



FOCJ: Competitive Governments for Europe

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While European integration and the four freedoms related to the movement of goods, services, labor, and capital strengthened economic competition, competition among governments has been rather muted. Thus, a future European constitution should unleash political competition by guaranteeing a fifth freedom that allows the evolution of functional, overlapping, and competing jurisdictions (FOCJ). These governmental units combine various welfare-enhancing theoretical concepts of the economic theory of federalism. FOCJ have existed (at least partially) in European history, and there are illustrative examples such as the U.S. special districts and Swiss functional, democratic, and overlapping communities.

I. Liberalized Economic and Restricted Political Markets in Europe

European integration was outstandingly successful at granting the four freedoms related to the movement of goods, services, labor, and capital. As a result of establishing a single, competitive European *economic* market, the citizens of the countries forming the European Union have certainly experienced a significant increase in welfare. However, no such open and competitive *market for politics* has been established. On the contrary: The competition between governments was successfully restricted by the various European treaties and institutions. While the European Union's power in politics, including economic policy, are still quite limited, no steps have been undertaken to actively institutionalize competition between governmental units at all levels. Such competition has only been considered for national governments. However, from a constitutional perspective other forms of political competition should be envisaged, too. We argue that welfare can be improved substantially by promoting competition between newly emerging jurisdictions that are organized along functions instead of territories. The *fifth freedom* we suggest allows for such *functional, overlapping, competing jurisdictions*.

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They will be called by their acronym *FOCJ* (one such jurisdiction will be called *FOCUS*). *FOCJ* form a federal system of governments that is not dictated from above, but emerges from below as a response to citizens' preferences. This fifth freedom requires a *constitutional decision* [see, e.g., Frey (1983), Mueller (1995)], which ensures that the emergence of *FOCJ* is not blocked by existing jurisdictions such as direct competitors or higher level governments. Every citizen and community must have the right to directly appeal to the European Court if barriers to the competition between governments are established. The European Constitution must give the lowest political units a measure of independence so that they can engage in forming *FOCJ*. The citizens must be given the right to establish *FOCJ* by popular referenda, and political entrepreneurs must be supported and controlled by the institution of popular initiatives. The *FOCJ* themselves must have the right to levy taxes to finance the public services they provide.

These *FOCJ* strongly contrast with the concepts of federalism currently existing or being proposed in the European Union. We intend to show that *FOCJ* are well grounded in economic theory. Successful precursors of these institutions existed in European history. Indeed, Europe owes its rise to an economic and intellectual center to the competition among governmental units. Moreover, such functional competing units already partially exist in present-day Europe and elsewhere, where they perform well within the room accorded to them. The idea of completing the European integration at different speeds, and thus having various subgroups of countries within the European Union, is also related, although it is far more restrictive than our concept of *FOCJ*.

The paper is organized as follows. Section II specifies the concept of *FOCJ* and puts it into theoretical perspective; our concept of competitive federalism is contrasted to all-purpose jurisdictions confined to one particular geographical area. The third section shows that *FOCJ* partially exist in European history and today. The relationship to U.S. special districts and, in particular, to functional communities in Switzerland is emphasized. The next section compares *FOCJ* to existing federal institutions in the European Union. Section V analyzes the workings of *FOCJ* and discusses how the problems related to this type of jurisdiction may be overcome. Concluding remarks are offered in the last section.

II. Constituting Elements

The federal units here proposed have four essential characteristics: they are

- *Functional (F)*, i.e., the new political units extend over areas defined by the tasks to be fulfilled;
- *Overlapping (O)*, i.e., in line with the many different tasks (functions there are), corresponding governmental units extending over different geographical areas;
- *Competing (C)*, i.e., individuals and/or communities may choose to what governmental unit they want to belong, and they have political rights to express their preferences directly via initiatives and referenda;
- *Jurisdictions (J)*, i.e., the units established are governmental, they have enforcement power and they can, in particular, levy taxes.

FOCJ are based on theoretical propositions advanced in the economic theory of federalism. They nevertheless form a governmental system completely different from the one suggested in that literature. While the economic theory of federalism [see Bird (1993) and Breton (1996) for surveys on its present state] analyzes the behavior of *given*

political units at the different levels of government [Weingast (1993), p. 292], *FOCJ* emerge in response to the "geography of problems."¹

The four elements of *FOCJ* are now related to economic theory as well as to existing federal institutions, pointing out both similarities and differences to existing concepts.

Functions

A particular public service that only benefits a certain geographical area should be financed by the people living in this area, i.e., there should be no spillovers. Under this rule, the different political units can cater to differences in the populations' preferences or, more precisely, to its demands. To minimize cost, these units have to exploit economies of scale in production. As these may strongly differ between functions (e.g., between schools, police, hospitals, power plants, and defense), there is an additional reason for unifunctional (or few-functional) governmental units of different sizes. While this idea is central to "fiscal equivalence," as proposed by Olson (1969) and Oates (1972), the endogeneity of the size of governmental units constitutes an essential part of *FOCJ*.

However, fiscal equivalence theory has been little concerned with decision-making within functional units. The supply process is either left unspecified or it is assumed that the mobility of persons (and of firms, a fact rarely mentioned) automatically induces these units to cater to individual preferences. This criticism also applies to a closely related concept of fiscal federalism, namely "voting by foot" [Tiebout (1956)]. This preference-revealing mechanism makes comparatively efficient suppliers grow in size and makes the others shrink. According to this model of federalism, the political jurisdictions are exogenously given, are multipurpose, and do not overlap, while the political supply process is left unspecified. In contrast, we emphasize the need to explicitly study the political supply process. In line with Epple and Zelenitz (1981), exit and entry is considered insufficient to eliminate rent extraction by governments. Individuals must have the possibility to raise voice in the form of voting. Buchanan's (1965) "clubs" are similar to *FOCJ* because their size is determined endogenously by the benefits and costs of the club members.

Overlaps

FOCJ may overlap in two respects: (i) Two or more *FOCJ* catering to the same function may geographically intersect (e.g., a multitude of school *FOCJ* may exist in the same geographical area); and (ii) *FOCJ* catering to different functions may overlap. The two types of overlap may coexist; however, to alleviate free-riding problems, *FOCJ* serving specific functions can be restricted from the first type of overlap by a constitutional decision (see below). An individual or a political community normally belongs to various *FOCJ* at the same time. *FOCJ* need not be physically contiguous, and they need

¹As always, there are precursors to *FOCJ*. The general idea has already been advanced by Montesquieu, but it has, to our knowledge, not been applied to the European Union. In the economics literature a related concept has been pioneered by Tullock (1994), who somewhat misleadingly speaks of "sociological federalism." Casella and Frey (1992) discuss the concept and refer to relevant literature. A recent Centre for Economic Policy Research Publication [CEPR (1993)] briefly mentions the possibility of establishing overlapping jurisdictions in Europe (pp. 54-55) but does not work out the concept, nor does it refer to previous research [except for Drèze (1993) on secession].

not have a monopoly over a certain area of land. Thus, this concept completely differs from archaic nationalism with its fighting over pieces of land. It also breaks with the notion of federalist theory that units at the same level may not overlap. On the other hand, in this respect it is similar to Buchanan-type clubs, which may intersect.

Competition

The heads of FOCJ are induced to conform closely to their members' preferences by two mechanisms: while the individuals' and communities' possibilities to *exit* mimics market competition [Hirschman (1970)], their right to *vote* establishes political competition [see Mueller (1989)]. It should be noted that migration is only one means of exit; often, membership in a particular FOCUS can be discontinued without changing one's location. Exit is not restricted to individuals or firms; as was said before, political communities as a whole, or parts of them, may also exercise this option. Moreover, exit may be total or only partial. In the latter case, an individual or community only participates in a restricted set of FOCUS activities. This enlarged set of exit options makes "voting by foot" function properly.

The importance of "secession" (i.e., exit of jurisdictions such as communities) for restricting the power of central states has been recognized in the literature [e.g., Zarkovic Bookman (1992); Drèze (1993)]. Secession has been suggested as an important ingredient for a future European constitution [Buchanan (1991); European Constitutional Group (1993)]. The right to secede stands in stark contrast to the prevailing concepts of nation states and federations where this is strictly forbidden and often prevented by force, as is illustrated, e.g., by the American Civil War, 1861 to 1865, by the Swiss "*Sonderbundskrieg*," 1847, or more recently by the wars in Katanga (1960 to 1963), Biafra (1967 to 1970), Bangladesh (1970 to 1971), and presently in the former Yugoslavia. Current European treaties do not provide for the secession of a nation from the European Union, and *a fortiori* for part of a nation. The possibility of lower-level jurisdictions to exit at low cost from the European Union as a whole as well as from particular subunits (nations, states, *Länder*, autonomous regions, etc.) thus depends strongly on the future European constitution.

For FOCJ to establish competition between governments, exit should be as unrestrained as possible. In contrast, entry need not necessarily be free. As for individuals in Buchanan-type clubs, jurisdictions may be asked a price, if they want to join a particular FOCUS and benefit from its public goods. The existing members of the particular FOCUS have to democratically decide whether a new member pays an adequate entry price and thus is welcome. "Free" mobility in the sense of a disregard for the cost imposed on others is overcome by internalizing the external cost of movement. In addition, FOCJ do not have to restrict entry by administrative and legal means, such as zoning laws. Explicit, openly declared entry fees substitute for implicit restrictions, resulting in high land prices and housing rents. The commonly raised concern that pricing could be exploitative and mobility strongly curtailed is unwarranted, as FOCJ are subject to competitive pressure. Moreover, the possibility of imposing an explicit entry fee gives incentives to FOCJ governments to care not only for the preferences of actual members, but also of prospective members.

Competition needs to be furthered by political institutions, as the exit option does not suffice to induce governments to act efficiently. The citizens should directly elect the persons managing the FOCJ, and should be given the right to initiate popular referenda on specific issues. These democratic institutions are known to raise efficiency

in the sense of caring well for individual preferences [for elections, see Downs (1957); Mueller (1989); for referenda, see Frey (1994)].

Jurisdictions

A FOCUS is a democratic governmental unit with authority over its citizens, including the power to tax. According to the two types of overlap, two forms of membership can be distinguished: (i) The lowest political unit (normally the community) is a member, and all corresponding citizens automatically become citizens of the FOCJ to which their community belongs. In that case, an individual can only exit via mobility; and (ii) individuals may freely choose whether they want to belong to a particular FOCUS, but while they are its citizen, they are subject to its authority. Such FOCJ may be nonvoluntary in the sense that one must belong to a FOCUS providing for a certain function, e.g., to a school-FOCUS, and must pay the corresponding taxes (an analogy here is health insurance, which in many countries is obligatory but where individuals are allowed to choose an insurance company). The citizens of such a school-FOCUS may then decide that everyone must pay taxes to finance a particular school, irrespective of whether one has children. With respect to FOCJ providing functions with significant redistributive effects, a minimal regulation by the central government may be in order so that, e.g., citizens without children do not join "school-FOCJ," which in effect do not offer any schooling but have correspondingly low (or zero) taxes. In this respect, Buchanan-type clubs differ from FOCJ, because they are always voluntary whereas membership in a FOCUS can be obligatory.

FOCJ as jurisdictions provide particular services but do not necessarily produce them themselves if contracting-out to a public or private enterprise is advantageous. It is noteworthy that present-day outsourcing by communities does not automatically lead to FOCJ. The former is restricted to production, while FOCJ care for provision and are directly democratically controlled. FOCJ also differ from existing functional and overlapping institutions such as the various kinds of specific administration unions (or *Zweckverbände*, as they are aptly called in German-speaking countries). These institutions normally do not have the legal status of governments but are purely administrative units. The same applies to the many types of corporations that usually have no power to tax but have to rely on charges.

Beneficial Effects

Due to its four essential characteristics, FOCJ compare favorably to traditional forms of federalism. One aspect concerns the governments' incentives and possibilities to satisfy heterogeneous preferences of individuals. As a consequence of the concentration on one functional area, the citizens of a particular FOCUS have better information on its activity and are in a better position to compare its performance to other governments. As many benefits and costs extend over a quite limited geographic area, we envisage FOCJ often to be small, which is also helpful for voters' evaluations. The exit option opened by the existence of overlapping jurisdictions is not only an important means to make one's preferences known to governmental suppliers, but it also strengthens the citizens' incentives to be informed about politics [Eichenberger (1994)].

On the other hand, FOCJ are able to provide public services at low cost because they are formed to minimize interjurisdictional spillovers and to exploit economies of scale. When the benefits of a specific activity extend indivisibly over large areas, and there are

decreasing cost, the corresponding optimal FOCUS may cover many communities, several nations, or even Europe as a whole. An example may be defense against outward aggression where the appropriate FOCUS may most likely extend over the whole of Europe (even beyond the European Union). That such adjustment to efficient size is indeed undertaken in reality is shown by the Swiss experience. Communities decided by referendum whether they wanted to join the new canton Jura established in 1978, and in 1993 communities in the Laufental opted to belong to the canton Basel-Land instead of Berne. Communities also frequently change districts (the federal level below cantons) by referendum vote, which suggests that voters perceive the new size of jurisdictions and the new bundle of services to be more efficient. The same holds for American special districts.

The specialization on one or a few functions further contributes to cost efficiency due to the advantages of specialization. As FOCJ levy their own taxes to finance their activity, it pays to be economical. In contrast, in all-purpose jurisdictions (APJ), which are financed from outside and lack such fiscal equivalence, politicians have an incentive to lobby for ever-increasing funds, thereby pushing up government expenditures. The incentive to economize in a FOCUS induces its managers to contract-out whenever production cost can thereby be reduced. While FOCJ are more market oriented than APJ, they reduce the size of the public sector. However, they differ from today's one-shot privatization, which usually does not impact on the governments' basic incentives and thus is often reversed by reregulation and deprivatization. In contrast, in a system of FOCJ privatization emerges endogenously and is sustainable, as the politicians incentives are changed dramatically.

The threat of dissatisfied citizens or communities to exit the FOCUS, and the benefit of new citizens and communities joining, gives an incentive to take individual preferences into account and to provide the public services efficiently. Quite another advantage of FOCJ is that they open up the politicians' cartel ("classe politique") to functionally competent outsiders. While all-purpose jurisdictions attract persons with broad and nonspecialized knowledge to become politicians, in FOCJ it is rather persons with a well-grounded knowledge in a particular functional area (say education or refuse collection) who are successful.

The possibility to form FOCJ helps to deal with issues raised by fundamentalist sentiments. Political movements focused on a single issue (e.g., ethnicity, religion, environment, etc.) are not forced to take over governments *in toto* but can concentrate on those functions that they are really interested in. An ethnic group need not disassociate itself from the state they live in as a whole but may found FOCJ that care for their particular preferences. South Tyroleans, for example, unhappy with the language domination imposed by the Italian state, need not leave Italy to have their demands for cultural autonomy fulfilled, but may establish corresponding FOCJ. Such partial exit (e.g., only with respect to ethnic issues) does not lead to trade barriers, often going with the establishment of newly formed all purpose political jurisdictions. FOCJ thus meet the criteria of market-preserving federalism [see Weingast (1993)].

III. A Realistic Concept

From a narrow EU perspective it could be argued that FOCJ and the fifth freedom break away too radically from present realities to have a chance to be implemented, thus being a utopian concept. However, from a more historical and international point of view, things look different.

European History

Decentralized, overlapping political units have been an important feature of European history. The competition between governments in the Holy Roman Empire of German Nations, especially in today's Italy and Germany, has been intensive. Many of these governments were of small size. Not a few scholars attribute the rise of Europe to this diversity and competition of governmental units, which fostered technical, economic, and artistic innovation [see, e.g., Hayek (1960); Jones (1981); Weede (1993); and Baumol and Baumol (1994), who also give a lively account of how the musical genius of Wolfgang Amadeus Mozart benefited from this system of government]. While the Chinese were more advanced in very many respects, their superiority ended with the establishment of a centralized Chinese Empire [Pak (1995); Rosenberg and Birdzell (1986)]. The unification of Italy and Germany in the 19th century, which has often been praised as a major advance, partially ended this stimulating competition between governments and led to deadly struggles between nation states.² Some smaller states escaped unification; Liechtenstein, Luxembourg, Monaco, San Marino, and Switzerland stayed politically independent and at the same time grew rich.

The above-mentioned governmental units were not FOCJ in the sense outlined in this contribution, but they shared the characteristic of competing for labor and capital (including artistic capital) among each other. However, history also reveals examples of jurisdictions close to FOCJ. The problems connected with Poland's strong ethnic and religious diversity (Catholics, Protestants, and Jews) were at least partly overcome by jurisdictions organized along these features, and not along geography [see, e.g., Haumann (1990)]. The highly successful Hanse prospered from the 12th to the 16th century, and comprised *inter alia* Lübeck, Bremen, Köln (today German), Stettin and Danzig (today Polish), Kaliningrad (today Russian), Riga, Reval and Dorpat (today parts of the Baltic republics), and Groningen and Deventer (today Dutch); furthermore, London (England), Bruges and Antwerp (today Belgian), and Novgorod (today Russian) were *Handelshontore*, or associated members. It clearly was a functional governmental unit providing for trade rules and facilities and was not geographically contiguous.

Contemporary Examples

The European Community started out as a FOCUS designed to establish free trade in Europe, and was from the very beginning in competition with other trade areas, in particular North America, Japan, and EFTA (European Free Trade Association). Due to its economic success, it has attracted almost all European countries. But entry has not been free; the nations determined to enter had to pay a price. They have to accept (with partial exceptions) the "*acquis communautaire*" as well as to pay their share to the Communities' outlays, which to a large extent serve redistributive purposes. In several respects there exist FOCJ-like units within Europe such as police, education, environment, transport, culture, or sports, although they have been prevented from becoming autonomous jurisdictions with taxing power.

There are two major examples of functional, overlapping, and competing jurisdic-

²According to Sperber (1994, p. 24), in the first half of the 19th century average income was higher in strongly decentralized Germany than in strongly centralized France, which may at least partly be attributed to the difference in the degree of centralization.

tions (though they do not in all cases meet the full requirements of FOCJ specified above). One is the U.S. *special districts* with which American readers are familiar.³ The other relates to Switzerland. Many Swiss cantons have a structure of overlapping and competing functional jurisdictions that share many features of FOCJ. In the canton Zurich (with a population of 1.2 million), e.g., there are 171 geographical communities that in themselves are composed of three to six independently managed, direct-democratically organized communities devoted to specific functions and levying their own taxes on personal income. Besides general purpose communities, there are communities that exclusively provide for elementary schools and other ones specializing in junior high schools, and there are the communities of three different churches. All these governmental units have widely differing rates of income taxes. Moreover, there is a vast number of "civil communities" (*Zivilgemeinden*), providing water, electricity, TV antennas, etc., which are direct-democratic but finance themselves by user charges. These communities often overlap with neighboring political communities. In addition there are 174 functional units (*Zweckverbände*) whose members are not individual citizens but communities. These *Zweckverbände* care, e.g., for waste water and purification plants, cemeteries, hospitals, and regional planning. The canton Zurich is no exception in Switzerland concerning the multitude of types of functional communities. A similar structure exists, e.g., in the canton Glarus or Thurgau [for the latter, see Casella and Frey (1992)]. Various efforts have been made to suppress this diversity of functional communities, usually initiated by the cantonal bureaucracy and politicians. However, most of these attempts were thwarted because the population is mostly satisfied with the public supply provided. The example of Switzerland, which is generally considered to be a well-organized and administered country, shows that a multiplicity of functional jurisdictions under democratic control is not a theorist's wishful thinking but has worked well in reality.

IV. Comparison to Federalism in Europe

Although institutions similar to FOCJ play an important role in European history and in today's United States and Switzerland, they are largely absent from the EU's political landscape and intellectual debate. Most notably, FOCJ differ in many crucial respects from scholarly *proposals* for a future European constitution. One of the most prominent proposals was Buchanan's (1991), which stresses an individual nation's right to secede but, somewhat surprisingly, does not build on Buchanan-type clubs. The European Constitutional Group (1993) focuses on the example of the American constitution and presents detailed proposals with respect to the houses of parliament and the respective voting weights of the various countries. Overlapping jurisdictions and referenda are not allowed for, and the exit option is strongly restricted. Other economics scholars [e.g., Blöchliger and Frey (1992); Schneider (1992)] suggest a strengthening of federalism in the traditional sense (i.e., with multipurpose federal units) but do not envisage overlapping jurisdictions. The report by the Centre for Economic Policy Research (1993) criticizes "subsidiarity" (as used in the Maastricht Treaty) as an empty concept, arguing that good theoretical reasons must be provided for central government intervention. But the report does not deal with the institutions necessary to guarantee that policy

³Empirical research reveals special districts to be a highly efficient form of local government; see, e.g., Mehay (1984), Zax (1988); see also ACIR (1987).

follows such theoretical advice. The idea of overlapping, not geographically based jurisdictions is briefly raised (pp. 54–55) but is not institutionally or practically worked out, nor is the need for a democratic organization and the power to tax acknowledged.

The recent proposal from politicians [Herman report of the European Parliament (1994)] mainly deals with the organization of the parliamentary system (the houses of parliament and the national vote weights) and to a substantial extent accepts the existing treaties as the founding blocks of the European constitution. The idea of competition between governments (which is basic for FOCJ) is neglected or even rejected in favor of "cooperation" between governments.

FOCJ are also quite different from the regions envisaged in existing *European treaties* and *institutions* [see, e.g., Adonis and Jones (1991)]. A major difference is that FOCJ emerge from below while the "European regions" tend to be established from above. Moreover, their existence strongly depends on the subsidies flowing from the European Union and the nation states [Sharpe (1993)]. In contrast, the concept of FOCJ corresponds to Hayek's (1960) (and Buchanan's) nonconstructivist process view. It cannot *a priori* be determined from outside and from above which FOCJ will be efficient in the future. This must be left entirely to the competitive democratic process taking place at the level of individuals and communities. The central European constitution must only make sure that no other government units, in particular the nations, may obstruct the emergence of FOCJ. In contrast to Hayek, however, our scheme allows for a (closely restricted) set of central regulations, as mentioned above. Moreover, Hayek measures efficiency by survival in the evolutionary process, whereas we define efficiency more directly in terms of the fulfillment of citizens' demands.

"Subsidiarity" as proclaimed in the Maastricht Treaty is generally recognized to be more a vague goal than a concept with content [see, e.g., Centre for Economic Policy Research (1993), pp. 19–23]. Even if subsidiarity were taken seriously, it would not lead to a real federal structure, because many (actual or prospective) members of the European Union are essentially unitary states without federal subunits of significant competence (examples are the Netherlands, France, or Sweden). The "regions" existing in the European Union (examples are Galicia and Cataluña in Spain, or South Tyrol and Sicily in Italy) are far from being units with significant autonomous functional competencies.

The idea of FOCJ also contrast with the EU's reluctance to grant exceptions to specific aspects of agreements already reached (as in the Maastricht Treaty concerning the European Monetary Union and the Protocol on Social Policy, or in the Schengen Treaty concerning the free movement of persons). Indeed, they are seen as damaging the "spirit of Europe." Whether differential degrees of European integration are framed as models of variable geometry, multitier, multispeed, two-tier, hard-core, concentric circles, or as Europe *à la carte* (*The Economist*, 1994, Oct. 22, "Survey of the European Union," p. 15), they always evoke fierce opposition. In a system of FOCJ, in contrast, functional units not covering everyone are taken as a welcome expression of heterogeneous demands among Europeans.

FOCJ are relevant for all levels of government and major issues. An example would be Corsica, which according to Drèze's (1993) suggestion should form an independent region of Europe because of its dissatisfaction with France. However, most likely the Corsicans are only *partially* dissatisfied with France. This suggests that one or several FOCJ provide a better solution in this case; they may, e.g., especially focus on ethnic or language boundaries, or on Corsica's economic problems as an island. This allows the Corsicans to exit France only partially instead of totally. Quite generally, tourism and

transport issues, in particular railroads, are important areas for FOCJ. It should be noted that, despite the membership of various countries in the (then) European Community, railroad policy was not coordinated to exploit possible economies of scale; a FOCUS may constitute a well-suited organization to overcome such shortcomings.

V. Overcoming Problems

Up to this point we have emphasized the beneficial effects of FOCJ. However, there are also some alleged problems with our concept, which will be discussed now.

Overburdened citizens. In a federal system of FOCJ, each individual is a citizen of various jurisdictions. As a consequence, individuals may be overburdened by voting in elections and referenda taking place in each FOCUS. However, citizens in a direct-democratic FOCUS find it much easier to participate politically as they have only to assess one or a few concrete issues at a time. In contrast, in representative-democratic APJ citizens have to evaluate all political aspects simultaneously, and they have to speculate what position a political candidate will take over the next election term. If the citizens find it nonetheless burdensome to vote on each governmental function separately, they can rely on institutions emerging to deal with the problem. For instance, in referenda they may simply follow parties' recommendations.

Overburdened consumers. An individual is confronted with a multitude of suppliers of public services, which, it is argued, makes life difficult. This is the logical consequence of having more options to choose from and is similar to supply in the private sector. If citizens find it nevertheless to be a problem, a governmental or a private advisory service can be established that offers information and support for the consumers' decisions. It should, moreover, be observed that in APJ the same problem exists. There is no all-enhancing administration managing all public services. Rather, the responsibility is divided up among specialized government departments so that the citizens/consumers are also effectively confronted with many different agencies supplying public services.

"Need" to coordinate the activities of FOCJ. Coordination between governments—while obviously often needed—is not always beneficial. It sometimes serves to build cartels among the members of the "*classe politique*" who then evade or even exploit the populations's wishes [see CEPR (1993); Vaubel (1994); Frey (1994)]. As far as welfare increasing coordination is concerned, its need is reduced compared to APJ, because the FOCJ emerge to minimize externalities. If major spillovers between FOCJ exist, new FOCJ will be founded, taking care of these externalities. As the number of FOCJ is restricted due to the transactions cost involved, less important externalities between FOCJ will remain. However, spillovers also exist in a system of APJ between administrative units, e.g., between the department for environment and the department of transport. The crucial question therefore is in what system *N*-player Coase-type interfunctional bargaining is more likely to arise. The respective civil servants in APJ have a muted incentive to take these spillovers into account by bargaining. On the one hand, their sphere of influence may be curtailed if they coordinate decisions among various departments effectively. On the other hand, their income and other benefits are essentially unconnected to the possible benefits to the citizens. In contrast, the political managers of a FOCUS have a self-interest to seriously engage in Coasian bargaining as

the support received from the members of their FOCUS depends on how much they raise their members' utility. This responsiveness is achieved by the institutions of re-election and by popular initiatives and referenda on specific issues. To the extent that the citizens of a FOCUS value coordination, it behooves FOCJ governments to provide it. Thus, coordination among FOCJ is not inherently different from coordination in economic markets, where similar problems occur all the time and are analyzed in depth by much recent research in industrial organization [e.g., Farrell and Saloner (1988); Milgrom and Roberts (1990)].

Redistribution. It is claimed that all forms of federalism—including FOCJ—undermine redistribution. Moreover, FOCJ are said to emerge on the basis of income. As far as redistribution is based on the citizens' solidarity or on insurance principles, this fear is unwarranted. Only as far as redistribution is a pure public good and thus must be enforced to prevent free-riding, a problem may arise. However, recent empirical research [Gold (1991); Kirchgässner and Pommerehne (1996)] suggests that substantial redistribution is feasible in federal systems. In the United States and especially in Switzerland, lower level and even local governments strongly engage in redistribution activities and are responsible for a substantive share of redistribution. In these countries, mobility is obviously not enough to render redistribution impossible. As concerns Europe, mobility is also quite low. Less than 5% of EU citizens live outside their country of citizenship. This low level of mobility can be interpreted in two ways: (i) In decentralized systems mobility by persons (and to a lesser extent also firms) is countervailed by strong local attachment; and (ii) redistribution does not constitute a pure public good but does provide localized benefits. However, if decentralized redistribution is considered insufficient, a FOCUS specialized on interregional redistribution may emerge, but this presupposes barriers to entry (in analogy to insurance systems with cross-subsidization). Moreover, centralization of redistribution is still possible, of course. The European constitution may give central government the power to impose a limited amount of income redistribution.

VI. Conclusions

Europe owes its position as an economically rich and intellectually and artistically powerful continent in a large measure to the great variety of governmental jurisdictions in competition with each other. This basic insight was overshadowed by the unification movements, especially in Italy and Germany. The European movement follows the historic lesson by opening up trade barriers and supporting economic competition, and does this with great success. However, the historic lesson has not been followed with respect to establishing competition between existing and new governments.

This paper proposes that the future European constitution should allow, and actively promote, the evolution of FOCJ. They fulfill many of the welfare-enhancing qualities of theoretical concepts such as Tiebout's voting by foot, Olson's and Oates' fiscal equivalence, or Buchanan's clubs. It is shown that FOCJ are feasible, that there are successful historical examples, and that they partially exist in the form of U.S. special districts and Swiss functional, democratic, and overlapping communities.

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