

DEBATING FISCAL FEDERALISM DAFFLON, BERNARD (1992): “THE ASSIGNMENT OF FUNCTION TO DECENTRALIZED GOVERNMENT: FROM THEORY TO PRACTICE”. GOVERNMENT AND POLICY, VOL. 10, PP. 283-298.

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ABSTRACT: *Reviewing a book generally has twofold advantages: first to understand the central ideas of the book, to dig out the shortcomings and strong sides of the authors view as it evaluated on the eyes of others. The second advantage of reviewing is to investigate various contestable facts and scholarly debate on a certain issues and hence, it enables the readers to know what the book is all about, and to have one’s position of argument. Therefore, dealing with review of Bernard Dafflon’s book which is entitled as: “The Assignment of Functions to Decentralized Government: From Theory to Practice” and his assumption regarding theory of the assignment of function to different levels of governments make possible us to broaden our level understanding on the issues in advance. The reviewing process is embarked on based on the principle of grand assignment of functions such as macroeconomic stabilization function, redistribution function and allocation role that are traditionally assigned to the central government nexus Dafflon’s view. Moreover, different scholars’ arguments regarding assignment of function at each level of government are also included.*

KEYWORDS: Assignment of functions, sub-national and local government, Macroeconomic stabilization, Redistribution.

INTRODUCTION

Assignment of functions refers to the systematic allocation of fiscal powers such as expenditure and revenue collection powers to different echelons of government within a federation. Each order of government does have a specified list of powers assigned to it. Accordingly, allocation responsibilities of public services are left to local government, and tasks such as redistributive and macroeconomic stabilization are exclusively given to the central government. These forms of divisions of assignments however are not universally accepted among scholars of fiscal federalism. There is no clarity regarding who does what and when?, and hence, it is subjected to persistent debate among academicians.

Later on, this assumption has been seriously challenged by the proponents of Second Generation Theory of Fiscal Federalism (SGTFF). According to this theory, besides the central government, it is quite possible for local government to play a role in macroeconomic stabilization and redistribution functions with the virtue of fiscal power. Unlike the scholars of the economic Theory of Fiscal Federalism, Bernard Dafflon- whom we are going to review his book, and belongs to the second generation theory argue that local governments should also take part in those functions that are exclusively given to the central government.

In this particular review paper, we tried to assess Dafflon’s book so as to excavate various contested arguments regarding assignment of functions to local governments. To do so, first

attempts are done to recapitulate the overall arguments of Dafflon's book and then to review it based on other scholars' point of view.

Dafflon B.(1992) in his book entitled: "*The Assignment of Functions to Decentralized Government: From Theory to Practice*"- put his efforts to summarize the general principle employed to assign various function to different echelons of governments. In the book, the view points of traditional economic theory of fiscal federalism regarding the assignment of functions which recognized Macroeconomic stabilizations and income distributions are the responsibilities of the central government, and Allocative functions are assigned to lower level of governments on efficiency considerations are assessed. In addition, the book also articulated the existing discrepancy between theory and practice since functions are not assigned according to what the economic theory dictates but rather according to political and social considerations. As a result, decentralization of functions are not derived from the very notion of economic theory but from the political, social and cultural conditions (Dafflon, 1992).

Finally, the book also recommends the policy proposal that should be considered in the discourses of assigning of functions to different levels of government. Besides to economic criteria, some other criterion such as Socio- cultural and political reality of local governments, managerial capacity, poverty reduction and fiscal competition among multitier of governments are some of the relevant non- economic criteria that has to be take in to consideration.

Macroeconomic stabilization- pertaining to macroeconomic stabilization, economic theory of Fiscal Federalism scholars like Oates insists that it is only the centre that has prerogative of stabilization role. The justification behind this is that it needs a cautious regulation, administration and implementation of monetary and fiscal policy such as controlling circulation and printing of money in the market. Moreover, local governments because of Openness of their economics-which leads outflow of finance; Fee riding- a strategic behaviors of one jurisdiction to benefit from other jurisdictions' spillovers; and the possibility of Deficit in financing due to uncontrolled borrowing and mismanagement of budget, and cyclical variation in the economy collectively results immense destabilization of the economy. However, Dafflon challenges the assertion of deficit financing that can lead to destabilization. This can be only true in a situation where there incompatibility between the assigned functions/ responsibilities and the granted revenues sources. Otherwise, allowing them to borrow just for infrastructure and investment purpose will mitigate such kinds of problems (Dafflon, 1992). On the contrary, unlike Dafflon's view, others are skeptical of decentralizing monetary power which might brings unnecessary destabilization of national economy like increase inflation and unemployment rates (Musgrave, 1959; Oates, 1972). Their basic argument is that there are some fundamental constraints on lower level governments. For instance, in the absence of monetary and exchange-rate prerogatives and with highly open economies that cannot contain much of the expansionary impact of fiscal incentive, regional or state, and local governments simply have very limited means for macroeconomic control of their economies. Here, we can reaffirm their arguments by taking the premises that in all federation monetary power is exclusively given to the centre. It seems quite right since local governments in the absence of monetary power and monetary policy instruments to regulate macroeconomic stabilization is far from reality, but is an utopia. Unlike the Sub-National Governments and Local Governments, it is therefore the centre that can perform it effectively. This argument is strengthened by the prominent works of Bahl and Linn (1992), who insisted that greater centralization improves producer efficiency at a time when public service provisions cause economies of scale or externalities (Bahl and Linn, 1992).

In contrast to this, Dafflon debate the exclusive power of the central government over macroeconomic stabilization functions. Although, sub-national government lacks the capacity to have monetary power, still they do have role in macroeconomic stabilization function through fiscal policy devices, by manipulating tax rate, spending and by borrowing from financial institution from domestics or abroad. This condition will leads to Fiscal competition and it may force governments to provide services at the minimum possible cost, so that it enhances producer efficiency; even though the degree of efficiency enhancement capacity widely varied between jurisdictions (Bodman, 2008; Oates, 1999). As Dafflon attempts to explain, in practice, cantons and communes in federation like Switzerland engages in the stabilization function. Accordingly, macroeconomic stabilization in Swiss is not the sole function of the confederation (Dafflon, 1992). His argument will be correct only in a federation where Sub National Governments like Swiss are constitutionally granted the right to have fiscal autonomy and let alone them to borrow from financial institutions. Moreover, Martinez-Vazquez and McNab (1997) and Theissen (2000) also asserted that fiscal decentralization can encourage policy experimentation and innovation in the production and supply of public goods and services. If such innovation leads to greater producer efficiency, then the higher quantity or quality of public goods and services could sooner or later result in increased income, and marked economic development would follow.

In contrast to this, in a country like Ethiopia in which regions without having power to borrow money from international and even from domestic government owned financial institution unless the centre give permission to them to borrow through federal collateral, they have insignificant roles in the stabilization process. Beyond to this, his argument might overlook the problems of co-ordinations that arise because of absence of equal commitment among regional governments. In other words, it is so challenging to coordinate Sub National Governments to have a common consensus regarding say for example, the means of attaining macroeconomic stabilization. But rather they might have personal agenda that they can manipulate and give priorities (Gebre-Hiwot, 2013). In this regard, a prominent scholar like Prud'homme (1995) visualized the potential danger of devolving fiscal powers to lower levels of governments. In certain scenario, it can provide a vehicle through which regional or local governments can exploit what he termed the "fiscal commons" by effectively shifting the burdens of local programs onto the nation as a whole (Prud'homme, 1995). In addition, he also argues that fiscal decentralization may increase regional inequality (disparity). This unhealthy competition arise between different tiers of government greatly affect those jurisdiction which are poorly endowed by attracting potential business men towards their jurisdiction through overcutting the amount of tax burden imposes and services recipients payment (Bodman, 2008). To address such a problem centralized fiscal system is needed to provide public infrastructures for all regions and reduces regional inequality in their developmental discourse (Bahl and Linn, 1992). Taking such point as a premises, one can argue that economic Theory of Fiscal Federalism by far seems realistic than what Dafflon suggested.

Redistribution policy- regarding redistribution function, Dafflon also insisted that it is not the centre only to have such function, but also Sub-National Government and local government play a role in income redistribution from the rich to the poor. Redistribution is therefore a shared responsibility among the centre, Sub National Governments and local governments. Scholars such as Padovano, reaffirm and even goes beyond the views of Dafflon by arguing that regional governments by far are better than central government in establishing redistribution function efficiently. According to him, central government creates inefficient inter-regional redistributive programs and it causes exploitation of some region by others. In

order to overcome such exploitative practice, he proposes an exclusive assignment of redistribution function to regions so that each region would rely on its own resources for redistribution (Padovano, 2004). To the extreme end, (Pauly, 1973) considers redistribution as a local public good and concludes that a local level redistribution policy would be more efficient than a centralized one as utility of the poor people and disposable income of rich people increases concurrently. To this end, Pauly forwarded two assumptions: first, rich people within their locality are concerned about the wellbeing of poor people who resides in their own community, and second, household are immobile. Though the mobility argument is so fundamental in the redistribution function, the assumption of immobility seems close to practical and it is not as such a precluding factor in assigning redistribution function to local governments. Poor and rich people might not leave their residency as what 'Tiebout claim *'vote-by –own feet'* by simple reason to enjoy social aids and low tax burden that exist in the other jurisdictions (Tiebout, 1956). This is because of the following reasons as pauly stress: *i*) Outmigration is not something happen without cost. Migration (especially labour) will dependent on social, cultural, linguistic, family tie and psychological perception towards their local area may keep people attached in to their local place though there is high tax burden. Immobility will be more visible and migration problem will be less if the federation is structured along with ethnic, linguistic and or religious line. Quebec in Canada is the best example. Even though high tax burden is there in Quebec province, there is a lowest out migration among the Canadian provinces. It is true because just the majority of its population is French speaker and catholic dominant, contrary to the rest of Canadian provinces that are dominated by protestant religion and English speakers which in turn curtail the feeling of migration from Quebec (Pauly, 1973; Watts, 1999). *ii*) Local Governments are more informed than the centre in distinguishing needy groups who requires help in certain social assistance system. Hence, they are cost effective in managing redistribution function than the centre. *iii*) Social assistance to targeted or needy groups are usually undertaken by local governments with time bounded and defined eligible criteria. Such a system ties poor people to stay in their original jurisdictions (Dafflon, 2006).

Moreover, according to king, 1984, higher business profit tax may not necessarily lead to capital migration for many reasons. *First*, wealthy business men might not perceive a local progressive tax rate for redistribution purpose as painful burden. They may appreciate such a policy that it will creates positive spill over effects to them in reducing crime, in increasing directly or indirectly the demand for their products and supplying trained labour (King, 1984), and *secondly*, even if the costs of the business become visible, going out from their original jurisdiction simply because of higher tax burden might not be perfect option. Nevertheless, king stood himself against Dafflon's views of coordination redistribution assignment among different levels of governments. He comments two protestations regarding coordination principle: *first*, legislation of common or universal policy via cooperation might be ignored by the majority of the population at local levels if they feel no comfort by the existing policy and it in turn brings cost ineffectiveness. Uniform policy done by the centre is more cost effective than what sub national government does-which is based on compromise. *Secondly*, in most cases redistribution tasks requires to a progressive tax rate, which mostly hated by the rich business men groups. These factors in combination might yields ineffectiveness of having common policy vis-à-vis redistribution (king, 1992).

Vis-à-Vis criteria being applied to assigned responsibilities, unlike economic theory of fiscal federalism which takes economic criteria as a sole determining factors regarding what responsibilities should be allocate to which level of government. Besides to economic criteria,

Dafflon argue that devolved public service is not something limited only by economic factors, instead it includes various variables such as political culture (accountability, solidarity, participatory democracy and information availability), principle of subsidiarity, history, social factors, administrative feasibility, managerial and institutional capacities, cultural values, poverty alleviation, and demographic situations etc as criteria should be considered in allocating responsibilities (Gebre-Hiwot, 2013). Consequently, he understands the existing status quo realities that can strongly influence on the assignment of responsibilities to lower level of government- in which the predecessor theory overlooked. It is worth to note that the most parts of the public functions or services are delivered through shared principle among the different levels of governments.

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