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Merit Pay and Pain: Linking Congressional Pay to Performance

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INTRODUCTION

The American people have consistently expressed less confidence in Congress as an institution than in the other two branches of the federal government.[1] In 2010,

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1. *Confidence in Institutions*, GALLUP, INC. (last visited July 11, 2010), http://www.gallup.com/poll/1597/Confidence-Institutions.aspx [hereinafter *Confidence*, GALLUP, INC.] (showing less confidence in Congress than in the U.S. Supreme Court since 1973, when the survey first started asking about the Court, and less confidence in Congress than in the presidency since 1991, when the survey first started asking about the presidency). Since 1979, the public's confidence in Congress as an institution has nearly always underperformed public approval of the job Congress was doing at any given time by several percentage points. *Compare Confidence*, GALLUP, INC., *supra*, *and* Lydia Saad, *Congress Ranks Last in Confidence in Institutions: Fifty Percent "Very Little"/"No" Confidence in Congress Reading Is Record High*, GALLUP, INC. (last visited July 22, 2010), http://www.gallup.com/poll/141512/Congress-Ranks-Last-Confidence-Institutions.aspx [hereinafter *Congress Ranks Last*, GALLUP, INC.], *with Congress and the Public*, GALLUP, INC. (last visited Dec. 12, 2010), http://www.gallup.com/poll/1600/Congress-Public.aspx [hereinafter *Congress*, GALLUP, INC.].

confidence in Congress as an institution fell to an all-time low, below that of any other major institution in American life, including big business.[2] This was quite an accomplishment given the fact that some of Wall Street's most innovative financial products, such as subprime loans, mortgage-backed securities, and credit default swaps, nearly brought the economy to its knees between 2007 and 2010.[3] Congress earned the distinction by passing unpopular pieces of legislation like the Troubled Asset Relief Program (TARP),[4] the $787 billion stimulus bill,[5] and the health care reform act.[6] In the process, Congress added roughly $3 trillion to the national debt[7] while close to 10% of the labor force was unemployed.[8] As a result, political commentators in the media started speculating as early as the summer of 2010 that Congress would suffer its third wave election in a row for the first time since just after World War II.[9] All of this raises a simple question: How is it that a legislature whose members are directly elected can so consistently disappoint the citizens it serves?

The irony, given the democratic nature of congressional elections, would not be lost on the Founding Fathers, who noticed the same feelings toward the state legislatures of their day.[10] Of course, the Founding Fathers no more intended to set

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2. *Congress Ranks Last*, GALLUP, INC., *supra* note 1.

3. *See generally This American Life: The Giant Pool of Money* (NPR radio broadcast May 9, 2008). Although history has not yet named this turbulent time in the economy, the "Great Recession" appears to be the frontrunner for the dubious honor. *See* 2010 AP STYLEBOOK AND BRIEFING ON MEDIA LAW 127 (Darrell Christian, Sally Jacobsen & David Minthorn eds., 2010).

4. Emergency Economic Stabilization Act of 2008, Pub. L. No. 110-343, 122 Stat. 3765; *see also* Naftali Bendavid, *Rage at Government for Doing Too Much and Not Enough*, WALL ST. J., Oct. 13, 2009, at A5.

5. American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5, 123 Stat. 115; *see also* David Wessel, *Stimulus Remains Unpopular Even as It Boosts Growth*, WALL ST. J., Aug. 20, 2009, at A2.

6. Patient Protection and Affordable Care Act, Pub. L. No. 111-148, 124 Stat. 119 (2010); *see also* Scott Rasmussen & Doug Schoen, *Why Obama Can't Move the Health Care Numbers*, WALL ST. J., Mar. 10, 2010, at A21.

7. *See* U.S. DEP'T OF THE TREASURY, 2009 FINANCIAL REPORT OF THE UNITED STATES GOVERNMENT 47 (2009) [hereinafter U.S. DEP'T OF THE TREASURY, 2009 REPORT]; U.S. DEP'T OF THE TREASURY, 2008 FINANCIAL REPORT OF THE UNITED STATES GOVERNMENT 37 (2008); U.S. DEP'T OF THE TREASURY, 2007 FINANCIAL REPORT OF THE UNITED STATES GOVERNMENT 43 (2007). Although neither the *2010 Financial Report of the United States Government* nor its accrual-based financial statements were available by the time this Note went to press, the Treasury Department recorded a deficit of roughly $1.3 trillion on a modified cash basis for the 2010 fiscal year. U.S. DEP'T OF THE TREASURY, FINAL MONTHLY TREASURY STATEMENT OF RECEIPTS AND OUTLAYS OF THE UNITED STATES GOVERNMENT: FOR FISCAL YEAR 2010 THROUGH SEPTEMBER 30, 2010, AND OTHER PERIODS 2 tbl.1 (2010).

8. *Household Data Historical, Table A-1: Employment Status of the Civilian Noninstitutional Population 16 Years and Over, 1970 to Date*, BUREAU OF LABOR STATISTICS (last visited Aug. 9, 2010), http://www.bls.gov/web/empsit/cpseea1.pdf.

9. *See, e.g.*, George F. Will, *Obama's Apogee in His Rearview Mirror: After Two Wave Elections, Democrats at Risk*, NEWSWEEK, July 12, 2010, at 29.

10. *See* 1 JAMES MADISON, THE DEBATES IN THE FEDERAL CONVENTION OF 1787 WHICH FRAMED THE CONSTITUTION OF THE UNITED STATES OF AMERICA 33 (Gaillard Hunt & James

up a democracy than they did a monarchy.[11] Instead, they thought that a constitutional republic would be best suited to ensuring liberty, protecting private property, and advancing the public interest.[12] As James Madison understood, however, the central challenge of any constitutional republic was to keep the representatives just close enough to the people that the representatives would have to follow the public will when it served the public interest, but also to keep the representatives just far enough away from the people that the representatives would be able to disregard the public will when it did not.[13] Instead of incentivizing members of Congress to act in the best interests of the American people, however, the Founding Fathers adopted a strategy of checks and balances that would hopefully frustrate political action whenever it was *not* in the best interests of the American people.[14] To the extent that any political mechanism could sufficiently motivate Congress to affirmatively act in the best interests of the American people, the Founding Fathers concluded that only directly electing members of Congress was likely to do so.[15]

Brown Scott eds., Prometheus Books 1987) (1787) (citing the viewpoint of one delegate, Elbridge Gerry, who believed that "Experience . . . had shewn that the State legislatures drawn immediately from the people did not always possess their confidence.").

11. *See* THE FEDERALIST NO. 10, at 57 (James Madison) (E.H. Scott ed., William S. Hein & Co., Inc. 2002) ("[A] pure democracy . . . can admit of no cure for the mischiefs of faction."). In Madison's view,

> [S]uch democracies have ever been spectacles of turbulence and contention; have ever been found incompatible with personal security, or the rights of property; and have, in general, been as short in their lives, as they have been violent in their deaths. Theoretic politicians, who have patronized this species of government, have erroneously supposed, that by reducing mankind to a perfect equality in their political rights, they would, at the same time, be perfectly equalized and assimilated in their possessions, their opinions, and their passions.

Id.

12. *See id.* at 57–58.

13. *See id.* at 58. As Madison explained,

> [I]t may well happen, that the public voice, pronounced by the representatives of the people, will be more consonant to the public good, than if pronounced by the people themselves, convened for the purpose. On the other hand, the effect may be inverted. Men of factious tempers, of local prejudices, or of sinister designs, may by intrigue, by corruption, or by other means, first obtain the suffrages, and then betray the interest of the people.

Id.

14. *See id.* at 56–57. Of the possible scenarios, Madison wrote,

> If a faction consists of less than a majority, relief is supplied by the republican principle, which enables the majority to defeat its sinister views, by regular vote. . . . When a majority is included in a faction . . . [they] must be rendered, by their number and local situation, unable to concert and carry into effect schemes of oppression.

Id.

15. *See* THE FEDERALIST NO. 52, *supra* note 11, at 291 (Alexander Hamilton). According to Hamilton,

> As it is essential to liberty, that the Government in general should have a common interest with the people; so it is particularly essential, that the

Despite the Founding Fathers' careful planning, the reason for the public's lack of confidence in Congress is that elections, like the institutional checks and balances of federalism and separation of powers, are necessary but not sufficient to ensure that Congress acts in the best interests of the American people.[16] Elections are not sufficient to resolve principal-agent conflicts between members of Congress and their respective constituents,[17] and even if they were, then it would still be a fallacy of composition to conclude that elections were therefore sufficient to resolve the larger-scale principal-agent conflict between the American people as a whole and Congress as an institution.[18] This Note proposes linking congressional pay to performance to incentivize members of Congress to maximize the nation's economic welfare in a way the Constitution's system of checks and balances does not.

Part I argues that principal-agent conflicts between members of Congress and their respective constituents create large agency costs in the form of severe fiscal irresponsibility. Part II describes two attempts to control narrower principal-agent conflicts at the state level—New York's No Budget, No Pay Law and California's Proposition 1F—as well as similar congressional proposals that failed during the 1990s. Part III argues that supplementing elections with financial incentives is necessary to ensure that members of Congress will maximize the nation's economic welfare and proposes a formula called Merit Pay and Pain for determining congressional pay raises—and pay cuts—based on the performance of macroeconomic indicators. Part IV, however, argues that both No Budget, No Pay and Proposition 1F, if applied to congressional pay, would authorize future Congresses to violate the 27th Amendment, but that Merit Pay and Pain would not. Finally, Part V responds to possible counterarguments and identifies ways to improve Merit Pay and Pain depending on the results it actually produces.

I. THE ELECTORAL AGENCY CONFLICT

The American people's lack of confidence in Congress is the result of principal-agent conflicts that impose large agency costs on the nation in the form of severe fiscal irresponsibility.[19] Based on polling and focus groups, Luntz argued that the American people's anger at the federal government during the Great Recession arose from their inability to impose accountability for poor results.[20] This popular

> [legislative branch] should have an immediate dependence on, and an intimate sympathy with, the people. Frequent elections, are unquestionably the only policy, by which this dependence and sympathy can be effectually secured.

Id.

16. *See infra* Parts I.B, III.A.

17. *See infra* notes 208–14 and accompanying text.

18. *See generally* JAMES M. BUCHANAN & GORDON TULLOCK, THE CALCULUS OF CONSENT: LOGICAL FOUNDATIONS OF CONSTITUTIONAL DEMOCRACY 220–22 (1962) (describing institutional mechanisms like bicameralism as attempts to limit the ability of electoral coalitions as small as one-quarter of a population from acting against the best interests of the rest of the population by successfully electing and controlling a majority of the representatives in the legislature).

19. *See id.* Buchanan and Tullock would label these costs "external costs." *See id.*

20. FRANK I. LUNTZ, WHAT AMERICANS REALLY WANT . . . REALLY: THE TRUTH ABOUT

criticism of Congress suggests the presence of electoral agency conflicts in which members of Congress have an interest in enacting policies against the best interests of their respective constituents.[21] This criticism also closely parallels both the scholarly debate over the existence of government failures[22] and Madison's concerns over the structure of the Constitution and the federal government.[23] When viewed through the lens of an electoral agency conflict, the chronically poor fiscal performances of the federal government and state governments like those of New York and California bear a striking resemblance to the agency costs a rational principal should try to minimize.[24]

A. Politicians as Agents

The concept of agency is critical to understanding economic and legal relationships between people.[25] In economic theory, a principal-agent relationship arises when a principal engages an agent to perform services on the principal's behalf and delegates some decision-making authority to the agent.[26] The agent has an advantage over the principal because the agent has superior information about the wisdom of decisions he makes and the level of effort he exerts.[27] Because both the principal and the agent seek to maximize their own welfare, the agent will not always act in the principal's best interests.[28] This principal-agent conflict—the divergence between the agent's decisions and those that would serve the principal's

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OUR HOPES, DREAMS, AND FEARS 121 (2009) ("Americans have seen politicians govern without accountability and spend money with abandon while we fall further into personal, national, and generational debt.").

21. *See* John R. Hibbing, *How to Make Congress Popular*, 27 LEGIS. STUD. Q. 219, 238 (2002). According to Hibbing,

> Many ordinary people are convinced that the relatively large congressional salary . . . and accompanying package of perquisites . . . is so desirable that members become primarily concerned with getting reelected so that they can continue to belly up to the public trough. The professionalization of government has led many people to conclude that members' desire for reelection is entirely self-serving.

Id.

22. *See infra* notes 52–64 and accompanying text.

23. *See infra* notes 70–71 and accompanying text.

24. *See infra* Part I.B.

25. *See* RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 114, 419–21 (7th ed. 2007).

26. Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305, 308 (1976). There may be more than one principal or more than one agent involved in any given principal-agent relationship. *Id.*

27. POSNER, *supra* note 25, at 114. Thus the quip that "[a]ll professions are conspiracies against the laity." GEORGE BERNARD SHAW, THE DOCTOR'S DILEMMA (1906), *reprinted in* THE DOCTOR'S DILEMMA, GETTING MARRIED, & THE SHEWING-UP OF BLANCO POSNET 81, 106 (Constable & Co. Ltd. 1947).

28. Jensen & Meckling, *supra* note 26, at 308. Because the agent bears the full cost of his effort but does not enjoy the full benefit of his effort—at least some of which should accrue to the principal—he will not exert as much effort as would maximize the principal's welfare. LUCIAN BEBCHUK & JESSE FRIED, PAY WITHOUT PERFORMANCE: THE UNFULFILLED PROMISE OF EXECUTIVE COMPENSATION 16 (2004).

best interests—results in a loss of the welfare the principal could otherwise have expected to gain from the transaction.[29]

For the principal to maximize the welfare he actually gains from the transaction, either the principal must bear monitoring costs to ensure that the agent will act in his best interests, the agent must bear bonding costs to guarantee that he will not act against the principal's best interests, or both.[30] Agency costs represent the principal's total loss in expected welfare that results from monitoring costs, bonding costs, and any other residual losses in expected welfare that the principal was not able to incentivize away.[31] The principal-agent problem is simply a question of how to reduce these agency costs to the greatest possible extent and at the lowest possible cost.[32]

In agency law, the definition is much narrower, with a principal-agent relationship arising only when a principal manifests his consent to an agent acting on his behalf and subject to his control, and when the agent consents to act accordingly.[33] This moment is important because from this point forward, the agent has a fiduciary duty to act in the principal's best interests in all matters connected with the principal-agent relationship.[34] Specific duties may vary in their contours across states, but they will generally fall into the categories of the duty of loyalty[35] and the duty of care.[36] If the agent breaches or threatens to breach any of these duties, then the principal can sue for legal damages or equitable relief, respectively.[37] Imposing fiduciary duties on the agent gives him an incentive to reduce agency costs by forcing the agent to internalize those costs.[38] As a practical matter, however, the agent's desire to protect his professional reputation and to earn repeat business also gives the agent an incentive to reduce agency costs.[39]

Perhaps the most familiar context in which fiduciary duties arise is in the corporate setting.[40] In an economic sense, corporate directors and officers act as the agents of the shareholders, but to maintain the legal fiction necessary for limited liability, the courts view the directors and officers as agents of the corporation.[41]

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29. Jensen & Meckling, *supra* note 26, at 308.

30. *Id.*

31. *Id.* These losses resemble the deadweight loss that results from monopoly power or excise taxes. *See* POSNER, *supra* note 25, at 284–87, 515–18.

32. *See* Sanford J. Grossman & Oliver D. Hart, *An Analysis of the Principal-Agent Problem*, 51 ECONOMETRICA 7, 9–10 (1983).

33. *See, e.g.*, RESTATEMENT (THIRD) OF AGENCY § 1.01 (2006). Agency law uses this narrower definition in part to draw one of the major lines between the cases in which a principal will bear liability for his contracting party's contracts and torts, and those in which he will not. *See* POSNER, *supra* note 25, at 114 ("In all these cases the law is allocating responsibility to the person who can avoid the mistake at lowest cost . . . .").

34. *See, e.g.*, RESTATEMENT (THIRD) OF AGENCY § 8.01 (2006).

35. *See, e.g.*, *id.* §§ 8.02–8.06.

36. *See, e.g.*, *id.* §§ 8.07–8.12.

37. *See, e.g.*, *id.* § 8.01 cmt. d; *see also* RESTATEMENT (SECOND) OF TORTS § 874 (1979).

38. *See* POSNER, *supra* note 25, at 114.

39. *See* Robert Cooter & Bradley J. Freedman, *The Fiduciary Relationship: Its Economic Character and Legal Consequences*, 66 N.Y.U. L. REV. 1045, 1073 (1991).

40. *See* BEBCHUK & FRIED, *supra* note 28, at 45–48.

41. *See* Lynn A. Stout, *The Mythical Benefits of Shareholder Control*, 93 VA. L. REV.

Under the influential corporate law of Delaware, for example, directors and officers owe the corporation a duty of loyalty[42] and a duty of care.[43] If a director or an officer breaches or threatens to breach any of these duties, then a shareholder can bring a derivative suit to obtain legal damages or equitable relief for the corporation.[44] Imposing these duties on directors and officers gives them an incentive to reduce agency costs by forcing directors and officers to internalize those costs.[45] Again, as a practical matter, a director or officer's desire to protect his professional reputation and to earn repeat business also gives him an incentive to reduce agency costs.[46]

Although scholars usually apply the principal-agent model to contractual dealings and business transactions, many scholars have applied it to the relationships between Congress and executive agencies.[47] These scholars cast Congress as the principal trying to control an agency whose interests conflicted with Congress's interests when Congress had imperfect information.[48] Wittman has

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789, 804–05 (2007).

42. *E.g.*, Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1280 (Del. 1989) (oral decision issued 1988). The duty of loyalty includes lesser duties that are specific applications of the duty of loyalty. *E.g.*, Broz v. Cellular Info. Sys. Inc., 673 A.2d 148, 154–55 (Del. 1996) (corporate opportunity doctrine); Sinclair Oil Corp. v. Levien, 280 A.2d 717, 720 (Del. 1971) (dominant shareholder's duty to minority shareholders). The language of a triad of fiduciary duties including a duty of good faith became popular after the Delaware Supreme Court suggested that the duty of good faith was an independent fiduciary duty. *E.g.*, Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 361 (Del. 1993). The Delaware Supreme Court has since disapproved of this interpretation, explaining that the duty of good faith was not a separate fiduciary duty in its own right but rather a specific application of the duty of loyalty. Stone v. Ritter, 911 A.2d 362, 370 (Del. 2006).

43. *E.g.*, *In re* Caremark Int'l Inc. Derivative Litig., 698 A.2d 959, 967–70 (Del. Ch. 1996). The duty of care includes a duty not to waste corporate assets, but it is extremely limited because the business judgment rule subjects claims of waste to what amounts to a rational-basis test. *See, e.g.*, Shlensky v. Wrigley, 237 N.E.2d 776, 779–81 (Ill. App. Ct. 1968). For a rare example of a successful waste claim, see Dodge v. Ford Motor Co., 170 N.W. 668, 683–85 (Mich. 1919).

44. *See* Tooley v. Donaldson, Lufkin & Jenrette, Inc., 845 A.2d 1031, 1036–39 (Del. 2004) (explaining the difference between a derivative suit and a direct suit).

45. Roberta Romano, *The Shareholder Suit: Litigation Without Foundation?*, 7 J.L. ECON. & ORG. 55, 55 (1991).

46. Eugene F. Fama & Michael C. Jensen, *Separation of Ownership and Control*, 26 J.L. & ECON. 301, 313–15 (1983). *But see* BEBCHUK & FRIED, *supra* note 28, at 35–36 (describing this as the "official story" in the context of executive compensation and expressing skepticism of its veracity in that context).

47. *E.g.*, Jeffrey S. Banks & Barry R. Weingast, *The Political Control of Bureaucracies Under Asymmetric Information*, 36 AM. J. POL. SCI. 509, 512–15 (1992); Dietmar Braun, *Who Governs Intermediary Agencies? Principal-Agent Relations in Research Policy-Making*, 13 J. PUB. POL'Y 135, 136–41 (1993); Randall L. Calvert, Mathew D. McCubbins & Barry R. Weingast, *A Theory of Political Control and Agency Discretion*, 33 AM. J. POL. SCI. 588, 590–95 (1989); M. Albert Vachris, *Federal Antitrust Enforcement: A Principal-Agent Perspective*, 88 PUB. CHOICE 223, 224–27 (1996); Barry R. Weingast, *The Congressional-Bureaucratic System: A Principal Agent Perspective (with Applications to the SEC)*, 44 PUB. CHOICE 147, 151–58 (1984).

48. *See, e.g.*, Weingast, *supra* note 47, at 153–55 (arguing, however, that competition

argued that this model could be theoretically unsound if one underestimated the effect of long-term relationships on the asymmetry of information between Congress and the executive agency.[49] He argued that repeated interactions with an agency gave Congress sufficient information to enforce its goals on the agency.[50] To arrive at the conclusion that agency costs were minimal in these settings, however, Wittman effectively had to assume that Congress's goals were indistinguishable from Congress's best interests.[51]

Although its degree may vary in different situations, asymmetry of information is one of the premises that drive principal-agent conflicts at the individual and organizational level, as well as market failures and government failures in the aggregate.[52] A market failure occurs when an economy produces results that are inefficient.[53] The usual causes of these failures include imperfect competition, imperfect information, externalities, and public goods.[54] For years, economists advised policy makers to adopt policies that would address these market failures whenever they arose.[55] The problem with such advice, according to public choice scholars, was that it incorrectly assumed that government intervention was costless.[56] Instead, when the government attempts to resolve a market failure and produces a result that is even less efficient than the market failure, a government failure occurs.[57] The usual causes of these failures include voting rules, imperfect competition among governments, imperfect information, and rent seeking.[58]

The popular and academic concern over government failures warrants more emphasis on the obvious application of the principal-agent model to the familiar relationship between members of Congress and their constituents.[59] At least in the

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among agencies for budgetary resources would reduce asymmetric information).

49. DONALD A. WITTMAN, THE MYTH OF DEMOCRATIC FAILURE: WHY POLITICAL INSTITUTIONS ARE EFFICIENT 102–08 (1995).

50. *Id.*

51. *See id.*

52. *See* Charles Wolf, Jr., *Market and Non-Market Failures: Comparison and Assessment*, 7 J. PUB. POL'Y 43, 51, 60–61 (1987).

53. Francis M. Bator, *The Anatomy of Market Failure*, 72 Q.J. ECON. 351, 351 (1958). For a basic overview of the precise meanings of Pareto efficiency and Kaldor-Hicks efficiency, see DAVID W. BARNES & LYNN A. STOUT, THE ECONOMICS OF CONSTITUTIONAL LAW AND PUBLIC CHOICE 1–3 (1992).

54. *See generally* N. GREGORY MANKIW, PRINCIPLES OF MICROECONOMICS (5th ed. 2009).

55. GORDON TULLOCK, ARTHUR SELDON & GORDON L. BRADY, GOVERNMENT FAILURE: A PRIMER IN PUBLIC CHOICE ix (2002).

56. *See* BUCHANAN & TULLOCK, *supra* note 18, at 43–46 (arguing that consenting to collective action required an individual to endure external costs and decision-making costs).

57. Roland N. McKean, *The Unseen Hand in Government*, 55 AM. ECON. REV. 496, 497–502, 505 (1965).

58. *See generally* TULLOCK ET AL., *supra* note 55.

59. *See* Terry M. Moe, *The New Economics of Organization*, 28 AM. J. POL. SCI. 739, 765–66 (1984) ("Citizens are principals, politicians are their agents. Politicians are principals, bureaucrats are their agents."). For an overview of theoretical work applying the principal-agent model to the relationship between members of Congress and their respective constituents, see generally TIMOTHY BESLEY, PRINCIPLED AGENTS? THE POLITICAL ECONOMY OF GOOD GOVERNMENT (2006). For specific examples, see HANS GERSBACH, DESIGNING

economic sense, members of Congress clearly act as the agents of their constituents by representing them and making laws on their behalf[60] after receiving their consent in elections.[61] Downs's theory of rational ignorance would suggest an asymmetry of information that would give politicians space to pursue their own interests at the expense of their constituents' interests.[62] Wittman countered that long-term relationships could mitigate problems of asymmetrical information in this context, too.[63] Again, however, to arrive at the conclusion that agency costs were minimal in these settings, Wittman had to implicitly assume that the popular will was indistinguishable from the public interest.[64]

The classical formulation of the principal-agent conflict, however, does not require an assumption that the public will is congruent with the public interest.[65] Indeed, scholars have been fond of pointing to the story of Odysseus's men ignoring his orders to steer his ship toward the sirens' song[66] as an example of agents serving the principal's best interests by ignoring his express wishes.[67] Arguably, several empirical studies on "shirking" and "slacking" in congressional voting did not even expressly address the issue of whether to equate the popular will with the public interest in their research designs.[68] More importantly, the theoretical literature on the application of the principal-agent model to the relationship between a government's political branches and its central bank has expressly acknowledged that a legislature might want to empower the central bank

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DEMOCRACY: IDEAS FOR BETTER RULES 11–17 (2005); Robert J. Barro, *The Control of Politicians: An Economic Model*, 14 PUB. CHOICE 19, 26–32 (1973); Stephen Coate & Stephen Morris, *On the Form of Transfers to Special Interests*, 103 J. POL. ECON. 1210, 1214–15 (1995); John Ferejohn, *Incumbent Performance and Electoral Control*, 50 PUB. CHOICE 5, 11–14 (1986); Markus Müller, *Motivation of Politicians and Long-Term Policies*, 132 PUB. CHOICE 273, 275–78 (2007); Torsten Persson, Gerard Roland & Guido Tabellini, *Separation of Powers and Political Accountability*, 112 Q.J. ECON. 1163, 1165–67 (1997).

60. *See* U.S. CONST. art. I, § 8.

61. *See id.* art. I, § 2, cl. 1; *id.* amend. XVII. The choice between a democracy and a constitutional republic is a question of whether to bear the higher decision-making costs of bargaining with more decision makers or to accept the higher external costs that arise from delegating decision-making authority to an agent who may not always be loyal. *See* BUCHANAN & TULLOCK, *supra* note 18, at 220–22.

62. *See* ANTHONY DOWNS, AN ECONOMIC THEORY OF DEMOCRACY 214–16, 247–57 (1957).

63. WITTMAN, *supra* note 49, at 20–27.

64. *See id.* at 27–30.

65. *See supra* notes 26–32 and accompanying text.

66. HOMER, THE ODYSSEY 136 (Samuel Butler trans., Red & Black Publishers 2008) ("'Therefore, take me and bind me to the crosspiece half way up the mast; bind me as I stand upright, with a bond so fast that I cannot possibly break away, and lash the rope's ends to the mast itself. If I beg and pray you to set me free, then bind me more tightly still.'").

67. *See, e.g.*, Stephen M. Bainbridge, *Precommitment Strategies in Corporate Law: The Case of Dead Hand and No Hand Pills*, 29 J. CORP. L. 1, 1–2 (2003).

68. *See, e.g.*, Joseph P. Kalt & Mark A. Zupan, *The Apparent Ideological Behavior of Legislators: Testing for Principal-Agent Slack in Political Institutions*, 33 J.L. & ECON. 103, 110–11 (1990); Keith T. Poole & Thomas Romer, *Ideology, "Shirking," and Representation*, 77 PUB. CHOICE 185, 186–88 (1993); Lawrence S. Rothenberg & Mitchell S. Sanders, *Severing the Electoral Connection: Shirking in the Contemporary Congress*, 44 AM. J. POL. SCI. 316, 317–19 (2000).

to ignore the legislature's demands for an inflationary monetary policy on the ex ante understanding that a stable currency better served the legislature's interests.[69]

Likewise, James Madison's goal of controlling factions resembled Odysseus's precommitment strategy and contravened Wittman's implicit assumption that the public will and the public interest were the same thing.[70] As Madison observed, "[I]t may well happen, that the public voice, pronounced by the representatives of the people, will be more consonant to the public good, than if pronounced by the people themselves, convened for the purpose."[71] Moreover, it is easy to see why members of Congress might pursue policies that are not in the best interests of their respective constituents but *appear* to be in their constituents' best interests if one accepts Mayhew's assumption that members of Congress are single-minded reelection seekers.[72] As Mayhew argued,

> [C]ongressmen are judged by positions rather than effects, . . . [so] they are much inclined to incorporate popular conceptions of instrumental rationality into the statute books. Attentive publics judge positions on means as well as on ends. Hence the congressional penchant for the blunt, simple action—the national debt limit, the minimum wage, the price rollback, the 10 percent across-the-board budget slash, the amendment cutting off aid to Communist countries, the amendment ending the Vietnam War in ninety days.[73]

In other words, in order to get reelected, a member of Congress might have to take symbolic positions and even particular actions that a majority of his constituents favored, even though he knew full well that these actions would harm his constituents' interests.[74] The darker view from the Virginia school of public choice

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69. *E.g.*, Ben Lockwood, *State-Contingent Inflation Contracts and Unemployment Persistence*, 29 J. MONEY, CREDIT & BANKING 286, 289–91 (1997); Torsten Persson & Guido Tabellini, *Designing Institutions for Monetary Stability*, 39 CARNEGIE-ROCHESTER CONF. SERIES ON PUB. POL'Y 53, 56–60 (1993); Lars E.O. Svensson, *Optimal Inflation Targets, "Conservative" Central Banks, and Linear Inflation Contracts*, 87 AM. ECON. REV. 98, 98–100 (1997); Carl E. Walsh, *Optimal Contracts for Central Bankers*, 85 AM. ECON. REV. 150, 151–52 (1995).

70. *See* THE FEDERALIST NO. 10, *supra* note 11, at 54 (James Madison) ("By a faction, I understand a number of citizens, whether amounting to a majority or minority of the whole, who are united and actuated by some common impulse of passion, or of interest, *adverse to* the rights of other citizens, or to the permanent and *aggregate interests of the community*." (emphasis added)); 2 MADISON, *supra* note 10, at 619 (noting that countries in which suffrage was contingent on owning property risked oppressing personal rights, but countries in which suffrage was universal risked oppressing property rights).

71. THE FEDERALIST NO. 10, *supra* note 11, at 58 (James Madison).

72. DAVID R. MAYHEW, CONGRESS: THE ELECTORAL CONNECTION 16 (1974) (acknowledging that members of Congress might have additional goals but arguing that reelection was "the *proximate* goal of everyone, the goal that must be achieved over and over if other ends are to be entertained" (emphasis in original)); *see also* RICHARD F. FENNO, JR., CONGRESSMEN IN COMMITTEES 1 (1973) (listing getting reelected, achieving influence in Congress, and making good public policy as possible goals that sometimes conflict).

73. MAYHEW, *supra* note 72, at 138 (citations omitted).

74. *See id.*

is that the majority vote of a legislative body composed of members elected by a majority vote could actually express the will of as little as one-fourth of the total population to form logrolling coalitions to impose external costs on other citizens.[75]

Regardless of the exact nature of an electoral agency conflict, it is not at all clear that fiduciary lawsuits and performance-based pay are sufficient to eliminate agency costs in the corporate context.[76] In the political context, however, neither fiduciary duties, let alone causes of action to enforce them, nor performance-based pay even exist.[77] Even so, several scholars who have applied the principal-agent model to central bankers have considered which types of incentive contracts would best align the banker's interests with the public's interest in sound monetary policy.[78] Likewise, several scholars have also considered which types of incentive contracts would resolve electoral agency conflicts between constituents and politicians.[79] Given the lack of such mechanisms to resolve electoral agency conflicts in the real world, however, the principal-agent model would predict that the American people are suffering very real electoral agency costs as a result.[80]

B. Fiscal Irresponsibility as an Agency Cost

The most visible electoral agency cost is the national debt, which the federal government has traditionally characterized as federal debt held by the public and federal debt held by government trust funds and other government accounts.[81] In 2010, the Congressional Budget Office (CBO) predicted that public debt would reach 62% of the nation's gross domestic product (GDP) by the end of fiscal year (FY) 2010.[82] The CBO also predicted that intragovernmental debt would surpass 30% of GDP by the same time.[83] The CBO has justified distinguishing between the

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75. BUCHANAN & TULLOCK, *supra* note 18, at 220–22. As an example, Buchanan and Tullock considered a nation of twenty-five voters organized into five equal constituencies that elected representatives by a majority vote. *Id.* If the legislature also followed a simple majority rule, then the will of the legislature might reflect the will of only nine of the twenty-five voters. *Id.* Voters would simply have to rely on the structure of the legislature to mitigate this risk. *Id.*

76. *See* BEBCHUK & FRIED, *supra* note 28, at 23–52.

77. POSNER, *supra* note 25, at 564; Timothy Besley, *Paying Politicians: Theory and Evidence*, 2 J. EURO. ECON. ASS'N 193, 197 (2004).

78. *E.g.*, Lockwood, *supra* note 69, at 293–96; Persson & Tabellini, *supra* note 69, at 66–70; Svensson, *supra* note 69, at 105; Walsh, *supra* note 69, at 158–60.

79. *E.g.*, GERSBACH, *supra* note 59, at 11–17; Barro, *supra* note 59, at 26–32; Coate & Morris, *supra* note 59, at 1214–15; Ferejohn, *supra* note 59, at 11–14; Müller, *supra* note 59, at 275–78; Persson et al., *supra* note 59, at 1165–67.

80. *See supra* notes 26–32 and accompanying text.

81. CONG. BUDGET OFFICE, THE BUDGET AND ECONOMIC OUTLOOK: FISCAL YEARS 2010 TO 2020, at 117 (2010) [hereinafter CONG. BUDGET OFFICE, BUDGET AND ECONOMIC OUTLOOK]. Government agencies customarily refer to federal debt held by the public as "public debt," debt held by government trust funds and other accounts as "intragovernmental debt," and the total national debt as "gross debt." *Id.* at 148.

82. CONG. BUDGET OFFICE, THE LONG-TERM BUDGET OUTLOOK 1 (2010) [hereinafter CONG. BUDGET OFFICE, LONG-TERM BUDGET OUTLOOK].

83. *See* CONG. BUDGET OFFICE, BUDGET AND ECONOMIC OUTLOOK, *supra* note 81, at 118

two components of gross debt on the grounds that unlike holding intragovernmental debt, only issuing public debt would crowd out private investment by encouraging investors to buy government bonds with funds they could have invested in private companies.[84] At least with respect to public debt, however, the CBO has warned that high levels of debt as a percentage of GDP reduce economic growth by crowding out private investment.[85]

Evidence suggests that this distinction between public and intragovernmental debt is not necessarily meaningful.[86] Using data from 1790 to 2009, Reinhart and Rogoff found that annual real GDP growth rates in the United States averaged 4.0% when gross debt remained below 30% of GDP.[87] Annual real GDP growth rates slowly declined to an average of 3.4% as gross debt grew from 30% to 60% of GDP and then declined to an average of 3.3% as gross debt grew from 60% to 90% of GDP.[88] When gross debt surpassed 90% of GDP, however, annual real GDP growth rates plummeted to an average of –1.8%.[89] Although some scholars have questioned the extent to which this correlation suggests causation,[90] acting on the theory that it does not would be taking a very large risk given the CBO's prediction that gross debt would surpass 90% of GDP by the end of FY 2010.[91] Regardless, even assuming public debt were a more consequential measure than gross debt, the CBO's most conservative forecasts predicted that public debt alone would approach 80% by the end of FY 2035.[92]

An even greater risk, however, is that growing fiscal deficits would push debt service to unsustainable levels.[93] The CBO based its official forecasts on the unrealistic assumption that current federal law would remain in place, but it also forecasted an alternative fiscal scenario based on the assumption that widely expected changes in federal law would take effect.[94] Under this gloomier forecast,

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tbl.D-2, 122 tbl.E-1 (predicting that intragovernmental debt would reach $4.5 trillion as GDP reached $14.7 trillion).

84. *Id.* at 117.

85. CONG. BUDGET OFFICE, THE FEDERAL DEBT AND THE RISK OF A FISCAL CRISIS 3 (2010) [hereinafter CONG. BUDGET OFFICE, FEDERAL DEBT].

86. Carmen M. Reinhart & Kenneth S. Rogoff, *Growth in a Time of Debt*, 100 AM. ECON. REV. 573, 573 (2010) (finding a correlation between gross debt in excess of 90% of GDP and lower average annual GDP growth rates for both advanced countries and emerging market countries).

87. *Id.* at 576 tbl.1.

88. *Id.*

89. *Id.*

90. *E.g.*, Yeva Nersisyan & L. Randall Wray, *Does Excessive Sovereign Debt Really Hurt Growth? A Critique of* This Time Is Different*, by Reinhart and Rogoff* 10–12 (Levy Econ. Inst., Working Paper No. 603, 2010).

91. *See* CONG. BUDGET OFFICE, BUDGET AND ECONOMIC OUTLOOK, *supra* note 81, at 118 tbl.D-2, 122 tbl.E-1 (predicting that gross debt would reach $13.3 trillion as GDP reached $14.7 trillion).

92. CONG. BUDGET OFFICE, LONG-TERM BUDGET OUTLOOK, *supra* note 82, at 4–7. The CBO referred to its official forecasts as its extended-baseline scenario. *Id.*

93. CONG. BUDGET OFFICE, FEDERAL DEBT, *supra* note 85, at 1, 3.

94. CONG. BUDGET OFFICE, LONG-TERM BUDGET OUTLOOK, *supra* note 82, at 2. Noting that the extended-baseline scenario did not account for changes to federal law that Congress had routinely made in the past, such as changes to the Alternative Minimum Tax and

public debt would approach 90% of GDP by FY 2020 and soar to 185% of GDP by FY 2035.[95] In a sobering report called *Federal Debt and the Risk of a Fiscal Crisis*, the CBO repeated its warning that rising levels of debt would reduce economic growth by crowding out private investment.[96] As a result, the United States would be less capable of responding to future economic downturns and international crises.[97] Instead, the nation would have no choice but to raise taxes or cut spending to reassure bond traders lest interest rates on government debt rise so sharply that the federal government could not make its payments.[98] The CBO emphasized this point with a startling review of infamous fiscal crises in Argentina, Ireland, and Greece.[99] Surprising though the implicit comparison may have been, credit rating agencies had already started warning that the federal government might lose its AAA credit rating as fears of a sovereign debt default, although still highly unlikely, rose.[100]

Although the nation's daunting fiscal position certainly looks like an agency cost resulting from the American people's inability to control their members of Congress, one could just as easily argue that it is a consequence of members of Congress following the public will when they should have been guarding the public interest.[101] For example, as popular as Social Security and Medicare may be,[102] the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance (OASDI) Trust Funds predicted in 2010 that Social Security's Old Age Survivors and Disability Insurance Trust Fund would operate in a deficit during 2010 and 2011, briefly recover from 2012 to 2014, and then operate in a deficit for the duration of the seventy-five-year period for which the trustees produced actuarial projections.[103] Medicare's Hospital Insurance (HI) Trust Fund started operating in a deficit as early as 2008.[104] The trustees predicted that these trust funds would be completely exhausted as soon as 2037 (OASDI)[105] and 2029

Medicare reimbursement rates for doctors, the CBO implied that its alternative fiscal scenario was actually the more realistic of the two. *See id.*

95. *Id.* at 6–7 & tbl.1-2.

96. CONG. BUDGET OFFICE, FEDERAL DEBT, *supra* note 85, at 3.

97. *Id.* at 4.

98. *Id.*

99. *Id.* at 4–7.

100. Joanna Slater, *Moody's Puts U.S., U.K. on Chopping Block*, WALL ST. J., Dec. 8, 2009, at C2.

101. *See* THE FEDERALIST NO. 10, *supra* note 11, at 58 (James Madison).

102. Greg M. Shaw & Sarah E. Mysiewicz, *Trends: Social Security and Medicare*, 68 PUB. OPINION Q. 394, 397 (2004); *see also* Sheryl Gay Stolberg, *Political Jitters and Social Security*, N.Y. TIMES, Feb. 6, 2005, at 4-2 (Week in Review Desk) ("The former House Speaker Thomas P. O'Neill called Social Security 'the third rail of politics,' fatal to any elected official who touched it. So when President Bush, who no longer faces re-election, grabbed hold of that rail last week, the shock coursed through those who do.").

103. BD. OF TRS., FED. OLD-AGE & SURVIVORS INS. & FED. DISABILITY INS. TRUST FUNDS, THE 2010 ANNUAL REPORT OF THE BOARD OF TRUSTEES OF THE FEDERAL OLD-AGE AND SURVIVORS INSURANCE AND FEDERAL DISABILITY INSURANCE TRUST FUNDS 2–3 (2010).

104. BDS. OF TRS., FED. HOSP. INS. & FED. SUPPLEMENTARY MED. INS. TRUST FUNDS, 2010 ANNUAL REPORT OF THE BOARDS OF TRUSTEES OF THE FEDERAL HOSPITAL INSURANCE AND FEDERAL SUPPLEMENTARY MEDICAL INSURANCE TRUST FUNDS 5 (2010).

105. BD. OF TRS., FED. OLD-AGE & SURVIVORS INS. & FED. DISABILITY INS. TRUST FUNDS,

(HI).[106] As if the long-range solvency of these two trust funds were not cause enough for concern, the present value of the unfunded liabilities of all of the federal government's social insurance programs totaled more than $45 trillion at the end of FY 2009.[107] The magnitude of the government's so-called off-budget obligations dwarfs even the gross debt about which Reinhart and Rogoff were so concerned because of its negative effects on the nation's economic welfare.[108]

At the state level, examples of far smaller electoral agency costs include New York's chronic inability to even pass budgets on time, a recurring issue since the 1970s.[109] At one point, the state legislature went some twenty years without passing a budget on time.[110] Unlike California, however, New York could not point to an initiative process that made it difficult to raise taxes and reduce spending as an excuse.[111] Regardless, the New York state legislature developed several mechanisms, such as interim appropriations bills, that allowed it to fund the state government for months without actually passing a budget.[112] Benjamin attributed this neglect in part to the trend towards professionalization in New York's state legislature, which started in the 1960s.[113] Increased institutional support made it easier for state legislators to get reelected and insulated them from external political forces.[114] As a result, New York's budget problems came to mirror the electoral agency conflict that existed at the federal level: "Majority members in both houses . . . learned from experience over decades that persistent budget imbalances, chronic lateness in budgeting, ever increasing debt burdens and attendant fiscal issues [did] not increase electoral risk. Re-election rates [were] not affected. Majority control in both houses [did] not change."[115]

California's budget problems are even worse than New York's.[116] Of forty-seven states facing projected budgets deficits in FY 2009 or FY 2010, California's were the largest, weighing in at $37.1 billion in FY 2009 and $45.5 billion in FY 2010.[117] In September 2008, the state legislature passed the 2008–2009 budget

supra note 103, at 3.

106. BDS. OF TRS., FED. HOSP. INS. & FED. SUPPLEMENTARY MED. INS. TRUST FUNDS, *supra* note 104, at 5.

107. U.S. DEP'T OF THE TREASURY, 2009 REPORT, *supra* note 7, at 51.

108. *See* Reinhart & Rogoff, *supra* note 86; *see also supra* notes 87–89 and accompanying text.

109. Gerald Benjamin, *Reform in New York: The Budget, the Legislature, and the Governance Process*, 67 ALB. L. REV. 1021, 1023 (2004).

110. *Id.* at 1022.

111. *Id.*

112. *Id.* at 1023.

113. *Id.* at 1031–38.

114. *Id.* at 1042–46; *see also id.* at 1039 (noting that New York's legislature was one of the most professionalized in the entire United States (citing Peverill Squire, *Legislative Professionalization and Membership Diversity in State Legislatures*, 17 LEGIS. STUD. Q. 69, 71–72 (1992))).

115. *Id.* at 1062.

116. *See* PEW CTR. ON THE STATES, BEYOND CALIFORNIA: STATES IN FISCAL PERIL 1–2, 64–65 (2009), http://downloads.pewcenteronthestates.org/BeyondCalifornia.pdf (discussing how fiscal problems in California overshadowed fiscal problems in other states).

117. Elizabeth McNichol, Phil Oliff & Nicholas Johnson, *Recession Continues to Batter State Budgets; State Responses Could Slow Recovery*, CTR. ON BUDGET AND POL'Y

nearly three months late only to see the budget deficit swell as the economy collapsed.[118] For the next several months, California Governor Arnold Schwarzenegger and the state legislature argued over spending cuts and tax increases while Schwarzenegger furloughed state workers and the state comptroller delayed $3.7 billion in state payments, such as tax refunds, to control cash flow problems.[119] Passing a budget was no easy task thanks to Proposition 13, a 1979 referendum that amended the California Constitution to require a two-thirds vote before the state legislature could raise taxes or revenue.[120] State legislators only passed a revised 2008–2009 budget in February 2009 after agreeing to send voters a list of proposed constitutional amendments that would reform tax and fiscal policy.[121] After five of six proposals failed in a special election,[122] however, the state comptroller started issuing IOUs,[123] prompting Fitch Ratings to lower California's bond ratings from A– to BBB.[124] Unsurprisingly, talk of letting California go bankrupt was common in early 2009.[125]

II. HALF-MEASURES

As acts of desperation, both New York and California adopted rudimentary incentive contracts to control the electoral agency conflicts in their budget processes.[126] New York's No Budget, No Pay Law withholds pay from state legislators while their annual budget is late.[127] California's Proposition 1F prevents

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PRIORITIES, tbls. 3–4 (July 15, 2010), http://www.cbpp.org/files/9-8-08sfp.pdf.

118. Evan Halper, *Legislators to Revisit the Budget; With the State's Deficit Growing, the Governor Calls an Emergency Session for Next Week to Deal with the Crisis*, L.A. TIMES, Oct. 28, 2008, at B1; Evan Halper, *State Analyst Offers Own Formula on Budget Gap; Elizabeth Hill Calls the Governor's Plan Inadequate to Close the $16-Billion Shortfall*, L.A. TIMES, Feb. 21, 2008, at B1.

119. Evan Halper & Patrick McGreevy, *Controller 'Pulls Trigger,' Suspends State Tax Refunds*, L.A. TIMES, Jan. 17, 2009, at A1.

120. CAL. CONST. art. XIIIA, § 3. Proposition 13 was far better known for capping property taxes in one of the earliest tax revolts leading up to President Ronald Regan's election in 1980. *See* Stephen M. Griffin, *California Constitutionalism: Trust in Government and Direct Democracy*, 11 U. PA. J. CONST. L. 551, 551–52, 566 (2009); *see also* CAL. CONST. art. XIIIA, § 1.

121. Patrick McGreevy, *State Resumes Tax Refunds; New Budget Allows Payments to Proceed, Ends 'Furlough Fridays,'* L.A. TIMES, Mar. 7, 2009, at A3.

122. Eric Bailey, *California Elections: Measures Spurned; Unmet Challenges; School Board Ousted; Voters Kill Budget Measures*, L.A. TIMES, May 20, 2009, at A1.

123. Eric Bailey & Patrick McGreevy, *Deadlocked State Sends Out IOUs; Nearly $5 Billion in Vouchers Could Be Issued Through August. Some Banks Will Take Them Until July 10*, L.A. TIMES, July 3, 2009, at A1; *see also* Tom Petruno, *State Set to Redeem Its IOUs*, L.A. TIMES, Aug. 28, 2009, at B5.

124. Ryan Knutson, *Big Banks Don't Want California's IOUs*, WALL ST. J., July 7, 2009, at A3.

125. *E.g.*, Steven Malanga, *Should We Let California Go Bankrupt?*, REALCLEARMARKETS (Feb. 25, 2009), http://www.realclearmarkets.com/articles/2009/02/should_we_let_california_go_ba.html (noting that California, as a sovereign state, technically could not declare bankruptcy but expressing skepticism of a government bailout).

126. *See infra* Part II.A.

127. N.Y. LEGIS. LAW § 5 (McKinney 1991 & Supp. 2010).

state legislators from receiving a pay raise in any year in which the state runs a deficit.[128] Although these laws suggest that even politicians intuitively appreciate the need for financial incentives to align their interests with those of their respective constituents, they also suggest that politicians would be characteristically shortsighted in designing their own incentive contracts.[129] Indeed, as Congress's consideration of similar proposals makes clear, politicians would also let partisan motives guide them if left to design their own incentive contracts.[130]

A. No Budget, No Pay and Proposition 1F

New York's No Budget, No Pay Law was the product of power struggles and institutional rivalries between the state's executive and legislative branches.[131] Sensing the public's displeasure with the state legislature's failure to pass its 1995 budget on time, New York Governor George Pataki threatened to withhold pay from state legislators and their staff members if the state legislature did not pass a budget by April 1, 1995.[132] For leverage, Pataki relied on a provision in the state constitution that prevented the state legislature from considering any appropriations bill without a "message from the governor certifying to the necessity of the immediate passage of such a bill" before taking action on any other appropriations bill the governor had already submitted.[133] When the state legislature failed to pass a budget by the deadline, Pataki submitted an interim appropriations bill without a provision for any legislative salaries, prompting several legislative staff members to challenge his actions in court.[134] To comply with a preliminary injunction against his actions, Pataki submitted another interim appropriations bill with a salary provision for legislative staff members but not the state legislators, drawing a challenge to his actions from several state legislators.[135] Pataki lost again, this time on the grounds of the separation of powers,[136] but the state legislature eventually passed a budget that Pataki signed on June 8, 1995.[137]

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128. CAL. CONST. art. III, § 8 (amended 2009).

129. *See* PAUL MILGROM & JOHN ROBERTS, ECONOMICS, ORGANIZATION & MANAGEMENT 228–32 (1992) (explaining that incentive contracts should equally weight all tasks of equal performance lest the agent neglect those on which compensation did not depend).

130. *See infra* notes 192–95 and accompanying text.

131. *See generally* L. Anthony Sutin, *Check, Please: Constitutional Dimensions of Halting the Pay of Public Officials*, 26 J. LEGIS. 221, 243–45 (2000) (describing the same battles between Pataki and the New York legislature recounted here).

132. Haley v. Pataki, 883 F. Supp. 816, 820, 824–25 (N.D.N.Y. 1995) (issuing a preliminary injunction on the grounds that Pataki's actions probably violated the Contracts Clause of the U.S. Constitution), *vacated as moot*, 60 F.3d 137 (2d Cir. 1995).

133. N.Y. CONST. art. VII, § 5.

134. *Haley*, 883 F. Supp. at 816.

135. Dugan v. Pataki, No. 16441/95 (Sup. Ct. Kings County, N.Y. May 30, 1995).

136. *Id.* at 5–6.

137. Haley v. Pataki, 60 F.3d 137, 140 (2d Cir. 1995) (holding that Pataki's appeal was moot because he had submitted an interim appropriations bill to pay legislative staff members in compliance with the trial court's preliminary injunction and no action the court could take could change its contents).

Pataki's maneuver to force a budget out of the state legislature may have been heavy-handed,[138] but the state legislature grudgingly acknowledged his point in 1998, when it passed No Budget, No Pay to prevent state legislators from receiving their salaries between the date a budget was due and the date the budget actually passed.[139] In particular, however, No Budget, No Pay required that once the state legislature did pass a budget, "an amount equal to the accrued, withheld and unpaid installments [should] be promptly paid to each member."[140] Nevertheless, a group of state legislators who voted against the bill filed a third lawsuit challenging its constitutionality.[141] With an actual statute on his side, however, Pataki finally prevailed, but only on appeal.[142] Calling the statute "procedural oil" for the budget process,[143] the appellate court reversed the trial court's decision in language that strongly recalled using financial incentives to solve a principal-agent problem:

> The Legislature has decided to restrict itself and discipline its own work and power . . . . [W]e view the adopted control mechanism as a credit to the Legislative Branch's internal management practices, not a mark of some ultra vires surrender of power to any other Branch. Moreover, it should not be overlooked that . . . both Houses came together with an identical bill in an effort and as an incentive to fulfill in a timely fashion their prescribed budget-related duties to the People of the State.[144]

As the appellate court seemed to appreciate, the skirmishes between the governor and the state legislature suggested that both branches recognized the existence of an electoral agency conflict and would eventually hammer out a solution as the two branches maneuvered for political position.[145]

Critics, however, perhaps failing to grasp that an electoral agency conflict was responsible for the budget's chronic lateness,[146] dismissed No Budget, No Pay as ineffective and irrational at best, and dangerous and undemocratic at worst.[147]

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138. *See* Sutin, *supra* note 131, at 245 (comparing Pataki's actions to the "reduction by famine" that Alexander Hamilton warned of in *The Federalist* No. 73).

139. N.Y. LEGIS. LAW § 5 (McKinney 1991 & Supp. 2010).

140. *Id.* § 5(1).

141. Cohen v. State, 694 N.Y.S.2d 840, 842 (N.Y. Sup. Ct. 1999), *rev'd*, 720 N.E.2d 850 (N.Y. 1999).

142. *Cohen*, 720 N.E.2d at 854 (reversing the trial court's determination that the statute violated the separation of powers doctrine and dismissing the trial court's reasoning as rhetorical flourishes).

143. *Id.* at 855.

144. *Id.* at 856.

145. *See id.*

146. *See supra* notes 109–15 and accompanying text.

147. *Compare* Editorial, *Pay the Legislators*, N.Y. TIMES, May 8, 1999, at A14 [hereinafter Editorial, *Pay the Legislators*] ("It is not acceptable for such pressure to fall unevenly on the legislators, some of whom may face tight economic circumstances."), *with* Cohen v. State, 694 N.Y.S.2d 840, 843 (N.Y. Sup. Ct. 1999) ("To place any legislator or anyone in any branch of government under undue economic pressure in exercising his or her judgment, while expecting that person to act in accordance with his or her oath of office, is

Although Sutin defended the constitutionality of the measure, he found it "curious" that No Budget, No Pay did not subject the governor's pay to the same treatment as the state legislators' pay.[148] This became the main sticking point the year after the law went into effect, when the budget was late only because the two houses of the state legislature had passed different versions of the budget.[149] As the *New York Times* complained,

> Both the Democratic-controlled Assembly and Republican-controlled Senate have passed their own versions of the budget this year. Democrats favor more spending for education and health programs than either Mr. Pataki or the Republicans in the Legislature. . . .
>
> Since the stalemate has as much to do with political advantage as principle, it is not easy to think of incentives to force a meeting of the minds.[150]

Like New York's No Budget, No Pay Law, California's attempt to use legislative pay to resolve an electoral agency conflict was also born of necessity.[151] The only way Governor Schwarzenegger and the state legislature could agree to pass their revised 2008–2009 budget and close a $24 billion shortfall[152] was if the budget resolution included six proposed constitutional amendments regarding tax and fiscal policy for the public to consider using the ballot initiative process.[153] One of those six, Proposition 1F, proposed by Republican State Senator Abel Maldonado,[154] would have prevented the state legislature and the governor from receiving pay raises in any year in which the state expected its General Fund to run a deficit.[155] In selling the measure, Maldonado remarked, "When you work hard, you ought to be proud of the work you do, and when times are good, you should be rewarded . . . . But why do we get rewarded when we do a horrible job in

illogical, unsound, and unconstitutional. The withholding of pay is palpably coercive and manifestly inhibits legislators from performing their function as an independent branch of government.").

148. Sutin, *supra* note 131, at 246.

149. *See* Editorial, *Pay the Legislators*, *supra* note 147.

150. *Id.*

151. *See supra* notes 116–25 and accompanying text.

152. Jennifer Steinhauer, *California's Solution to $24 Billion Budget Gap Is Going to Bring Some Pain*, N.Y. TIMES, June 22, 2009, at A12.

153. S.B. 19, 2009 Leg., 3d Extraordinary Sess. (Cal. 2009).

154. Wyatt Buchanan, *Move to Bar Raises If State Is in Red*, S.F. CHRON., Apr. 27, 2009, at B1.

155. DEBRA BOWEN, CAL. SEC'Y OF STATE, CALIFORNIA STATEWIDE SPECIAL ELECTION, TUESDAY, MAY 19, 2009: OFFICIAL VOTER INFORMATION GUIDE 42–43 (2009), *available at* http://voterguide.sos.ca.gov/past/2009/special/pdf-guide/complete-vig-may192009.pdf. The official procedure required the Director of Finance to certify whether he expected the Special Fund for Economic Uncertainties to run a deficit of more than 1% of the General Fund by June 30th of any given year. *Id.* If he did so, then the California Citizens Compensation Commission could not award the legislature a raise that would normally take effect in December of that year. *Id.* The restriction also applied to the governor, lieutenant governor, and several other high-ranking state officials. *Id.*

Sacramento?"[156] Maldonado had been trying unsuccessfully to get Proposition 1F on the ballot for two years, and getting it on the ballot was the price he exacted for his vote on the budget.[157] Of the six proposed constitutional amendments, only Proposition 1F passed both houses of the state legislature unanimously.[158]

Despite elite indifference[159] and occasional opposition,[160] the success of Proposition 1F was never in doubt.[161] In one poll, an overwhelming 90% of Californians supported the idea of withholding pay raises from the state legislature if it could not pass a balanced budget, and 70% supported going even further and significantly cutting state legislative pay if the budget was running a deficit.[162] On Election Day, Proposition 1F carried every county in California and passed with a popular vote of over 70%;[163] Propositions 1A through 1E all failed as spectacularly as Proposition 1F passed.[164] These other five propositions would have increased the size of the state's rainy day fund, forced the state legislature to fund local schools and community colleges, allowed the state to borrow against future lottery profits, and redirected funding from children's services and mental health programs into the General Fund.[165] They would also have had a much larger effect on California's fiscal position.[166] That voters rejected all of these propositions and approved only the one proposition that imposed any discipline on their representatives suggests that voters were most concerned about holding their electoral agents accountable.[167]

Critics of Proposition 1F argued that even if withholding a pay raise from state legislators could provide a large enough incentive to change legislative behavior, Proposition 1F's precise mechanism itself would completely undermine this incentive.[168] In fact, Proposition 1F did not amend the rule in the California Constitution that legislative pay could not decrease during a state legislator's

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156. Buchanan, *supra* note 154 (internal quotation marks omitted).

157. *Id.*

158. BOWEN, *supra* note 155, at 10, 18, 24, 32, 38, 42.

159. *E.g.*, Editorial, *It Can't Hurt; Proposition 1F Won't Do Much, but in the Spirit of Compromise, We Urge a Yes Vote*, L.A. TIMES, Apr. 28, 2009, at A22 [hereinafter Editorial, *It Can't Hurt*] ("Proposition 1F is dumb but relatively harmless.").

160. *E.g.*, Buchanan, *supra* note 154 (noting that Maldonado's own Republican Party opposed Proposition 1F).

161. *See* John Wildermuth, *5 of the 6 Measures Trailing in Poll; State's Special Election*, S.F. CHRON., Apr. 29, 2009, at A1 (reporting that 71% of voters supported Proposition 1F and only 24% opposed it as of two weeks before the election).

162. *California Voters Say Cut Government Spending, Don't Raise Taxes*, RASMUSSEN REPORTS (May 14, 2009), http://www.rasmussenreports.com/public_content/politics/general_state_surveys/california/california_voters_say_cut_government_spending_don_t_raise_taxes (subscription required).

163. DEBRA BOWEN, CAL. SEC'Y OF STATE, STATEMENT OF VOTE: MAY 19, 2009, STATEWIDE SPECIAL ELECTION 8–10, 18–20 (2009), *available at* http://www.sos.ca.gov/elections/sov/2009-special/complete-sov.pdf.

164. *Id.*

165. BOWEN, *supra* note 155, at 5–7.

166. *Id.*

167. *See* LUNTZ, *supra* note 20, at 121.

168. *E.g.*, Editorial, *It Can't Hurt*, *supra* note 159.

term.[169] Instead, Proposition 1F prevented the California Citizens Compensation Commission, a seven-member commission appointed by the governor[170] that approved pay raises for high-ranking state officials,[171] from approving pay raises for state legislators in any year in which the Director of Finance certified by June 30th that the state would run a deficit in that year.[172] As critics noted, however, since the Commission had broad discretion to approve pay raises in years when the budget ran a surplus, the Commission could simply approve larger pay raises in those years to compensate for any lost raises during deficit years.[173] In order to test this theory, however, the state legislature would first have to balance the budget just once, and there seems to be no danger of that happening given its record.[174]

B. Congressional Posturing

As in New York, a budget crisis also spurred efforts to introduce a federal version of No Budget, No Pay in 1995 and 1996, when House Speaker Newt Gingrich risked a government shutdown despite falling poll numbers and the prospect of government workers not getting paid in order to balance the budget.[175] The contrast between members of Congress receiving their paychecks and government workers not receiving theirs presented Speaker Gingrich's opponents with an obvious political incentive to introduce federal versions of No Budget, No Pay.[176] Although at least one such bill in the Senate received bipartisan support,[177] Democrats offered their own bills independently,[178] as did Republican members who objected to Speaker Gingrich's tactics and offered their own bills in protest.[179] However, the most vocal supporters of No Budget, No Pay in Congress, and the only ones who actually referred to their bills as No Budget, No Pay, were decidedly Democrats.[180] For example, then-Representative Dick Durbin, a Democrat from

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169. *See* CAL. CONST. art. III, § 4(a).

170. *Id.* § 8(a).

171. *Id.* § 8(*l*).

172. BOWEN, *supra* note 155, at 42–43.

173. *E.g.*, Editorial, *It Can't Hurt*, *supra* note 159 ("[T]here's nothing to stop the commission that sets pay levels from enacting the same raise the following year (or a larger one, for that matter, to make up for the missed months).").

174. *See supra* notes 116–25 and accompanying text.

175. Jackie Calmes, *Fight over Balanced Budget Could Prove to Be Defining Moment for Gingrich and His Agenda*, WALL ST. J., Dec. 6, 1995, at A22.

176. *See* 142 CONG. REC. 173–74 (1996) (statement of Senator Leahy) ("Speaker Gingrich and the House Republicans are all accepting their pay while Federal workers are working without pay or forced to stay home without pay. . . . I believe it is the height of arrogance for them to accept it. . . . If the Speaker and his followers would also give up their pay as I am, I believe the House would quickly vote to reopen the Government.").

177. *E.g.*, S. 1428, 104th Cong. (1995) (offered by Senator Snowe and cosponsored by twenty-nine other senators).

178. *E.g.*, S. 1480, 104th Cong. (1995) (offered by Senator Boxer and cosponsored by Senator Harkin).

179. *E.g.*, H.R. 2828, 104th Cong. (1995) (offered by Representative Stearns and cosponsored by fourteen other Republicans).

180. *E.g.*, H.R. 2281, 104th Cong. (1995) (offered by Representative Durbin); S. 1480.

Illinois, spoke early and often in support of No Budget, No Pay bills while accusing House Republicans of trying to punish federal workers.[181] Likewise, Senator Barbara Boxer, a Democrat from California, pushed a 1997 version of No Budget, No Pay in the hopes of furthering President Clinton's budget, arguing, "The Republicans do not like that budget. Fair enough. That is why they are Republicans."[182]

Many of these bills required only that congressional pay be treated in the same manner as the pay of federal workers who were adversely affected during a government shutdown and gave no more specifics beyond the equal treatment mandate.[183] Others, such as one bill by Representative Bob Franks, a Republican from New Jersey, seemed to deviate from this pattern in form—but not in substance—by expressly stating that members of Congress would receive their back pay in full "upon enactment of legislation restoring pay for all Federal employees for the period involved."[184] Only a few federal versions of No Budget, No Pay expressly dispensed with the possibility of restoring back pay on some triggering event like passing the budget.[185] Whether the bills that would have eventually restored congressional pay would have been as effective as Senator Durbin hoped was not clear.[186]

In contrast, the members of Congress who introduced federal versions of California's Proposition 1F were mostly Republicans like Representative Dick Armey, a Texan who served as the Republican majority leader in the House of Representatives for the 104th through 107th Congresses.[187] In 1989, Armey introduced his own version of Proposition 1F, House Bill 68, and included among his findings of fact that

> the failure of Congress and its individual members to make tough, responsible decisions on Federal spending has led to fiscal profligacy unparalleled in the annals of human history; this failure has resulted in Federal budget deficits in 25 of the last 26 years, the deficit for fiscal year 1986 alone exceeding $220 billion; . . . [and] a national debt of this magnitude imposes an unconscionable burden on future generations of Americans . . . .[188]

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181. *E.g.*, 142 CONG. REC. 84–85, 91–92 (1996) (statement of Representative Durbin).

182. 143 CONG. REC. 5385–86 (1997) (statement of Senator Boxer).

183. *E.g.*, S. 1480 § 1(a) ("The basic pay of Members of Congress shall be treated in the same manner as the basic pay of the most adversely affected Federal employees who are not compensated [during a government shutdown].").

184. H.R. 2855, 104th Cong. § 2 (1996).

185. *E.g.*, H.R. 2373, 104th Cong. § 2 (1995) (offered by Representative Bonilla) (prohibiting retroactive pay); H.R. 2281 § 2.

186. *Cf. supra* note 173 and accompanying text.

187. 1 BIOGRAPHICAL DIRECTORY OF THE U.S. CONGRESS, 1774–2005, at 576 (2005).

188. H.R. 68, 101st Cong. § 1(2)–(3), (5) (1989). In language that foreshadowed State Senator Maldonado's views, Armey also claimed that "as in the private sector of this country, pay increases for Members of Congress should be a product of merit." *Id.* § 1(1); *see supra* note 156 and accompanying text.

Both House Bill 68 and a shorter version of the same bill that Armey introduced in 1992 would have prevented members of Congress from receiving a raise in years in which Congress failed to balance the budget.[189] Among the other members of Congress who introduced federal versions of Proposition 1F were then-Representative Jon Kyl, a Republican from Arizona, who introduced the Congressional Pay Freeze Act of 1993,[190] and Representative Cliff Stearns, a Republican from Florida, who introduced a bill to the same effect in several different Congresses.[191]

Boxer and Durbin's language on both the House and Senate floors strongly suggests that they were pushing their federal versions of No Budget, No Pay for a very partisan reason—to undermine congressional Republicans, who controlled both houses of Congress at the time.[192] Armey's language, however, suggests that his motives for introducing his federal version of Proposition 1F were much more ideological in nature.[193] Regardless, although it might be possible to conclude from these events that Democrats would naturally favor a federal version of No Budget, No Pay and that Republicans would naturally favor a federal version of Proposition 1F, it is also worth noting that Governor Pataki, a Republican, was the driving force behind No Budget, No Pay in New York.[194] Given the more bipartisan nature of support for No Budget, No Pay in Congress, the larger lesson is more likely that regardless of which approach members of a particular party are more likely to support, members of both parties will find ways to use either plan to their own political advantage.[195]

III. MERIT PAY AND PAIN

The clumsy attempts to design incentive contracts for state and federal legislators suggest the need to devise optimal incentive contracts before politicians create truly perverse incentives for themselves.[196] Moreover, elections alone are not sufficient to incentivize members of Congress to act in the best interests of their respective constituents.[197] Game theory suggests that without optimal financial incentives, elections can sometimes create a perverse Nash equilibrium in which

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189. H.R. 4778, 102d Cong. § 1 (1992); H.R. 68 § 3 (1989).

190. H.R. 2541, 103d Cong. (1993).

191. *E.g.*, Deficit Accountability Act of 2009, H.R. 201, 111th Cong.; Deficit Accountability Act of 1993, H.R. 407, 103d Cong.; Deficit Accountability Act of 1992, H.R. 4692, 102d Cong.

192. *See supra* notes 181–82 and accompanying text.

193. *See supra* note 188 and accompanying text.

194. *See supra* notes 131–50 and accompanying text. Given the clear difference in partisan use of No Budget, No Pay from New York to Congress, the most likely conclusion is that No Budget, No Pay multiplies the power of the party that already has the upper hand in the budget process. *See supra* notes 131–50 and accompanying text.

195. *See supra* notes 177–79 and accompanying text.

196. *See* MILGROM & ROBERTS, *supra* note 129, at 228–32. Linking pay to such narrow measures of performance violates Milgrom and Roberts's equal compensation principle, which states that all tasks of equal importance should receive equal weight in an incentive contract lest the agent neglect those on which his pay does not depend. *See id.*

197. *See infra* Part III.A.

members of Congress enact policies that reduce the nation's long-term economic welfare and their constituents reelect them for doing so.[198] Unfortunately, since 1989, Congress has linked its pay to aggregate wage inflation, so congressional pay bears no relation to the actual performance of individual members of Congress or Congress as an institution.[199] Using growth in the private sector of the economy to create upward pressure on congressional pay and price instability to create downward pressure on congressional pay would provide that accountability by rewarding members of Congress for strong economic growth and punishing them for weak economic growth.[200]

A. Elections and Incentives

Once one accepts the premise that a rational individual might choose to live in a coercive political state because he thinks collective action might make him better off, then "it seems natural that [he] should also prefer the political structure that makes [him] *best* off."[201] In their classic work, *The Calculus of Consent: Logical Foundations of Constitutional Democracy*, Buchanan and Tullock argued that collective action might also impose costs on an individual in the form of

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198. *See infra* notes 208–14 and accompanying text.

199. *See infra* notes 236–56 and accompanying text. Congressional pay bears more resemblance to the practice of setting executive compensation with reference only to the salaries of other corporate executives. *See* ALAN GREENSPAN, THE AGE OF TURBULENCE: ADVENTURES IN A NEW WORLD 427 (2007) (telling how executive compensation consultant Graef Crystal advised Mobil to set its executive pay "above average," prompting a director to ask him if he thought all corporate executives should be paid above average); *see also* GRAEF S. CRYSTAL, IN SEARCH OF EXCESS: THE OVERCOMPENSATION OF AMERICAN EXECUTIVES 10–11 (1991) ("I never focused very well on the fact that unless other companies were willing to pay their executives *below* market levels, the market would simply explode. And explode it did. . . . I helped create the phenomenon we see today: huge and surging pay for good performance, and huge and surging pay for bad performance, too."). Comparatively few business and political commentators, however, have pointed out the lack of accountability in congressional pay. *E.g.*, Brett Arends, *Time to Bring Financial Incentives to Washington: Why Congress Needs a Pay Cut, or a Threat of One*, MARKETWATCH (Nov. 17, 2009), http://www.marketwatch.com/story/why-congress-needs-a-pay-cut-or-threat-of-one-2009-11-17 ("Best practice in business would say that congressmen and senators should have their pay and pensions tied to their performance on key measures important to the country."); Patrick Basham, *Merit Pay for Pols*, CATO (July 29, 2002), http://www.cato.org/pub_display.php?pub_id=6519 (suggesting linking congressional pay to several different weighted factors, including but not limited to "personal and corporate tax levels, the regulatory burden, and the nation's overall fiscal position").

200. *See infra* notes 257–74 and accompanying text.

201. BARNES & STOUT, *supra* note 53, at 13 (emphasis in original); *see also* BUCHANAN & TULLOCK, *supra* note 18, at 43. Arguably, drafting the Constitution was an exercise in creating just such a political structure. *See* Donald Wittman, *The Constitution as an Optimal Social Contract: A Transaction Cost Analysis of* The Federalist Papers, *in* THE FEDERALIST PAPERS AND THE NEW INSTITUTIONALISM 73, 73–74 (Bernard Grofman & Donald Wittman eds., 1989); Frank H. Easterbrook, *The State of Madison's Vision of the State: A Public Choice Perspective*, 107 HARV. L. REV. 1328, 1328–30 (1994).

externalities when the group decided contrary to his interests and in the form of time and effort spent reaching agreements and making decisions with the group.[202] The risk of external costs should fall as the percentage of the group required to make a decision increased because it would be easier for the individual to veto any decision that ran counter to his interests.[203] In contrast, decision-making costs should rise because it would take longer to reach a decision.[204] A rational individual should prefer constitutional rules and procedures that minimized the sum of those two types of costs.[205] One example of external costs arises from the imperfect ability of voting mechanisms to translate individual preferences into group preferences.[206] Moreover, delegating decision-making authority to representatives would reduce decision-making costs, but it would add to whatever external costs would have arisen from the prevailing voting mechanism anyway.[207]

Game theory also suggests that without financial incentives to supplement elections, those representatives will frequently fail to act in the best interests of their respective constituents.[208] For example, Gersbach proposed a two-period game in which a politician serving in office in the first period was running for reelection to a term in the second period.[209] Suppose that during his first term, the politician could only choose one of three policy options: (1) a short-term policy that generated temporary economic benefits in the first period but imposed much larger costs in the second period; (2) a long-term policy that generated large economic benefits in the second period but only small or nonexistent economic benefits in the first period; and (3) a status quo policy that had no effect in either time period.[210] Gersbach assumed that the public could not tell whether the politician was pursuing a policy with substantial long-term benefits or one with substantial long-term costs based solely on the benefits it generated in the first period.[211] Gersbach also

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202. BUCHANAN & TULLOCK, *supra* note 18, at 43–46.

203. *Id.* at 63–68.

204. *Id.* at 68–69.

205. *Id.* at 69–72.

206. *See, e.g.*, KENNETH J. ARROW, SOCIAL CHOICE AND INDIVIDUAL VALUES 46–60 (1951) (setting out Arrow's Impossibility Theorem that no voting system could translate individuals' ranked preferences into an aggregate ranking of preferences when voters had more than two policy choices while still satisfying several fairness criteria); *see also* AMARTY K. SEN, COLLECTIVE CHOICE AND SOCIAL WELFARE 87–88 (1970) (discussing Sen's Liberal Paradox that no voting system could satisfy the conditions of minimal liberty and Paretian optimality).

207. BUCHANAN & TULLOCK, *supra* note 18, at 220–22.

208. GERSBACH, *supra* note 59, at 3. Gersbach stressed that such financial incentives should *supplement* elections, not replace them. *Id.* at 8.

209. *Id.* at 14–15.

210. *Id.* at 14.

211. *Id.* at 15. This is consistent with Downs's theory of the rationally ignorant voter. *See* DOWNS, *supra* note 62, at 253. As Mayhew argued, incentivizing members of Congress to take appropriate action using elections as their sole tool would only be possible "if the public grasp of means-end relationships [were] reasonably sophisticated." MAYHEW, *supra* note 72, at 140. In Gersbach's model, the benefits from the long-term policy in the first period at most could be equal to the benefits from the short-term policy in the first period, or they could be equal to the benefits from the status quo policy—nonexistent. GERSBACH, *supra*

assumed that the politician wanted to get reelected and could generate some private returns for himself from any policy that created benefits above the status quo.[212] Under these circumstances, the politician would always chose the short-term policy whenever his chances of getting reelected were fixed, no matter how high or how low they were.[213] In a more realistic scenario in which the politician's chances of getting reelected were uncertain, he would still never choose the long-term policy.[214]

Gersbach did not argue for something as extreme as doing away with elections altogether; instead, he argued that elections should be combined with financial incentives that would incentivize optimal policy outcomes while still making room for electoral control.[215] Gersbach's proposed solutions included requiring candidates to accept incentive contracts as a condition for seeking reelection,[216] allowing candidates to offer competing incentive contracts to their constituents,[217] setting minimum thresholds for politicians to achieve in order to be eligible for reelection,[218] and paying politicians according to self-financing incentive contracts.[219] This last solution optimized a politician's behavior because it paid him more in the second period of Gersbach's game if certain benefits materialized in the first period.[220] In order for this type of incentive contract to be sustainable over the long term, however, the public's expected costs could not rise faster than the marginal benefits the politician's effort provided.[221]

Designing an optimal incentive contract is usually difficult because measuring an agent's level of effort is usually difficult.[222] A principal may be able to infer the agent's level of effort from his level of output, but to the extent that a measure of

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note 59, at 15. If he had no other information, then a voter would have to cast his vote on that information alone. *See id.* One might expect a rationally ignorant voter in the real world to vote for the politician whenever short-term benefits materialized. *See id.*

212. GERSBACH, *supra* note 59, at 15–19. By private returns, Gersbach meant the ability to channel benefits to one's supporters, and perhaps even to himself. *Id.* at 15–16. These can be thought of as the "trappings of power," and may include congressional pay. *Id.* at 17.

213. *Id.* at 18–19. In essence, the politician's goal is to maximize the utility he derives from serving in office and from the private returns he can generate for himself. *Id.* at 16–17. Although the short-term policy would maximize the politician's utility no matter what his chances of reelection, only the long-term policy would maximize the public's utility. *Id.* at 18–19. Thus the Nash equilibrium: neither party could improve his own situation by acting unilaterally. *Id.*

214. *Id.* at 19–20.

215. *Id.* at 3.

216. *Id.* at 21–24. This solution would almost certainly be unconstitutional under the current 5–4 theory that the Qualifications Clause is an exhaustive list of qualifications for serving in Congress and that the Tenth Amendment does not allow the states to add qualifications. *See* U.S. Term Limits, Inc. v. Thornton, 514 U.S. 779, 800–02 (1995) (invalidating an Arkansas law imposing term limits on members of Congress).

217. GERSBACH, *supra* note 59, at 41–44.

218. *Id.* at 62–66. The same constitutional problem over qualifications arises here, too. *See supra* note 216 and accompanying text.

219. GERSBACH, *supra* note 59, at 80–84.

220. *Id.* at 80–81.

221. *See id.* at 84.

222. MILGROM & ROBERTS, *supra* note 129, at 206–09.

the agent's output also depends on factors outside the agent's control, basing the agent's compensation on this output measure will subject him to additional risk.[223] Suppose the principal cannot measure the agent's effort but can observe some measure of output, variable z, such that

$$z = e + x$$

where e is the agent's level of effort and x is a random variable.[224] Suppose the principal can also observe some other variable y that does not depend on the agent's level of effort but does correlate with x.[225] In this case, the principal can establish an incentive contract that is linear in y and z such that

$$w = \alpha + \beta(z + \gamma y)$$

where w is the wage the principal pays the agent, α is a base amount of pay, β is an intensity coefficient, and γ is a parameter that can assign different weights to the information variable y.[226] Whether the actual values the principal assigns to the parameters β and γ create an optimal incentive contract depends on how well they balance the costs of the agent bearing more risk with the increased gains that result.[227]

Milgrom and Roberts judged the optimality of incentive contracts according to the informativeness principle,[228] the incentive-intensity principle,[229] the monitoring intensity principle,[230] and the equal compensation principle.[231] The ease of

223. *Id.* at 207–08.

224. *Id.* at 215–17. In this case, the principal could infer e from observing z, but not perfectly. *See id.* The random variable x represents the factors outside the agent's control that will affect the observed level of output z. *Id.*

225. *Id.* at 215. This variable y would allow the principal to correct for some of the statistical noise from x in z. *See id.*

226. *Id.* at 215–16. Linear incentive contracts are popular because of their simplicity. *Id.* at 17. In practice, however, nonlinear incentive contracts may be necessary to motivate the wealthy because of their declining marginal utility of income and increased demand for leisure. *See* Canice Prendergast, *The Provision of Incentives in Firms*, 37 J. ECON. LIT. 7, 50 (1999).

227. *See* MILGROM & ROBERTS, *supra* note 129, at 208–09. Because people are risk-averse, an agent would demand a higher expected salary to compensate for the increased risk. *See* Prendergast, *supra* note 226, at 8. Paying an agent according to an incentive contract would only be in the principal's best interests to the extent that the productivity gains outweighed the additional cost in wages. *See id.*

228. MILGROM & ROBERTS, *supra* note 129, at 219–21. The optimal measure of incentives requires including any performance measures that decrease the statistical error with which the principal estimates the agent's effort and excluding any performance measures that increase that error. *Id.* at 219.

229. *Id.* at 221–26. Essentially, the optimal intensity of the incentives depends on the incremental profits created by additional effort, the precision with which the principal can measure the output, the agent's risk tolerance, and the agent's responsiveness to incentives. *Id.* at 221.

230. *Id.* at 226–28. The optimal amount of effort spent monitoring the agent depends on how sensitive the agent's pay is to performance. *Id.* at 226.

231. *Id.* at 228–32. The incentive contract must weight all tasks that the principal cannot

complying with these principles in different situations tends to explain why different forms of incentive contracts prevail in different settings.[232] Despite the academic emphasis on incentive contracts for individuals, however, Milgrom and Roberts noted that the most common explicit incentive contracts applied to whole groups of employees.[233] They noted several reasons why group incentives might actually be more effective than individual incentive contracts, including the employer's inability to determine individual contributions to outcomes, the group's superior knowledge concerning individual contributions, the group's superior ability to monitor its individual members, and individuals' tendency to resist the employer's wishes when they seemed to conflict with the group's interests.[234] All of these circumstances would appear to apply to Congress, but Congress has ignored the basics of incentive contract design in setting its own pay by divorcing its pay from performance.[235]

B. Creating a Performance Index

As of 2010, members of Congress can receive an annual pay raise no matter how good or bad a job they do.[236] In 1989, Congress linked its pay raises to the Employment Cost Index (ECI),[237] which measures the increase in the average cost of labor in wages and benefits in the economy.[238] The precise formula increases congressional pay every year by a percentage equal to the percentage increase in the ECI less 0.5%, up to a maximum of 5.0%[239] or the level of increase in General Schedule employees' pay, whichever is less.[240] For example, congressional pay

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monitor equally or the agent will spend no time on those that receive any less weight. *Id.* at 228.

232. *See id.* at 388–408, 413–18.

233. *Id.* at 413.

234. *Id.* at 416.

235. *See id.* at 215–17.

236. *See* 2 U.S.C. § 31(2)(A) (2006) (providing that congressional pay raises should take effect automatically, effectively requiring Congress to expressly decline a pay raise in order to stop the operation of the statute).

237. Ethics Reform Act of 1989, Pub. L. No. 101-194, § 704(a)(2)(B), 103 Stat. 1716, 1769 (codified at 2 U.S.C. § 31(2)(A) (2006)).

238. BUREAU OF LABOR STATISTICS, BLS HANDBOOK OF METHODS: CHAPTER 8. NATIONAL COMPENSATION MEASURES 10–14 (last visited Dec. 13, 2010), http://www.bls.gov/opub/hom/pdf/homch8.pdf.

239. Ethics Reform Act § 704(a)(1) (set out at 5 U.S.C. § 5318 note (2006) (Revision in Method by Which Annual Pay Adjustments for Certain Executive, Legislative, and Judicial Positions Are To Be Made)). The formula uses the change in the ECI from the second–most recent quarter of a year to the most recent quarter of a year immediately preceding the year in which the official rate of congressional pay will change. *Id.* Members of Congress do not actually start receiving the higher rate of pay until the following year. *See infra* note 241 and accompanying text. In other words, the increase in the ECI from the fourth quarter of Year 1 to the fourth quarter of Year 2 will determine the official rate of congressional pay set in Year 3 that members of Congress will start receiving in Year 4.

240. 2 U.S.C. § 31(2)(B) (2006). The General Schedule is the basic pay schedule that sets pay scales for most federal employees. 5 U.S.C. §§ 5102, 5331–32 (2006 & Supps. 2009, 2010).

rose 2.5% in 2008 because the ECI rose 2.7% from the fourth quarter of 2005 to the fourth quarter of 2006, but General Schedule pay only rose 2.5%.[241] The most recent congressional pay raise of 2.8% in 2009 brought congressional pay to $174,000 per year.[242]

Although even opponents of indexing congressional pay to the ECI have described these raises as cost-of-living adjustments (COLAs),[243] this is slightly misleading. Members of Congress discovered as much in 2009, when they received a 2.8% pay raise but Social Security recipients, whose benefits are indexed to the Consumer Price Index (CPI),[244] did not receive a COLA at all.[245] This same disparity has persisted even over the long term: from the fourth quarter of 1989 to the fourth quarter of 2007, the ECI rose by 3.55% on an annualized basis[246] but the CPI only rose 2.88%.[247] Even after reducing this annualized percentage change in

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241. IDA A. BRUDNICK, CONG. RESEARCH SERV., 97-1011, SALARIES OF MEMBERS OF CONGRESS: RECENT ACTIONS AND HISTORICAL TABLES 3, 7 tbl.2 (2010).

242. *Id.* at 2–3 & n.9.

243. *E.g.*, 155 CONG. REC. S2947 (daily ed. Mar. 10, 2009) (statement of Senator Casey); *see also* Schaffer v. Clinton, 240 F.3d 878, 880 (10th Cir. 2001) ("Bob Schaffer, a United States Congressman, appeals the district court's dismissal of a challenge, on Twenty-Seventh Amendment grounds, to the Cost of Living Adjustment ('COLA') provision of the Ethics Reform Act of 1989."); Boehner v. Anderson, 30 F.3d 156, 158 (D.C. Cir. 1994) ("John Boehner and 27 other Members of Congress . . . sought declaratory and injunctive relief on the ground that the provisions of the Ethics Reform Act that set up a mechanism for an annual cost of living adjustment (COLA) . . . violate the newly ratified Twenty-seventh Amendment . . . .").

244. 42 U.S.C. § 415 (2006). Social Security benefits are indexed to the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W). *Id.* For reasons of data accessibility, however, I use the Consumer Price Index for All Urban Consumers (CPI-U) for the remaining calculations in this Part. Unless otherwise noted, "CPI" refers to the CPI-U.

245. *E.g.*, Press Release, Representative Bill Posey, Congress Should Give Back Their Raise; Provide Relief to Seniors and Veterans (Oct. 15, 2009) (on file with the author).

246. Unless otherwise noted, the calculations in this Part annualize rates of change in congressional pay, GDP, and inflation by finding the discount rate that equates the values of the given term at two separate points in time. In general, the process involves solving the following equation for r:

$$PV = FV/(1 + r)^n$$

where PV is the present value of the term at any given time, FV is the future value of the term at time n, r is the discount rate, and n is the number of periods between the two points in time. The resulting rate of change is not the actual rate of change for every year, but rather the rate of change at which the term would have had to grow to change at the same rate continuously to reach the ending value. For any given example, there will always be some degree of subjectivity in choosing the starting and ending dates of the analysis.

247. *Compare* Bureau of Labor Statistics, *Employment Cost Index Historical Listing: Continuous Occupational and Industry Series, September 1975–June 2010*, at 3 tbl.4 (last visited Oct. 29, 2010), http://www.bls.gov/web/ecicois.pdf [hereinafter Bureau of Labor Statistics, *ECI*], *with* Bureau of Labor Statistics, *Consumer Price Index: All Urban Consumers–(CPI-U), U.S. City Average, All Items* (last visited Nov. 17, 2010), ftp://ftp.bls.gov/pub/special.requests/cpi/cpiai.txt [hereinafter Bureau of Labor Statistics, *CPI*]. The starting and ending dates for these calculations approximate the lag between the dates on which the formula provided for pay raises and the date on which members of

the ECI by 0.5%, the formula is still systematically biased in favor of raising congressional pay in real terms over time.[248] Only by taking separate action to expressly decline pay raises, as Congress did one-third of the time between 1989 and 2009,[249] has Congress reduced the effective annualized rate of its pay raises to less than the annualized change in the CPI.[250]

In doing so, however, Congress severed any link between congressional pay and performance.[251] Between the fourth quarter of 1993 and the fourth quarter of 1999, when Congress accepted only one pay raise, real GDP grew at an annualized rate of 4.12%,[252] but congressional pay rose at a meager annualized rate of only 0.38%.[253] Perversely, between the fourth quarter of 1999 and the fourth quarter of 2009, when Congress expressly declined only one pay raise, real GDP grew at an annualized rate of only 1.69%,[254] but congressional pay rose at a more impressive annualized rate of 2.44%.[255] In other words, congressional pay raises are a distant function of rising labor costs in the private sector when Congress arbitrarily chooses to accept them, not a function of the value that members of Congress actually provide to the nation.[256]

Congress should link its pay to performance instead.[257] A much more sensible formula would increase congressional pay every year by a percentage equal to the percentage change in the size of the private economy less some scaled value of inflation.[258] Suppose the size of the private economy (*PE*) is the sum of the

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Congress actually received them in 1991 and 2009.

248. *See supra* note 247 and accompanying text.

249. BRUDNICK, *supra* note 241, at 1 (noting that Congress expressly declined pay raises between 1994 and 1997, as well as in 1999 and 2007).

250. *See id.* at 5–6 tbl.1. Annualizing the rate of growth in congressional pay from the fourth quarter of 1991 to the fourth quarter of 2009 returns a rate of 1.85%. *See id.*

251. *See id.*

252. *See Table 1.1.6. Real Gross Domestic Product, Chained Dollars*, BUREAU OF ECONOMIC ANALYSIS (last visited Dec. 22, 2010), http://www.bea.gov/National/nipaweb/SelectTable.asp (follow "Table 1.1.6. Real Gross Domestic Product, Chained Dollars (A) (Q)" hyperlink; then enter "1989" for "First Year" and "2009" for "Last Year" under "Data Table Options") [hereinafter BUREAU OF ECONOMIC ANALYSIS, *Real GDP*].

253. *See* BRUDNICK, *supra* note 241, at 6 tbl.1.

254. *See* BUREAU OF ECONOMIC ANALYSIS, *Real GDP*, *supra* note 252.

255. *See* BRUDNICK, *supra* note 241, at 6 tbl.1.

256. *See supra* notes 244–47 and accompanying text.

257. *See* MILGROM & ROBERTS, *supra* note 129, at 206–07 (implying that a principal should be able to infer something about the agent's level of effort from the measure that determines the agent's compensation).

258. *See id.* at 207, 215–16. To the extent that congressional policies have an effect on the economy, the American people may be able to infer Congress's level of effort from the health of the economy. *See supra* notes 86–89 and accompanying text. Inflation may provide a proxy for other factors that also affect economic growth to the extent that increases in aggregate demand drive up prices. *See* N. GREGORY MANKIW, PRINCIPLES OF MACROECONOMICS 457–63 (5th ed. 2009). *But see id.* at 463–67 (explaining how decreases in aggregate supply could also drive up prices in the short run). Absent a stronger information variable, however, the best justification for choosing inflation as the information variable may be providing Congress with an extra disincentive to adopt policies that result in price instability given the harm it can do to an economy in the long run. *See id.* at 551–54 (noting that increases in inflation would reduce economic output).

National Income and Product Accounts (NIPAs) for consumption (*C*), investment (*I*), and net exports (*NX*);[259] and that inflation (*i*) is the annual percentage change in the CPI.[260] The precise formula can be expressed as follows:

$$\%\Delta S = \%\Delta PE - m|\ i\ |$$

where *S* is the salary that members of Congress receive and *m* is a scalar that can give different weights to the absolute value of inflation (*i*) in the formula.[261]

This Merit Pay and Pain formula would reward members of Congress for strong economic performance with pay raises and punish them for weak economic performance with pay cuts.[262] For example, the ECI formula provided that members of Congress would receive a 2.1% pay raise in 2010 despite the fact that inflation only rose 1.60% and the private economy actually shrank by 4.27% from the fourth quarter of 2007 to the fourth quarter of 2008.[263] If, however, congressional pay had been subject to Merit Pay and Pain, then assuming for the moment that *m* were equal to 1, members of Congress would have taken a 5.87% pay *cut* in 2010.[264] Excluding government spending from Merit Pay and Pain would ensure that members of Congress would not have an added financial incentive to spend money.[265] To the extent that high levels of government debt as a percentage of GDP reduce economic growth,[266] including activity from the private sector of the economy in Merit Pay and Pain would incentivize reducing the national debt.[267]

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259. BUREAU OF ECON. ANALYSIS, MEASURING THE ECONOMY: A PRIMER ON GDP AND THE NATIONAL INCOME AND PRODUCT ACCOUNTS 8 (2007) [hereinafter BUREAU OF ECONOMIC ANALYSIS, MEASURING THE ECONOMY], *available at* http://www.bea.gov/national/pdf/nipa_primer.pdf.

260. BUREAU OF LABOR STATISTICS, BLS HANDBOOK OF METHODS: CHAPTER 17. THE CONSUMER PRICE INDEX 1 (last visited Dec. 13, 2010), http://www.bls.gov/opub/hom/pdf/homch17.pdf.

261. *See* MILGROM & ROBERTS, *supra* note 129, at 215–17. Milgrom and Roberts specified an equation in which wages were a linear function of the observed variables. *Id.* Although Merit Pay and Pain shows the percentage change in salary as a linear function of the percentage change in the observed variables because of the magnitude of the numbers involved in national income accounting, congressional pay would still be linear in the observed variables. *See id.*

262. *See id.*

263. BRUDNICK, *supra* note 241, at 2; *see also* BUREAU OF ECONOMIC ANALYSIS, *Real GDP*, *supra* note 252; Bureau of Labor Statistics, *CPI*, *supra* note 247. Members of Congress wisely chose to reject this pay raise even though the General Schedule ceiling would have reduced it to 1.5%. BRUDNICK, *supra* note 241, at 2.

264. *See* BUREAU OF ECONOMIC ANALYSIS, *Real GDP*, *supra* note 252; Bureau of Labor Statistics, *CPI*, *supra* note 247; *see also supra* note 261 and accompanying text.

265. *Cf.* MILGROM & ROBERTS, *supra* note 129, at 228–32. In a sense, excluding government spending from Merit Pay and Pain would be no different than excluding the proceeds of a loan from gross income for purposes of the federal income tax. *See* MARVIN A. CHIRELSTEIN, FEDERAL INCOME TAXATION 45 (11th ed. 2009). Similar to the situation with a loan, there would be an expectation that the government would either have to repay what it borrowed or tax the private economy because it would not have generated any new wealth. *See id.*

266. *See supra* notes 86–89 and accompanying text.

267. *Cf.* MILGROM & ROBERTS, *supra* note 129, at 228–32.

On a more fundamental level, however, Merit Pay and Pain would move towards resolving the electoral agency conflict by giving members of Congress a financial incentive to take collective action only when the benefits outweighed the costs.[268]

Setting the actual value of *m* is equivalent to setting the parameter γ in the linear incentive contract model, so choosing the theoretically optimal value of *m* would require choosing *m* to minimize the variance between *x* and $m|\, i\, |$.[269] As a practical matter, *m* represents how much downward pressure price instability would exert on congressional pay.[270] If it were necessary, as a political matter, to ensure that members of Congress would receive the same annualized pay raises in the long term under Merit Pay and Pain that they have received between 1991 and 2009, then *m* would have to be set at approximately 0.47 for Merit Pay and Pain to produce the same annualized pay raise of 1.85%.[271] Even granting members of Congress this concession over the long term, however, this value of *m* would have resulted in an annualized raise of 3.06% between the fourth quarter of 1993 and the fourth quarter of 1999, but an annualized raise of only 1.81% between the fourth quarter of 1999 and the fourth quarter of 2009.[272] Although the long-term results would have been the same, the short-term results would have been the polar opposite of the results the ECI formula and Congress's discretion produced,[273] and therefore much more in line with popular perceptions of the two time periods.[274]

IV. CONSTITUTIONALITY

Any attempt to pay members of Congress according to incentive contracts would have to pass constitutional muster under the 27th Amendment.[275] The U.S.

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268. *See* BUCHANAN & TULLOCK, *supra* note 18, at 43–46, 63–72, 220–22; *cf.* MILGROM & ROBERTS, *supra* note 129, at 228–32.

269. *See* MILGROM & ROBERTS, *supra* note 129, at 219–21.

270. *See id.* at 215–17.

271. *See* BUREAU OF ECONOMIC ANALYSIS, *Real GDP*, *supra* note 252; Bureau of Labor Statistics, *CPI*, *supra* note 247; *see also supra* note 261 and accompanying text. These results obtain from applying Merit Pay and Pain to the actual congressional salary of $125,100 in 1991 using the percentage change in the private economy and the CPI from 1989 to 1990, and then sequentially applying Merit Pay and Pain to the salaries resulting from each previous application, using more recent values for the percentage change in the private economy and the CPI, until finally producing a salary for 2009. Although a more elegant way of calculating *m* is beyond the scope of this Note, repeated trials reveal that setting *m* at approximately 0.47 would produce a final salary of just under $174,000 such that a discount rate of 1.85% would equate it with the $125,100 salary in 1991.

272. *See* BUREAU OF ECONOMIC ANALYSIS, *Real GDP*, *supra* note 252; Bureau of Labor Statistics, *CPI*, *supra* note 247; *see also supra* note 261 and accompanying text. These results likewise obtain from applying Merit Pay and Pain sequentially and then equating the final salaries with their respective starting salaries and solving for the discount rates.

273. *See supra* notes 252–55 and accompanying text.

274. *See Satisfaction with the United States*, GALLUP, INC. (last visited Nov. 7, 2010), http://www.gallup.com/poll/1669/General-Mood-Country.aspx (showing satisfaction with the United States rising from a low of 14% in 1992 to a high of 71% in 1999 before falling to a low of 7% in 2008); *see also* Andy Serwer, *The Decade from Hell . . . and How the Next One Can Be Better*, TIME, Dec. 7, 2009, at 30.

275. U.S. CONST. amend. XXVII ("No law varying the compensation for the services of

Supreme Court has never heard a case under the 27th Amendment,[276] and the D.C. Circuit Court of Appeals has set a very low procedural standard for complying with it in the only case on point.[277] Members of Congress, however, have repeatedly introduced federal versions of No Budget, No Pay and Proposition 1F.[278] For the sake of simplicity in analyzing their constitutionality, one could fairly describe those bills as following either a New York Plan or a California Plan to reform congressional pay.[279] These plans come dangerously close to authorizing future Congresses to violate the 27th Amendment's procedural requirements and therefore also implicate some of the 27th Amendment's concerns about self-dealing.[280] Merit Pay and Pain, however, would pass constitutional muster under the D.C. Circuit's basic analysis of the 27th Amendment's procedural requirements.[281]

A. Of the New York and California Plans

Under the Ascertainment Clause, statutory law must determine congressional pay,[282] but that does not mean that Congress must pass a separate statute to authorize every change in congressional pay.[283] In fact, Congress may delegate to a commission the power to set congressional pay in future years, so long as Congress does so by statute.[284] In *Pressler v. Simon*,[285] the District Court for the District of Columbia upheld the Federal Salary Act of 1967,[286] which gave the Commission on

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the Senators and Representatives shall take effect, until an election of Representatives shall have intervened."). Most of the legal scholarship on the 27th Amendment has only considered whether its 203-year ratification process satisfied the requirements set out in Article V. *E.g.*, Michael Stokes Paulsen, *A General Theory of Article V: The Constitutional Lessons of the Twenty-Seventh Amendment*, 103 YALE L.J. 677, 721–33 (1993). The 27th Amendment originated from one of the twelve constitutional amendments Madison proposed in the First Congress in 1789. *Id.* at 678. The states quickly ratified ten of them, which became the Bill of Rights, but only six states ratified the amendment on congressional pay until Ohio ratified it in 1873. *Id.* The 27th Amendment failed to win approval from a sufficient number of states until 1992. *Id.*

276. *See* Schaffer v. Clinton, 240 F.3d 878, 886 (10th Cir. 2001) (holding that the plaintiffs did not have standing to sue), *cert. denied*, 534 U.S. 992 (2001).

277. Boehner v. Anderson, 30 F.3d 156 (D.C. Cir. 1994).

278. *See supra* Part II.B.

279. *See supra* Part II.B. There are comparatively few comprehensive analyses of whether specific legislative acts violate the Constitution's provisions on compensation. *See, e.g.*, Adrian Vermeule, *The Constitutional Law of Official Compensation*, 102 COLUM. L. REV. 501, 514–21 (2002); *see also* Sutin, *supra* note 131, at 245–55.

280. *See infra* notes 282–315 and accompanying text.

281. *See infra* Part IV.B.

282. U.S. CONST. art. I, § 6, cl. 1 ("The Senators and Representatives shall receive a Compensation for their Services, to be ascertained by Law, and paid out of the Treasury of the United States.").

283. Pressler v. Simon, 428 F. Supp. 302, 305–06 (D.D.C. 1976), *aff'd sub nom.* Pressler v. Blumenthal, 434 U.S. 1028 (1978) (mem.); *see also* Humphrey v. Baker, 848 F.2d 211, 215–16 (D.C. Cir. 1988).

284. *Pressler*, 428 F. Supp. at 305–06; *see also Humphrey*, 848 F.2d at 215–16.

285. 428 F. Supp. at 305–06.

286. Postal Revenue and Federal Salary Act of 1967, Pub. L. No. 90-206, § 225, 81 Stat. 613, 642–45 (codified at 2 U.S.C. §§ 351–61).

Executive, Legislative, and Judicial Salaries the power to make recommendations on congressional pay to the President.[287] The President's recommendations to Congress would then go into effect automatically unless Congress expressly declined them.[288] After receiving a raise in 1975,[289] Representative Larry Pressler sued to enjoin this practice, arguing that the Ascertainment Clause prevented congressional pay from changing unless Congress passed a new statute that expressly stated the new level of congressional pay.[290] In rejecting his argument, the court held that the verb "ascertain" did not have "such a narrow and limiting effect that . . . it was intended to prevent the Congress from developing rational procedures . . . for fixing congressional compensation by means other than enacting a specific statute fixing each pay change."[291]

The 27th Amendment did not change this result because it did not enact any affirmative requirement that Congress pass a new statute to account for every change in congressional pay.[292] In *Boehner v. Anderson*,[293] then-Representative John Boehner challenged the Ethics Reform Act of 1989,[294] which made cost-of-

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287. *Id.*

288. *Id.*

289. *Pressler*, 428 F. Supp. at 303–04. Representative Pressler actually received this raise under the Executive Salary Cost-of-Living Adjustment Act, Pub. L. No. 94-82, § 204(a), 89 Stat. 419, 421 (codified as amended in scattered sections of 5 U.S.C.) (1975). *Pressler*, 428 F. Supp. at 303–04. The court appeared ready to deny Pressler standing to challenge the Federal Salary Act, Pub. L. No. 90-206, § 225, 81 Stat. 613, 642–45 (codified at 2 U.S.C. §§ 351–61), on the grounds that the Senate rejected the only recommendations the President made under the Federal Salary Act after Pressler took office. *See Pressler*, 428 F. Supp. at 304–05. Because the Adjustment Act raised congressional pay by a percentage of the level of congressional pay that the Federal Salary Act established, however, the court narrowly held that Pressler's standing to challenge the Adjustment Act extended to the Federal Salary Act as well. *Id.* at 305. For a discussion of the mechanics and the constitutionality of the Adjustment Act, see *infra* notes 332–43 and accompanying text.

290. *Pressler*, 428 F. Supp. at 305. Vermeule has called this interpretation the strong reading of the Ascertainment Clause. Vermeule, *supra* note 279, at 514–16.

291. *Pressler*, 428 F. Supp. at 305–06. The D.C. Circuit essentially adopted this interpretation of the Ascertainment Clause when it upheld the Federal Salary Act in *Humphrey v. Baker*, 848 F.2d 211, 215–16 (D.C. Cir. 1988), relying heavily on *Pressler* as it did so. Senator Gordon Humphrey filed suit on exactly the same grounds as Pressler after he received a raise under the Federal Salary Act in 1987. *Id.* at 213. Humphrey's standing was stronger than Pressler's, but the D.C. Circuit only reached the merits of his case in the alternative after holding that its doctrine of equitable discretion counseled against hearing the case. *Id.* at 214.

292. *See* Boehner v. Anderson, 30 F.3d 156, 161–62 (D.C. Cir. 1994); *see also* Shaffer v. Clinton, 54 F. Supp. 2d 1014 (D. Colo. 1999), *aff'd on other grounds sub nom.* Schaffer v. Clinton, 240 F.3d 878 (10th Cir. 2001) (holding that the plaintiff did not have standing to sue). Indeed, Vermeule has accurately described Boehner's suit as an attempt to resurrect the strong reading of the Ascertainment Clause through the machinery of the 27th Amendment. Vermeule, *supra* note 279, at 519.

293. 30 F.3d at 158–59. In the interest of full disclosure, I should point out that I worked for Boehner for one summer during college, but not until thirteen years after the D.C. Circuit decided his case.

294. Ethics Reform Act of 1989, Pub. L. 101-194, 103 Stat. 1716 (codified in scattered

living adjustments to congressional pay according to the ECI.[295] Boehner argued that each COLA constituted a separate law that took effect every time a COLA raised congressional pay.[296] In rejecting Boehner's argument, the D.C. Circuit noted that the 27th Amendment only enacted a bar against Congress passing any laws varying congressional pay that would go into effect before the next election of representatives.[297] Because the COLAs did not constitute separate laws, they could not violate the 27th Amendment.[298] Instead, the D.C. Circuit noted that the only actual law in question was the Ethics Reform Act, which Congress passed on November 30, 1989.[299] The bill, however, expressly stated that it would not go into effect until January 1, 1991—after the 1990 election—thus satisfying the procedural requirements of the 27th Amendment.[300] The District of Colorado essentially adopted this same reasoning when it dismissed a similar challenge from Representative Bob Schaffer.[301]

Neither the D.C. Circuit nor the District of Colorado, however, held that the 27th Amendment allowed Congress to condition future congressional pay raises on discrete legislative actions completely within the discretion of the future Congresses that would receive them.[302] In fact, the District of Colorado noted that

> [a]djustments to congressional salaries under the Ethics Reform Act are not discretionary acts of Congress. The adjustments are calculations performed by non-legislative administrative staff, following a specific formula provided by Congress in the Act. Members of Congress do not participate in the calculation of pay increases. . . . The Act eliminates the possibility that Congress will grant itself a new pay raise during its current session.[303]

Only the D.C. Circuit, however, even had an opportunity to consider facts suggesting that Congress had done so.[304] In *Boehner*, Representative Boehner also challenged a separate law that expressly declined the congressional pay raise

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sections).

295. *Id.* § 704(a)(2)(B) (codified at 2 U.S.C. § 31(2)(A) (2006)).

296. *Boehner*, 30 F.3d at 161.

297. *Id.* at 161–62.

298. *Id.*

299. *Id.*

300. *Id.* In fact, the Ethics Reform Act actually took effect before Michigan became the thirty-eighth and final state necessary to ratify the 27th Amendment, making it constitutional in any event. *See id.* at 159. For an overview of how college sophomore Gregory Watson launched an improbable, ten-year campaign to convince state legislatures to ratify the 27th Amendment, see Richard B. Bernstein, *The Sleeper Wakes: The History and Legacy of the Twenty-Seventh Amendment*, 61 FORDHAM L. REV. 497, 536–42 (1992) (telling how receiving a C on a paper in which he argued that Madison's congressional pay amendment was still a live proposal motivated Watson to contact state legislatures across the country).

301. *See* Shaffer v. Clinton, 54 F. Supp. 2d 1014, 1024–25 (D. Colo. 1999), *aff'd on other grounds sub nom.* Schaffer v. Clinton, 240 F.3d 878 (10th Cir. 2001).

302. *See Boehner*, 30 F.3d at 161–62; *see also Shaffer*, 54 F. Supp. 2d at 1023–25.

303. *Shaffer*, 54 F. Supp. 2d at 1024.

304. *See Boehner*, 30 F.3d at 162–63.

scheduled to take effect on January 1, 1994.[305] Congress expressly declined the pay raise on March 4, 1993, when it passed the Emergency Unemployment Compensation Amendments of 1993.[306] As the D.C. Circuit restated Boehner's argument, the law in effect before March 4, 1993 had fixed the level of congressional pay that would be in effect on January 1, 1994, but then Congress passed a law to change that level of congressional pay some ten months before the next congressional elections.[307] Then-Judge Ginsburg only avoided deciding this claim on the grounds that Boehner had not raised it before the trial court.[308]

As Vermeule has argued, if the D.C. Circuit had heard this claim, then it should have held for Boehner.[309] Because the text of the 27th Amendment says that no law "varying" the congressional pay shall take effect before an intervening election, a law that actually decreased congressional pay before the next election would violate the 27th Amendment.[310] To further hold that declining a scheduled future pay raise that had not yet taken effect would likewise violate the 27th Amendment would require holding that it vested as soon as Congress passed a bill to schedule it.[311] Doing so would be consistent with the veil of ignorance theory of the 27th Amendment, which was designed to prevent members of Congress from using their ability to set their own pay to their own advantage.[312] Decreasing their own pay would serve their electoral interests just as much as increasing their own pay would serve their financial interests.[313] Electoral politics being what they are,[314] declining a pay raise that had not yet taken effect would give a member of Congress the same chance to engage in that electoral self-dealing as decreasing the pay he was currently receiving.[315]

One could argue that a scheduled COLA did not vest until it became effective.[316] In fact, the U.S. Supreme Court upheld a law that rescinded scheduled future pay raises for judges on the theory that those pay raises did not vest until they became

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305. *Id.* at 162.

306. Emergency Unemployment Compensation Amendments of 1993, Pub. L. No. 103-6, § 7(a), 107 Stat. 33, 35 (set out at 2 U.S.C. § 31 note (2006) (Cost of Living Adjustment)).

307. *Boehner*, 30 F.3d at 162.

308. *Id.* at 163.

309. Vermeule, *supra* note 279, at 520–21.

310. *Id.*

311. *Id.*

312. *Id.* at 503, 511.

313. *Id.* at 520.

314. *See generally* LUNTZ, *supra* note 20, at 125 ("Politicians who refuse the cost-of-living adjustment and tie their decision to the lack of a balanced budget or to the inability to give our soldiers a pay increase or to the principle of 'shared sacrifice' are usually rewarded with reelection.").

315. *See, e.g.*, Stop the Congressional Pay Raise Act, H.R. 156, 111th Cong. (2009) (offered by Representative Mitchell and over one hundred cosponsors).

316. *See* Boehner v. Anderson, 30 F.3d 156, 162 (D.C. Cir. 1994) ("The President and the Secretary of the Senate argue further that Mr. Boehner could not prevail on the merits in any case because legislation foregoing a COLA is not a 'law varying compensation' . . . but rather a law extending the period during which their compensation remains unchanged. (The defendants do not argue that a law decreasing congressional compensation is outside the intended reach of the Madison amendment . . . .)").

effective.[317] Extending this reasoning to congressional pay would be a mistake because different policy rationales guided the Founding Fathers in framing congressional and judicial pay provisions in the Constitution.[318] As the *Will* Court noted, the Founding Fathers prevented Congress from reducing judicial pay below its current level to undermine the independence of the judiciary, which rescinding scheduled future pay raises would not do.[319] One of the reasons the Founding Fathers wanted members of Congress to receive a salary from the federal government, however, was to prevent members of Congress from grandstanding by publicly refusing to accept salaries from the states.[320] Allowing members of Congress to magnanimously refuse pay raises would allow them to engage in a similar type of grandstanding.[321] Even worse, the erosion of congressional pay over time could have negative effects on the quality of its membership as the most qualified candidates chose to enter other professions.[322]

Moreover, to hold otherwise would create an absurd result in which Congress could effectively grant a future Congress the power to raise its own pay. Suppose Congress 1 passed a law stating, "Congress 3 shall have the power to set its own pay by enacting a statute that takes effect *before* the intervening election of representatives to Congress 4, but *this statute* shall not take effect until *after* the intervening election of representatives to Congress 2." The authorizing statute would clearly satisfy both the Ascertainment Clause[323] and the procedural requirements of the 27th Amendment,[324] but it would authorize a future Congress to violate the procedural requirements of the 27th Amendment.[325] Now suppose Congress 1 simply passed a law conditioning a pay raise on Congress 3 naming a post office before an intervening election of representatives. These two scenarios are not substantively different. Congress 1 would have given Congress 3 the ability to raise its own pay by passing a bill. In order to avoid this result, however, the U.S. Supreme Court would have to establish a rule to determine the criteria on which Congress could and could not condition future increases in congressional

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317. United States v. Will, 449 U.S. 200, 228–29 (1980).

318. Vermeule, *supra* note 279, at 505–14, 527.

319. *Will*, 449 U.S. at 217–18, 227–28.

320. *See* 1 MADISON, *supra* note 10, at 93 (noting George Mason's concern that in such a situation, the question in an election would not be "who [was] most fit to be chosen, but who [was] most willing to serve"); *see also* Bernstein, *supra* note 300, at 499–515 (describing the debate over Madison's original congressional pay amendment in light of British practices of constituents paying Parliamentary salaries, candidates bidding for office by refusing to accept them, and office holders eventually personally underwriting some of the costs of local government).

321. *See supra* note 315 and accompanying text.

322. *See* Franklin G. Mixon, Jr., *Formal Human Capital Attainment of Career Legislators in the U.S. Congress: Modeling Legislatures as Unions*, 108 PUB. CHOICE 369, 378–81 (2001) (finding that non-career politicians serving as members of Congress had higher levels of human capital, suggesting adverse selection based on wages); Peverill Squire, *Uncontested Seats in State Legislative Elections*, 25 LEGIS. STUD. Q. 131, 137–42 (2000) (finding that more state legislative seats went uncontested in states with lower legislative pay).

323. *See* Pressler v. Simon, 428 F. Supp. 302, 305–06 (D.D.C. 1976), *aff'd sub nom*. Pressler v. Blumenthal, 434 U.S. 1028 (1978) (mem.).

324. *See* Boehner v. Anderson, 30 F.3d 156, 161–62 (D.C. Cir. 1994).

325. *See id.*

pay. The rule that adheres most closely to the text and the purpose of the 27th Amendment would be that Congress could not condition future changes in congressional pay on any future Congress passing a law.

The constitutional problem with the New York and California Plans is that they would make changes in congressional pay conditional on a discrete legislative action within the complete discretion of Congress.[326] Like New York's No Budget, No Pay Law, similar bills introduced in Congress would delay congressional pay until members of Congress exercised one of Congress's enumerated powers.[327] As Sutin has noted, because there is a time-value of money, this condition necessarily changes congressional pay.[328] The distinguishing factor between this situation and the COLAs at issue in *Boehner* is that here the passage of a law, the annual budget, is the triggering event, not some mechanical formula.[329] In other words, the timing of Congress passing a particular statute will vary congressional pay before an intervening election of representatives, a very literal violation of the 27th Amendment.[330] The same analysis applies to bills modeled on the California Plan, which would simply vary congressional pay based on whether a future Congress passed a bill with a certain characteristic or that had a certain consequence.[331]

B. Of Merit Pay and Pain

As with a statute that delegates the power to set congressional pay to a commission, a statute that specifies an index to increase congressional pay every year does not violate the Ascertainment Clause either.[332] In *Pressler v. Simon*,[333]

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326. *Cf.* Shaffer v. Clinton, 54 F. Supp. 2d 1021, 1024 (D. Colo. 1999), *aff'd on other grounds sub nom.* Schaffer v. Clinton, 240 F.3d 878 (10th Cir. 2001).

327. *Compare* S. 1480, 104th Cong. § 1(a) (1995) ("The basic pay of Members of Congress shall be treated in the same manner as the basic pay of the most adversely affected Federal employees who are not compensated for any period in which there is more than a 24-hour lapse in appropriations for any Federal agency or department as a result of *a failure to enact a regular appropriations bill* or continuing resolution . . . ." (emphasis added)), *with* N.Y. LEGIS. LAW § 5(1) (Supp. 2010) ("[B]i-weekly salary installment payments to be paid on or after such day shall be withheld and not paid until *such legislative passage of the budget has occurred* . . . ." (emphasis added)). For a list of actions within the complete discretion of Congress on which Congress could therefore not condition future increases in congressional pay, see U.S. CONST. art. I, § 8.

328. Sutin, *supra* note 131, at 245 ("[T]here is a time value of money and withheld salary paid months from now without interest is not the same as salary paid today . . . .").

329. *See Boehner*, 30 F.3d at 161–62.

330. Vermeule, *supra* note 279, at 520–21 ("On the veil of ignorance account, this should be held a straightforward violation of the Amendment. Legislators voting on the January 3 statute presumptively suffer from the very decisionmaking distortion that provoked the Amendment; the new Congress has, in effect, knowingly adjusted its own salary.").

331. *See, e.g.*, H.R. 68, 101st Cong. § 3(a) (1989) ("No adjustment increasing the rate of basic pay . . . may be made in any fiscal year . . . unless the Federal budget is balanced, as determined under subsection (b).").

332. Pressler v. Simon, 428 F. Supp. 302, 305–06 (D.D.C. 1976), *aff'd sub nom.* Pressler v. Blumenthal, 434 U.S. 1028 (1978) (mem.); Humphrey v. Baker, 848 F.2d 211 (D.C. Cir. 1988).

333. 428 F. Supp. at 305–06.

the court also upheld the Executive Salary Cost-of-Living Adjustment Act,[334] which made cost-of-living adjustments to congressional pay according to the General Schedule.[335] The court noted that this practice represented an abrupt break with history, as Congress had always enacted separate statutes to raise congressional pay in the past.[336] Looking to the debates in the Constitutional Convention and *The Federalist*, the court found no help in determining the meaning of the verb "ascertain" from the assorted proposals for fixing the amount of congressional pay in the Constitution itself or indexing it to the price of a bushel of wheat, as Madison once suggested.[337] As with delegating the power to set congressional pay to a commission, the *Pressler* court simply concluded that the Ascertainment Clause was not "intended to prevent the Congress from developing rational procedures of this type for fixing congressional compensation by means other than enacting a specific statute fixing each pay change."[338]

Vermeule's theory explaining why indexing congressional pay did not violate the Ascertainment Clause is more satisfying.[339] According to Vermeule, Senator Humphrey and Representative Pressler's arguments in favor of requiring Congress to pass a new law to authorize each change in congressional pay were really just attempts to reduce the risk of Congress engaging in self-dealing.[340] After all, the President would have the ability to veto congressional pay raises under this reading of the Ascertainment Clause.[341] As Vermeule pointed out, however, even under this strong reading, Congress 1 could pass four separate laws in the same year to set congressional pay for each of Congresses 2, 3, and 4.[342] Because this procedure would not violate the rule that Humphrey and Pressler advocated, it was hard to see why an index that achieved exactly the same result should violate the Ascertainment Clause.[343]

The D.C. Circuit's decision to uphold COLAs under the 27th Amendment in *Boehner* actually provided the earliest statement of the hypothetical that Vermeule used to explain the results of *Humphrey* and *Pressler* under the Ascertainment Clause.[344] After then-Judge Ginsburg dismissed Representative Boehner's argument that each COLA constituted a separate law, she noted that the 27th Amendment allowed Congress to set congressional pay for all future Congresses, so there was no reason why Congress could not do so using an index for its own convenience.[345] All that Judge Ginsburg's test required was that the original

334. Executive Salary Cost-of-Living Adjustment Act, Pub L. No. 94-82, § 204(a), 89 Stat. 419, 421 (1975).
335. *Id.*
336. *Pressler*, 428 F. Supp. at 303.
337. *Id.* at 305–06.
338. *Id.*
339. *See* Vermeule, *supra* note 279, at 514–16, 519.
340. *Id.* at 514–15.
341. *Id.*
342. *Id.* at 516.
343. *Id.*
344. *See* Boehner v. Anderson, 30 F.3d 156, 161–62 (D.C. Cir. 1994).
345. *Id.*

authorizing statute that specified the index contain a section delaying its effective date until after the next election of representatives.[346]

Although Merit Pay and Pain would differ substantively from the ECI formula, an analysis of Merit Pay and Pain's annual congressional pay raises would proceed along the same lines as the D.C. Circuit's analysis of congressional pay raises under the Ethics Reform Act.[347] Suppose Congress 1 enacted Merit Pay and Pain for determining congressional pay for all future Congresses.[348] Because Congress 1 could have done so by passing separate statutes for each future Congress, there would be no reason to prevent Congress from specifying Merit Pay and Pain as its particular formula for achieving the same result out of convenience.[349] In order to pass constitutional muster, a law enacting Merit Pay and Pain would simply have to expressly state that it would not take effect until after an intervening election of representatives, and no congressional pay raise or pay cut under Merit Pay and Pain could occur until after that intervening election of representatives, either.[350]

One could argue, however, that Merit Pay and Pain would violate the proposed rule that Congress could not link congressional pay to any discrete legislative action within the discretion of any future Congress.[351] Merit Pay and Pain is easily distinguishable from the New York and California Plans in this sense because GDP is so broadly inclusive a measure that Merit Pay and Pain would not clearly incentivize members of Congress to take any discrete legislative action.[352] Instead, Merit Pay and Pain would incentivize members of Congress to achieve certain ends and leave the means up to them.[353] In contrast, the New York and California Plans would clearly elevate certain discrete legislative actions over all others by attaching financial incentives to means, not ends.[354]

V. COUNTERARGUMENTS AND EXTENSIONS

By increasing congressional pay based on expansions in the private economy and price stability, and by decreasing it based on contractions in the private economy and price instability, Merit Pay and Pain should incentivize fiscal discipline and pro-growth economic policies to at least some degree.[355] Merit Pay and Pain would do so more effectively than unconstitutional alternatives like the New York and California Plans because it would incentivize ends, not means.[356]

346. *Id.*
347. *See id.*
348. *See id.*
349. *See id.*
350. *E.g.*, Ethics Reform Act of 1989, Pub. L. No. 101-194, § 704(b), 103 Stat. 1716, 1769 (set out at 5 U.S.C. § 5318 note (2006) (Effective Date of 1989 Amendment)) ("This section and the amendments made by this section shall take effect on January 1, 1991.").
351. *See supra* notes 302–31 and accompanying text.
352. *See* BUREAU OF ECONOMIC ANALYSIS, MEASURING THE ECONOMY, *supra* note 259, at 8; *cf.* MILGROM & ROBERTS, *supra* note 129, at 228–32.
353. *See supra* notes 257–68 and accompanying text.
354. *See supra* Part II.
355. *See supra* notes 86–100 and accompanying text.
356. *See supra* notes 257–68 and accompanying text.

Counterarguments against Merit Pay and Pain, however, are likely to fall into two categories: those that assume Merit Pay and Pain would have some effect—but a deleterious one—on congressional behavior[357] and those that assume it would have no effect whatsoever.[358] Some of these fears are misplaced, but the more serious concerns could be addressed fairly easily if actual experience with Merit Pay and Pain showed that they were warranted.[359]

A. Assuming Effectiveness

Of the counterarguments against Merit Pay and Pain that assume it would have some effect on congressional behavior, the most fundamental counterargument an opponent could make is that Congress should not concern itself with economic growth because doing so would lead to society consuming the planet's resources at a faster and ultimately unsustainable rate.[360] This lack of faith in economic growth dates all the way back to Malthus, who argued that the human population tended to grow exponentially while food production tended to grow only linearly.[361] When the Club of Rome raised this concern again in *The Limits to Growth* in 1972, it argued that the planet would reach the limit of its ability to support a growing economy within the next one hundred years.[362] Based on their computer modeling, the Club of Rome claimed that society would have to limit economic activity, consumption, and the human population to levels not seen for years in order to avoid a total collapse of the system.[363] Along with the work of Georgescu-Roegen[364] and Daly,[365] this criticism provided the foundation for the field of ecological economics.[366] Daly, while acknowledging the political infeasibility, advocated creating formal institutions to limit the accumulation of wealth, the depletion of resources, and even population growth to attain these goals.[367]

The Malthusian predictions of *The Limits to Growth* and other methodologies were unlikely to come to pass so soon, in part because ecological economists underestimated the ability of prices to shift consumption away from scarce

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357. *See infra* Part V.A.

358. *See infra* Part V.B.

359. *See infra* notes 401–07 and accompanying text.

360. *See* DONELLA H. MEADOWS, DENNIS L. MEADOWS, JØRGEN RANDERS & WILLIAM W. BEHRENS III, THE LIMITS TO GROWTH: A REPORT FOR THE CLUB OF ROME'S PROJECT ON THE PREDICAMENT OF MANKIND 23–24 (1972).

361. T.R. MALTHUS, AN ESSAY ON THE PRINCIPLE OF POPULATION; OR A VIEW OF ITS PAST AND PRESENT EFFECTS ON HUMAN HAPPINESS; WITH AN INQUIRY INTO OUR PROSPECTS RESPECTING THE FUTURE REMOVAL OR MITIGATION OF THE EVILS WHICH IT OCCASIONS 13–30 (Donald Winch ed., Cambridge Univ. Press 1992) (1798).

362. MEADOWS ET AL., *supra* note 360, at 23–24.

363. *Id.* at 158–70.

364. *E.g.*, NICHOLAS GEORGESCU-ROEGEN, THE ENTROPY LAW AND THE ECONOMIC PROCESS (1971).

365. *E.g.*, HERMAN E. DALY, STEADY-STATE ECONOMICS: THE ECONOMICS OF BIOPHYSICAL EQUILIBRIUM AND MORAL GROWTH (1977).

366. *See generally* ROBERT COSTANZA, JOHN CUMBERLAND, HERMAN DALY, ROBERT GOODLAND & RICHARD NORGAARD, AN INTRODUCTION TO ECOLOGICAL ECONOMICS (1997).

367. DALY, *supra* note 365, at 50–75.

resources, of economic growth to decouple itself from material production, and of technological progress to grow exponentially.[368] Regardless, one might as well accept the presence of a binary opposition when one side of the debate aspires to "apply the stomach pump to the doctrines of economic growth that we have been force-fed for the past four decades"[369] and the other believes that economic freedom is a necessary condition for political freedom.[370] In Friedman's words, "a major source of objection to a free economy is precisely that it does [its] task so well. It gives people what they want instead of what a particular group thinks they ought to want."[371] Indeed, the fundamental assumption underlying this Note is the belief that on the whole, economic growth is a good thing.[372]

Even having accepted the premise that economic growth is a good thing, an opponent of Merit Pay and Pain could nonetheless argue that congressional pay should not depend so heavily on GDP because of its inherently overinclusive and underinclusive nature.[373] As Senator Robert F. Kennedy famously said in a speech at the University of Kansas,

> [t]oo much and for too long, we seemed to have surrendered personal excellence and community values in the mere accumulation of material things. Our Gross National Product now, is over $800 billion dollars [sic] a year, but that Gross National Product—if we judge the United States of America by that—that Gross National Product counts air pollution and cigarette advertising, and ambulances to clear our highways of carnage. It counts special locks for our doors and the jails for the people who break them. It counts the destruction of the redwood and the loss of our natural wonder in chaotic sprawl. It counts napalm and counts nuclear warheads and armored cars for the police to fight

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368. Carl Kaysen, *The Computer That Printed Out W*O*L*F**, 50 FOREIGN AFF. 660, 664–65 (1972); *see also* William D. Nordhaus, *World Dynamics: Measurement Without Data*, 83 ECON. J. 1156, 1182–83 (1973) (criticizing the earlier but similar work of Jay W. Forrester).

369. DALY, *supra* note 365, at 98.

370. MILTON FRIEDMAN, CAPITALISM AND FREEDOM 8 (1962) ("[E]conomic freedom is . . . an indispensible means toward the achievement of political freedom."); *see also id.* at 15 ("Underlying most arguments against the free market is a lack of belief in freedom itself."); FRIEDRICH A. HAYEK, THE ROAD TO SERFDOM 88 (1944) ("Most planners who have seriously considered the practical aspects of their task have little doubt that a directed economy must be run on more or less dictatorial lines.").

371. FRIEDMAN, *supra* note 370, at 15.

372. *See* Betsey Stevenson & Justin Wolfers, *Economic Growth and Subjective Well-Being: Reassessing the Easterlin Paradox*, BROOKINGS PAPERS ON ECON. ACTIVITY, Spring 2008, at 1, 35–41 (finding a statistically significant link between growth in GDP per capita and subjective well-being across a large number of countries). *But see* Richard A. Easterlin, *Will Raising the Incomes of All Increase the Happiness of All?*, 27 J. ECON. BEHAV. & ORG. 35, 37–44 (1995) (finding no statistically significant link across a smaller number of countries).

373. *See, e.g.*, COMM'N ON THE MEASUREMENT OF ECON. PERFORMANCE & SOC. PROGRESS, REPORT 7, 21–40 (2008) [hereinafter SARKOZY REPORT] (responding to a request from French President Nicolas Sarkozy to identify the limits of using GDP as an indicator of economic performance and social progress, and to suggest possible alternative measures).

> the riots in our cities. It counts Whitman's rifle and Speck's knife, and the television programs which glorify violence in order to sell toys to our children. Yet the Gross National Product does not allow for the health of our children, the quality of their education or the joy of their play. It does not include the beauty of our poetry or the strength of our marriages, the intelligence of our public debate or the integrity of our public officials. It measures neither our wit nor our courage, neither our wisdom nor our learning, neither our compassion nor our devotion to our country, it measures everything in short, except that which makes life worthwhile. And it can tell us everything about America except why we are proud that we are Americans.[374]

Likewise, a 2009 report to French President Nicolas Sarkozy set out many of these same criticisms, noting, for example, that GDP inadequately accounted for various forms of imputed income and depreciation of both capital and natural assets.[375] Indeed, perhaps the strongest of these criticisms is that national income accounting doubly undervalues natural assets because it also counts the activity that depletes natural resources as income.[376]

Even so, a general objection that national income accounting tends to be both overinclusive and underinclusive at the same time—just like any heuristic when a case-by-case analysis is too costly to justify—is no reason not to try to create a rule.[377] For example, Kennedy's ruminations over what should and should not be included in national income essentially rephrased on a national scale the same debate that occurs over what should and should not be included in gross income for purposes of the federal income tax.[378] Regardless, just as scholars have argued that common law rules continually evolved toward greater efficiency,[379] Merit Pay and Pain could evolve to incorporate new indicators of economic progress if they

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374. Robert F. Kennedy, Address at the University of Kansas (Mar. 18, 1968). The statistically negligible difference between GDP and GNP is that GDP does not include the production of American citizens overseas, but it does include foreign production within the United States. *See* BUREAU OF ECONOMIC ANALYSIS, MEASURING THE ECONOMY, *supra* note 259, at 8–11.

375. SARKOZY REPORT, *supra* note 373, at 88–93.

376. *See generally* ROBERT REPETTO, WILLIAM MAGRATH, MICHAEL WELLS, CHRISTINE BEER & FABRIZIO ROSSINI, WASTING ASSETS: NATURAL RESOURCES IN THE NATIONAL INCOME ACCOUNTS (1989) (urging countries and the United Nations to develop methods of accounting for natural resources to prevent overconsumption).

377. *See* Richard A. Epstein, *The Optimal Complexity of Legal Rules*, *in* HEURISTICS AND THE LAW 141, 141–44 (Gerd Gigerenzer & Christoph Engel eds., 2006).

378. *See, e.g.*, WILLIAM A. KLEIN, JOSEPH BANKMAN, DANIEL N. SHAVIRO & KIRK J. STARK, FEDERAL INCOME TAXATION 47–49 (2009) (discussing the infeasibility of including in gross income everything that would constitute income in the economically accurate sense); *see also* HENRY C. SIMONS, PERSONAL INCOME TAXATION: THE DEFINITION OF INCOME AS A PROBLEM OF FISCAL POLICY 50 (1938); Robert Murray Haig, *The Concept of Income—Economic and Legal Aspects*, *in* THE FEDERAL INCOME TAX 1, 7 (Robert Murray Haig ed., 1921).

379. POSNER, *supra* note 25, at 24–26.

represented an improved basis for inferring the value that members of Congress actually produced.[380]

Finally, an opponent of Merit Pay and Pain might argue that linking congressional pay to an index based on GDP would result in Congress failing to supply public goods or services that the index did not measure.[381] This argument would essentially rely on Milgrom and Roberts's equal compensation principle, which states that an agent would completely neglect any activity that received any less weight in his incentive contract than any other determinant of his compensation.[382] This would seem unlikely because providing a public good confers benefits on others in the form of positive externalities.[383] Members of Congress would therefore still have an incentive to supply those public goods to the extent that their positive externalities registered in other national product accounts by making other areas of the economy more productive.[384] Moreover, regardless of the theoretical superiority of other measures of well-being over GDP, there is some evidence that GDP is highly correlated with subjective well-being.[385] The higher the degree of correlation, the greater the possibility that collecting data for the more advanced measures of well-being would not be worth the additional cost.[386]

B. Assuming Ineffectiveness

The main counterargument an opponent could make under the assumption that Merit Pay and Pain would have no effect on congressional behavior would be that it would not produce financial incentives large enough to change congressional behavior.[387] For example, in Gersbach's two-period game with self-financing contracts, the optimal solution was to defer all of the politician's salary to the second period,[388] which Merit Pay and Pain would not do.[389] Moreover, although scholars have regularly suggested that linear incentive contracts were optimal for solving principal-agent problems,[390] they generally assume the absence of any income effects.[391] In general, linear incentive contracts might not be sufficient to motivate an agent as his income grows because of the diminishing marginal utility of wealth.[392]

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380. *See* MILGROM & ROBERTS, *supra* note 129, at 219–21.
381. *See id.* at 228–32.
382. *See id.*
383. MANKIW, *supra* note 54, at 207–09, 226–32.
384. *See* MILGROM & ROBERTS, *supra* note 129, at 228–32.
385. *See* Stevenson & Wolfers, *supra* note 372, at 35–41.
386. *See id.*
387. *See* GERSBACH, *supra* note 59, at 80–84.
388. *Id.*
389. *See supra* notes 257–68 and accompanying text.
390. *E.g.*, MILGROM & ROBERTS, *supra* note 129, at 215–17; Bengt Holmstrom & Paul Milgrom, *Aggregation and Linearity in the Provision of Intertemporal Incentives*, 55 ECONOMETRICA 303, 325 (1987).
391. Prendergast, *supra* note 226, at 50 & n.75 ("Quite simply, it may take more money to induce effort from the rich than from the less well off.").
392. *Id.* An alternative way of expressing the same idea is that as one acquires more wealth, his demand for leisure—or shirking, in the principal-agent model—increases. *See id.*

Assuming for the moment that Merit Pay and Pain would not have any effect on congressional behavior, it is still possible that it would improve the legitimacy of congressional pay raises by aligning them with the economic fortunes of the nation.[393] Historically, the public has reacted very negatively to congressional pay raises, in part because members of Congress allowed so much time to elapse between congressional pay raises that they felt justified in granting themselves large—and occasionally retroactive—pay raises to compensate for the real decline in their pay.[394] Although the American people may think that members of Congress are dramatically overpaid, evidence from the human capital attainment of career and non-career politicians in Congress has raised the concern that underpaying members of Congress might lead to the adverse selection of less capable individuals.[395] To the extent that this argument has merit, linking congressional pay to performance may make it politically more acceptable for congressional pay to rise and encourage more talented people to run for office.[396]

Regardless, the marginal decreases in congressional pay that Merit Pay and Pain would produce in bad economic times should increase the likelihood that a member of Congress would choose to retire instead of running for reelection.[397] For example, Hibbing found that simply not getting a raise increased the likelihood that a member of Congress would choose to retire at the end of that session of Congress by a statistically significant amount.[398] As a result, one should expect slightly more retirements from Congress in years when Merit Pay and Pain decreased congressional pay and fewer retirements in years when it increased congressional pay.[399] Even if Merit Pay and Pain had little effect on the decision making of individual members of Congress with respect to the cost-effectiveness of any given

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393. *See supra* notes 257–74 and accompanying text.

394. *See* Lee J. Alston, Jeffery A. Jenkins & Tomas Nonnenmacher, *Who Should Govern Congress? Access to Power and the Salary Grab of 1873*, 66 J. ECON. HIST. 674, 676–81 (2006); William T. Bianco, David B. Spence & John D. Wilkerson, *The Electoral Connection in the Early Congress: The Case of the Compensation Act of 1816*, 40 AM. J. POL. SCI. 145, 147–49 (1996).

395. Mixon, *supra* note 322, at 378–81 (finding that non-career politicians serving as members of Congress had higher levels of human capital, suggesting adverse selection based on wages).

396. *See* Squire, *supra* note 322, at 137–42 (finding an inverse relationship between the level of legislative pay and the number of uncontested state legislative seats in state elections).

397. *See* John R. Hibbing, *Voluntary Retirements from the House in the Twentieth Century*, 44 J. POL. 1020, 1028–33 (1982) (finding that seniority, real salaries, and salary increases had a statistically significant effect on voluntary retirements).

398. *Id.* Other research has also suggested that financial considerations have an impact on the career moves of members of Congress. *E.g.*, Richard L. Hall & Robert P. van Houweling, *Avarice and Ambition in Congress: Representatives' Decisions to Run or Retire from the U.S. House*, 89 AM. POL. SCI. REV. 121, 127–28 (1995) (finding that additional pension rights vesting in the next Congress reduced the likelihood that a member of Congress would retire at the end of his current term to a statistically significant degree).

399. *See id.*

policy, it should still tend to change congressional behavior by changing Congress's composition.[400]

Finally, if this were still not a large enough incentive to affect congressional behavior, then some percentage of the total annual pay set by Merit Pay and Pain could be made contingent on meeting certain benchmarks, much like performance-conditioned stock options in the corporate context.[401] Performance-conditioned stock options allow the holder to realize the gain between the exercise price and the grant-date price of the stock only if the stock has surpassed some threshold or outperformed some index of similar stocks by a certain amount.[402] By analogy, while Merit Pay and Pain could determine the amount of congressional pay raises in any given year, whether members of Congress would actually receive a set-aside portion of the resulting total salary could be made conditional on economic growth exceeding a certain threshold.[403] A similar mechanism could govern the pensions that members of Congress receive,[404] thus approximating the effects of deferred compensation in Gersbach's model.[405] The most obvious value of Merit Pain and Pain is that it would inject some much-needed rationality into the manner of calculating congressional pay raises.[406] If Merit Pay and Pain did not succeed in incentivizing fiscal discipline and pro-growth economic policies initially, however, then nothing about it would preclude increasing the intensity of its incentives by forcing members of Congress to bear more of the risk of their policies.[407]

CONCLUSION

The scarcest commodity in America these days is neither gold nor oil nor platinum nor uranium—it is integrity. Like character, integrity is what someone does when no one else is watching. Members of Congress and Congress as an institution have proven themselves untrustworthy agents by imposing large agency costs on the nation when the American people were not watching—and sometimes even when the American people *were* watching. The accumulated agency costs of members of Congress pursuing reelection strategies that produced short-term benefits at the expense of much larger long-term costs have put the nation's economic competitiveness and maybe even its national security at risk. By rewarding members of Congress for facilitating economic growth and punishing them for enacting costly and ineffective policies, Merit Pay and Pain would represent a low-cost strategy for resolving this electoral agency conflict.

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400. *See id.*

401. *See* BEBCHUK & FRIED, *supra* note 28, at 140–43.

402. *Id.*

403. *See id.* In essence, this would make the incentive contract nonlinear, which may be a necessary way to intensify the financial incentives to the point where they could overcome the income effects of the wealth that members of Congress tend to have. *See* Prendergast, *supra* note 226, at 50.

404. *See generally* KATELIN P. ISAACS, CONG. RESEARCH SERV., RL 30631, RETIREMENT BENEFITS FOR MEMBERS OF CONGRESS (2010).

405. *See* GERSBACH, *supra* note 59, at 80–82.

406. *See supra* notes 271–74 and accompanying text.

407. *See* MILGROM & ROBERTS, *supra* note 129, at 221–26.