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An Economic Approach to the Federal Structure

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AN ECONOMIC APPROACH TO THE FEDERAL STRUCTURE

Anthony Scott

THE SHORT RUN VERSUS THE LONG RUN

We are considering the future of Canada's federal structure of government. Many voices are heard. When we render them all down we are left with two arguments. The first argument is about what path Canada should follow now, in the short run; the second is about what kind of governmental structure Canada should be trying to build in the long run.

In my opinion, the first argument, immediate and urgent as it is, concerns means rather than ends. What strategy should be followed by the various governments and political actors this year? What should be said to the press? What stance should the Atlantic provinces and western Canada strike? These are all short-run problems. The second, remote and abstract by comparison with the fire and fury of the first, concerns the ends (that is, long-run goals). Those who are engaged in this debate are disputing the merits and demerits of alternative structures of government. On one side are ranged the enthusiasts for a more centralized structure; on the other the champions of a decentralized, dispersed pattern of government authority and power.

These two arguments are not independent of each other. If we can agree on our long-run goal, we must still make a decision about a transformation period. Should it be brief or protracted? Should it build on a series of intergovernmental conferences, or place more emphasis on revolutionary, violent, or individualistic gestures and phrases? How will the manner and speed of transformation affect the attitudes of the various parts of the country to each other? If the immediate crisis is prolonged, citizens' tastes and attitudes to, for example, Québec's place in the ultimate structure may become harder or softer. Indeed, Keynes wrote that it is this short run, this transitional period, that really matters, "for in the long run we are all dead".

Nevertheless, in matters of government structure, the transformation period, no matter how important it may become in historical retrospect, has no force, unless it is seen by contemporaries as transition towards some new structure, or set of institutions. Some eventual shape of society must be the goal. The basic energy for short-run decisions and activities is drawn from men's resolutions to achieve (or to retain) some long-run steady state for government and society. The transitional strategy is the means, the chosen structure of government is the end.

The purpose of this essay is to say something helpful about the selection of the long-run ends to which our current discussion of the constitution may lead us. Ideally, we should compare a variety of attainable alternative government structures towards which we might wish to progress. Recognizing that some of these structures can never materialize because the sort of transition they require would be too painful or too protracted, we should nevertheless exercise the "constitutional" part of our imaginations to survey or review the choices open to us. We may then compare the net benefits of the preferred constitution with the net costs of the transitional steps we must take to reach it, and try to decide whether the end justifies the means.

My aim here is to stimulate discussion about the long run. What sort of "governmental structure" should we be working for - or, perhaps, trying to retain? I would like first to introduce the idea of an *economic* approach to the constitution (that is, to the structure of government) and then to develop and refine some questions which this approach raises.

THE CHOICE AMONG FEDERAL STRUCTURES

By "federal structure" I mean the pattern made by the levels of government which symbolize our nation, implement our choices, and provide our public goods and services.

You may find it helpful to think of the structure of our government as it would appear in a diagram of a federal pyramid. At the top is a single block representing the single central government. Next down is a wider band of blocks, each representing the government of a state or province. These do not overlap, but have each their own territory. All of them lie within the territory of the central government. As we climb down to lower levels, we find local-government strata. There are many of these units, and to the architectural eye they look more like rubble than the foundation blocks of a great pyramid, for they differ greatly in size, sometimes overlap territorially, and do not have a uniform height from the ground. On inspection we do find that each of them lies within the territory of only one provincial government, but this is almost their only regularity.

This structure can be modified in a number of ways. The height of the pyramid can be changed by inserting or removing whole jurisdictional levels, or by doing this under only a part of the level above. The width and breadth of the pyramid can also be changed by replacing each block at one level with several blocks, thus, for example, changing from a federation with only a few constituent republics or provinces to one with many states, and so on to the French idea of a level with dozens, even hundreds, of *départements*.

If one looks around the world, one can find many types of pyramids. Yet to focus attention on the mere shape of this pyramid and the number of its levels is to run the danger of attributing importance to jurisdictional levels where in fact governments have little or no significance, but are mere hollow shells. What, then, are the criteria for an "important" level of government? We can suggest three: (i) how many citizens it has; (ii) what it stands for; and (iii) the character of the decisions it may make.

As an economist, I am inclined to give weight to the third of these: a governmental level's importance depends on the importance of the decisions which it can make. The other two criteria are also important, however, and I will consider them briefly.

The most frequently used criterion for size is population. This criterion however is both trivial and misleading. It is trivial because it must *always* tell us that the senior level, governing the whole country from the top of the pyramid, is more important than levels further down. History is replete with examples of top-level, high-population jurisdictions that are powerless. One need only reflect on the Emperors of China, Japan, and the Holy Roman Empire at certain periods, to find confirmation that smaller, subordinate, lower-level jurisdictions are those to which attention should be paid.

What it stands for, however, is another matter entirely. A government and its territory are symbols of all the history and all the aspirations of a society. Such concepts as legitimacy, sovereignty, and representativeness are preoccupations of those who consider the merits and demerits of a governmental structure. There are, of course, easily understood reasons for this. In international relations, especially in periods of war, it is the government that assumes the role of ethical and social and economic spokesman and representative for all its population, *vis-à-vis* the rest of the world. And in time of peace, the power to use compulsion to make policies, collect revenues, and provide services also endows a distinct territorial jurisdiction with a symbolic importance; such jurisdiction may attract like-minded immigrants, repel those who find its actions objectionable, and gradually become a home, a fortress, a bastion, an academy, or even a temple, for its own kind of people.

It seems to me that the Canadian debate about our structure of government has centred on this definition of government: what it stands for, who it speaks for, what rival jurisdictions may claim to speak for the same principles and people. Historians and political scientists have focused our attention on these questions, and on their consequences for our national political parties, pressure groups, and churches, almost to the exclusion of any other way of identifying the importance and role of the state.

THE DEGREE OF CENTRALIZATION - GENERAL ARGUMENTS

In this section I shall discuss the best-known arguments for and against a federal form of government. The Canadian federal structure was coolly and pragmatically modelled on previously constituted examples by working politicians and British public servants. It is often argued that, because already by the 1860s both separation of the Canadian colonies and Union had been tried without success, federation was the next candidate for a form of government. But federation is not a single form of style of government; it is a bundle of characteristics pulled together by theorists and practical men in different places to deal with different problems. What kind of federation should they adopt?

The negotiators from the Canadian colonies were obviously most aware of the American example. It too had been pulled together pragmatically, to meet the different demands of the states who previously had been little more than members of a confederation or alliance against the British; and by 1867 it had been somewhat modified by the slavery issue, territorial expansion, and the influence of industrial technology. It is easy to forget how much fundamental, long-run, economic reasoning about centralization and decentralization went into the original Philadelphia recipe. Athens and the Holy Roman Empire, the writings of Hume and the newly published Adam Smith, such French philosophers of the Enlightenment as Rousseau and Montesquieu were all consulted. Thus, in adapting the American model, the Canadians were in fact reacting to the earlier American constituent assembly's application of ideas from many European sources.

The Canadian governmental structure was also influenced by the nineteenth-century British experience. In the aftermath of the Napoleonic wars Britain had, around the world, been experimenting with new forms and patterns of control; military and mercantile authorities were giving place to independent colonies. Even more important was the century-long development of a tier of local government for Wales, Ireland, and Scotland. Great Britain was gradually rationalizing its disorderly mosaic of counties, boroughs, districts, provinces, regions, and authorities. Parliament had been progressively setting up new decentralized territories for the administration or provision of education, welfare, and housing. Many philosophers and politicians, from Wilberforce to John Stuart Mill, asked themselves whether these new bodies should be self-governing, on the American pattern, or under rigorous central control, as in France. There was much agreement that Parliament could not handle the great variety of local situations; but there was also gloomy agreement that unfettered local democracy, a counter to the unlimited power of the Victorian Parliament, was to be avoided at all costs. Mill agreed with Alexander Hamilton a century earlier, and with many European writers,

that the pool of talent of men and women suitable for leadership was too small for a decentralized government: thus centralization was seen as a means for economizing on the time and powers of the scarce governing elite. It is a fair conjecture that, when the Canadian Fathers of Confederation were negotiating in London on the future structure of Canadian government, their British hosts inserted many of the current British notions about the desirable and practicable extent of decentralization.

The arguments of those days are still in use today, and we can summarize them briefly. It is assumed that government is democratic and representative. And it is assumed that the essence of the argument is whether, at one jurisdictional level in the pyramid, it is better to have a few large, or many small, governments. Under either system, the same total group of citizens would be served, taxed, and regulated. This question produces almost the same answers as a similar one: is it better that most power and responsibility should be centralized in the single block at the top of the pyramid, or decentralized in many blocks at a lower level? Both ways of posing the question raise a further question: can we pinpoint the chief advantages of decentralization, and the chief advantages of centralization? As it happens, this is fairly straightforward. The advantages of decentralization all have to do with precisely satisfying individuals' demands and preferences by setting up small governmental units that can listen to their demands and attempt to satisfy only them. Ideally, the outcome is that diversity among citizens' demands is satisfied by diversity among actions of small governmental units.

That is the "demand" side. On the "supply" side, the factors entering into government provision of its policies seem always to reveal economies of scale. The costs of serving a large population are not much larger than those of serving a small population; hence, there are gains to be harvested from entrusting the provision of public goods and services, the work of bureaucrats and regulators, and the protection of police, military, and the courts, to the highest level of government. From this point of view, centralization is the escape route from the high taxes and second-rate services afforded by the tiny state or parish. Obviously, we must choose. We cannot have a government structure which is both centralized and decentralized - in which all territories and populations are both big and small. The centralization debate may lead to compromise, but there is really no happy mixture of the two forms: they pull in opposite directions. Let us examine their details briefly.

The decentralization argument really is an amalgam of many propositions and assertions about the relations between citizens and their politicians and bureaucrats. First, and most important, is the capacity of decentralized governments to escape from a

uniformity of policy decided upon by a nation-wide majority. It can adopt policies that reflect varying regional tastes, preferences, industries, and geographies. The politicians of each jurisdiction can stay in office only by doing what local citizens demand, regardless of what is demanded and supplied elsewhere in the nation. Furthermore, if a nation that is divided among majority and minority parties (or interest groups) is cut up at random into small territorial jurisdictions, the total number of citizens who must suffer as minorities from the policies of majorities will decline; that is, the number of people who are left in disagreement with their local governments' decisions will decrease. This has been the great attraction of federalism in modern western and colonial history: decentralization has allowed regional jurisdictions to develop or retain their own policies not only as regards regulation, industrialization, labour conditions, debt, taxes, expenditures, and other aspects of economic policy, but also as regards education, religion, language, law, and citizenship.

There are still other benefits. Local or provincial government can be less impersonal, less remote, more responsive, more involved than national governments. John Stuart Mill advocated small and local governments because they could become the training ground of ordinary persons in citizenship and of more gifted persons in taking a role in national affairs. A more recent discovery has been that citizens' demands on local governments are reasonable and moderate because they associate the cost of whatever they demand with their own tax bill; whereas their demands on central governments are more irresponsible and carefree.

Nevertheless, common observation and history show, not the gradual adoption of communal or grass-roots democracy, but the amalgamation of local authorities and the union of provinces, states, and nations into today's sovereign nation-states. In many of them centralization of powers, taxation, and social policy have reached a very high level.

How are we to explain this? Granted, no economic model is adequate to account for the unsettled, kaleidoscopic variety of governmental structures to be seen around the globe today. Nevertheless, widespread democratic consent to politicians' centralizing tendencies must have some common basis. The explanation in economic terms is simple. Many government activities can equally well serve many or few people, large regions or small, many businesses or few. The area where this principle is most readily seen is defence. A military shield costs the same and affords the same defence regardless of the number of people sheltering behind it. But the actual tax and human cost per citizen falls as the size of the state rises. The same is true of many other kinds of protection: dams and dykes for flood protection; lighthouses and dredging for safe navigation; police, coastguards, and fire marshals for deterring criminals;

parliaments and news media for obtaining and exchanging political information. All these *and most other* public goods are technically capable of extending their benefits far and wide without a proportionate increase in citizens' taxes.

The benefits of centralization may also extend to improvements in the quality of the environment, as for instance, in reducing the amount of industrial air pollution emitted from a single source. The new benefit can be enjoyed equally by all citizens, and neighbouring citizens who live outside the jurisdiction that is providing and paying for the government service may get a "free ride". They are not called upon to pay, even though they may enjoy the benefits just as much as those citizens who stump up the finances. Situations like this (all too familiar these days in city finance) have for centuries motivated kings and politicians to amalgamate their tiny states into cost-reducing super-states. In the jargon or lingo of economics, centralizing the structure of government both "internalizes" the financial costs of public services and "internalizes" the political decisions about what extent, quality, or type of service is to be provided into a single Parliament. Without "internalization" a state may suffer from "externalities". When a state is too small, both its services and its disservices spill over into neighbouring jurisdictions. These neighbours become either free riders or innocent victims of the policies of external governments. And the government that is causing or permitting the external spillovers cannot be deterred from harming its neighbours or rewarded for serving them better.

Thus, in economists' jargon, a government structure that is made up of small units fails on two related but separate counts. First, it fails to profit from the economies of large-scale provision of public services: it under-utilizes the potential of its government. Second, because it is providing free services to neighbours who neither pay taxes nor vote, it tends to provide too few of these spillover services. The neighbours who now get a free ride would, if they were able to vote, support an expansion of the spillover services, even if they had to pay all the tax bill for the expansion. In short, setting up very small jurisdictions is uneconomic both because they must levy taxes that are too high for the services performed, and because each of them excludes neighbours who cannot exercise a financial demand for extended services. To most writers, the remedy for these two evils has long been obvious: turn over the provision of public services to larger governmental units. Centralize the provision of public goods and services, and internalize the decisions that affect neighbouring people and regions.

This centralization vs. decentralization dichotomy presents the structure-of-government question in terms that do not assist us to perceive our choices. First, it does not really allow of

compromise, because even the extremes of the opposing tendencies can be justified. The argument for decentralization, based on fully recognizing the variety of demands existing in different regions, suggests no limits to how small a government might be. A district, a parish, even a family might be too large a unit to give full weight to the preferences and incomes of different citizens. Indeed, political and economic philosophers who wish to get away from government, and get as close to *laissez-faire* as modern society and population pressure will permit, have urged that the sub-structure of governments should be visualized like a series of "clubs" - small bodies like town meetings and village councils, each controlling as few persons as possible, and each giving citizens a market-like opportunity, through migration and moving, to select the club that offers the mixture of taxes and services that they prefer. By this criterion the province or state and most metropolitan areas are already too large!

The argument for full centralization also seems unfounded. Pointing as it does towards the large jurisdiction, the unitary state, and the abolition of spillovers between neighbouring units, it tells us that in order to avoid the damages of harmful spillovers and in order to reap the full economies of large-scale production of public goods and services, the government structure should be revised until there is only one super-jurisdiction.

The tension between these two principles is often left unresolved by writers and speechmakers. Instead of acknowledging their incompatibility, commentators comfortingly describe them as a source of "balance", leading us to have a structure of government in which the units at the various levels are "not too big, not too small, but just right".

To some political scientists, the tension or antagonism between the two principles is a matter for congratulation. This is because political scientists, and legal scholars too, if I may venture to paint their approaches in very broad strokes, do not see the role of government in terms of what it can do for the individual. They do not see it as providing public services for the citizen and the business, as the private firm does in the private sector. Instead, they see government in "symbolic" terms. They talk about "nation-building", as though that in itself were the goal of patterning a constitution. In my eyes, they walk into the problem backwards. They assume that there must be a nation, and a structure of government within it. That structure has then to be reshaped so that the various political units and levels within it can survive and flourish. The structure of government has to be reformed only to the extent that the various units are failing to achieve their own purposes - their own purposes - not the purposes and preferences of the citizens whom the economist thinks they exist to serve. Far too many of our political thinkers believe that the

health of the governments in our federal mosaic is the objective of constitutional revision. They are concerned with shadowy aims like "province-building" or "nation-building". They think of the constituent provinces and the nation as though they were organic minds or spirits in search of goals, like the hippies of the 1960s who had lots of time to study their destination but no place to go. And they think of constitutional change in terms of reforming the pattern or pyramid of jurisdictional units, instead of better providing the public with services, goods, regulations, and protection.

AN ECONOMIC APPROACH

In the remainder of this essay I wish to discuss centralization and decentralization in what is sometimes called a "functional" way. Instead of starting with the pyramid of governmental units, and reforming the constitution to make each of them more viable, we start with the citizens. Not for the first time, I suggest that governments are institutions that people create themselves for the purpose of resolving essentially collective issues about the provision of public services.

The centralization criterion told us, to begin with, that we should eschew the proliferation of small governments because we as citizens also wish to reap the benefits of large-scale production and enjoyment of public services. My point is that this "balancing" approach collapses once we recognize that the economies of scale in production of public services are independent of the size of the government that makes the decisions to provide and pay for them.

Let me offer two examples, over-simplified but suggestive. Take local fire services. Assume that the chief element in fire protection is the public provision of fire engines. Now we all know from inspecting the mass-production facilities of General Motors, that there are giant economies of scale in the production of fire engines. But this economy of scale may benefit many different sizes of governmental unit. Production of fire engines is carried out in the private sector to serve many kinds of public jurisdiction, each of which reaps economies of scale from this production, regardless of its size and population.

Or take medical services. Assume that although a good public health system generally utilizes large treatment centres, hospitals, clinics, etc., the optimum size of territory which can be served by such units need not exactly "match" the jurisdiction of the government which supplies them. Decision making and financing concerning the services of the public medical units can then be divided among many smaller territorial units; you have all seen examples of that approach. Or, one huge political unit can easily include several parallel medical units.

By the same token, international military alliances are essentially very specialized and loose federations, or *con-* federations. The alliance puts together whatever armada or chain of fortifications it needs for joint military action. NATO is just such an alliance. But there is no necessary connection between the size or level of each of the governments that participates in decisions about military policies and the militarily optimum size of the defence activity they have jointly caused to be produced.

In brief, there is no necessary connection between economies of scale in production of services and the level or jurisdictional scope of the government that provides them. Centralization may be a good thing, but it is not rationalized, explained, or furthered by reference to economies of scale in production.

Our own economic approach therefore requires identification of a different limiting factor, that will allow economies of scale and production and yet limit the proliferation of small units of government. What is it that keeps us from living in a world of many small governments, or even clubs? The answer is simple. What keeps government from becoming subdivided into family-size molecules is the unit cost of setting up *governments* and the costs of operating them. Thus our approach is an economic one. Freed from considerations of symbolism and public purpose, we need only investigate the more mundane question of how the citizen can get his government to provide (not produce, but provide) the services he demands at reasonable cost by means of economy in government organization, bureaucracy, political participation and so forth.

Now this economic approach is, actually, compatible with an older "economic principle", which is embodied in sections 91 and 92 of the BNA Act and in many subsequent federal documents. There, the "national interest" and "local interests" are used as criteria to be played off against each other in the assignment of functions to provinces and to Canada. Railways and their regulation, for example, are assigned to Ottawa. The Fathers of Confederation knew that in Europe railways successfully cross national borders without any fuss. There is no imperative *technical* reason for having such international transportation problems under international jurisdiction; and there is no technical reason for the railways of Canada to be controlled by Ottawa. Or take criminal law. To Canadians it has always seemed mandatory that the prevention and control of crime must be regulated by the national criminal code. But in fact decisions about prosecution are made locally; in the United States, too, much criminal law making is also a local function. Or take Ottawa's regulation of combines in restraint of trade. In Europe they are experimenting with monopoly regulations which stretch across national boundaries, and in Canada, much of whatever successful use has been made of our combines law has been of a strictly local character. Indeed, the more one looks into the

differentiates the various assignments is that some ways of trying to make a government structure work are very costly, in the men, time, and materials making up organization costs, and some are more economical. The economist claims that in the past those who framed our constitution were aware of these costs, and that those who would build a constitution for tomorrow should, likewise, make them a major determinant of the assignment of powers.

For example, not only the Fathers of Confederation, but those who have later, by agreement or amendment, altered our constitution may be represented as arguing that, although railways *could* be controlled by each of the provinces (as in the Australian states), the *cost* of negotiation and co-ordination among provinces would be so high that citizens would gladly yield this power to the central government, where matters of safety, freight rates, gauge of tracks, etc. are all "internalized". Or take radio and TV. There is no reason why the allocation of radio waves among transmitters, and the allocation of time to commercial broadcasting stations should not be arranged in each province. Of course, there would then be interregional conflict. But "conflict" only means that there is a need for negotiation and co-ordination in order to arrive at some workable division of the radio-wave spectrum and the hours of the day. This co-ordination already works between adjoining small countries in Europe, and between the United States and Canada. It is a source of co-ordination and negotiation costs. But these costs need not be overwhelming, and they may well be less than the government-organization costs that would be involved in trying to settle such questions internally under a more unitary government. The prevailing practice of assigning most such spillover functions to the central government reflects to my mind a belief that the external co-ordinating and negotiating costs are often higher than the internal agreement and the information costs. That is why we find that, in the past, constitution builders have made many of the assignments that otherwise have no technical explanation.

For a final example, take the difficult subject of the co-ordination of provincial government spending in order to flatten out the business cycle. No one says that such co-ordination is impossible. But it would be so time consuming and so draining of the energy of eleven governments, that it is not seriously advocated or attempted. Once again, it is the costs of organization, not the technical feasibility, that is decisive.

Albert Breton and I have divided organization costs of government into four quite different sorts of activities. One pair we have already referred to: the costs that small units of government have in negotiating the co-ordination of their policies with those of their neighbours. These are common in urban situations, and also between national units. The larger the economies of scale in the production of some government services, and the larger the

scope of environmental policies, the higher will be the expenditures that must be made on external co-ordination. As against these, each government has internal costs of government. These are associated with administration, information, agreement, enforcement, and the mere setting up of a government apparatus. When we decide that a function is to be assigned to a certain government level, we must forecast how it will affect the total external and internal organization costs of that government.

There is another pair of organization costs. These are borne directly by the citizen. Citizens incur costs when they vote to obtain a particular package of public services. The most visible cost is that of voting, but there are further costs of political action; all the activities which signal to government what bundles of policies the different groups of citizens demand are costly. Furthermore, disgusted citizens may take the final step in political action, and move out. The cost to them of moving is also an organization cost.

Costs from this pair of organization activities are related to the structure of government. When functions have been assigned to governments, levels of governments, or sizes of territory in an irrational way, citizens with very different tastes or preferences for public goods and services will be grouped together. The problem may be schooling, language, street-cleaning, religion, weights and measures - anything. Ways of assigning functions that will keep citizen discontent to a minimum, as revealed by the costs they incur in political action or moving to obtain a better bundle of services must, then, be found.

It should now be clear that the economic approach links well with traditional historical or journalistic accounts of the origins of federalism. Those accounts stress racial, religious, or linguistic differences. Our account stresses the diversity among citizen tastes. We may be talking about the same thing. Their account says that, if the differences are too great, the unitary state will fail and a federal structure will take its place.

I disagree. Many peoples of diverse tastes and incomes live together in the same jurisdictions in the government structures of many countries. But it is pertinent to ask when such strong preferences, such diversities, will be recognized in the allocation of functions so that each sub-group of the population can have the policies it desires. It is true that diversities of taste, preference, and need may and usually do increase the social cost incurred by citizens who feel impelled to move or to engage in other forms of political action and signalling. Whether the cost of maintaining an established form of government despite social pressures will exceed the costs of co-ordination and administration that might arise from a more decentralized structure must also be

examined. That is the key to the economic approach to the constitution. We attempt to quantify the cost of the divisive forces in each jurisdiction, as they bear on both the costs borne by citizens and the internal administrative costs of governing. And we attempt to confront the total of these costs with the total organization costs that would arise if the division were dealt with by subdividing the country, or by assigning the functions to lower levels. These solutions could lead to lower costs of governing, higher costs of moving, and a far more costly array of organization for the co-ordination and partnership of small units in Balkan arrangement with each other.

There is nothing theoretical about this economic approach today. Every time the European Economic Community turns to the question of internalizing another function of government, the constitution makers with their critics must compare today's staggering costs of external diplomacy among the nine EEC members with the equally staggering costs of trying to agree on and administer a uniform European policy on such functions. Who can say which has the higher costs? Centralization is sometimes more expensive, sometimes less expensive, than decentralization. Or, consider the attempts in London to unscramble the United Kingdom omelette. Admittedly, there are many party-political and short-run reasons for and against devolving certain functions and taxes to Scotland. In the long run, however, the new constitution makers must also consider the social costs. Given a desire to have a certain uniformity on many policies, and a certain diversity on others, is there some structure of government that can manage both the increased internal domestic costs in London and the increased co-ordination costs between the semi-autonomous kingdoms? All government costs would seem to rise - will these be offset by falling political, signalling, and mobility costs of discontented individual Scots and Englishmen? This, we submit, is not an empty or useless question - it is an abstract but constructive way of organizing the considerations that must, *in the long run*, play a decisive role in deciding upon the future degree of centralization of the United Kingdom.

SOME OBJECTIONS ANSWERED

Let me begin this concluding section by summarizing matters thus far. In previous sections, I have distinguished between the long-run and short-run views of the structure of a nation's government. I have shown, so far as the long run is concerned, that the "degree of centralization" is a distinguishing characteristic of a country's existing structure of government, and that this does differ among federal countries and among different time-periods in the same country. I have argued, however, that the "degree of decentralization" of a country is not in itself a suitable subject for discussion or resolution, as it is merely the visible outcome of

the crude forces of local decision making and centralization (such as the alleged economies of scale in the provision of public goods) pulling in opposite directions. Finally, I suggest that what matters is not the visible over-all extent of centralization or decentralization, but the assignment of each and every function to a jurisdictional level in the national pyramid in such a way as to cut to the bone the total of organization, administration, co-ordination, signalling, and mobility costs of various assignments of functions. I suggest, too, that this "economic" approach is already implicit in the assignment embodied in sections 91 and 92 of the BNA Act - many of these assignments were made "as if" the Fathers of Confederation, the courts, and those who have made federal-provincial reassignments by agreement were motivated by a desire to minimize organization costs.

There will be plenty of objections to this view. Some will argue that it is not a helpful way to approach the long-run problem of the Canadian constitution. Others will argue that the theory destroys itself by internal contradictions.

As to whether it is helpful or relevant, you must be the judge. The fact that such issues as cablevision, the provincial ownership of airlines under federal regulation, agricultural policy, pipelines, and social policy with respect to family matters like abortion, divorce, desertion, and maintenance are all being continually revised with an eye to simplifying the problems of administration, co-ordination, and citizen compliance, suggests to me that Canadians *do* favour simple, rational, and low-cost ways of administering policies and so are implicitly acting as my economic approach suggests. Thus I believe it to be a helpful and relevant abstraction of the process of making and re-making the structure of government.

It may rightly be asked whether citizens ever are consulted about their preferred assignment of functions. My response is twofold. In the first place, I do not think that citizens care much about the structure of government, if that is defined in the precise assignment of particular functions and powers. What they want can be summarized in the following triad: policies they agree with, at a tax-price they can afford, provided by an overall structure that is not costly. Within these rules, they are largely indifferent and ignorant about which government is entrusted with what responsibility.

But who is responsible for seeing that a cost-minimizing structure is adopted? Recent Canadian authorities have argued that our politicians and top civil servants are unlikely to follow the authors of the *American Federalist Papers* in pointing the way to an economical assignment of powers. The attainment of an efficient assignment of functions among all levels of government is rarely a

political goal. Bureaucrats and top advisors are more flexible in their motivation, but they too are more likely to seek power and status than to support the assignment of their responsibilities to other levels of government. Failing politicians and their civil servant advisors, which persons - or what mechanisms - can bring about the best allocation of powers? Pondering this question, I feel great sympathy for those who have argued that we ought now to look outside government for the members of a national constituent assembly. The economic approach I have outlined can save its members from wallowing in spirals of do-good platitudes. Like a jury, they would have a job to do: find the most economical assignment of functions. Obviously, leaders of ruling parties and their politicians and public servants and harassed officials must necessarily have a point of view that is too short run to take into account the minimization of organization costs in the long run. There is instead much to be said for the *ad hoc* council, assembly, or gathering. I do not feel strongly about its membership, except that it should be broadly and visibly representative of regions, parties, languages, and social classes. It is important that its members should be neither neophytes in political matters, nor in a position to gain personally from the structure on which their assembly finally agrees. Such a detached assembly may even be capable of defining justice and equity. Maybe so. I feel more confident that it could at least suggest long-run modifications to our constitution such that our mosaic of citizens with their variety of preferences can obtain the policies they desire with a minimum of government or voter organization costs.

Finally, I would like to address the almost cynical view that what matters, what really determines the assignment of functions, is the power of taxation. Whichever level gets the most prolific tax bases finds that all the other powers and duties are also given to it.

As historical generalization about the economy, this may be correct. The power of the purse, the power to pay, and to make grants may have seemed to explain everything else. Certainly many Royal Commissions have acted as though they felt the assignment of the power to tax must be the essence of constitution making.

I say that the assignment of tax bases, like the assignment of expenditure and regulatory functions, can be included in the economic approach I have advocated. Tax bases can be subdivided and shared, and, along with grants, abatements, and subsidies, can be entrenched in the constitutional assignment of functions. The rationale for matching powers and revenues should, once again, be to minimize organization and compliance costs.

No one can deny that money matters to the long-run structure of government. But the sources of revenue should be treated

differently from other powers and responsibilities. Both can be approached simultaneously from the organization-cost perspective.

Too often the assignment of functions is examined as though it were a game between contending jurisdictional levels. Let us try another metaphor. Let us imagine a deal in which powers are assigned like cards. Sources of revenue are dealt out in the same neutral fashion as spending responsibilities. The dealer is not one whose own career depends on how the assignment comes out. The object of the game is to achieve a distribution of functions that reduces to a minimum the cost of implementing them, not to make any particular card trumps, or any particular player the winner.

NOTE

¹ One handy consequence of using "economic activity", rather than "size", or "symbolism", as a measure of the importance of the level of the governmental pyramid is that it allows us to hammer out a crude measure of the degree of centralization implicit in our present structure of government. Consider two pyramids, for three nations. In one, all the spending, taxation, and regulation is undertaken by the lowest level of government: the upper tiers are splendid but inactive. In the second, the top-most block undertakes all the expenditure, taxing, and regulating. In the third, the middle tier, the provinces, have the main economic impact. Albert Breton and I have evolved an index of centralization that would take into account the amount of government expenditure at each level. If all of it goes to the top, then that society has a structure of government with an index of 1.0; if all is done by the lowest-level jurisdictions, the index value is close to zero; and if most of the activity and spending is undertaken by the middle-level governments, the index takes on a value of close to one-half (0.5).

We have applied this "index of centralization" to our own and to other federations. International comparisons are obviously difficult, because definitions of the role of government vary from place to place and from time to time. Nevertheless, our suggested index has proved itself by showing that Canada's degree of centralization is not unduly high compared to that of the United States and of Switzerland and that, like theirs, it has been declining since the 1930s and 1940s. (Figure 5:1, below.) For Canada alone we have also divided up the various kinds of government activity. In Figure 5:2 (below) we see from the lowest line that government expenditure on goods and services (excluding defence

expenditure) has been almost constant, and highly decentralized, since 1926. Transfer payments, on the other hand, have become centralized (top line).

FIGURE 5:1 INDEX OF CENTRALIZATION
Total Expenditure—Includes Transfers and Military

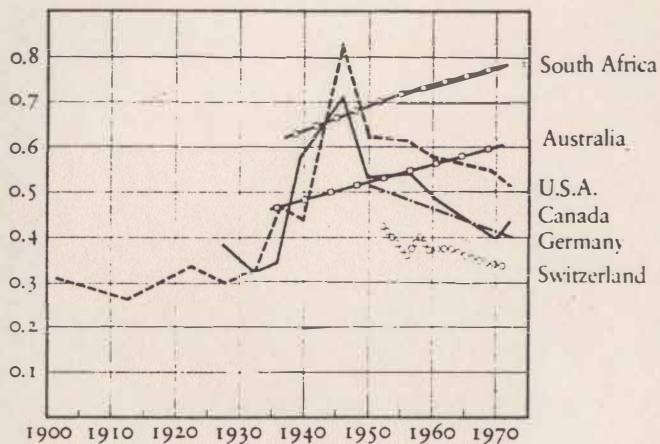
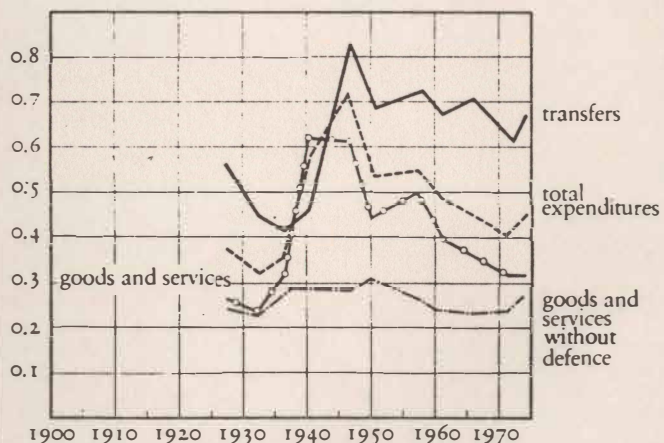
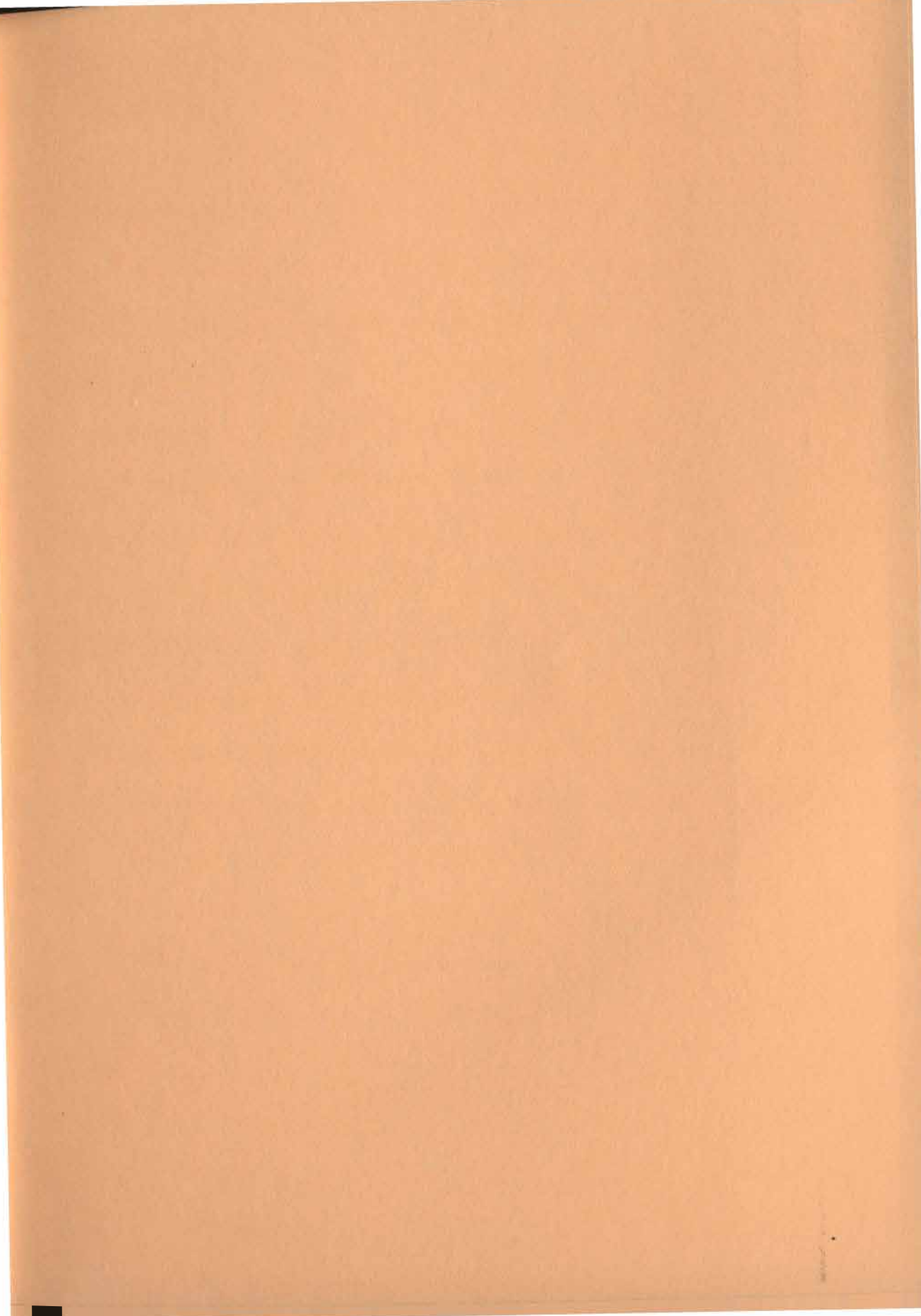


FIGURE 5:2 INDEX OF CENTRALIZATION—CANADA
Four Categories of Expenditure—1926-1970





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