

“The Principle of Subsidiarity”

article 5, section 3 of the Treaty of Lisbon (which governs the European Union)

“Under the principle of subsidiarity, in areas which do not fall within its exclusive competence, the Union shall act only if and insofar as the objectives of the proposed action cannot be sufficiently achieved by the Member States, either at central level or at regional and local level, but can rather, by reason of the scale or effects of the proposed action, be better achieved at Union level.”

Central Government Provision

ASSUMPTION V If a high-level government, which is divided into many regions, provides some public output, then provision is **uniform** : everyone in every region must get the same level of the publicly provided output, if it is provided by the central government.

RESULT : If there is a federal government, comprising many lower-level jurisdictions, under assumptions $I-V$, everyone is better off if the lower-level jurisdictions provide the public expenditure, not the federal government.

Economies of Scale in Population

one of the justifications (in the Treaty) for provision at a high level of government is “the scale..of the proposed action”

economies of scale in population in the provision of some good
→ Assumption // doesn't hold

θ^f : unit cost of the public output, if provided by central government

θ : unit cost of the public output, if provided by lower-level government

economies of scale in population : $\theta^f < \theta$

Who Wants Centralized Provision?

if the federal government chooses $g^f = g^*(y^i)$, then income group i will be better under centralization

$$U^{iF} = u(y^i - \theta^f g^*(y_i), g^*(y^i)) > u(y^i - \theta g^*(y^i), g^*(y^i)) \quad (1)$$

but if $y^k \neq y^k$, centralization gives group k cheaper public output, but not the quantity that they want

if taste differences are large, then it may be impossible to make everyone better off under centralization, even when the economies of scale in population are substantial

Promises, Promises

In some cases, it might be **possible** to make everyone better off under centralization (and uniform provision) than they are under decentralization, if scale economies are large, and if taste differences are not too large

in this example, a central government would somehow have to commit to a public output level in the “central better” region, in order to get both groups to agree to let a central government take over provision of g

Giving people in the minority group the right to secede might also work well as a commitment device

Spillovers

other justification for central government provision in the Treaty of Lisbon is “the effects of the proposed action”

implicit in analysis so far : the assumption that one lower-level jurisdiction’s public expenditure has no effect on residents of other jurisdictions

spillovers : externalities (usually positive) between jurisdictions

example of spillovers

$$u(c, g, \tilde{g}) = cg + 2\tilde{g} \quad (2)$$

where \tilde{g} is the level of public output in the other town

$$y^1 = 12, y^2 = 24$$

decentralized, and ignoring spillovers : $g^1 = 6, g^2 = 12$.

better (for everyone) : $g^1 = 7, g^2 = 13$

Is Centralization Better?

(when there are spillovers and when lower-level governments ignore spillovers)

maybe, maybe not

in the example (above) , actually both groups would be worse off under central provision

With the low-income people in charge, the central government would choose g so as to maximize

$$(12 - g)g + 2g \tag{3}$$

which is the utility of the (majority) low-income people when they must choose the same level of g for every region.

solution to maximization : $g = 7$

so that $u^1 = (5)(7) + 2(7) = 49$ and $u^2 = (17)(7) + 2(7) = 133$