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The political economy of centralization and the European Community*

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Abstract. Since 1972, the share of central government expenditure in total public expenditure has continued to increase in most industrial countries. In an international cross-section analysis, it has a significant positive effect on the share of government spending in GDP. The actors who have an interest in centralization are analyzed. The dynamics of centralization are attributed to a response asymmetry and two thresholds. "Popitz' law" of the attraction of the larger budget is tested with respect to the EC Commission: high-ranking politicians come mainly from the smaller member states. The voters' attitudes toward European unification are analyzed in a pooled regression.

> Ten years hence, 80% of our economic legislation, and perhaps even our fiscal and social legislation as well, will be of Community origin
> (Jacques Delors, Debates of the European Parliament, 6 July, 1988, No. 2-367/140).

1. Introduction

Most federal states have experienced a secular trend of centralization. For example, from 1900 to 1971 the share of central government expenditure in total government expenditure has increased from 34.1 per cent to 48.1 per cent in the United States[1] and from 20.4 per cent to 25.0 per cent in Switzerland (Pommerehne, 1977; Table 15-12). In Germany, it rose from zero in 1866 to 36.7 per cent in 1913 and 37.9 per cent in 1971; only Canada has been an exception (ibid.). In most countries, the long-run trend of centralization was temporarily reversed after World War II but, as *Table 1* shows, it has resumed its momentum in 1972–86: the share of central government expenditure in total government expenditure increased on average by 2.1 percentage points in the sixteen industrial countries for which the data are available and by 2.5 percentage points in the six federal states among them (Australia, Austria, Canada,

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Table 1. The centralization of government expenditure in the industrial countries, 1972–86

Country	Total outlays of government as a percentage of GDP[a]			Central government expenditure as a percentage of general government expenditure[b]			Transfers from central government to other levels of government as a percentage of general government expenditure[b]		
	1972–74	1984–86	Change	1972–74	1984–86	Change	1972–74	1984–86	Change
Australia	27.8	38.8	+11.0	75.4	77.6	+ 2.2	24.8	24.3	– .5
Austria	41.0	51.0	+10.0	72.7[d]	76.1	+ 3.4	7.9[d]	1.0	–6.9
Belgium	39.1	53.7	+14.6	–	(95.2)	–	–	(7.7)	–
Canada	36.9	46.8	+ 9.9	53.8[d]	51.6	– 2.2	13.1[d]	10.3	–2.8
Denmark	42.1	58.4	+16.3	71.8	73.1[d]	+ 1.3	29.9	27.1[d]	–2.8
Finland	32.7	41.2	+ 8.5	75.0	71.3	– 3.7	11.0	14.9[d]	+3.9
France	38.8	51.9	+13.1	89.8	90.0	+ .2	7.4	5.9	–1.5
Germany, F.R.	41.2	47.5	+ 6.3	60.2	63.6	+ 3.4	5.0	5.0	0
Greece	29.5[bc]	37.4[bcd]	+ 7.9	(96.3)	–	–	(.4)	–	–
Ireland	39.7	54.7	+15.0	90.4	96.5	+ 6.1	21.9	22.5	+ .6
Israel	58.5[c]	73.1[c]	+14.6	95.6[d]	95.3[d]	– .3	6.0[d]	3.6	–2.4
Japan	23.0	33.0	+10.0	(85.4)	–	–	(48.6)	–	–
Netherlands	49.2	60.1	+10.9	97.1[d]	93.9	– 3.2	30.6[d]	24.8	–5.8
Norway	44.6	47.3	+ 2.7	70.4	82.1	+11.7	6.4	14.4	+8.0
Spain	23.1	41.0	+17.9	94.7	87.3	– 7.4	4.3	7.2	+2.9
Sweden	46.5	63.7	+17.2	67.3	74.3	+ 7.0	11.0	10.3	– .7
Switzerland	32.8[bc]	38.0[bcd]	+ 5.2	51.0	56.4[d]	+ 5.4	10.1	7.1[d]	–3.0
United Kingdom	41.5	46.1	+ 4.6	83.3	89.5	+ 6.2	16.0	16.3	+ .3
United States	32.0	36.5	+ 4.5	64.1	67.1	+ 3.0	8.9	6.7	–2.2
Unweighted average[e]	37.9	48.4	+10.5	75.8	77.9	+ 2.1	13.4	12.6	– .8

[a] OECD, Economic Outlook.
[b] International Monetary Fund, Government Finance Statistics Yearbooks, consolidated expenditure plus lending minus repayments, includes social insurance and transfers to other levels of government.
[c] International Monetary Fund, International Financial Statistics.
[d] owing to data gaps, these ratios refer to one or two years only.
[e] excludes figures in parenthesis.

Germany, Switzerland, United States). Only five countries (Spain, Finland, the Netherlands, Canada and Israel) have not experienced an increase. At the same time, transfers from central government to lower levels of government as a share of total government expenditure have on average declined by .8 percentage points so that final expenditure by central governments has increased even more than their budgets. It has also been shown that more and more functions have been transferred to central government[2] and that the share of mandated expenditures has increased.

This raises two important questions which have been neglected in the literature and which are the subject of this paper:

1. Can the process of centralization be explained on efficiency grounds, or does it also or even primarily require a public choice explanation? (Section 2)
2. To what extent are such public choice mechanisms at work in the European Community? (Section 3)

2. Elements of a general politico-economic theory of centralization

Popitz (1927) and his school have attributed his "law" of secular centralization to technical progress that increases the scope of interregional externalities and generates spatial economies of scale in the public sector as well as to a shift of preferences in favor of interpersonal redistribution and interregional equality of living conditions. He also mentions the centralizing effect of wars and possible ratchet effects[3] but an analysis of the political process is not provided. The need for a public choice analysis is indicated by the fact that many policies have been centralized that do not satisfy these criteria.[4]

In a public choice analysis, it is important to identify the political actors who have an interest in excessive centralization. Several propositions can be derived.

1. Clearly, the *politicians and bureaucrats of the central government* wish to increase their power and prestige by expanding the budget, personnel and functions of the central government. This is also true of the members of the *federal parliament*.[5]
2. The *judges of the federal court(s)* can enhance their power and prestige by interpreting the law in a way that increases the number of issues to be decided at the federal level. The U.S. Supreme Court and the European Court of Justice are no exceptions to this rule.[6] In the long run, a federal constitutional court does not represent a "bulwark" against centralization but, in euro-speak, "an engine of integration."
3. *Pressure groups* that represent *regionally homogeneous* interests can obtain

more subsidies, regulations and protection from the central government than from lower-level governments because centralization increases the information cost of the other members of the ruling coalition (Vaubel, 1986) and weakens their incentive to be informed (Lee, 1985; Aranson, 1990).[7] Moreover, centralization reduces the transaction cost of rent-seeking. Within such pressure groups, the lobbyists at the central office try to increase their power and remuneration at the expense of the regional member associations by advocating the centralization of government expenditure and regulatory power.

4. Even the *politicians and bureaucrats of the lower-level governments* may be in favor of centralization if one of the following conditions is met.
   (i) Some form of centralization may be the only way of preserving their power in the face of a common external threat. Probably almost all federations or federal states that have been founded on a voluntary basis owe their existence to this cause (e.g., the Swiss cantons against the Habsburg empire, the Dutch provinces against Spain, the American colonies against England,[8] to some extent also the European Community under the Soviet threat).[9] Since the threat from Eastern Europe has diminished, the recent attempt to establish a European Political Union with a common EC foreign and security policy is more likely to signal a desire for political disintegration (of the Atlantic alliance) than integration (within Europe).
   (ii) Expansion of the central government does not have to be at the expense of the lower-level governments, it may be an opportunity to develop complementary activities at the state or local level (Breton and Scott, 1978: 98). The distribution of grants-in-aid to lower-level governments is a case in point. Alternatively, joint decision making of federal and lower-level politicians and bureaucrats can facilitate the growth of government expenditure at both levels because voters do not know who is to be held responsible. Thus, even though the central government's share of public expenditure grows, politicians and bureaucrats of the lower-level governments may be willing to cooperate because "cooperative federalism" also weakens their budget constraint.

The hypothesis that centralization favors government growth has repeatedly been tested fo the U.S..[10] It has generally been found to be consistent with the evidence. Here, we are primarily interested in an international cross-section analysis for the industrial countries. While Oates (1985) has conducted such a test for the total tax share in GDP, our measure of government size is expenditure. Total public expenditure as a percentage of Gross Domestic Product in 1980–86 has been regressed on

- the density of population,
- central government expenditure as a share of total government expenditure,
- central government transfers to lower-level governments as a share of central government expenditure,
- GDP per capita, and
- the years of continuous popular elections.

The cross-section relates to the seventeen industrial countries for which the required data are available.[11] Contrary to Oates' results, the estimates reported in *Table 2* are consistent with the hypothesis that centralization is conducive to larger government.[12] The regression coefficients of the other variables are not significant (at the 10 per cent level). If GDP per capita is added to the first equation, it takes a negative coefficient that is totally insignificant ($t = -.01$). It bears a significantly negative correlation with the share of central government in total government expenditure ($r = -.64$).

The constant elasticity of approximately .5 for the centralization variable $\ln(G^C/G)$ implies that the share of central government expenditure in GDP ($\ln(G^C/Y)$) affects the share of general government expenditure in GDP ($\ln(G/Y)$) with an elasticity of approximately 1/3. Since G^C/G is about 78 per cent (Table 1), the elasticity of 1/3 implies that central government tends to grow at the expense of the lower-level governments.[13]

(iii) If interregional market integration grows as a result of technical progress in transport and communications, the politicians and bureaucrats of the lower-level governments – especially in the small, central and open regions – gradually lose their regulatory and taxing power and increasingly welcome "political integration", i.e., collusion or monopolization (Vaubel, 1986). Only if this attempt fails does market integration lead to deregulation (Peltzman, 1989). Tax collusion frequently takes the form of revenue-sharing (McKenzie and Staaf, 1978; Brennan and Buchanan, 1980: 182 f.). If political integration is collusive rather than monopolistic, the lower-level politicians will insist that the central government must be controlled by the member governments or their delegates (Congress under the Articles of Confederation, the U.S. Senate until 1913, the Council in the European Community) rather than by a directly elected parliament. It is typical of the ensuing dynamics of centralization that a directly elected union parliament is added at a later stage (the U.S. House of Representatives in 1789, the direct election of the European Parliament since 1979), that it gradually increases its power at the expense of the federal chamber and that, at some point, the state legislatures even lose their right to

Table 2. The share of government in seventeen industrial countries[a]

Intercept	Density of population	Central government expenditure/general government expenditure	Central government transfers to lower level governments/central government expenditure	Years of continuous popular elections (Rustow)	R^2 $\bar{R}^2$
24.167	.024	.261	.173		.294
(1.70)	(1.08)	(1.46)	(.72)		.131
27.718	.022	.253			.266
(2.11)	(1.02)	(1.45)			.161
24.882		.323			.211
(1.94)		(2.00+)			.159
1.547	0.037 ln	.421 ln		.266 ln	.332
(1.28)	(1.05)	(1.58)		(1.37)	.178
1.224		.531 ln		.254 ln	.275
(1.05)		(2.16+)		(1.30)	.172

t-statistics in parentheses.

+ Significant at 10 per cent level.

[a] The countries are the same as in Table 1 with the exception of Greece and Japan for which some of the data are not available.

Sources: International Monetary Fund, Government Finance Statistics Yearbook; International Bank for Reconstruction and Development, World Development Report; D. Rustow (1976), Table 5.

nominate the members of the second chamber (the U.S. Senate since 1913).

(iv) The lower-level politicians may want to use the central government as a scapegoat for unpopular policies (Vaubel, 1986). For example, they may encourage or oblige the higher-level government to provide regulations and subsidies to the special interest groups on whose support they depend, or they may peg their exchange rate to the rest of the group so as to shirk responsibility for a stabilization recession or an inflationary pre-election boom.

(v) Politicians and bureaucrats of the member governments are willing to transfer the powers of still lower governments and of independent governmental agencies to the central government if they can obtain a quid pro quo from the central government (logrolling). In Germany, for example, the Bundestag (first chamber) was, until recently, entitled to transfer exclusive powers of the Länder (states) to the European Community even if, in the Bundesrat (second chamber), all Länder governments voted against the transfer.

(vi) Centralization and cooperation with the central government are advocated by those lower-level politicians and bureaucrats who hope to be promoted to the central government or who are generally responsible for negotiations with the central government. In relation to an international organization, this is primarily the Secretary for Foreign Affairs and his diplomats. If a federal state is established, the members of the new government or administration are typically selected from the group that has advocated the centralization; good examples are the first aministration and Supreme Court under the U.S. Constitution – notably George Washington, Alexander Hamilton (Secretary of the Treasury), Edmund Randolph (Attorney General) and John Jay (Chief Justice) –, the EEC Commission of 1958 and the first EC Commissioners from Denmark, Ireland, Greece and Spain (see appendix).

5. Centralization tends to be favored by those *voters* who supply factors of production in the region of the *federal capital* (unless the disadvantages of congestion outweigh the gains).

6. In the federal parliament or council, the representatives of the more highly taxed and regulated regions may combine to impose their regulations and tax rates on the other members through federal legislation. In this way, a majority coalition can suppress competition from the others. In an interest group setting, this is Goldberg's theory of regulation (1982). Heller (1986: 271f., 277) suggests that the centralization of the United States has proceeded along these lines and that the North East has used federal regulation, e.g., the national minimum wage, to reduce the competitive advantage of the South and the West. Note that the regulations may also benefit, and be supported by, some interest groups in the hitherto unregulated regions.

7. If the distribution of income is skewed to the right in the whole federation so that the median voter in the median income region has an income that is below the average income in the federation, the government of the median income region has an incentive to vote in favor of larger central government spending on federal public goods even if this is financed from a proportional federal income tax (or, as in the EC, from a value-added tax).[14]

The foregoing analysis has shown that many influential political actors are interested in bringing about a more centralized system of government than is warranted on efficiency grounds. But while it may explain the existing degree of overcentralization, it cannot explain the secular trend of increasing centralization. If we move from the statics to the dynamics of centralization, the following three explanations are particularly important.

1. Just as the growth of government depends positively on the current size of government (Mueller, 1987: 138 f.), "centralization ... breeds further centralization" (Beer, 1973: 75). This is because the establishment or expansion of central government alters the political equilibrium and the way in which the political system responds to changes in the demand for central government output. It is easier to found a new institution than to abolish it (Olson, 1982: 34, 10).

   Formally, this idea may be represented by the following (non-linear) first-order difference equation:

$$\Delta L = \beta^{1+\gamma \cdot (\Delta Q/|\Delta Q|) \cdot L} \cdot \Delta Q$$

   where

   L is the amount of labor employed by the central government (or alternatively its budget),
   Q is the output which the decisive voter demands from the central government,
   β is the (positive) impact coefficient at the time the central government is set up ($L=0$).

   If demand increases ($\Delta Q>0$), the central government's *positive* supply response is *stronger* the higher the level which L has reached. If demand falls ($\Delta Q<0$), the central government's *negative* supply response is *smaller* the higher L because $\Delta Q/|\Delta Q| = -1$. Thus, the "acquis communautaire", as it is called in euro-parlance, may not operate as a simple ratchet but it introduces a general response asymmetry. Even if demand for central government output fluctuates around a constant mean ($\sum_t \Delta Q_t=0$), L tends to increase: it fluctuates with a positive drift component. If the increasing inefficiency of overcentralized government does not act as a sufficient counterweight at some point, only complete centralization is a long run equilibrium. Temporary phases of decentralization (the postwar period, France in 1982/3, Spain in the 1980s, the Soviet Union and Yugoslavia in 1991/2), would then be due to negative demand shifts; in a more complicated model, there may also be lagged feedbacks from the inefficiency of prior centralization.[15]

Even if voters are assumed to be rationally ignorant, politicians and bureaucrats of the regional governments are likely to anticipate the dynamics of this process. Why do they take the first step and trigger a process that gradually deprives them of their power and prestige? They may be interested in centralization for one of the reasons mentioned above (4(i) – (vi)) but they may also be indifferent because their electoral time horizon is short.[16] They are least likely to resist in the case of additional expenditures, especially if these concern new policy fields (rapid deployment force, environmental protection etc.) in which they do not have a stake to defend (Teutemann, 1992).

2. Whether regional politicians and bureaucrats are interested in moving to the central government (4(vi)) depends on the relative power and prestige of the central government and on relative salaries. This introduces a threshold into the dynamic analysis: once the budget and personnel of the central government exceeds that of a regional government, the most competitive politicians and bureaucrats of the region will want and manage to move to the central government. This natural selection effect strenghtens the central government and weakens the regional government(s). Once a majority of the population lives in regions whose government budgets are smaller than the central government budget, complete centralization may be the only long-run equilibrium.
3. Another threshold is reached if the central government's resources exceed those of all regional governments combined. At this point the central government can overcome the joint resistance of all regional governments.

In the United States, both thresholds have been passed.[17] This stands in marked contrast to the prediction which James Madison made two hundred years ago:

> The number of individuals employed under the Constitution of the United States will be much smaller than the number employed under the particular states (Federalist Paper No. 45, 1787/1987: 291).

Well-known authors have suggested that the United States, which was founded as a classical federal state, has degenerated into a highly and excessively centralized state:

Table 3. The growth of the budget and personnel of the European Community

Years	Rate of growth of EC budget in UA/EUA/ECU	Rate of growth of EC GDP in UA/EUA/ECU	Rate of growth of the ratio EC budget/EC GDP	Rate of growth of EC personnel	Rate of growth of EC population	Rate of growth of ratio EC personnel/EC population
	per cent per annum	per cent per annum	per cent per annum	per cent per annum	per cent per annum	per cent per annum
1960–72	30.6	10.3	18.4	11.6.	.9	10.7
1972–80	22.4	16.5	5.0	6.9	4.0	2.8
1980–85	11.9	8.6	3.0	3.0	.7	2.4
1985–90	10.6	8.8	1.6	3.9	4.0	0
1960–90	21.7	11.4	9.2	7.6	2.2	5.3

Sources: European Economy, 1991 (annual review); budgets of the European Communities; Statistisches Jahrbuch der Bundesrepublik Deutschland 1990, annex.

> The 'ground rules' defining the distribution of federal power have been recently and radically changed by decisions of the Court, Congress and the President, with the result that a system of rules which for some long period of time had limited federal power now permits great and, indeed, excessive centralization (Beer, 1973: 52).

> There should be no doubt, however, that the Constitution was designed to provide a strong but limited federal role ... Most of these rules, unfortunately, have now been stretched beyond recognition (Niskanen, 1988: XII).

> It is mockery to use 'federalism' or 'federal union' in descriptive reference to the United States of 1990, which is, of course, simply a very large nation-state'' (Buchanan, 1990: 6).

According to Aranson (1990: 494), ''the economic and political development of the United States suggests that great dangers lie in the development of a unified Europe''. Will Europe commit the same mistakes?

3. The political economy of EC centralization

Table 3 shows the growth of the EC budget (relative to EC Gross Domestic Product) and the expansion of EC personnel (relative to EC population) in 1960–90 and various subperiods. The years before 1960 are excluded because they represent a start-up phase. 1972, 1980 and 1985 are chosen as dividing years because each precedes an enlargement and therefore comes closest to a state of maturity for a given membership. Over the whole period, budget growth has been twice as large as GDP growth in nominal (ECU) terms, and personnel has grown three times as fast as total population. The budget/GDP ratio has increased in all subperiods, and with one exception (1985–90) the same is true of the personnel/population ratio, but the rates of increase decline monotonically. The budget deal of 1992 confirms this trend. It restricts the average rate of increase of the budget/GNP ratio to 0.8 per cent per annum until 1999. Thus, the pace of centralization seems to be gradually decelerating.

How large is the EC budget relative to central government expenditure in the member countries? *Table 4* reveals that in 1988 it amounted to only 2.8 per cent of their combined expenditure. But this ratio has been increasing: in 1973 it was still 1.7 per cent. This may contribute to explaining why a post with the EC Commission has become increasingly attractive for politicians and bureaucrats from the various member countries.

As can also been seen in Table 4, the EC budget is larger than the budget of the national central government in five of the member countries (Luxembourg, Ireland, Portugal, Greece and Denmark). Clearly, the lower threshold of our dynamic analysis has not yet been reached but the Community is moving in its direction.

The natural selection hypothesis implies that EC Commissioners from the smaller member countries have enjoyed a higher political status in their home country than the EC Commissioners from the larger member countries did.[18] To examine this hypothesis, all 75 EEC and EC Commissioners appointed in 1958–92 have been ranked according to the following formal criteria:

Rank 1: a person who has been a minister in the central government of his home country within one year prior to his being appointed an EC Commissioner,
Rank 2: a person who has been a state secretary in the central government of his home country or shadow minister or minister in a provincial government in the year prior to his appointment.
Rank 3: all others.

The data on the individual Commissioners and their ranks are given in the Appendix. The average ranks reported in Table 4 are in line with the natural selection hypothesis. There is a high positive correlation between the average rank number of the country's Commissioners and its central government budget ($r = .55$ for the whole period and $r = .26$ for the period since 1973).

To analyze this relationship more closely, the rank numbers of the individual Commissioners have been regressed on the following explanatory variables[19]:

- the budget of the central government of the Commissioner's home country in 1973 in ECU millions (C) or, in the estimate for the subperiod 1973–92, the budget of the central government of his home country relative to the EC budget in the year of his first appointment (C_t);
- the population of his home country as a share of the population of the Community of Twelve in the year of his first appointment (P_t);
- the deviation of his home country's GDP per capita from the EC average in the year of his first appointment (Y_t);
- his home country's net receipts per capita from the EC in 1975–89 per annum (N) or, in the estimate for the subperiod 1973–92, his home country's net receipts per capita from the EC, deflated by the consumer price index, in the year of his first appointment (NR_t);
- the absolute value of N or NR_t, respectively;
- the average of his home country's exports to, and imports from, the rest of the EC relative to national GDP in the year of his first appointment (TR_t);

Table 4. Consolidated expenditure of central government in the EC countries (1988) and the political status of their Commissioners

Country	In national currency			In ECU millions		Average rank[a] of the country's Commissioners		Average term of office of the country's Commissioners	
						1958–1992	1973–1992	1958–1992	1973–1992
Luxembourg	LuxFr	115,421	million	2,658		2.4	2.0	5.3	4.1
Ireland (1987)	Ir £	10,470	million	13,502			1.2		4.4
Portugal	Esc.	2,517.9	million	14,806			3.0		7.0
Greece (1985)	Dr.	2,331.4	billion	22,049			2.0		4.0
Denmark	Dkr	289,930	million	36,462			1.7		6.7
Belgium	BF	2,845.7	billion	65,526		1.7	2.0	10.0	5.3
Spain (1987)	Pes.	12,138.6	billion	85,384			2.5		7.0
Netherlands	Dfl	251.44	billion	107,693		1.4	1.0	9.5	6.7
United Kingdom	£	161,795	million	243,508			2.3		4.0
Germany, F.R.	DM	638.96	billion	308,022		2.5	2.4	8.2	5.6
Italy	Lire	504,525	billion	328,183		2.5	2.0	5.6	8.0
France	FF	2,454.4	billion	348,813		2.4	2.5	7.3	8.4
total				1,576,606	mean (12):		2.05		5.93
					mean (6):	2.15	1.98	7.65	6.80
Budget of the European Communities				43,828					
Coefficient of correlation with expenditure of national central government (ECU)						.55	.26	–.19	.46

[a] Based on political status before entering EC Commission (see Appendix).

Sources: International Monetary Fund, Government Finance Statistics Yearbook 14, 1990; Deutsche Bundesbank, Statistische Beihefte zu den Monatsberichten, Reihe 5, Die Währungen der Welt, Mai 1991.

Table 5. The political status of EC Commissioners before entering the Commission (rank numbers)

Intercept	Central government budget in 1973 C	Central government /EC budget in year t C_t	Population share in EC-12 P_t	Net receipts from EC per capita in 1975–89 per annum NR	Foreign trade with EC/GDP in year t TR_t	Distance of national capital from Brussels D	R^2 $\bar{R}^2$
	1958–92						
1.84	.009						.077
(10.62*)	(2.47+)						.064
	[2.38+]						
2.10	.009			.002	– .026		.167
(5.76*)	(1.67°)			(2.30+)	(–2.21+)		.132
	[1.64]			[2.25+]	[–2.18+]		
1.11	.019			.002		.286	.155
(3.33*)	(3.51*)			(2.23+)		(1.96°)	.119
	[3.33*]			[2.18+]		[1.91°]	
1.31			.065	.002			.168
(4.99*)			(3.77*)	(2.23+)			.145
			[3.49*]	[2.12+]			
	1973–92						
2.18		.042		.005	– .027		.210
(5.60*)		(1.23)		(2.68+)	(–2.07+)		.158
		[1.29]		[2.30+]	[–2.11+]		

t-statistics in parentheses for OLS and in brackets for probit.
* Significant at 1 per cent level.
+ Significant at 5 per cent level.
° Significant at 10 per cent level.

- the distance between Brussels and the capital of his home country in thousands of kilometers (D);
- the share of respondents in his home country who are in favor of (i) "efforts to unify Western Europe" (EU_t) or (ii) their country's membership in the EEC or EC (EC_t) in the year of his first appointment;
- the absolute deviation of EU_t or EC_t, respectively, from the EC average;
- a time trend (only in regressions with C, i.e., in the full sample);
- a dummy (DO = 1) for members of the opposition since, by definition, they cannot be of rank 1.

While the variables C, C_t and P_t capture the budgetary motive of the Commissioner (the agent), the variables Y_t, N, NR_t, TR_t, EU_t, EC_t and their transformations proxy the demand of the population (the principal). However, if the population has a stronger interest in EC centralization, its Commissioners also enjoy more prestige at home so that high-level politicians are more likely to accept this position. The distance from Brussels also affects the preferences of both politicians and voters: those at the periphery are less interested in the EC Commission.

Table 5 reports the OLS estimates for those variables that turned out to be significant.[20] As predicted by the natural selection hypothesis, C and P_t take significantly positive coefficients in the full sample. The regression coefficient of C_t in the subsample is also positive but not significant. The significantly positive coefficients of NR imply that high-quality politicians are sent by the net payers rather than by the net recipients. As was to be expected, the rank number of a country's Commissioners tends to be lower, the larger its trade with the EC relative to its GDP or the more central it is.

Since the dependent variable is a qualitative variable, an ordered probit analysis has been conducted to check on the t-statistics of the OLS regressions. The probit t-statistics are shown in brackets. They hardly differ from the OLS results.

According to a widespread popular view, politicians who have been unsuccessful in the national arena, are particularly prone to be nominated for the EC Commission or the European Parliament as a form of retirement. I shall call this the "grandfather hypothesis." If it is correct, the older Commissioners should have lower political status, i.e., they should represent member countries whose central government budget (or population) is large. Moreover, the age of the Commissioners may depend on the preferences of the country's population. To test this hypothesis, the Commissioners' age at the time of their first appointment has been regressed on the same variables as have their rank numbers. The results are very similar (*Table 6*). The only major difference is that the national capital's distance from Brussels (D) always takes the place of the trade variable (TR_t). However, both variables are highly collinear ($r = -.32$).

Table 6. The age of EC Commissioners at the time of their first appointment

Intercept	Central government budget in 1973	Central government /EC budget in year t	Population share in EC-12	Net receipts from EC per capita in 1975–89 per annum	Distance of national capital from Brussels	Dummy for opposition member	R^2 $\bar{R}^2$
	C	C_t	P_t	NR	D	DO	
	1958–92						
42.4	.136			.020	3.11	6.63	.202
(15.36*)	(2.95*)			(2.75*)	(2.56+)	(2.15+)	.156
44.4			.381	.017	1.86	6.71	.178
(18.04*)			(2.54+)	2.39+	(1.63)	(2.14+)	.131
49.7			.195				.041
(32.18*)			(1.76°)				.027
	1973–92						
49.9		.437					.068
(30.20*)		(1.85°)					.048

t-statistics in parentheses.
* Significant at 1 per cent level.
+ Significant at 5 per cent level.
° Significant at 10 per cent level.

Table 7. The term of office of EC Commissioners

Intercept	Time	Central government /EC budget C_t	Distance of national capital from Brussels D	Dummy for member of opposition DO	R^2 $\bar{R}^2$
1958–92					
9.72	− .147		− .917		.210
(11.27*)	(−3.76*)		(−1.64)		.188
1973–92					
4.60		.171			.077
(7.64*)		(1.98°)			.058
4.60		.209		−1.98	.012
(7.73*)		(2.35+)		(−1.50)	.082

t-statistics in parentheses.
* Significant at 1 per cent level.
\+ Significant at 5 per cent level.
° Significant at 10 per cent level.

The significantly positive coefficient of DO seems to reflect the fact that, after a lost election, the opposition party has few posts to offer to its elder politicians (who lost the election). Even though this part of the evidence seems to support the "grandfather hypothesis," the simple correlation between the rank number and the age of the Commissioners is only weakly positive ($r = .11$).

If the government or voters of a member country attribute considerable importance to the European Community, they prefer their Commissioner(s) to stay long enough to acquire expertise and establish contacts in EC politics. On this account, we would expect the term of office to be longer, the lower the rank number of the Commissioner. However, this is only the principal's perspective. From the point of view of the agent, a highly qualified politician is not likely to stay in Brussels for very long because he has the option of returning to the domestic political arena. To investigatte this question, the Commissioners' terms of office have been regressed on the same set of variables as before. As *Table 7* shows, C and P_t do not take significant regression coefficients over the full sample. (The same is true for the coefficient of correlation between the country averages reported in Table 4.) The evidence merely indicates that the terms of office tend to shorten (see also Table 4) and that Commissioners from the more central member countries tend to stay longer (which can easily be explained from an agent perspective). For the subperiod 1973–92, however, C_t takes a significantly positive regression coefficient. Thus, on balance, high-quality politicians who are attracted by the larger EC budget do not stay for very long because they can advance at home. The agent's interest dominates.

Politicians and bureaucrats may also be attracted to the EC Commission by the very high after-tax salaries which it offers. The net salary of an EC official is between 72 and 89 per cent higher than the net salary of a comparable official in a German federal ministry (Frey, 1985; Table 8-3). The President of the EC Commission is known to have received a net salary of $ 145,000 plus a tax-free expense allowance of $ 15,000 in 1989, the other commissioners earned $ 115,000 to $ 130,000 plus $ 4,750. The fact that international organizations pay much higher salaries than national governments[21] tends to confirm the theoretical hypothesis that higher-level governments are subject to less control because centralization raises the voters' cost of information and weakens their incentive to control. If this is true, employment with higher-level governments is also more attractive in terms of slack and discretion. On average, 47 persons apply for one post advertised by the EC Commission; for this reason, applications are invited at increasingly irregular intervals (Staufenbiel, 1992: 384).

Another public choice aspect that can be clarified with the help of EC budgetary data is the question whether the member country with the median per capita income[22] has an incentive to increase EC expenditure on EC public goods. *Table 8* reveals that Italy is the median country regardless of whether EC

Table 8. Decisive voters among EC member countries by income and financial contribution per head

Country	GDP per head (ECU, 1990)	Cumulative shares of EC population[a]	Cumulative votes in EC Council of Ministers	Country	Contribution to EC budget per head (ECU, 1989)	Cumulative shares of EC population[a]	Cumulative votes in EC Council of Ministers
Portugal	4,737	3.0	5	Portugal	46.78	3.0	8
Greece	5,339	6.1	10	Greece	56.43	6.1	10
Ireland	9,325	7.2	13	Spain	91.40	18.1	18
Spain	9,749	19.2	21	Ireland	104.98	19.2	21
U.K.	13,496	36.7	31	U.K.	114.76	36.8	31
Netherlands	14,634	41.3	36	Italy	132.21	*54.5*	*41*
Italy	14,831	*58.9*	*46*	France	153.74	71.7	51
Belgium	15,175	61.9	51	Denmark	169.26	73.3	54
France	16,469	79.1	61	Germany, F.R.	179.14	92.3	64
Luxembourg	17,628	79.2	63	Netherlands	181.86	96.9	69
Germany, F.R.	18,596[a]	98.5	73	Belgium	181.99	99.9	74
Denmark	19,627	100.1	76	Luxembourg	194.39	100.0	76
EC	14,426[a]	100.0	76	EC	136.13[b]	100.0	76

[a] Excluding former GDR.

[b] So-called "own resources", i.e., including financial contributions from member states.

Sources: European Economy, 1990 (annual review); The Community Budget: The Facts in Figures, 1991.

Table 9. Percentage of population favoring EC responsibility with respect to

	F	B	N	I	D	L	IRL	E	UK	GR	DK	P	EC
Scientific and technological research	85	84	82	82	77	82	73	74	69	66	72	54	77
Cooperation with developing countries	81	76	75	83	77	72	73	70	76	56	64	54	76
Protection of the environment	73	69	82	64	77	63	44	63	63	50	44	42	67
Foreign policy toward third countries	73	78	68	78	67	63	64	58	61	36	47	41	66
Currency	72	67	53	68	59	56	57	46	42	44	54	28	57
Rates of value added tax	74	77	73	44	53	30	58	44	37	35	49	25	51
Security and defence	51	58	63	56	58	63	25	37	39	23	33	24	48
Basis rules for broadcasting and the press	57	53	55	48	51	51	43	47	35	39	20	36	47
Protection of computer-based information on individuals	39	45	38	37	52	30	36	35	32	36	16	22	39
Health and social welfare	34	35	41	48	37	31	35	40	35	45	11	36	38
Worker participation	41	37	38	37	36	22	43	31	36	31	12	22	36
Education	42	28	31	42	32	34	29	33	23	40	15	28	34
Average	60	59	58	57	56	50	48	48	46	42	36	34	53
Receipts from EC minus payments to EC per capita p.a. (ECU, 1985–89)	−2	+63	+77	+23	−72	+1,150	+394	+19	−65	+128	+91	+48	–
GDP per capita (ECU '000, 1990)	16.5	15.2	14.6	14.8	18.6	17.6	9.3	9.7	13.5	5.3	19.6	4.7	14.4

Sources: Eurobarometer, No. 32, December 1989; The Community Budget: The Facts in Figures, 1991; European Economy, 1990 (annual review) expenditure is financed from a proportional income tax or the current revenue system and whether the actual voting weights used in the Council or population weights are applied. However, whereas under a proportional income tax (or value-added tax) EC budgetary expansion would involve a redistributive loss for Italy, she gains under the current financing mechanism (because Italy's contribution per head is smaller than the average contribution per head). At present this perverse incentive is hardly operative because, according to Art. 203, the Council has to adopt the budget with a qualified majority (54 out of 76 votes) and because the decisive voter, Denmark, contributes more revenue per head than the average. However, as proposed by the EC Commission, the required majority is being reduced for more and more issues including spending decisions. The Enlargement Task Force of the Commission suggests to "freeze the qualified majority at its present level of 54 votes so that each successive enlargement (with more votes added to the total) reduces the relative level from 71 per cent progressively towards 50 per cent" (as quoted in Financial Times, 18 May 1992).

Since the bulk of EC expenditures is spent on transfers rather than public goods, revenue sources and spending outlets should be compared on a geographical basis. *Table 9* (second line from below) shows that, in 1985–89, only the three largest member countries (Germany, United Kingdom and France) paid in more than they received back[23] as public choice theory would predict (Olson and Zeckhauser, 1966; Brennan and Buchanan, 1980: 182), and that France is the decisive voter under qualified majority voting. The largest net receipts per capita are obtained by Luxembourg but in the case of Luxembourg and Belgium these net receipts are likely to represent income from the provision of services rather than transfers.

Do the national net receipts from, or payments to, the EC explain the preference for EC centralization in the individual member countries? To investigate this question, annual averages of the variables EU_t have been regressed on N or NR_t, Y_t, P_t, TR_t, D, the years of membership (T_t) and a dummy for the EC presidency (it takes the value of one if a compatriot is president of the EC Commission). The time dimension of this pooled analysis is 1962, 1970, 1973, 1975 and 1978–92 for EU_t and 1973–92 for EC_t. *Table 10* contains the results. *European unification* turns out to be more popular, the larger the country's share in EC population, the higher its net receipts from the EC, the lower its GDP per capita and the longer its period of EC membership. Enthusiasm for *EC membership* is also stronger, the longer the country has been a member; moreover, trade with the EC has a significantly positive effect on it. NR_t does not take a significant regression coefficient but its simple correlation with EC_t is clearly positive ($r = .21$). If country dummies are added (except for Germany), only T_t keeps its significant coefficient. Thus, the other variables contribute little to explaining variability over time. The coefficients of the country

Table 10. Share of population favoring European unification or EC membership, pooled analysis, 1962–92

Explanatory variables	European unification	European unification	EC membership	EC membership
Population share in EC-12	.631	− .026		
(P_t)	(5.82*)	(− .06)		
Net receipts from EC per capita in 1975–89	.019	− .031		
per annum (NR)	(3.72*)	(− .43)		
Percentage deviation from EC GDP	− .162	.014		
per capita (Y_t)	(−6.80*)	(.29)		
Foreign trade with EC/GDP			.286	− .069
(TR_t)			(4.23*)	(− .323)
Years of	.803	.481	.804	.714
membership (T_t)	(10.63*)	(6.41*)	(9.03*)	(6.87*)
Intercept	49.71	65.22	40.62	43.09
	(28.32*)	(9.97*)	(20.84*)	(16.15*)
Country dummies				
Belgium		−4.08		5.30
		(− .81)		(.85)
Denmark		−21.89		−10.13
		(−3.32*)		(−3.85*)
France		1.79		1.89
		(.68)		(.89)
Ireland		.64		9.35
		(.05)		(1.50)
Italy		6.90		14.40
		(1.95°)		(6.61*)
Luxembourg		18.75		18.77
		(.52)		(3.02*)
Netherlands		2.11		19.05
		(.45)		(4.40*)
United Kingdom		−7.77		−10.78
		(−3.15*)		(−4.49*)
Greece		4.94		8.51
		(.78)		(2.76*)
Spain		13.33		22.75
		(3.51*)		(6.50*)
Portugal		10.04		24.36
		(1.80°)		(5.00*)
R^2	.518	.767	.411	.827
$\bar{R}^2$	.507	.746	.405	.815

dummies indicate that, given the duration of their membership, the respondents in Italy, Portugal and Spain are particularly European-minded and that the Danes and the British are particularly sceptical.

Finally, the more recent and disaggregated data of Table 9 ought to be analyzed. In 1989, the proportion of the population that favors policy centralization in the EC was on average largest in France and Belgium – the two member countries which host the most important Community institutions, the EC Commission and the European Parliament. Moreover, at the time of the opinion poll, a Frenchman was president of the EC Commission. As Table 1 has shown, both countries were also among the most centralized states of the Community in terms of expenditure concentration. More generally, the preference for EC centralization is strongest among the original six founding members of the Community who are also the most central member countries and probably gain most from EC market integration. Apparently, the man in the street finds it difficult to distinguish between the benefits of market integration and the effects of further political integration, i.e., centralization.

In 1989, on a pure cross-section basis, the average proportion in favor of EC centralization is virtually uncorrelated with net receipts per capita (r = – .055) and positively correlated with GDP per capita (r = .473). This high positive correlation may be due to the fact that the high-income countries of the Community have highly regulated economies and that political centralization serves to extend these regulations to the lower-income countries. The disaggregated data of Table 9 enable us to specifically measure the preference for EC centralization in the field of health and social welfare and to analyze it in a redistributive context. However, its simple correlation with net receipts per capita in 1989 is also negative (r = – .177). If there is a redistributive intention, it can only be inferred from the high negative correlation with GDP per capita (r = – .480): the low-income countries are in favor of centralizing social policy in the European Community. However, since the correlation between net receipts per capita and GDP per capita is positive (r = .127), EC redistribution seems to be regressive.

The other hypotheses of Section 2 cannot be checked with quantitative data but some striking examples will be given from EC history. It will be helpful to proceed in chronological order.

The first major policy instrument to be centralized was *agricultural policy*. The Common Agricultural Policy (CAP) cannot be justified on efficiency grounds. Transfers to farmers, it is true, may be justifiable as part of social or environmental policy. But if social policy is the reason, income maintenance should allow for the average level of regional income which differs greatly among the EC member countries (Table 5). If farmers are to be paid for their environmental services, such compensation payments ought to take into account the interregional differences with respect to environmental preferences.[24]

If the centralization of agricultural subsidization cannot be justified on efficiency grounds, a public choice explanation is needed. The standard explanation has been that the establishment of the EC customs union for manufactured goods was expected to benefit Germany at the expense of France and that the Common Agricultural Policy served as a Paretian compensation for France. Similar arguments have been adduced by the Mediterranean member countries to obtain a doubling of the EC structural funds in connection with the internal market programme, the creation of a "cohesion fund" to be financed by the EFTA countries in the European Economic Area (EEA)[25] and the planned EC cohesion fund for environmental and labor market policies in the context of European Monetary Union. There are several problems with this explanation:

1. There is no convincing economic theory and no empirical evidence that market integration hurts the low-wage regions. On the contrary, classical trade and allocation theory predicts that the labor-abundant countries should be the main beneficiaries (Peck, 1989: 294). For example, France has increased its EC market share in the export of manufactures since 1957.
2. The deadweight losses from CAP render it a highly inefficient mechanism of effecting the transfer from Germany to France. There must have been less costly ways of hiding the tribute (if it had to be concealed at all). Moreover, France herself has become a net contributor to the EC budget.
3. For a long time, the German government has been the main opponent of agricultural reform. It was only in the context of the Uruguay Round (which offers large benefits to Germany) that it abandoned this position. The EC Commission was even more reform-minded than the Council because bureaucrats, unlike politicians, are not interested in the farmers' vote but in the prestige of their own organization (for which CAP is a liability).[26] As a general rule, bureaucrats are more responsive to capital-intensive than to labor-intensive rent-seeking.

As these considerations show, the introduction and especially the expansion and survival of CAP is more convincingly explained by the political economy of interest groups. It is an instance of the rule that regionally homogeneous interest groups can gain from centralization (proposition 3 in Section 2). The national politicians, too, may prefer to delegate the ugly work of satisfying the farm lobby to the EC Commission because the payment of subsidies is unpopular with the other voters of their ruling coalition (proposition 4 (iv)).

Other EC policy instruments which are primarily used to cater for interest groups are the highly protectionist trade policy, the steel cartel, industrial policy, research subsidies and the fisheries policy. Together with CAP these policies account for 72.6 per cent of EC expenditure (1989). Moreover, in terms of pages, at least 78 per cent of EC legislation are devoted to interest groups

(Peirce, 1991a: Table 3). Thus, the European Community has specialized in the supply of privileges to interest groups. As Peirce (1991a: Table 4) has shown, the number of European interest groups has increased from 59 in 1954 to 546 in 1984. 44 per cent of the new associations were established shortly before or after the foundation of the European Economic Community (1955–64). As public choice theory would predict, most European pressure groups (83 per cent) promote the interests of industry, commerce and the professions, and very few represent consumers, taxpayers, environmentalists or small enterprises.

Another major step on the way toward centralized policy making has been the establishment of the *European Monetary System* (EMS) in 1979. Several authors have suggested that the German chancellor was primarily interested in preventing the independent German central bank from pursuing a more restrictive monetary policy than the other member central banks in the approach to the German federal election of 1980.[27] From the point of view of the other participating governments, the EMS was attractive as a device to stifle competition from the most successful performer, the Bundesbank (a variant of proposition 6). When they realized, by 1983, that they could not control the monetary policies of the Bundesbank, they decided to use it as a scapegoat for the stabilization recession which, by that time, had become inevitable (proposition 4 (iv)).

The political economy of the *internal market* project and the Single European Act (1987) has been discussed by several authors. Katseli (1989: 5 ff.) believes that the programme has been pushed through by the large corporations of Europe in order to reap economies of scale and improve their strategic position vis-à-vis competitors in the rest of the world. There is no evidence for this, however. The initiative came from the EC Commission, especially Lord Cockfield and Jacques Delors (Calingaert, 1988: 9). When the new president of the EC Commission travelled to the capitals of the member countries in the winter of 1984/85 and suggested initiatives for a common defense policy, monetary union and the internal market, he realized that only the latter would be unanimously accepted (Katseli, 1989: 6; Nevin, 1990: 333 f.). Apart from market integration, the aim of the Commission was to replace the national trade restrictions by additional budgetary resources for the structural funds and to centralize further policy instruments in the wake of the internal market programme (Urwin, 1991: 232, 240). The strategy of establishing linkages with the internal market programme is particularly apparent in the so-called Delors Report (Committee for the Study of Economic and Monetary Union, 1989: para. 33):

> The completion of the internal market will result in a marked easing of the overall burden of regulation, but for the Community institutions it will mean a substantial addition to their executive and policing functions.

The Commissions's roundabout approach to centralization proved to be highly effective. First of all, the Single European Act gave it additional powers in the field of exchange rate policy (Art. 102 a), social policy (Art. 118 a), research promotion (Art. 130 f-g) and environmental protection (Art. 130 r-t). Second, in December 1989, the common control of mergers and the Social Charter were adopted. Finally, at the Maastricht summit (1991), Delors even obtained an agreement on monetary union and defense, targets which he had to postpone but never abandoned.

Before we turn to these elements of policy centralization, we should consider an important puzzle posed by the internal market programme. Why have Commission and Council accepted the principle of mutual recognition of national regulations even though it will weaken their power? Why has it not been warded off by the national member governments and interest groups even though it leads to competitive deregulation?

Bernholz (1990: 96) believes that interest groups were simply taken by surprise. If Peltzman's theory of deregulation (1989) is applied to Europe, resistance from interest groups may have been weak because past and anticipated market integration in the Community dissipates the rents from national regulations. In Katseli's framework (1989), big business in Europe was more interested in gaining competitiveness vis-à-vis third countries than in national rent-seeking. Moreover, it may have hoped to obtain encompassing EC regulations in the longer run when the national regulations would be shown to be ineffective.[28]

We can dispense with all these explanations if we bear in mind that the principle of mutual recognition of national regulations is due to the European Court of Justice (the Cassis de Dijon case, 120/78). The EC judges are interested to exercise their power by removing barriers to European market integration. Even though some of them later return to the national ministries or courts, national interest groups find them less accessible than EC bureaucrats or national regulators.[29] The preferences of the Commission and the member governments are revealed by the Single European Act which calls upon the Commission to propose common regulations in the fields of health, safety, environmental and consumer protection (Art. 100A (3)) and facilitates EC regulation by abandoning the unanimity requirement in exchange for qualified majority voting (Art. 100A (1)). Moreover, Art. 100B (1) SEA was designed to avoid the automatic mutual recognition of national regulations implied by the Cassis Dijon judgement: conformity with the regulations of the exporting member country was not supposed to be sufficient unless the Council decides so with a qualified majority and has failed to agree on a common regulation by the end of 1992.[30] The European Court of Justice has chosen to ignore Art. 100B (1) SEA and to give priority to Art. 30. But it is not true that the Commission has promoted the principle of mutual recognition because harmonization proved too difficult (as Calingaert, 1988: 33 believes); on the contrary, it has tried to control the potential effects of the Cassis de Dijon precedent (as Kirchner, 1992: 15, 19 f., suggests).[31]

The *Social Charter*, the *common environmental policy* and *EC merger control* have all been advocated by the German government. In the case of EC social policy, this may seem to be especially surprising because, at the time, Germany had a non-socialist government and its demands for EC labor market regulation were even supported by the German employers' association in a joint declaration with the unions (June 1989). However, in all three instances, the position of the German government and interest groups can easily be explained on the lines of proposition 6: regulations may be demanded by the competitors of those to be regulated because they reduce the competitiveness of the regulated. Germany has a tightly regulated labor market, an expensive system of occupational training, high environmental standards and – together with the U.K.[32] – the most restrictive anti-trust legislation in the EC. Thus, the liberalization of trade and capital movements under the internal market programme exposes German producers to stronger competition from other EC suppliers who bear a lighter burden of regulation and therefore produce at lower cost. The French government has pursued a similar strategy since 1958 (Urwin, 1991: 78).

The demand for EC regulations by interest groups in the highly regulated member countries seems to be based on the assumption that the internal market programme will not bring about a high degree of international labor mobility within the Community and that only a small part of the cost of higher unemployment in the low-wage countries will have to be borne by workers and employers in the other countries through international resource transfers. In most of the low-wage and less regulated countries, the Community seems to have turned the balance of power in favor of rent-seekers and regulators and against the marginal workers who represent a minority and are not well organized. Where this is not the case, the country can gain by agreeing to central regulation of the other low-income countries and opting out for itself. This is the British approach to the Social Chapter.

As a result of EC *merger control*, the European Commission has become the sole supplier of large-firm monopoly rights in the Community (Peirce, 1991b: 530). The national anti-trust agencies which have lost this power are largely independent of their national governments. Thus, the centralization of competition policy confirms proposition 4 (v): the national governments tend to trade the powers of independent national institutions in exchange for EC benefits. In Germany, the Bundesbank, the supervisory office for the insurance industry and the Länder's constitutional competence over *education*, *occupational training*, *television*, etc. provide further examples. Similarly, the independent national judiciaries are losing out to the European Court of Justice.

The Maastricht agreement on *monetary union* goes back to the initiative of the German minister of foreign affairs (Genscher Memorandum of February 1988). From a public choice perspective, this is not surprising (Vaubel, 1991b). By 1987, the EMS had returned to low rates of inflation (2.2 per cent on average), and the Bundesbank was no longer needed as a political scapegoat for the stabilization recession which disinflation had generated in France and Italy. Moreover, the liberalization of capital movements under the internal market programme was likely to increase the Bundesbank's dominance. The German minister of foreign affairs and his diplomats had to bear the brunt of foreign discontent with the Bundesbank's uncompromising monetary stance, and he could hope to obtain agreement on an common EC foreign and defense policy which would enhance Germany's international influence.

Finally, the harmonization of *taxation* in the European Community can serve to illustrate proposition 4(iii). According to the theory of optimal taxation, the optimal tax structure and tax rates depend on the elasticities of demand and supply in the economy concerned. As these elasticities and the cost and effectiveness of tax collection differ among the member countries, uniform tax rates are not desirable. Moreover, to the extent that tax rates may have to converge, the appropriate range is more likely to be found by competition than collusion. However, the EC Council of Ministers has agreed that, from 1993 onward, the rate of value-added tax should be no less than 15 per cent in all member countries. Three member countries (Germany, Spain and Luxembourg) had to raise their tax rates. In March 1992, a study group appointed by the EC Commission has proposed to introduce a minimum corporate income tax of 30 per cent from 1994 onward and a minimum of 40 per cent later on. Even if convergence by agreement is considered preferable to convergence by competition, the choice of minimum rather than maximum tax rates is revealing. The EC agreement makes it easier for the German Minister of Finance to obtain the tax hike which he desires for other reasons,[33] and the government of the more highly taxed member countries welcome the opportunity to suppress or weaken the competition from "tax havens" such as Luxembourg.

4. Conclusion

What precautions can be taken to ensure that a community or union of individual states that has been conceived as a classic federal state does not gradually degenerate into a highly centralist state? Many useful proposals have been submitted (see notably Bernholz, 1992) but in the context of this analysis the following five stand out:

1. The budget, the personnel and the net wage at the central government must not be permitted to exceed that of the median member state (or even that of any member state).
2. The constitution would have to prohibit the reelection of politicians to the federal parliament and any federal office as well as the reappointment of members of the federal administration and the federal court(s).[34]
3. The safest way to avoid centralization is to withhold the power to tax and to issue debt from the central government. As under the U.S. Articles of Confederation, in Bismarcks Reich and presently in the European Community, the central government would be exclusively financed by contributions from the member states. They could be fixed as a proportion of the tax revenue raised by each member state (Lee, 1985). If federal taxation was admitted, however, it would be important to require a referendum (as in Switzerland) whenever a tax rate is to be raised.
4. The median or decisive voter must not have an interest in increasing central government expenditure for purely redistributive reasons. The safest way of avoiding such perverse incentives is a constitutional clause that prohibits transfer payments by the central government (Bernholz, 1992) or requires unanimity among the member governments. Similarly, all amendments to the federal constitution that increase the power of the central government, would have to require the unanimous consent of the member states (as under the U.S. Articles of Confederation and as yet in the European Community).
5. Each member state would have the explicit right to leave the union at any time, if a simple majority of its population voted in favor of secession (Buchanan, 1990; Bernholz, 1992).[35]

Notes

1. Further back, the share of U.S. domestic central government expenditure in total U.S. domestic government expenditure rose from 16 per cent in 1840 to 27 per cent in 1902 (Alexander, 1973/87: 103, Table 5-1).
2. For the U.S. see the index of functional centralization constructed by Riker (1964: 81 ff.). In postwar Germany, 24 out of 25 constitutional changes affecting the division of powers between central and state governments were transfers of functions to the central government (Edling, 1984, 1987).
3. The two world wars have had centralizing ratchet effects on non-military government expenditure in the U.K. (Peacock and Wiseman, 1967: 109) and Switzerland (Kraus, 1983: 185) but only partly so in Canada and Germany and not at all in the United States (Kraus, ibid.).
4. With respect to the EC, this will be shown in Section 3.
5. This point is also of relevance to constitutional conventions. For example, about three-fourth of the members of the U.S. Constitutional Convention in 1787 were or had been members of the national Congress (Potter, 1955: 18). With very few exceptions, "all the delegates ... were nationalists in the narrow sense that they believed it necessary to reorganize and strenghten the

central authority" (McDonald, 1985: 185; Riker, 1987: 12 ff.). By contrast, "there is little doubt that the Anti-Federalists would have won a Gallup poll" (Morison and Commager I, 1962: 290).

6. Jacobs and Karst (1986: 177) note that "the European Court does not seem ever to have ruled a Community measure unlawful ... for encroaching on the competence of the Member States". Moreover, it has invented the principle of the supremacy of Community law: "There is no express provision in the Community Treaties ... for the primacy of Community law over Member State law ... The primacy of Community law is a principle developed by the Court ... Community law prevails even over the Member State constitutions (case 11/70) so that ... the humblest Community provision prevails over the highest Member State law" (ibid., p. 233). The principle has met reservations from the German and the Italian Constitutional Courts (Elazar and Greilsammer, 1986: 103). In the German literature, the centralist tendencies of the European Court have been criticized, e.g., by Wienke (1990), Borchmann (1988) and Niederleithinger (1990).
7. Only in the case of regionally heterogeneous interests ("local factions") does centralization reduce the influence of pressure groups as Madison (1787/1987) has argued in his Federalist Paper No. 10.

   Another qualification is that the centralization of government may hamper the establishment of new pressure groups owing to the free-rider problem (Olson, 1965).

   Our hypothesis is not inconsistent with the finding of Mueller and Murrell (1986: Table 5) that the centralization of government has a significantly negative effect on the *number* of interest groups. We would expect their number to diminish but their influence to increase.
8. Riker (1964) and Aranson (1990) argue that the external threat from the British Crown explains the adoption of both the Articles of Confederation (1781) and the Federal Constitution (1789). This comes out most clearly in Federalist Paper No. 3 (Jay).
9. In most other cases, the federation or federal state has been imposed by a former colonial or occupying power which dismissed the country into independence (several former British colonies, the Federal Republic of Germany, the Federal Republic of Austria) or by a victor who wanted to consolidate his power after a war (Germany in 1867 and 1871, to some extent also the foundation of the European Coal and Steel Community, Euratom and the European Economic Community in the 1950s). For the view that the French government viewed the European institutions primarily as a means of containing West Germany see notably Swann (1988: 6), Harrop (1989: 11f.) and Urwin (1991: 45).
10. For time series analyses see Marlow (1988) and Grossman (1989). The cross-section studies have been surveyed by Joulfaian and Marlow (1991). Similar results are reached by Blum and Dudley for Germany (1991: Table 1).
11. With the exception of Iceland and Luxembourg which have been omitted, these are the industrial countries for which the IMF Government Finance Statistics contain data on the central government's share in government expenditure for most of the period. For most of these countries, these are the most recent data to be published in the IMF Government Finance Statistics. All data relate to consolidated expenditure plus lending minus repayments.
12. Apart from the measurement of government size, Oates' analysis differs from ours in that he uses data for individual years (mostly 1981 or 1982) and population rather than population density. As Joulfaian and Marlow (1991) have shown, Oates' estimates for a U.S. cross-section are not robust either if a more meaningful specification is chosen.
13. If the original regression $\ln (G/Y) = \ldots + .5 \ln (G^C/G) + \ldots$ is rewritten as $\ln (G/Y) = \ldots + .5 \ln (G^C/Y) - .5 \ln (G/Y) + \ldots$, we get $1.5 \ln (G/Y) = \ldots + .5 \ln (G^C/Y) + \ldots$ or $\ln (G/Y) = \ldots + .33 \ln (G^C/Y) + \ldots$ Differentiating with respect to time, we can say that a one per cent increase in G^C/Y will raise G/Y by only .33 per cent. However, a .78 per cent increase in G/Y would be required to keep expenditure of the lower-level governments

(G^l) constant. To see this, take rates of change of the identity $G/Y = G^C/Y + G^l/Y$ so that $\hat{G} - \hat{Y} = (G^C/G)(\hat{G}^C - \hat{Y}) + (G^l/G)(\hat{G}^l - \hat{Y})$ and set $\hat{G}^l$ and $\hat{Y}$ equal to zero.

14. In the context of a unitary state, this theory has been modelled and tested by Meltzer and Richard (1983). Bös (1978) has shown that the distribution of average incomes among the West German Länder is skewed to the right.
15. As Salmon (1987: 37) points out, party competition at the center can force the central government and parliament to decentralize.
16. "As men engaged in expanding a government, (the writers of federal constitutions) are much more likely to be preoccupied with practical expedients for the moment than with provisions for the distant and not clearly foreseen future. As centralizers, they are much more concerned with centralization itself than with fears that centralization may go too far" (Riker, 1964: 14).
17. In 1987, for example, federal government expenditure in the United States was $ 1,004 billion and state government expenditure $ 404 billion; federal government personnel (including the armed forces) was 5,265,000, state government personnel 4,115,000 (Statistical Abstract of the United States). In Germany the federal government has a larger budget (1987: DM 271 b.) than the Länder (DM 263 b.) but its personnel (840,000) is still smaller than the Länder's personnel (1,487,300).
18. An alternative test would be to follow their career after they have left the Commission. However, since most of them are no longer listed in "WHO is WHO?" once they have stepped down, this test is not feasible owing to data problems.
19. The following data sources have been used:
   - European Economy, annual review 1991, for P_t, Y_t, NR_t and TR_t,
   - budgets, European Communities, for C_t, N and NR_t,
   - IMF Government Finance Statistics for C and C_t,
   - Eurobarometer for EU_t and EC_t.
20. Initially, all explanatory variables have been included. Subsequently, variables with clearly insignificant coefficients were omitted in a stepwise procedure (starting with the lowest absolute t-statistics). The elimination of variables did not have a substantial effect on the coefficients of the remaining variables.
21. At the OECD, net salaries are 39–67 per cent higher than comparable German salaries (Frey, ibid.). Net salaries at the IMF exceed pre-tax salaries at the Federal Reserve Board on average by 64 per cent (Vaubel 1991a: Table 5).
22. The EC median of the national *averages* is used instead of the EC median of the national *medians* for computational convenience. The assumption is that the skewness of the income distribution is about the same in all member countries.
23. The net payments deficit of Germany, Britain and France amounted to 11.4 per cent, 9.5 per cent and .3 per cent of the EC budget, respectively.
24. Empirical work shows that the demand for environmental protection depends significantly on income, age etc. (e.g., Sinden and Worell, 1979: 333; Schneider, 1992: Table 1). In a cross-section analysis for the EC member countries, the share of the population that wishes more environmental protection (Eurobarometer 1979, 1981) bears a clear positive correlation with GDP per head ($r = .35$) and the density of population ($r = .31$). (As GDP per head and density of population are highly collinear simple correlation coefficients are reported. They relate to the logarithms.) Within the Community, the density of population varies between 50 inhabitants per km^2 in Ireland and 361 in the Netherlands.
25. Many textbooks on foreign trade analyze the substitution of tribute for protection. The draft treaty on the EEA offers EFTA free access to EC markets in exchange for regular tribute payable in terms of fishing and pollution rights as well as cash for the cohesion fund.
26. As Crain and McCormick (1984) have shown, the opposite is the case if the provision of rents impairs the politicians' electoral prospects.

27. See Willgerodt (1978), Sachverständigenrat (1978: para. 358), Vaubel (1980: 179 ff.). Between February 1977 and January 1980, the federal government did not command a majority in the central bank council of the Bundesbank (Vaubel, 1993). Putnam and Bayne (1984: 87) show that the German fiscal stimulus decided at the Bonn summit of 1978 was also part of this pre-election strategy.
28. For example, the industrial standards set by the European Committee for Standardization (CEN) are ultimately the result of compromise among the producing firms of the member countries. Peirce (1992) suggests that the producers are more likely to agree on standards that act as barriers to imports from third countries than on efficiency-enhancing standards because the latter would have to be agreed in highly fragmented industries.
29. While 50 per cent of the judges of the European Court of Justice have been reappointed at least once (Kuhn, 1993: 191), only 35 per cent of the EC Commissioners have. Kirchner (1992: 11) suggests that the EC judges find it difficult to return to the judiciary of their home country.
30. Kapteyn, Verloren van Themaat and Gormley (1989: 404 f.) consider this interpretation possible but "not imperative" and suggest that Art. 100B (1) may also be explained as a supplementary chance to make assessments of the equivalence of particular national provisions. Verloren van Themaat (1988: 125), however, warns that Art. 100B must not affect the competence of national courts and of the Court of Justice to declare national measures equivalent and restrictions unjustified.
31. For example, Verloren van Themaat (1988: 117) complains that "Article 100A in several respects seems to deviate from the body of case-law of the Court."
32. This may explain why EC competition policy is more popular in Britain than in France or Italy and why the EC commissioner for competition policy used to be a very active Briton.
33. It even enabled him to argue that the tax increase would go into effect without the consent of the Bundesrat. At the time, the opposition commanded a majority in the second chamber.
34. According to the Treaty of Maastricht (Art. 109 a IV), the directors of the European Central Bank may not be reappointed.
35. Scholars of European law disagree about whether the individual member states may secede from the European Community. The European Court of Justice has sustained the position that secession is impossible (Elazar and Greilsammer, 1986: 101 f.). If one member state withdraws, the Community dissolves.

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Appendix

Members of the Commission of the European Economic Community and the European Communities

Name	Member			Post before joining Commission		Age	Rank
	From	Until	Nat.				
Hallstein, Walter	1958	7/67	D	1951–57	Secretary of State in the Foreign Office	56	2
Malvestiti, Piero	1958	1963	I	1953–54	Minister of Trade and Industry	58	2
Mansholt, Sicco L.	1958	(1/73)	NL	1956–58	Minister of Agriculture	49	1
Marjolin, Robert	1958	1967	F	1955–57	Professor of Economics	46	3
Rey, Jean	1958	(1970)	B	1954–58	Minister of Economic Affairs	55	1
Lemaignen, Robert	1959	1/62	F		President of several companies	64	3
von der Groeben, Hans	1958	(1/70)	D		Ministerialdirigent in the Ministry of Economic Affairs	50	3
Petrilli, Giuseppe	1958	2/61	I		President of the National Institute of Health Insurance	44	3
Schaus, Lambert	1958	7/67	L	1955–57	Ambassador in Brussels	50	3
Sandri, Lionello, I.	2/61	(7/70)	I	since 1940	Professor of Law	50	3
Rochereau, Henri	1/62	(1970)	F	1959–61	Minister of Agriculture	53	1
Caron, Giuseppe	1963	9/64	I		Undersecretary to Public Works	64?	3
Colonna, Guido	9/64	(1970)	I	1962–64	Chief Delegate to NATO	56	3
Hellwig, Fritz	(1959)	6/70	D	1953–59	Member of Parliament	46	3
Barre, Raymond	7/67	12/72	F	1964–67	Member of the Planning Comission	43	3
Coppé, Albert	(1952)	12/72	B	1950–52	Minister, e.g., of Economic Affairs	40	1
Sassen, Emmanuel	(1958)	6/70	NL	1950–58	Member of the Administrative Court of Justice	46	3
Bodson, Victor	7/67	6/70	L	1964–67	President of the chamber of deputies	65	3
Martino, Edoardo	7/67	6/70	I	1962–63	Undersecretary at the Foreign Office	57	3
Haferkamp, Wilhelm	7/67	1/85	D	1958–67	Deputy in Nordrhein-Westfalen, board member of DGB	53	3

Appendix. Continued

Name	Member From	Until	Nat.	Post before joining Commission		Age	Rank
Deniau, Jean-François	7/67	4/73	F	1963–66	Ambassador to Mauretania	38	3
Malfatti, Franco Maria	7/70	3/72	I	1969–70	Minister for State Holdings, Postal Services and Telecommunication	43	1
Spinelli, Altiero	7/70	7/76	I	1966–70	Director of the Institute for International Affairs, Rome	62	3
Borschette, Albert	7/70	7/76	L	1958–70	Ambassador to the EC	50	3
Dahrendorf, Ralf	7/70	11/74	D	1969–70	Parliamentary Secretary of State in the Foreign Office	41	2
Mugnozza, Carlo	3/72	1/77	I	1953–72	Member of Parliament	52	3
Ortoli, François-Xavier	1/73	1/85	F	1968–69 1969–72	Minister Finance Minister of Industry and Science	47	1
Soames, Christopher, Sir	1/73	1/77	GB	1967–72	Ambassador to France	52	3
Hillery, Patrick John	1/73	1/77	IRL	1969–72	Minister of Foreign Affairs	49	1
Simonet, Henri	1/73	1/77	B	1972	Minister of Economic Affairs	41	1
Thomson, George	1/73	1/77	GB	1970–72	Opposition spokesman for defense	52	2
Lardinois, Petrus J.	1/73	1/77	NL	1967–72	Minister of Agriculture	48	1
Gundelach, Finn Olav	1/73	1/83	DK	1967–72	Ambassador, Head of the Delegation of DK to the EC	47	3
Cheysson, Claude	1/73 1/85	5/81 1/89	F	1970–73	President of Entreprise Minière et Chimique	52	3
Brunner, Guido	11/74	1/81	D	1972–74	Head of Planning Staff in the Foreign Office	44	3
Guazzaroni, Cesicio	7/76	1/77	I	1972–76	Ambassador	65	3

Appendix. Continued

Name	Member From	Member Until	Nat.	Post before joining Commission		Age	Rank
Vouel, Raymond	7/76	1/81	L	1974–76	Minister of Finance	53	1
Jenkins, Roy H.	1/77	1/81	GB	1974–76	Minister (Home Secretary)	56	1
Natali, Lorenzo	1/77	1/89	I	since 1966	various ministries, eventually Minister of Agriculture	54	1
Vredeling, Henk	1/77	1/81	NL	1973–76	Minister of Defense	52	1
Giolitti, Antonio	1/77	1/85	I	until 1974	Minister of the Budget	61	2
Burke, Richard	1/77	1/81	IRL	1973–76	Minister of Education	44	1
	1/83	1/85					
Davignon, Etienne	1/77	1/85	B	1969–76	Director General in the Foreign Office	44	3
Tugendhat, Christopher S.	1/77	1/85	GB	1970–77	Member of Parliament	39	3
Thorn, Gaston	1/81	1/85	L	1979–80	Deputy Prime Minister	52	1
Dalsager, Paul	1/81	1/85	DK	1979–80	Minister of Agriculture	51	1
Contogeorgis, Georges	1/81	1/85	GR	1977–80	Minister for Relations with the EC	68	1
Narjes, Karl-Heinz	1/81	1/89	D	1969–73	Economics Minister in Schleswig Holstein	57	3
				since 1972	Member of Parliament		
Andriessen, Frans	1/81	1/93	NL	1977–80	Minister of Finance	51	1
Richard, Ivor	1/81	1/85	GB	1974–79	permanent representative of the UK to the UN,	48	3
				1979–80	practising of the Bar		
O'Kennedy, Michael	1/81	1/83	IRL	1979–80	Minister for Finance	44	1
Pisani, Edgard	5/81	1/89	F	1978–81	Member of EP	62	3
Delors, Jacques	1/85	1/95	F	1981–84	Minister of Finance etc.	59	1
Cockfield, Lord	1/85	1/89	GB	1979–82	Minister of State at the Treasury	68	2

Appendix. Continued

Name	Member From	Member Until	Nat.	Post before joining Commission		Age	Rank
				1982–83	Secretary of State for Trade,		
				1983–84	Chancellor of the Duchy of Lancaster		
Christophersen, Henning	1/85		DK	1982–84	Minister for Finance and Deputy Prime Minister	45	1
Pfeiffer, Alois	1/85	9/87	D	since 1975	Board member of DGB	60	3
Varfis, Grigorios	1/85	1/89	GB	1981–83	Undersecretary at the Foreign Office	57	3
				1984	Member of EP		
De Clercq, Willy	1/85	1/89	B	1981–84	Deputy Prime Minister and Minister of Finance	57	1
Mosar, Nicolas	1/85	1/89	L	1980–84	Vice-president of the chamber of deputies	57	3
Davis, Stanley C.	1/85	1/89	GB	1979–81 1981–83	Opposition spokesman for trade and for foreign affairs	56	2
Ripa di Meana, Carlo	1/85	6/92	I	1979–84	Member of EP	55	3
Sutherland, Peter	1/85	1/89	IRL	1981–84	Member of the Council of Ireland, Attorney General	38	2
Marin Gonzales, Manuel	1/86		E	1983–85	Secretary of State for relations with EC	36	2
Carloso E. Cunha, Antonio J.B.	1/86	1/93	P	1980–81	Minister of Agriculture	52	3
				1983–85	Member of Parliament		
Matutes, Abel	1/86		E	1979–85	Member of Parliament	44	3
Schmidhuber, Peter	1/87		D	1978–87	Minister for Federal Affairs in Bavaria	55	2
Pandolfi, Filippo M.	1/89	1/93	I	1970–88	Minister, eventually Minister of Agriculture	61	1
Bangemann, Martin	1/89		D	1984–88	Minister of Economic Affairs	54	1
Brittan, Leon	1/89		GB	1985–86	Secretary of State for Trade and Industry	49	2

Appendix. Continued

Name	Member From	Member Until	Nat.	Post before joining Commission		Age	Rank
Scrivener, Christiane	1/89		F	1976–78	Secretary of State for Consumer Affairs,	63	3
				1979–89	Member of EP		
Millan, Bruce	1/89		GB	1983–88	Member of Parliament	61	3
Dondelinger, Jean	1/89	1/93	L	1984–88	Secretary General at the Foreign Office	58	3
MacSharry, Ray	1/89	1/93	IRL	1987–88	Minister of Finance	50	1
van Miert, Karel	1/89		B	1985–88	Member of Parliament	47	3
Papandreou, Vasso	1/89	1/93	GR	1985–86	Secretary of State for Industry,	44	2
				1986–88	Adjunct Minister of State at the Ministry of Commerce		

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Figures in parentheses relate to the High Authority of the European Coal and Steel Community and to the Commission of Euratom.