

Report on the conference **EX UNO PLURES.WELFARE
WITHOUT ILLUSION**
SAPIENZA University of Rome, Faculty of Economics
September 14-16, 2009

The conference was co-organized by the European Center for the Study of Public Choice (ECSPC) and the Research Centre for International Economics (CIDEI), with funding from Sapienza University of Rome, the Bank of Italy, the Department of Public Economics, CIDEI and Icoisa.

The conference format did not differ from the familiar: each paper-writer led off by presenting the paper, an official discussant offered his evaluation of it. Then a ten minute open discussion followed. Each session included two papers and two discussants.

The conference was officially opened by Attilio Celant, Dean of the Faculty of Economics and began with an introductory speech by Giuseppina Capaldo, Head of the Department of Law and Economics of Productive Activities.

The conference featured a number of the world's major scholars working on fiscal federalism and provided a forum to critically discuss the challenges facing federalism building. The event stimulated scholarly discussion on issues that can be encapsulated in the following points:

What is there in the-real-world federalisms which makes them different from the various forms of decentralization?

Can we distinguish genuine federalisms from spurious federalisms? And how?

What makes federal structures effective?

What is federalism supposed to deliver and what features determine how well it performs this task?

Following the remarks of welcome and a cocktail reception, the conference started with a session chaired by Giancarlo Gandolfo (Sapienza University of Rome). The first paper by Geoffrey Brennan and Jonathan J. Pincus, '*Fiscal Equity in Federal Systems*' was presented by Geoffrey Brennan (The Australian National University, Canberra ACT, Duke University, UNC, USA). His presentation began by reflecting on the normative foundations of fiscal

equalisation - an issue handled in a classic paper of Buchanan's (1950). Contrary to Buchanan's claims, he argued that fiscal equalisation requires extremely strong value judgements – at least in the case where fiscal differences arise from the interaction of public goods provision under different population size – effectively committing one to a Rawlsian maximin rule. He noted that much weaker forms of the 'social welfare function' in this public goods case will generate the requirement that private consumption levels be equalised, but specifically not public consumption levels - in which sense private goods equalisation seems normatively weaker than public goods equalisation. He concluded that the hope of justifying federal fiscal equalisation on the basis of relatively uncontroversial individualistic norms seems illusory. Richard E. Wagner (George Mason University, USA) commented on the paper.

It followed a paper by Giuseppe Eusepi and Richard E. Wagner, entitled '*Competitive Federalism: Can this Analytical Box Be Filled?*' Giuseppe Eusepi addressed the fundamental difference between fiscal federalism and decentralization. To this end he noted that federalism is commonly described in contradictory fashion as involving both competition and decentralization. These descriptions, which may appear similar on the surface, emanate from contradictory analytical orientations. Competition entails a *polycentric* arrangement of competitors where there is no locus of control over the arrangement. In contrast, decentralization is a *monocentric* arrangement that involves a locus of control. To treat federalism as a method for decentralizing governments leads to a spurious form of federalism because the object that has been identified is not genuinely a competitively organized system of government. He concluded by suggesting that genuine federalism requires a polycentric arrangement that is organized through openly competitive processes. In contrast, the spurious form of federalism allows hierarchy to trump open competition. Reiner Eichenberger (Freiburg University) discussed the paper.

On Tuesday, September 15, there were sessions in the morning and in the afternoon. The first morning session was chaired by Antonio Pedone

(Sapienza University of Rome). The opening paper entitled “Federalism, Budget Deficits and Public Debt: On the Reform of Germany’s Fiscal Constitution” was by Lars Feld. He brought the relevant economic literature to bear the issue of the reform of the German fiscal constitution aimed at limiting the debt/GDP ratio. He presented a rather detailed account of the mechanisms by which tax autonomy in a competitive federal setting might be expected to reduce the use of debt. The conclusion operated in terms of pulling together the evaluation of the German reforms. Geoffrey Brennan (The Australian National University, Canberra ACT, Duke University, UNC, USA) discussed the paper.

It followed a paper by Richard E. Wagner (George Mason University, USA) entitled “Polycentric Polity: Genuine vs. Spurious Federalism”. The main message of the paper was that real federalism is not achieved when decisions are only superficially decentralized since they are tightly constrained by centralized authority. According to Wagner federalism requires a polycentric process of competition which allows autonomous decisions to be made at local levels. This federalism would not be restricted to competition between governments geographically contained with arbitrary boundaries, but with governments whose size and shape are determined by peaceful competition for citizen support. He concluded by underlining that achieving such a genuinely competition federalism would require new institutional arrangements that would somehow have to come into existence. But the first prerequisite to realizing such institutional arrangements is to consider the possibility of such a competitive federalism, something that Wagner did in a powerful way. Norman Frohlich (University of Manitoba) discussed the paper.

The second morning session was chaired by Geoffrey Brennan and opened with a paper by Bruno Frey entitled “Federalism as an Effective Antidote to Terrorism”. According to Frey decentralizing the economy, the polity and other social institutions is certainly not a panacea to “solve” the problem of terrorism. However, decentralisation is likely to strongly reduce the incentives for terrorists to attack because the expected damage suffered is much smaller than in a centralized society. He emphasized that federalism would strengthen

society, as economic, political and social decentralization (or polycentricity) is an essential element of a free and vigorous society. He concluded that this would make a society less vulnerable to terrorist attacks. Indeed, terrorism has no chance of success against a society that actively guards its fundamental liberal institutions of which decentralized decision-making forms an essential. Luisa Giuriato (Sapienza University of Rome) commented on the paper.

It followed a paper jointly written by Laura Castellucci and Stefano Gorini, 'The Promise and Peril of Fiscal Federalism: the Case of Italy'. Laura Castellucci presented the paper. After noting that virtues have been analyzed with much more attention than perils, she focused on the Italian setting. She argued that Italy cannot expect any welfare gains from federalism due to (i) the huge income disparities among regions; (ii) corruption at local government level; (iii) low mobility and (iv) a constitutional provision assuring a uniform basic standard of public goods to all citizens. Friedrich Schneider commented on the paper.

The first afternoon session, chaired by Antonio Pedone, opened with Friedrich Schneider's paper "The Influence of Public Institutions on the Shadow Economy: An Empirical Investigation for OECD Countries". Using the MIMIC estimation procedure, he focused on the size and development of the shadow economy of 21 OECD-countries. He argued that the driving forces behind the shadow economy are the increased burden of taxation and social security payments, combined with intensive labor market regulation, quality of state institutions and the tax morale. The argument was concentrated on the demonstration that federalism has no statistically significant effect on the shadow economy. He concluded by suggesting incentive oriented policy means so that the "black" value added can be transformed into official value added.

The official discussant was unable to attend the conference, so the floor opened for a general discussion.

The second speaker was Reiner Eichenberger who presented a paper jointly written with David Stadelmann entitled 'Federalism is Fair: Debt Capitalization

as a Protector of Future Generations'. Eichenberger started by contrasting the view that sees public debt as a burden on future generations with the Ricardian equivalence based on the claim that the burden of the debt is not shifted between generations because of compensating intergenerational transfers. In pointing out that the Ricardian assumptions are too demanding to hold, Eichenberger introduced another equivalence mechanism which is supposed to work also with non-altruistic individuals: Public debts capitalize into property values. He argued that Jurisdictions with larger net debts exhibit, *ceteris paribus*, lower property prices. He provided empirical evidence for debt capitalization using unique data for the Swiss metropolitan area of Zurich.

Philip Jones offered his comments.

The second afternoon session, chaired by Bruno Frey, had only one presentation because the speaker in schedule was unable to attend.

A paper by Joe A. Oppenheimer, Norman Frohlich, Maria Dimitriu, Cyrus Aghamolla, 'Some Democracies are More Equal than Others: Using Need Satisfaction to Evaluate Democratic Performance' occupied the entire session. Norman Frohlich presented the paper. He started his presentation by noting that democracy is often justified as a political system which protects and increases the welfare of its citizens. His first point was that the welfare of an individual may be tractable, but citizens are a group, and so there is a need to characterize aggregate welfare. This requires some way of comparing and aggregating the welfare of individuals into a measure of social welfare. He moved on to focus on the growing body of ethical reasoning and empirical data that indicates a broad cross-national consensus on one central normative aspect of welfare: meeting the basic needs of the severely disadvantaged in society. He emphasized that all the developed liberal democracies have adequate resources to provide for these. To avoid the thorny problems of characterizing overall welfare, he proposed a new metric for evaluating the performance of the developed liberal democracies based on basic needs. He focused on some preliminary measures which demonstrate significant divergence across democracies in the OECD and showed some of the statistical patterns that emerge. Bruno Frey discussed the paper.

On Wednesday, September 16, there was only a morning session, chaired by Giuseppe Eusepi. The session opened with a paper by Alessandra Staderini, Emilio Vadalà, “Inter-regional Fiscal Flows: An Estimation for the Italian Case”. Emilio Vadalà presented the paper. He illustrated the methodology used in the paper for the estimation of public revenue and expenditure on regional scale with the view to quantify balances (fiscal residuals) for Italian regions. He clinched that, contrary to other works that reassess regional accounts for specific time frames, this procedure has the advantage of being easily applied without requiring ad hoc calculations. Monica Auteri commented on the paper. It then followed a paper by Philip Jones, written jointly with Nils Soguel, entitled ‘Fiscal Federalism at the Ballot Box: The Relevance of Expressive Voting’ exploring the impact of citizens’ motivation to vote on the pattern of fiscal federalism. Jones argued that if instrumental citizens’ only concern was *outcome* they would have little incentive to vote because the probability that a single vote might change an electoral outcome is usually minuscule. He stressed the weight expressive voters attach to instrumental evaluation of alternative outcomes and presented a case study analysis of the way Swiss voters assessed the role their local jurisdiction should play. Lars Feld discussed the paper.

The conference closed with a paper by Marina Brogi, ‘Better Regulation and the Cost of Controls’. She argued that state intervention to curb the global economic downturn triggered by the subprime crisis led to massive disbursements to support banks and the economy.

She presented the possible changes which may be required in corporate governance regulations and considerations on the cost of control. Laura Ferrari Bravo discussed the paper.

Giuseppe Eusepi closed the conference by thanking the speakers, the discussants and all those who took part in the lively discussion, which was helpful to the speakers and stimulating to the audience. He warmly congratulated those who acted as session chairmen on their efforts in ensuring that sessions did not exceed the allotted time-span. He thanked the

team hired by the ECSPC for their excellent job and a very special note of appreciation went to Maria Delle Grotti permanent secretary to the European Center for the Study of Public Choice. Finally, he expressed his gratitude to Sapienza University of Rome, the Bank of Italy, the Department of Public Economics and Icoisa for their financial support.

Seven of the papers presented at the conference have been selected for publication in a special issue of the Review of Law and Economics under the editorship of Geoffrey Brennan and Giuseppe Eusepi.