

RESEARCH PROPOSAL – Sandra León Alfonso/ Juan March Institute

WHY DO GOVERNMENTS UNDERTAKE FISCAL DECENTRALISATION?

The Italian parliament has recently passed a constitutional decree-law by which power is decentralised to regions. Regions are given the right to legislate on those political areas in which central government has not absolute power (such as immigration, Defence, Justice, territorial borders, currency and so on). That decree-law also introduces **fiscal federalism** since constitutional reform enshrines regions' right to exercise self-government with their own fiscal resources and therefore gives them the prerogative on tax powers. Up to a few years ago, Italian regions' financial autonomy was extremely modest and regions had heavy dependence on central government's transfers on those activities involving large sums of expenditure¹. In fact, during the post-war period they had become mere agencies of *administrative deconcentration* rather than self-governed territorial units with real powers to legislate and counterbalance central government's power.

The introduction of fiscal federalism by the new Italian constitution represents the most important advance towards federalism. Paradoxically, if we compare the new Italian territorial distribution of power with the Spanish one it turns out that in spite of having a considerably lower degree of political decentralisation, Italy has a more advanced form of federalism regarding fiscal decentralisation². Besides, the introduction of fiscal federalism has taken place in a country whose territorial cleavages are not similar to the cultural, linguistic or ethnic cleavages found in other countries such as Spain, Belgium, or Switzerland. Regional differences in Italy have not overlapped with the identification of sharp ethnic and/or linguistic differences so that Italy has only a pale imitation of the problem regarding strong demands for devolution that has shaped territorial distribution of power in Spain.

The previous paradox provides the empirical relevance of what is going to be core of my research project. The research question is: *why and when do governments undertake a process of decentralisation?. Why and when does a central government lose powers in favour of intermediate levels of government?. Specifically, why is it going to give subnational governments capacity to have their own fiscal resources (tax powers)?.* Therefore the research question deals with causes of decentralisation processes, which constitute the dependent variable of the research. I would like to find out which are the most important explanatory variables in explaining why governments undertake decentralisation processes. Research would not only be related to prediction of an association between the dependent variable and the independent ones but it would also be focused on understanding which mechanisms lie behind causal relationships.

As I made explicit in the last question, research specifically aims at concentrating on fiscal decentralisation and in order to justify such attention I present the following arguments.

¹ Hine, D. "Federalism, Regionalism and the Unitary State" in *Italian Regionalism*, 1996.

² Spanish self-governed regions (Comunidades Autónomas) have exclusive legislative powers in political areas such as trade, industry or agriculture. Besides, they share legislative powers with central government (those are concurrent areas) on health, education. On the contrary, Italian regions are not entitled to legislate on education, for example.

First of all, a striking study carried out by Jan-Erik Lane and Svante Ersson³ about unitary and federal states showed that, unlike neoinstitutional authors declare, the only dependent variable where federal institutions have an effect is fiscal decentralisation. So federalism basically means less spending power for central government and more powers to subnational governments over public expenditures. Therefore, fiscal decentralisation seems to be the most salient federal institution. Secondly, it is also necessary to take into account that even though regional autonomy might be recognised by the constitution in practice it has no sense in case regions lack of financial resources. All things considered, the analysis of those causal factors which bring into existence a new territorial distribution of power will mainly focus on those decisions over decentralisation of public expenditure and/or tax powers.

As far as I know, theoretical approaches to fiscal decentralisation have mainly come from the economic field. Economic theories about decentralisation have primarily come from two schools: the so-called Public Finance (Musgrave (1959) and Oates (1972)) and the Public Choice School (Brennan and Buchanan(1980)). Those theories have focused on the normative aspects of decentralisation. For instance, Oates argues that intermediate or lower levels of government (regional and local) are more capable than central governments to meet citizen's preferences and demands over public goods and services. By the other hand, Public Choice theorists highlight fiscal decentralisation may enhance fiscal competition among different territorial units and in consequence, increase efficiency in the allocation of public. However, and curiously enough, economic arguments in favour of decentralisation have been hardly present or notably absent from the debate of centralization/decentralization of power in some countries which have undertaken a new territorial organisation of the State⁴. As De Vries points out, the attention that political parties at the European level have given to centralization and decentralization issues "*reveals that decentralisation becomes an issue in these countries at different periods and as a cause of different arguments, which rather reflect the dominant values in the political culture than refer to inherent properties of decentralisation itself*"⁵. He shows theoretical arguments have been hardly convincing since in practice some of them, such as democratic character, legitimacy or efficiency, have been used to defend and promote both decentralisation and centralisation processes.

Since those theoretical arguments seem to have a limited role in explaining decentralisation processes, my work partly aims at covering such explanation gap. I would try to find out which are the socio-economic and political contextual variables that surround and provoke the incumbent government's decision to undertake fiscal decentralisation. The main purpose is to make a contribution to the understanding of the processes that lead to the establishment or modification of institutional arrangements. To some extent that purpose has something to do with Riker's approach to institutions, which he defined as medium-

³ *Political Institutions and Public Policy*, 85-113, Kluwer Academic Publishers B. Steunenberg and F.van Vught (eds.). Capítulo 5: "Is Federalism superior?". Jan-Erik Lane y Svante Ersson.

⁴ For example, in Spain or South Africa, where transition from a centralised state to a federal structure took place at the same time than transition to democracy.

⁵ De Vries; Michiel S.; "*The rise and fall of decentralisation: A comparative analysis of arguments and practices in European countries*". *European Journal of Political Research* 38: 193-224, 2000.

term *unstable* arrangements⁶. Institutions are not in equilibrium since there always exist groups with incentives to change them. I would like to find out what explanatory variables lie behind an institutional change such as the establishment of new arrangements regarding to territorial distribution of power.

The existing paradox between the Italian and the Spanish process provides the empirical relevance of the research question. However, in case I concentrate exclusively on those two cases I will be virtually no capable to come to valid and general conclusions regarding the establishment or modification of institutional arrangements. Rather, I believe the methodological design should concentrate on (or at least begin with) an overall analysis of recent decentralisation processes undertaken in western countries. In those processes I include both political and fiscal decentralisation, since it could be difficult to disentangle the causal factors underlying the latter without taking into account distribution of political power and its relationship with the distribution of tax powers. After the overall analysis and a deeper exploration of the literature I believe I will be able to set some *hypothesis* about the relationship between the dependent variable (decentralisation) and hypothetical explanatory variables. Then, I believe I will be able to select the proper *countries* for the comparison and finally the *methodology*.

⁶ Riker, W. 1980. "Implications from the disequilibrium of majority rule for the study of institutions". *American Political Science Review*, 74, 432-458.