

Functions of Government

Lectures 17 and 18

Connolly and Munro (1999): Chp 24

Griffiths and Wall (2007): Chp 29

Stiglitz (2000): Chp 26

Outline

- The assignment problem
 - The case for central govt
 - The case for local govt
 - In practice, multi-level govt
- Rules for assignment
- UK: a unitary state
- EU: a type of federalist state

In favour of Central Govt

- Pareto gains from higher level govt
- 1. Economies of scale
 - Shared fixed costs eg tax collection and civil service
 - Intermittent demand eg judicial system
- 2. Spillover effects
 - Direct cost and benefit spillovers (eg pollution and free-rider problem)
 - Strategic substitute eg defence (public goods and non-excludable)
 - Strategic complements eg education
 - Indirect spillovers: inter-related policies
- 3. Co-ordination
 - Policy harmonisation eg transport system, product and safety regulation, legal and trade

In favour of Local Govt

- Pareto gains from regional units of govt
- 1. Local information
 - Knowledge of costs and benefits of local public goods (non-rival goods)
 - Uniform information v local information: Figure 1
 - **Tiebout Theorem**: under certain conditions local provision of public goods is Pareto-efficient.
- 2. Public choice
 - Centralisation and bureaucracy
 - Decentralisation and ↓ expenditure
- 3. Autonomy
 - Voluntary provision and community



Figure 1 **A decentralised outcome**

In favour of Multi-level Govt

- In practice, most countries have several tiers of govt
 - UK: 2+ tiers
- Optimal decision depends on type of public good
 - National level eg defence
 - Local or state level eg education
 - Other areas of expenditure are subject to variation
 - ⇒ Separate jurisdictions v economies of scope in govt
 - Decentralisation and incomplete contracts?
- The Assignment Problem
 - The design of govt: which tier will deal with what function?
 - Trade-off: spillovers v local tastes/preferences
 - Issue of separability

How to Assign the Functions of Govt?

- Rules for Assignment of Taxes
 - Mobile factors: CG and a progressive, re-distributive taxation
 - Immobile factors: local taxes or user fees
 - Equity: CG to oversee re-distribution of uneven resources
- The Assignment problem and Institutions
 - A unitary state (UK, France)
CG decides nr of lower tiers, geographical jurisdictions, decentralised power
 - A federal state (US, EU, Germany, Australia)
CG is constrained: tiers of govt are constitutionally fixed, requires agreement, state functions
- Political decision-making
 - Sovereignty v autonomy debate

Assignment in the UK

- Unitary nature of the state
 - Allowed change in decision-making structures of local govt
- 1. Greater London Authority and Mayor of London
 - Strategic economic policy; transport policy
- 2. Compulsive competitive tendering v best value
 - Cost of service v quality, improvement and consultation
- 3. Directly elected regional assemblies
- 4. Social policy initiatives: key features
 - Role of local authorities
 - Partnership and collaboration across public, private and voluntary sectors
 - Audit and inspection of quality and standards
 - Devolved responsibilities

The EU and Federalism

- EU Institutions

- The European Commission: external rep; initiate & enforce legislation; mediator
- The Council of Ministers: agree legislation by QMV
- The European Parliament: co-decision making powers
- The European Court of Justice: supreme court

- EU v 'typical' Federalism

- Small EU budget constrains transfers & re-distribution of income
- Welfare concern of citizens
- Imperfect information sharing

- EU v Nation State

- Policy of subsidiarity
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EU Revenue

	1998	(%)	2000	(%)	2006	(%)
TOR	13,743.2	(16.7)	14,564.9	(16.4)	14,225.1	(12.9)
VAT	32,752.8	(39.7)	32,554.6	(36.7)	15,884.3	(14.3)
GNP	35,985.2	(43.6)	41,593.4	(46.9)	80,562.5	(72.8)
Total 'own resources'	82,481.1	(100.0)	88,712.9	(100.0)	110,671.9	(100.0)
Other revenue	1,628.0		674.0		1,297.6	
Total revenue	84,109.1		89,386.9		111,969.5	

Source: Adapted from European Commission (2006) *General Budget of the European Union for the Financial Year 2006*, January, and previous issues.

Table 1 Sources of Revenue for the EU budget (€m and %)

EU Expenditure

Budget heading	1998	2000	2002	2006
Agriculture	40,937.0	40,993.9	45,377	50,991.0
EAGGF guarantee	40,937.0	36,889.0	40,761	43,279.7
Rural Development (RDP)	–	4,104.9	4,616	7,711.3
Structural operations	28,594.7	32,678.0	32,998	35,639.6
Structural Funds	23,084.4	28,105.0	30,316	32,134.1
Community Initiatives	2,558.8	1,743.0	–	–
Cohesion Fund	2,648.8	2,659.0	2,682	3,505.5
Others	302.7	325.0	–	–
Internal policies	4,678.5	6,027.0	6,793	8,889.2
External policies	4,528.5	4,805.1	4,895	5,369.0
Administration	4,353.4	4,703.7	5,225	6,656.4
Other	437.0	4,072.7	3,754	4,424.3
Total	83,529.2	93,280.4	99,042	111,969.6

Source: As for Table 29.2.

Table 2 Budgetary Expenditure of the European Community (€m)

Summary

- CG and spillovers v local govt and local tastes
 - Tax assignment
 - Central govt tax and factor mobility
 - Local govt tax and factor immobility
 - UK: multi-level governance
 - EU: a political and economic entity
 - Driven by 4 freedoms (not spillovers)
 - Assignment in the EU: policy of subsidiarity
 - Assign functions to the centre only if inadequate nationally
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