman may be less likely to pay R to run in his place when campaign promises are not binding. Even if the businessman prefers that R run in his place against L, a contract to that effect will not be self-enforcing if the businessman will nonetheless enter even if R is already running against L (as will be the case when a three-candidate equilibrium exists). Further, as the following example shows, if policy is sufficiently important to the businessman, he may prefer to run against L on his own rather than pay R to run instead.

Example 2. *(Invulnerability of (L,B) equilibrium to pre-entry contracting) Follow the previous example, except now let γ_B go to infinity while holding γ_L and γ_R fixed. Then $\bar{x}(L) = \bar{x}(R) = x_B$, so the probability that R wins is zero when both L and B are candidates, while the probability that L wins is the same regardless of who else is in the race, so long as there is at least one other candidate (see the previous example). Consequently, for q and k sufficiently low, there will be an equilibrium in which L and B enter but R does not: both L and B will prefer staying in the race to leaving the field to the other alone, while R will not enter since he cannot win and cannot change the expected policy. Further, for k sufficiently low the businessman prefers this equilibrium to that in which R runs against L, since the probability that L wins is the same in either case, and by running the businessman may be able to save the cost of lobbying.*

In sum, businessman candidates will generally be more likely in institutional environments where candidates find it difficult to make binding campaign promises. Absent the disciplining effect of political campaigns when commitment is possible, a businessman may anticipate substantial gains from holding office. When the opportunity cost of running is not too great, the businessman may therefore choose to run even when the field is crowded, and will generally be reticent to fund somebody else's campaign rather than run himself.

3 Competition for Rents

Up to now, we have restricted attention to an environment in which there is a single businessman with an interest in influencing policy and potentially running for office. In this section we extend the model to examine the idea that competition for rents among businesses may make holding office more attractive, and therefore increase the likelihood that businessmen run for public office.

As we will see, this intuition holds only when commitment to policy is impossible. As in the basic model, the nature of political competition discourages entry by businessmen when campaign promises are credible.

To fix ideas, modify the environment of Section 2.1 so that now there is one professional politician P, with ideal point $x_P = \mu$, and two businessmen $B \in \{BL, BR\}$, with ideal points $x_{BL} < \mu < x_{BR}$ and $(x_{BR} - \mu) = (\mu - x_{BL}) \equiv \delta$. Both businessman have preferences analogous to those of the businessman in the previous section, with γ_B representing the degree to which each businessman values policy relative to other concerns. As before, there is uncertainty over the distribution of voters' ideal points, with x_m is distributed on some interval $T \subset [\mu - \delta, \mu + \delta]$, where $\mu = E(x_m)$.

In all other respects, the game is analogous to that presented above. Note that if the professional politician does not commit to any policy and subsequently wins, then at the policy choice/lobbying stage each businessman offers a compensation schedule $C(x)$. In contrast, if the winning candidate is a businessman who has not made any commitment, then the other businessman alone submits a schedule. Throughout we restrict ourselves to globally truthful compensation schedules, i.e. those for which the slope of a businessman's contribution schedule is equal to the marginal change in the businessman's policy payoff, wherever contributions are positive (for details, see Bernheim and Whinston (1986) and Grossman and Helpman (1994)).

We can think of the presence of a single "moderate" politician as the reduced-form approximation of an environment with sufficient political competition to encourage convergence to centrist policies when candidates are able to making binding campaign promises. As in the model of the previous section, this implies that no businessman will enter when commitment is possible.

Proposition 6. *In the model with competition for rents, there is no equilibrium where either of the two businessmen enters as a candidate when candidates can make binding campaign promises.*

Proof. See appendix.

□

In contrast, when commitment is impossible, then there will exist equilibria with one or more businessman candidates, as in the previous section. Such equilibria will be more more likely, the larger is the competition for rents (as reflected either in the value γ_B that the businessmen put on policy relative to other concerns, or the distance δ between their ideal points and that of the

expected position of the median voter.) To establish this, we first derive the policies chosen *ex post* when the winning candidate has not committed.

Proposition 7. *(Lobbying) In the model with competition for rents, any winning candidate who has not committed to some policy will implement* μ ex post. *If the winning candidate is a businessman* $B \in \{BL, BR\}$*, then the other businessman provides compensation:*

$$\hat{C}(B) = \gamma_B (\mu - x_B)^2 \tag{12}$$

If the winning candidate is the professional politician P, then BL and BR provide compensation $\hat{C}_{BL}(P)$ *and* $\hat{C}_{BR}(P)$*, respectively:*

$$\hat{C}_{BL}(P) = -\gamma_P (\hat{x}_{BR}(P) - \mu)^2 + \gamma_B \left[(\mu - x_{BR})^2 - (\hat{x}_{BR}(P) - x_{BR})^2 \right] \tag{13}$$

$$\hat{C}_{BR}(P) = -\gamma_P (\hat{x}_{BL}(P) - \mu)^2 + \gamma_B \left[(\mu - x_{BL})^2 - (\hat{x}_{BL}(P) - x_{BL})^2 \right] \tag{14}$$

where $\hat{x}_B(P) = \alpha x_P + (1-\alpha) x_B$*, with* $\alpha = \frac{\gamma_P}{\gamma_P + \gamma_B}$.

Proof. See appendix.

□

Proposition 7 suggests that the lobbying power of one businessmen offsets the other's, in the sense that when the winning candidate has not committed to any policy, then a centrist policy will be chosen *ex post* regardless of who was elected. However, as may be verified algebraically, an increase in competition for rents – either an increase in the value γ_B that the businessmen place on policy, or an increase in the distance of the businessmen's ideal points from the center – will result in larger compensation being paid by the businessmen. Intuitively, the more the businessmen care about policy, the more the elected politician (businessman or professional politician) will be able to demand. Since such an increase in stakes has no effect on the policies to be pursued in the absence of commitment, and hence no change in voters' preferences over the three candidates, the result will be a greater incentive for businessmen to enter the race as candidates.

Proposition 8. *The greater the competition for rents, the more "likely" will be an equilibrium with one or more businessman candidates.*[12]

[12] i.e. such an equilibrium will exist for a wider range of parameter values.

Proof. Omitted.

□

As competition for rents increases, each businessman will be more inclined to enter the race to earn rents for himself rather than transfer them to the winning candidate.

4 Businessman Candidates in Contemporary Russia

In this section we illustrate our arguments by drawing on post-communist Russia's experience with electoral politics. We describe the phenomenon of businessman candidacy in Russia, demonstrate that the emergence of such candidates is related to the weakness of democratic institutions and consequent inability of candidates to make binding campaign promises, and provide some evidence that strong competition for rents may increase the incentive of Russian businessmen to run for office.

4.1 The Phenomenon

Various scholars of contemporary Russia have noted the increasingly direct involvement of Russian businessmen in electoral politics. While the potential presidential aspirations of former Yukos head Mikhail Khodorkovskii may have made the headlines, the reality is that representatives of business occupy numerous elected positions at the federal, regional, and local level.[13]

To get a sense for the scale of the phenomenon, we compiled a list of "businessman candidates" in gubernatorial elections between 1997 and 2003, drawing on Russian Central Election Commission data and newspaper reports.[14] The appendix presents our (possibly incomplete) list. By our count, between 1997 and 2003 there were 38 non-trivial businessman candidacies for the post of regional executive, where "businessman candidate" is defined as a candidate serving as a manager or principal owner of a business at the time of the election, and "non-trivial" means that the candidate received at least 10 percent of the vote. The 35 elections with such candidacies (three regions had

[13] See, e.g., Barnes (2003); Orttung (2004); Ol'ga Kryshtanovskaia, "Kremlevskie Zavsegdatai [Kremlin Regulars]," *Vremia MN*, February 13, 2003.

[14] Regional executives in Russia are known variously as "governor," "president," and (in Moscow, which has regional status) "mayor." For simplicity, we use "gubernatorial election" to refer to any election for the post of regional executive.

multiple candidacies) account for slightly more than a quarter of all gubernatorial elections held during this period. As the list in the appendix indicates, such candidacies were increasingly effective over time. While none of the ten businessman candidacies between mid-1997 and November 2000 were effective, in the period which follows ten businessman candidates were elected, and a further five advanced to the second round of voting.

There is substantial evidence that businessmen are running in large numbers in other elections in Russia. For example, the Russian newspaper *Kommersant* reports that 77 members (out of 450) of the Duma which served between 1999 and 2003 were "direct representatives" of business, while 66 members of the Duma elected in 2003 were similarly affiliated.[15] Published and unpublished data on business representation in the 2003 Duma gathered by the *Moscow Times*, an English-language daily, suggests that the latter number may be a substantial underestimate.[16]

In the discussion which follows, we focus especially on gubernatorial elections in Russia. We do so because the environment in which such elections take place is closest to that in our model (in contrast, half the Duma is elected through party-list voting), and because – unlike Duma deputies – Russia's governors do not possess legal immunity. The latter distinction is important, as it is possible in principle that businessmen run for the Duma to avoid prosecution. That said, business representatives in the Duma are for the most part not the major shareholders and CEOs of their corporations who are most legally vulnerable.[17]

4.2 Reputational Mechanisms and Commitment in Russian Politics

A central proposition in the literature on electoral competition is that parties, longer-lived than candidates, develop policy reputations which their members ignore at their peril (Alesina and Spear, 1988; Cox and McCubbins, 1994; Aldrich, 1995). In Russia, parties are young and – especially in regional politics – weak. The consequence is that elected officials have greater opportunity to pursue their own preferences, increasing the incentive for businessmen to run for public office.

That Russia's parties are young is obvious: electoral politics in one form or another has existed

[15] Dmitrii Butrin, "Biznes i Vlast': Zakonodatel'nyi Sovet Direktorov [Business and Power: Legislative Board of Directors]," *Kommersant*, December 26, 2003.

[16] Francesca Mereu, "Duma Has a Big Business Lobby," *Moscow Times*, January 20, 2004; Francesca Mereu, private communication.

[17] See, for example, the list in Mereu, "Duma Has a Big Business Lobby," op. cit.

in Russia for only a bit over a decade. The one exception, of course, is the Communist Party, which not only inherited a substantial grass-roots network but a particular policy reputation from its predecessor, the Communist Party of the Soviet Union. Most of the remaining party system has been a kaleidescope, with parties emerging to contest one election, only to disappear the next. The record of these parties in establishing clearly-defined platforms is mixed, with the long succession of "parties of power" which have benefitted from Kremlin patronage especially notable for their lack of ideological underpinnings.[18]

Compounding the inability of parties to act as reputational mechanisms is the fact that many candidates run as independents rather than party nominees. This is especially the case in regional elections. Between 1995 and 1999, 45 percent of gubernatorial elections were not contested by a single party-nominated candidate; over the next four years, the figure was 63 percent (Golosov, 2004). Even this tends to overestimate the importance of parties at the regional level, with party nominees accounting for a mere 15 and 7 percent, respectively, of the winning candidates in the two electoral cycles. Further, many of the parties active at the regional level are not national but local parties with little ideological orientation (McFaul, 2001).

There is much investigation into the causes of Russia's weak party system (see, e.g., Stoner-Weiss, 2001; McFaul, 2001; Hale, forthcoming). We are interested in the consequences of this weakness for the nature of electoral competition. Some suggestive evidence is provided by Colton (2000, pp. 106-107), who cites survey evidence that only 17 percent of Russians trust or completely trust political parties, a figure lower than that for any state institution. This lack of trust in parties presumably translates into a lack of faith in party nominees' campaign promises. Combined with the fact that most regional candidates are not party nominees at all, the result is a politics that is highly "personalistic" (Hough, 1998; Stoner-Weiss, 2001). Candidate identity, rather than party platform, is what matters.

The importance of candidate identity came up frequently in conversations we had with individuals connected to a much-discussed businessman candidacy: the election to the Krasnoyarsk governorship of Aleksandr Khloponin, former general director of Norilsk Nickel, one of the two main industrial enterprises in the region.[19] Khloponin apparently received substantial financial

[18] Rose and Munro (2002) and Colton and McFaul (2003) discuss the nature of national political parties in Russia.

[19] Petrov (1999), Yorke (2003), and Ivanov (2002) describe the recent political history of the region. Krasnikov

support from Interros, the parent company of Norilsk Nickel, and Khloponin was widely seen as Interros's candidate. Indeed, Khloponin did overwhelmingly better among voters in areas dominated by Norilsk Nickel, suggesting that voters believed that he would protect the interests of the company from which he had emerged.

Khloponin's major competitor in the campaign was Aleksandr Uss, a professional politician with no direct connection to any enterprise in the region who, having been spurned by the Kremlin-backed Unity party, started his own regional party in 2001 (Krasnikov 2002). After some initial hesitation, Uss was backed in his campaign by Russian Aluminum (RusAl), the owner of Krasnoyarsk's other major industrial enterprise. One elected official from the region told us that RusAl wavered in its support of Uss, knowing that Uss might turn around and abandon the company after the election. However, in the end, they did support Uss, having less to fear from him than from Khloponin, a theme to which we turn in the next section.

4.3 Competition for Rents in Russia's Regions

As Section 3 showed, the incentive for businessmen to run for public office when campaign promises are not binding may be larger when competition for rents among businesses is strong. As any observer of postcommunist political economy would attest, competition for rents among Russian businesses over the past decade has been intense indeed.

Some evidence of the relative level of competition is provided by the World Business Environment Survey (WBES), conducted by the World Bank in 80 countries in 2000.[20] When asked how problematic was "anticompetitive behavior by other enterprises or the government," 55 percent of Russian firms responded that such behavior was a major or moderate obstacle. (The corresponding figure for countries at a similar income level was 52 percent, while the figure for OECD countries in which the WBES was conducted varied from 14 to 43 percent.) Consistent with our story, the competition for favorable treatment in Russia manifests itself in a high "bribe tax" which must be paid to government officials. 61 percent of Russian firms report that "unofficial payments to public officials" exceed one percent of total revenues, in contrast to 44 percent of firms in countries at a

(2003) is a major source on the 2002 gubernatorial elections. We conducted interviews with various individuals connected with the two major campaigns for the governorship.

[20] For details on the survey, see Batra, Kaufmann and Stone (2003).

similar income level and fewer than 30 percent of firms in OECD countries.

Such competition has been driven in part by the large rents to be earned from natural-resource extraction and government reliance on this sector for tax revenues. In Krasnoyarsk, the two major enterprises in the region account for the vast majority of taxes paid to the regional government, and the possibility that Khloponin would use his position to reapportion some of the tax burden from Norilsk Nickel to Russian Aluminum was much discussed by the individuals we interviewed. That possibility, together with regional government control over electricity production (critically important for metals processing), may have been instrumental in Khloponin's candidacy and RusAl's response to it.

While a full empirical study of the determinants of businessman candidacy in Russia is beyond the scope of this paper, examination of the list of businessman candidates in the appendix provides further evidence that competition for natural-resource rents in particular is driving businessman candidacy in Russia. Of the fourteen separate individuals who ran as businessman candidates and either won or lost but advanced to the second round of voting, nine were owners or top managers of natural-resource enterprises.[21] In addition, the pairwise correlation between the presence in an election of a businessman candidate who won or advanced to the second round, and an index of the region's natural-resource potential (developed by a panel of Russian experts – see Lavrov (1997)), is .271 ($p = .002$), evidence of a strong relationship between competition for rents and businessman candidacy.

5 Conclusion

In this paper we have presented a model of "businessman candidates." Our primary result is that businessmen will be more likely to bypass conventional means of influence and run for public office themselves when commitment mechanisms such as political parties which enable candidates to make binding campaign promises are weak or nonexistent. We have secondarily shown that, given the absence of such commitment mechanisms, the incentive for businessmen to enter may be greater when there is competition for rents among businesses.

[21] In particular, these candidates represented firms involved in metals (Loginov, Khloponin, Sovmen), diamonds (Tumusov, Shtyrov), oil (Abramovich, Zolotarev), gas (Sokolovskii), and fishing (Dar'kin).

While not a general theory of the "political boundaries of the firm," the model here does present an explanation for what seems to be a great deal of variation in the degree to which businesses contract out their influence activities. A question for further examination is whether our results are sensitive to the particular electoral rule – the runoff rule – which we chose to illustrate our argument (and which governs gubernatorial elections in contemporary Russia, the example on which we focus). Our intuition is that similar results will obtain under any electoral rule which encourages convergence to some set of policies among candidates able to make binding campaign promises. As emphasized by Cox (1990), for a wide class of electoral rules there will be convergence to centrist positions so long as the number of candidates in an election is sufficiently small. That said, our results do not necessarily hinge on "centripetal" pressures in electoral competition: if either a businessman or professional politician would be forced to adopt a particular position somewhere on the political spectrum when campaign promises are binding, then as in our model the businessman may pay the politician to run in his place.

6 Appendix

6.1 Proof of Proposition 2

Label the candidates $i = 1, 2$, and use $E_i \equiv E\left[-\gamma_i (x - x_i)^2\right]$ to refer to the expected policy payoff for candidate *i*, given commitment/noncommitment decisions by all the candidates. As in the body of the text, we use x_i to denote candidate *i*'s ideal point, and $\hat{x}_i$ the policy committed to by candidate *i*. In addition, we refer to the policy expected to be pursued *ex post* by a candidate *i* who has not committed as $\bar{x_i}$ (which for a professional politician *P* is $\bar{x}(P)$, given by Proposition 1, and for the businessman is x_B). We follow the convention that $-i$ refers to the candidate who is not candidate *i*.

First observe that $(\hat{x}_1, \hat{x}_2) = (x_m, x_m)$ *is an equilibrium*: if either candidate deviated, the other candidate would win for sure, resulting in the same expected policy payoff but a loss of $\frac{v}{2}$ (the exogenous rent obtained with probability $\frac{1}{2}$) for the candidate who deviated.

Next observe that there is *no equilibrium where each candidate commits, but at least one does not commit to* x_m. Assume to the contrary that such an equilibrium exists. There are three mutually

exclusive and exhaustive possibilities, depending on the configuration of positions chosen by the two candidates:

1. One of the candidates i wins with certainty. But then the other candidate $-i$ can adopt $\hat{x}_i$ and win with probability $\frac{1}{2}$ (gaining $\frac{v}{2}$). Since doing so does not change E_{-i} (since $\hat{x}_i$ is still adopted with certainty), this will always be preferable to not deviating.

2. Candidates 1 and 2 tie, with $\hat{x}_1 = \hat{x}_2 \neq x_m$. But then either of the two candidates has an incentive to move some infinitesimal ε towards x_m, resulting in essentially the same policy payoff but a gain of $\frac{v}{2}$ for the candidate deviating (since that candidate now wins with certainty).

3. Candidates 1 and 2 tie, with $\hat{x}_1$ and $\hat{x}_2$ some distance Δ on either side of x_m (so that the median voter is indifferent between the two policies). But then either candidate $i = 1,2$ has an incentive to commit instead to x_m, thus winning for sure (and therefore gaining $\frac{v}{2}$) while producing a higher E_i since:

$$-\gamma_i (x_m - x_i)^2 > -\frac{\gamma_i}{2}\left[(x_m - \Delta - x_i)^2 + (x_m + \Delta - x_i)^2\right] \tag{15}$$

Next we verify that there is *no equilibrium in which one candidate does not commit.* Assume to the contrary that such an equilibrium exists, and without loss of generality, assume that it is candidate 2 who has not committed. There are four mutually exclusive and exhaustive possibilities, depending on the position chosen by candidate 1:

1. Candidate 2 wins with certainty. But then candidate 1 can commit to $\bar{x_2}$ and win with probability $\frac{1}{2}$, gaining at least $\frac{v}{2}$ since E_1 remains the same. (Note that if candidate 1 is the businessman, then candidate 1 gains more than $\frac{v}{2}$ by this deviation, since with probability $\frac{1}{2}$ the businessman no longer need pay compensation to candidate 2 *ex post*.)

2. Candidate 1 wins with certainty. But then candidate 2 can do better by committing to $\hat{x}_1$, by the same logic as when both candidates commit.

3. Candidates 1 and 2 tie, with $\hat{x}_1 = \bar{x_2}$. But then candidate 1 has an incentive to move some infinitesimal ε towards x_m and win with certainty, resulting in essentially the same E_1 but gaining at least $\frac{v}{2}$ (where if candidate 1 is the businessman, the gain is greater than $\frac{v}{2}$, since the businessman no longer must pay compensation to candidate 2 with probability $\frac{1}{2}$).

4. Candidates 1 and 2 tie, with $\hat{x}_1 = x_m - (\bar{x_2} - x_m)$, so that the candidates are $\Delta \equiv |\bar{x_2} - x_m|$ on either side of x_m, implying that the median voter is indifferent between the two candidates. But then candidate 1 can instead commit to x_m, winning with certainty and gaining at least $\frac{v}{2}$ (more, if the deviating candidate is the businessman, who now with probability 0 must pay compensation *ex post*) while increasing E_1, by the same logic as in point 3 of the discussion of the case where both candidates commit.

Finally, we check that there is *no equilibrium in which neither candidate commits*. Assume to the contrary that such an equilibrium exists. There are two possibilities, depending on the prior history of the game:

1. $|\bar{x_1} - x_m| \neq |\bar{x_2} - x_m|$, so that the median voter prefers one candidate to the other. But then the losing candidate can always commit to $\bar{x_i}$, the policy that will be implemented by the winning candidate i, resulting in the same E_{-i} for the losing candidate $-i$ while gaining that candidate at least $\frac{v}{2}$ (more, if the deviating candidate is the businessman, who with probability $\frac{1}{2}$ no longer need pay compensation *ex post*).

2. $\bar{x_1}$ and $\bar{x_2}$ are located on opposite sides of x_m, with $|\bar{x_1} - x_m| = |\bar{x_2} - x_m|$, so that the median voter is indifferent between the two candidates. But then either candidate $i = 1, 2$ can instead commit to x_m and win for sure, gaining at least $\frac{v}{2}$ (more, if the deviating candidate is the businessman, who now with probability 0 must pay compensation *ex post*) while increasing E_i by the logic of the cases where one or both candidates commit. □

6.2 Proof of Proposition 3

We label the candidates and follow notation as in the proof of Proposition 2.

First observe that $(\hat{x}_1, \hat{x}_2, \hat{x}_3) = (x_m, x_m, x_m)$ *is an equilibrium*: if any candidate deviated, that candidate could not win the first round with certainty, and at best would enter the second round against one of the other two candidates, against whom he would lose (since the other candidate occupies x_m). Thus, a deviation results in the same expected policy payoff but a loss of $\frac{v}{3}$ (the exogenous rent obtained with probability $\frac{1}{3}$) for the candidate who deviated.

Next observe that there is *no equilibrium where all candidates commit, with at least one committing to a policy other than* x_m. Assume to the contrary that such an equilibrium exists. There

are six mutually exclusive and exhaustive possibilities, depending on the configuration of positions chosen by the three candidates:

1. One candidate i wins outright in the first round. Note that this implies that $\hat{x}_i$ is closer to x_m than is the position occupied by any other candidate. But then either of the other two candidates can adopt $\hat{x}_i$ and win with probability $\frac{1}{2}$ (either tying for first place or for second place in round 1, since the two candidates now occupying $\hat{x}_i$ will collectively gain at least the majority previously earned by candidate i alone), resulting in no change in the policy payoff for the deviating candidate but gaining him $\frac{v}{2}$.

2. One candidate i wins for sure in the second round. Note that this implies that $\hat{x}_i$ is closer to x_m than is the position occupied the other candidate who enters the second round. But then the candidate who fails to enter the second round can adopt $\hat{x}_i$ and win with probability $\frac{1}{2}$, resulting in no change in the policy payoff for that candidate but gaining him $\frac{v}{2}$. (In the event that the two losing candidates tie in the first round, then either of the two candidates may deviate in this manner.)

3. Exactly two candidates $i = 1,2$ have a chance of winning in the second round, with the two candidates occupying the same $\hat{x}_i \neq x_m$. But then the third candidate can adopt the same $\hat{x}_i$ and win with probability $\frac{1}{3}$, resulting in no change in the policy payoff E_3 for that candidate but gaining him $\frac{v}{3}$.

4. Exactly two candidates $i = 1,2$ have a chance of winning in the second round, with $\hat{x}_1$ and $\hat{x}_2$ some distance Δ on either side of x_m. But then the third candidate can adopt either $\hat{x}_1$ or $\hat{x}_2$. By doing so, this candidate ties for second in the first round and thus enter the second round with probability $\frac{1}{2}$, resulting in the same contest of positions in the second round and hence the same policy payoff E_3, but gaining that candidate $\frac{v}{4}$ (since he wins with probability $\frac{1}{4}$).

5. All three candidates have an equal probability of winning in the second round, with the three candidates $i = 1,2,3$ occupying the same $\hat{x}_i \neq x_m$. But then any of the three candidates can instead commit to a position some infinitesimal ε towards x_m and win outright, resulting in essentially the same policy payoff but gaining that candidate $\frac{2V}{3}$ (since he now wins with certainty rather than with probability $\frac{1}{3}$).

6. All three candidates win in the second round with some positive probability, with two candidates some distance Δ to one side of x_m, and the other candidate the same distance Δ to the other side. Thus, the candidate alone to one side always enters against one of the other two candidates, so that the second round always pits $(x_m - \Delta)$ against $(x_m + \Delta)$. But then the candidate i alone to one side of x_m can instead adopt x_m and win for sure, gaining that candidate $\frac{v}{2}$ (since he now wins with certainty rather than with probability $\frac{1}{2}$), while increasing his policy payoff E_i since:

$$-\gamma_i (x_m - x_i)^2 > -\frac{\gamma_i}{2}\left[(x_m - \Delta - x_i)^2 + (x_m + \Delta - x_i)^2\right] \tag{16}$$

Next we verify that there is *no equilibrium in which at least one candidate does not commit*. Assume to the contrary that such an equilibrium exists. There are six mutually exclusive and exhaustive possibilities, corresponding to the six cases when all three candidates have committed:

1. One candidate i wins outright in the first round. But then:

   (a) when the winning candidate has committed to some policy $\hat{x}_i$, by the logic of the case where all commit, one of the losing candidates can commit to $\hat{x}_i$ and win with probability $\frac{1}{2}$, gaining $\frac{v}{2}$.

   (b) when the winning candidate i has not committed to any policy (thus implying policy $\bar{x}_i$), by the same logic one of the losing candidates can commit to $\bar{x}_i$ and win with probability $\frac{1}{2}$,where the gain from doing so is at least $\frac{v}{2}$ (more, if the deviating candidate is the businessman, who with probability $\frac{1}{2}$ no longer need pay compensation *ex post*).

2. One candidate i wins for sure in the second round. But then:

   (a) when the winning candidate has committed to some policy $\hat{x}_i$, by the logic of the case where all commit, the candidate who fails to enter the second round (or one of the two remaining candidates, if those two candidates tie in the first round) can adopt $\hat{x}_i$ and win with probability $\frac{1}{2}$, gaining $\frac{v}{2}$.

   (b) when the winning candidate i has not committed to any policy (thus implying policy $\bar{x}_i$), by the same logic the candidate who fails to enter the second round (or one of the two remaining candidates, if those two candidates tie in the first round) can adopt $\bar{x}_i$

and win with probability $\frac{1}{2}$, gaining at least at least $\frac{v}{2}$ (more, if the deviating candidate is the businessman, who with probability $\frac{1}{2}$ no longer need pay compensation *ex post*).

3. Exactly two candidates $i = 1,2$ have a chance of winning in the second round, with the two candidates occupying (either through commitment to that policy or because that policy is implied by noncommitment) the same position. But then:

   (a) when both of the winning candidates have committed to the same policy $\hat{x}_i$, the third candidate can adopt the same $\hat{x}_i$ and win with probability $\frac{1}{3}$, thus gaining $\frac{v}{3}$.

   (b) when at least one of the winning candidates i has not committed (so that the winning candidates have each "adopted" $\overline{x_i}$), the third candidate can commit to $\overline{x_i}$ and win with probability $\frac{1}{3}$, thus gaining at least $\frac{v}{3}$ (more, if the deviating candidate is the businessman, who also reduces his expected compensation payment).

4. Exactly two candidates $i = 1,2$ have a chance of winning in the second round, with the two candidates occupying (either through commitment to that policy or because that policy is implied by noncommitment) positions some distance Δ on either side of x_m. But then:

   (a) when both of the winning candidates have committed to their policies, by the logic of the case where all commit, the third candidate can adopt either of the two winning positions, gaining $\frac{v}{4}$.

   (b) when one of the two winning candidates has not committed, the third candidate can adopt either of the winning positions and gain at least $\frac{v}{4}$ (and perhaps more, since if the deviating candidate is the businessman, he can adopt the policy $\overline{x_i}$ implied by the noncommitment of some winning candidate i and reduce his expected compensation payment).

5. All three candidates have an equal probability of winning in the second round, with the three candidates $i = 1,2,3$ occupying either through commitment or noncommitment the same position $x \neq x_m$. But then any of the three candidates can instead commit to a position some infinitesimal ε towards x_m and win outright, resulting in essentially the same policy payoff but gaining that candidate at least $\frac{2V}{3}$ (more, if the deviating candidate is the businessman

and one of the professional politicians has not committed, since the businessman no longer need pay compensation with positive probability).

6. All three candidates win in the second round with some positive probability, with two candidates occupying a position (either through commitment or noncommitment) some distance Δ to one side of x_m, and the other candidate a position the same distance Δ to the other side, where $\Delta \equiv (x_B - x_m)$. But then by the logic of point 6 in the discussion of the case where all commit, the candidate alone to one side of x_m can instead adopt x_m and win for sure, gaining that candidate at least $\frac{v}{2}$ (more, if the deviating candidate is the businessman and one of the professional politicians has not committed, since the businessman no longer need pay compensation with positive probability) while increasing his policy payoff. □

6.3 Proof of Proposition 4

We first show that for certain parameter values there exists an equilibrium in which L and B enter. By Proposition 2, in equilibrium each candidate will commit to x_m, giving an expected policy payoff of $-\gamma_i E(x_m - x_i)^2$ for player $i \in \{L, R, B\}$. (In all that follows, recall that by assumption q and v are vanishingly small and thus can be ignored whenever there is a discrete difference in utility from other factors.) Thus:

1. R will not enter if the cost of entry q is greater than his expected gain in exogenous rents from holding office $\frac{v}{3}$: If he enters, by Proposition 3 all candidates will commit to x_m, giving R the same expected policy payoff, gaining him $\frac{v}{3}$ (since he wins with probability $\frac{1}{3}$), and costing him q.

2. L will not exit, since then B will win unopposed, giving L a policy payoff of $-\gamma_L (x_B - x_L)^2$, which is less than $-\gamma_L E(x_m - x_L)^2$ due to our assumptions that a) x_m is distributed on some interval $T \subset [\mu - \delta, \mu + \delta]$, where $\mu = E(x_m)$ and $\delta = (x_B - \mu)$, and b) $(\mu - \delta) < x_L < \mu$. (To see this, note that (a) and (b) together imply that $(x_m - x_L)^2 \leq (x_B - x_L)^2$ for all realizations of x_m.)

3. B will not exit if his equilibrium payoff $\left(-\gamma_B E(x_m - x_B)^2 - k + \frac{v}{2}\right)$ is greater than his payoff from exiting. Clearly, his payoff from not entering depends on whether L will commit or not

commit when running unopposed off the equilibrium path, since in either case L will win. If L does commit, he will commit to x_L, his most preferred policy, and this is clearly less preferable to B than L's not committing (since then B has no opportunity to move L's policy by lobbying *ex post*). Thus, it is sufficient to show that for k sufficiently small B prefers the lottery from receiving an uncertain x_m to receiving x_L with certainty, i.e. to show that there exists some combination of x_L, x_B, and distribution $H(\cdot)$ (of x_m) such that:

$$-\gamma_B E(x_m - x_B)^2 > -\gamma_B (x_L - x_B)^2 \tag{17}$$

To verify that such an equilibrium exists, observe that for x_L arbitrarily close to $(\mu - \delta)$, where $\delta = (x_B - \mu)$, $(x_m - x_B)^2 \leq (x_L - x_B)^2$ for all realizations of x_m, since by assumption x_m is distributed on some interval $T \subset [\mu - \delta, \mu + \delta]$. (Note that this equilibrium will be more likely when a) k is small, and b) $(x_B - x_L)$ is large.)

Next we show that there exist no other equilibria where B enters. Assume to the contrary that such an equilibrium exists. There are three possibilities:

1. B enters alone. But then by the logic of point (2) above, L will also want to enter.

2. R and B enter, but L does not. But then B will want to exit, since by exiting R will implement (depending on his strategy off the equilibrium path) either x_R (if R commits when running unopposed, in which case R will commit to his most preferred policy) or $\bar{x}(R)$ (if R does not commit when running unopposed). (Recall that Proposition 1 shows that if R does not commit and wins, then he will be compensated by B such that he receives exactly the same utility as if he had implemented x_R.) Of these two possibilities, clearly implementing x_R is worse from B's point of view, so that if B prefers not to enter when R commits off the equilibrium path, he will also prefer not to enter when R does not commit off the equilibrium path. Thus, it is sufficient to show that the policy payoff from accepting the lottery over an uncertain x_m is worse than from accepting a certain x_R:

$$-\gamma_B E(x_m - x_B)^2 < -\gamma_B (x_R - x_B)^2 \tag{18}$$

$$(x_R - x_B)^2 < E(x_m - x_B)^2 \tag{19}$$

$$(x_R)^2 - 2x_B x_R < E\left[(x_m)^2\right] - 2x_B\mu \tag{20}$$

where we recall that $\mu = E(x_m)$. Denoting the variance of x_m as $v(x_m)$, we can use the fact that $v(x_m) = E\left[(x_m)^2\right] - \mu^2$ to rewrite (20) as:

$$(x_R)^2 - 2x_B x_R < v(x_m) + \mu^2 - 2x_B\mu \tag{21}$$

$$v(x_m) > (x_R)^2 - \mu^2 - 2x_B(x_R - \mu) \tag{22}$$

Since the variance of a random variable is always positive, for (22) to hold it is sufficient to show that the right-hand side is negative:

$$(x_R)^2 - \mu^2 - 2x_B(x_R - \mu) < 0 \tag{23}$$

$$(x_R + \mu)(x_R - \mu) < 2x_B(x_R - \mu) \tag{24}$$

which is true since $x_B > x_R > \mu$.

3. *L*, *R*, and *B* all enter. But then *B* will want to exit, since by Lemmas 2 and 3 the policy payoff is the same whether there are three candidates or two, and by exiting *B* can save the entry cost *k*.

6.4 Proof of Proposition 6

By Lemmas 2 and 3, in any equilibrium with two or three candidates all candidates commit to x_m. But then:

- There is no equilibrium where both businessmen and the professional politician enter, since either businessman may deviate and receive the same policy payoff while saving the cost of entry *k*.

- There is no equilibrium where one businessman and the professional politician enter. To see this, observe that if the businessman deviates so that the professional politician *P* is the only candidate, *P* will either commit to his ideal point μ or not commit. Clearly committing is worse for the businessman, since then he cannot lobby the politician *ex post*. But a commitment to μ is better for either businessman *B* than the lottery from receiving an uncertain x_m:

$$-\gamma_B(x_B - \mu)^2 > -\gamma_B E(x_B - x_m)^2 \tag{25}$$

since $\mu = E(x_m)$.

- There is no equilibrium where a businessman enters alone, by the logic of point 2 in the first part of the proof of Proposition 4.

6.5 Proof of Proposition 7

Policy choice and compensation when a businessman has won the election follow Proposition 1, since then there is only one businessman to lobby. Note in particular that the policy that maximizes the joint surplus of the two businessmen is $\left(\frac{\gamma_B}{\gamma_B+\gamma_B}x_{BL} + \frac{\gamma_B}{\gamma_B+\gamma_B}x_{BR}\right) = \mu$. When a politician has won the election, we exploit the fact that globally truthful compensation schedules imply that the policy chosen will maximize the joint surplus of the politician and the businessmen (which again means that the policy chosen will be μ), and that the compensation paid by either businessman must leave the politician with a payoff equal to that if the politician had instead chosen policy based on the other businessman's compensation schedule alone. For example, the compensation paid by *BL* must satisfy:

$$-\gamma_P(\mu-\mu)^2 + \hat{C}_{BL}(P) + \hat{C}_{BR}(P) = \tag{26}$$
$$-\gamma_P(\hat{x}_{BR}(P)-\mu)^2 + \left[\hat{C}_{BR}(P) + \gamma_{BR}(\mu - x_{BR})^2 - \gamma_{BR}(\hat{x}_{BR}(P) - x_{BR})^2\right]$$

The term in brackets represents the compensation paid by *BR* if $\hat{x}_{BR}(P)$ (the policy that maximizes the joint surplus of *BR* and *P*) rather than μ is implemented, reflecting the fact that *BR*'s compensation schedule is globally truthful. Simplifying gives the equilibrium contribution.

6.6 Businessman Candidates for Governor in Russia, 1997-2003

Note: The following (likely partial) list, derived from Russian Central Election Commission data and newspaper accounts, is limited to those businessman candidates who received at least 10 percent of the vote in the first round of voting. Winning candidates are listed in bold; candidates not winning but advancing to the second round of voting are listed in italics.

Sergei Levchenko (Irkutskskaia Oblast', 7/27/1997), 18.82%
Iurii Antaradonov (Republic of Altai, 12/14/1997), 23.28%
Aleksandr Tikhonov (Moskovskaia Oblast', 12/19/1999), 15.12%
Pavel Gurkalov (Orenburzhskaia Oblast', 12/19/1999), 23.16%

Aleksandr Kirilichev (Primorskii Krai, 12/19/1999), 20.46%
Sergei Potapov (Tverskaia Oblast', 12/19/1999), 12.49%
Boris Korsunskii (Evreiskaia Avtonomnaia Oblast', 3/26/2000), 25.71%
Andrei Soluianov (Republic of Udmurtiia, 10/15/2000), 12.17%
Viktor Bibikov (Pskovskaia Oblast', 11/12/2000), 15.12%
Nikolai Bagretsov (Kurganskaia Oblast', 11/26/2000), 22.05%
Georgii Greshnykh (Kamchatskaia Oblast', 12/3/2000), 15.78%
Valerii Van'kov (Komi-Permiatskii Avtonomnyi Okrug, 12/3/2000), 11.04%
Vladimir Loginov (Koriakskii Avtonomnyi Okrug, 12/3/2000), 50.68%
Vladimir Markov (Riazanskaia Oblast', 12/3/2000), 10.15%
Valerii Riumin (Riazanskaia Oblast', 12/3/2000), 12.36%
Nikolai Denin (Brianskaia Oblast', 12/10/2000), 21.15%
Leonid Markelov (Republic of Marii El, 12/17/2000), 58.23%
Oleg Savchenko (Volgogradskaia Oblast', 12/24/2000), 28.31%
Roman Abramovich (Chukotskii Avtonomnyi Okrug, 12/24/2000), 90.61%
Aleksandr Shmakov (Nenetskii Avtonomnyi Okrug, 1/14/2001), 13.67%
Aleksandr Khloponin (Taimyrskii (Dolgano-Nanetskii) Avtonomnyi Okrug, 1/28/2001), 61.97%
Iurii Bobylev (Amurskaia Oblast', 3/25/2001), 10.80%
Viktor Sokolovskii (Tul'skaia Oblast', 4/8/2001), 18.62%
Boris Zolotarev (Evenkiiskii Avtonomnyi Okrug, 4/8/2001), 51.8%
Sergei Dar'kin (Primorskii Krai, 5/27/2001), 23.94%
Andrei Kliment'ev (Nizhegorodskaia Oblast', 7/15/2001), 10.54%
Sergei Krechetov (Republic of Altai, 12/16/2001), 13.34%
Fedot Tumusov (Republic of Sakha (Iakutiia), 12/23/2001), 17.73%
Viacheslav Shtyrov (Republic of Sakha (Iakutiia), 12/23/2001), 45.39%
Khazret Sovmen (Republic of Adygeia, 1/13/2002), 62.84%
Vasilii Popov (Republic of Kareliia, 4/22/2002), 10.37%
Aleksandr Khloponin (Krasnoiarskii Krai, 9/8/2002), 25.25%
Nikolai Ochirov (Republic of Kalmykiia, 10/20/2002), 12.76%
Baatr Shondzhiev (Republic of Kalmykiia, 10/20/2002), 13.61%
Andrei Zinchenko (Magadanskaia Oblast', 1/26/2003), 10.20%
Mustafa Batdyev (Republic of Karachaevo-Cherkessiia, 8/17/2003), 41.67%
Anton Bakov (Sverdlovskaia Oblast', 9/7/2003), 14.43%
Sergei Veremeenko (Republic of Bashkortostan, 12/7/2003), 25.38%

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