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What Competences for the EU?

Towards a European Version of Fiscal Federalism

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ABSTRACT: The issue of *What the EU Should Do*, or what should be the competences of the European Union, is gaining more relevance with the increasing level of EU integration. The academic analysis on the competences of the EU has so far not fully answered this question. The political science literature has focused on the "democratic deficit" and lack of legitimacy of the EU, assuming that solving these problems would naturally lead to the correct allocation of competences. The economic literature on the contrary focuses on fiscal federalism, analysing which policies can be done more efficiently at the EU level, but ignoring whether it is seen as legitimate to reduce national sovereignty on those policies. This paper argues that only a combination of the two approaches can lead to useful results. It adapts the theory of fiscal federalism to the EU, by incorporating the concept of *legitimacy* into the analysis. Legitimacy is assessed through three factors proposed by the literature: normative justifiability, popular acceptability and accountability. The analysis is applied to different areas of policymaking. Results show that this modified form of fiscal federalism can lead to more complete and realistic insights.

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INTRODUCTION

The recent agreement on the EU Treaty of Lisbon appeared to solve the immediate crisis caused by the rejection of the Constitutional Treaty in the 2005 French and Dutch referenda. However, it did not address what was arguably the underlying problem: the EU has entered an “identity crisis”, as there is no agreement on what its functions should be. The academic literature on the competences of the EU has so far not fully answered this question. The political science literature has focused almost exclusively on the "democratic deficit" and lack of legitimacy of the EU, assuming that solving these problems would naturally lead to the correct allocation of competences. However, that would not necessarily be the case, as those are two different issues that need to be analyzed separately. Moreover, it is difficult to find the appropriate democratic setting for the EU without first knowing what its competences should be.

On the contrary, the economic literature has focused only on fiscal federalism, the field of economics that studies which policies should be allocated to a centralised level of government and which should be done at a decentralised level. These theories originated in the United States, but, as the integration of the European Union progressed, scholars began to apply them to the EU. However, the theories of fiscal federalism were designed to be applied to the US, which is a single country, as opposed to the EU, which is an economic and political union between sovereign countries. Therefore, although fiscal federalism provides useful insights to the analysis of the EU, the fact that the theories are most suited to one single country creates problems to the analysis, as several authors have admitted.

For example, Oates (2002) comments that *"much of the literature, especially the part addressing the assignment of functions, has been developed in the context of the modern nation-state. (...) As such, it doesn't seem to fit very well the cases of emerging «confederations» such as the European Union"*. Ackrill (2003) also argues that *"in the context of the European Union, this [fiscal federalism's] traditional paradigm is not only inadequate but confused, leading to a lack of clarity in the debate"*

In particular, for a political union such as the EU, the decision to centralise policies depends not only on efficiency considerations, but also on whether it is seen as *legitimate* to reduce national sovereignty over those policies. Therefore this paper proposes to integrate the economic literature on fiscal federalism with the political literature on the legitimacy of the EU. To that end, it adapts the theory of fiscal federalism to the EU, by incorporating the concept of legitimacy into the analysis.

Legitimacy is a concept used in the political science literature to express the notion that a government, or its actions, are rightful and justified. The academic literature on legitimacy proposes several ways to assess that rightfulness. This paper identifies three main factors of relevance for this analysis: public opinion – whether the citizens accept and support the government actions; accountability – whether the government actions were taken following a democratic political process; normative justifiability – this encompasses a number of subjective criteria to assess whether it is acceptable to have a certain policy at a certain level. The paper incorporates those factors into the fiscal federalism analysis and applies that analysis to different areas of policymaking, to find whether these should be allocated to the EU level or to the national level.

The paper will take as its starting point both traditional fiscal federalism and "second generation" fiscal federalism. In a nutshell, traditional fiscal federalism says that a certain policy should be done at a more central level if this permits to internalize externalities or to reap economies of scale¹; however, if there is a significant heterogeneity of preferences (that is, if the people in the different countries want different policies) it should be done at a more decentralized level. Second generation fiscal federalism adds considerations of political economy to the analysis – it takes under account the existence of political failures at all levels of government, and seeks to identify the level of government that minimizes those failures.

The rest of this paper is organised as follows. Section 2 reviews the political science literature on legitimacy and proposes how it can be incorporated into fiscal federalism. Section 3 analyses the different policy areas using traditional and second generation fiscal federalism together with legitimacy. The conclusion looks at the new insights originating from this approach.

2. MEASURING LEGITIMACY

The concept of legitimacy is normative and subjective, and can be interpreted in different ways. A great part of the wide political science literature on legitimacy is precisely dedicated to finding how to best define the concept. The most recent literature sees legitimacy as a multi-faceted concept and takes under account its different aspects (see, for example, Beetham (1993), Lord and Magnette (2002)). This paper follows that approach, as it is argued that a complex concept such as legitimacy should not be reduced to a single factor, but instead should be derived from a number of factors that, together, create a perception that a government and its policies are legitimate.

Six main factors of legitimacy were identified in the literature. Of these, three were considered to be useful for the analysis of how to allocate individual policies between the EU and the national level. I will begin by describing the three factors which will be used in the analysis. I will then briefly describe the other three factors and explain why they were not considered useful for this type of analysis.

2.1 Factors used in this analysis

Public Opinion

The notion of legitimacy is ultimately based on public acceptance. Although in representative democracies the actions of government are not due to follow directly public opinion (elected governments can take unpopular measures, without that going against legitimacy), public opinion has the last word as politicians need to be (re)elected. In the case of the EU, public opinion assumes even greater importance, due to the lack of direct elections (see next section). Therefore, it is necessary to take it under account when deciding whether to allocate policies at the EU level.

Public opinion can be measured through surveys. The Eurobarometer surveys are undertaken by the European Commission to measure the opinion of EU citizens with regards to the EU. The surveys include a question which was designed specifically to measure the opinion of

¹ Externalities occur when a decision by an economic agent causes costs (or benefits) to others, for which the agent does not bear the cost (or does not reap the gain). Economies of scale occur when average cost of producing a good decreases if the good is produced in a larger quantity.

people on which policies should be allocated to the EU level. The answers to that question will be used in this paper to approximate public opinion.²

Accountability

Another essential element of legitimacy is accountability. Policymakers are accountable to citizens if they are required to follow a democratic political process. Such a process is based on elections and direct contest for the political office, and a system of political institutions which guarantees checking mechanisms on political power.

The literature generally looks at the issue of accountability in the EU as a whole (often referred to as the *democratic deficit*), but not at the individual policies. However, in the EU the level of accountability varies widely between individual policy areas, as they are at different levels of integration, different legislative processes are applied to some areas are easier to follow by citizens at the EU level than others. This is therefore an important factor in assessing the legitimacy on different policies at EU level.

Normative justifiability

The concept of *normative justifiability* was proposed by David Beetham (1991). Beetham argued that one of the conditions for legitimacy was normative justifiability, whereby "rules should be justifiable by reference to shared beliefs" (Beetham, 1991). Those beliefs were of two types: "beliefs about the rightful source of political authority" and "beliefs about the appropriate ends or purposes that the government should serve" (Beetham, 1993).

The latter type of beliefs is relevant for this analysis – the beliefs about the appropriate ends and purposes of the European Union are of high relevance when analysing which policies should be done at the EU level. However, there is no universal agreement on what are those appropriate ends and purposes, as views on what the EU differ between countries and even from person to person. Therefore, an analysis based on normative justifiability will give different results depending on which set of beliefs on the purpose of the EU is used.

For the purposes of this analysis, this paper will propose a set of beliefs. It is argued that the EU was created with two main purposes, and that still today, despite the expansion in EU powers, it is still relevant to use those two purposes as guidance to what the EU should do. They are: economic integration and promoting peace in Europe. The EU was created with the purpose of avoiding future wars and tensions between its members, and that was to be done through the creation of a free trade area. Although since its creation the EU areas of activity have expanded, and many would argue that it has now much wider objectives, these are the only two objectives for which there is wide agreement that the EU should play a role.

To define these as the two objectives of the EU does not give specific guidance as to what the EU should do: the objective of economic integration can be seen either in its narrow sense, where it justifies only a simple free trade area between the Member States, or in its widest sense, where it justifies a complete harmonization of economic policies, which itself can be seen (or not) as justification for political integration. Similarly, the objective of promoting peace can be seen in its narrow sense - where no action by the EU is required in this field, because peace derives from the free trade area - or in its widest sense – where it justifies a

² Question A24 of Eurobarometer No. 66, December 2006: "For each of the following areas, do you think that decisions should be made by the (NATIONALITY) government or made jointly within the European Union?"

common defence policy, a common foreign policy and the harmonization of policies on home affairs.

This paper proposes to consider as most legitimate the policies that are closest to those two areas. It should be noted that the analysis could also be made with a different set of assumptions regarding the normative justifiability of the EU, which would lead to different results.

2.2 Factors not used in this analysis

Indirect/Legal Legitimacy

Legal legitimacy requires that the actions of the government are derived from a legal source, and that the government is following legal political procedures. In the case of the EU, all policies and interventions follow a pre-established legal procedure, and all EU powers and responsibilities have been given to the EU by the national governments, so legal legitimacy exists. Some authors have also argued that the EU has *indirect legitimacy* – since all EU initiatives must be approved by national governments, themselves legitimate, that makes the EU legitimate as well.

However, although some authors defend that legal legitimacy and indirect legitimacy are sufficient to ensure the legitimacy of the EU (Moravcsik, 2002), others argue that the fact that a government action is legal is not sufficient by itself to conclude that it is legitimate (Follesdal and Hix, 2002). This paper will not use the principle of legality in the analysis, as it is not helpful in distinguishing between the different policies, as all EU policies are strictly speaking legal. Moreover, this author shares the view that this condition by itself is not sufficient.

Technocratic Legitimacy

Another source of legitimacy is related to “output” or “efficiency”. Its defenders say that the fact that a government action is efficient makes it legitimate, or at least contributes towards its legitimacy. According to this view, the legitimacy of the EU derives from the fact that the EU enables the Member States to address "common interests" and the EU is legitimate because it provides benefits to citizens. This view would imply that fiscal federalism itself is a way of assessing legitimacy, as it would be legitimate to transfer a policy to the EU level as long as this increases efficiency. However, it is doubtful whether this can be seen as a source of legitimacy, as this would imply that a dictator, who would be ruling the country against the citizens' will, could be legitimate as long as he tried to rule it efficiently. It is of course highly desirable that government actions are efficient, but this should not be confused with legitimacy.

However, an exception could be made for certain policies, which can be done by "agencies". Moravcsik defends that the EU is an agency of the Member States and therefore it should be independent from the political process, and therefore not subjected to the democratic process. This paper argues that this cannot be said to apply to the EU as a whole, because EU policymaking is involved with so many areas and has so much power that it could not be acceptable to say that all that should be exempted from the political process. However, there are two areas where this reasoning could apply: monetary policy and competition policy.

These are two areas where there is wide agreement that they should be isolated from the political process, because the good functioning of the economy requires that they follow pre-set rules.

Collective identity/demos

Another factor of legitimacy is whether the government is representing citizens with a collective identity or "demos". In the case of the EU, this would require that citizens identify with the European Union or "feel European". To a large extent this is not the case, as surveys show that people identify much more with their nationality than with Europe. However, several authors have argued that this condition is not necessary, as long as the EU meets other requirements of legitimacy (for example, Scharpf, 1999).

This paper agrees with the latter view, for two reasons. Firstly, examples such as the UK show that a government can be legitimate even if its citizens identify more with their regional identities than with their national identity. Secondly, and most importantly, the EU is not replacing the Member States, and the powers of the EU are much smaller than those of the national governments. As long as national governments have more powers than the EU, the fact that national identity is felt more strongly than European identity is not a problem. This paper therefore does not see this condition as essential. Moreover, this factor would not provide guidance in the differentiation between policies.

3. APPLICATION TO POLICIES

This section will therefore focus on normative justifiability, public opinion and accountability. I now apply these criteria to different areas of EU policymaking. For each area, I will first briefly summarize the insights from traditional and second generation fiscal federalism, and then complete those with the analysis based on legitimacy.

Defence and Foreign Policy

Traditional fiscal federalism holds that defence policies should be centralised, to benefit from economies of scale: by pooling their resources, Member States could make their defence systems more efficient and save money by avoiding duplication. There are also economies of scale in the areas of foreign policy that are not directly related to defence, because by pooling their efforts the Member States can improve their standing in the international scene. However, there is a very significant problem of heterogeneity, because countries have very different foreign policies. Therefore, the solution generally advised by the literature is to centralize only the least sensitive areas.

Second generation fiscal federalism adds that there is a political failure at the EU level, which would justify keeping this policy at the national level: the incentive to free-ride, as some countries could choose to benefit from the spending of other countries, without spending themselves (Persson, Rolland and Tabellini, 1996). However, the authors conclude that the best solution is still to further integrate the policies, while being careful to prevent this problem.

I now move on to the analysis based on legitimacy. Concerning normative justifiability, defence and foreign policies are related with the objective of achieving an area of peace and security in Europe. However, "peace" was originally understood mostly as internal peace – avoiding wars and conflicts between Member States. Moreover, this was to be achieved

through the integration of economic interests. Therefore, if we take the narrow definition of this objective, a common foreign policy is not justified.

If we take a wider definition of this objective, we can conclude that there is legitimacy in harmonizing foreign policy and defence policy, at least in the areas that are most related with achieving a climate of peace and stability in Europe. For example, external policies that contribute towards fighting international terrorism can potentially have a great direct impact on the security of EU citizens. On the contrary, general foreign policy and diplomatic relations with other countries is only indirectly related with security within the EU, and there is therefore less justification for action at EU level.

In what concerns public opinion, the "subsidiarity question" in the Eurobarometer shows a very wide support for "defence and foreign affairs" at EU level: 64%. This may be due to a perception that, due to the relatively small size of EU countries, joining efforts will make EU countries safer and more powerful in the international scale (economies of scale).

Concerning accountability, defence is an area where, even at national level, decisions are often taken out of the public eye and/or without following public opinion. This is due to the need for confidentiality regarding some public safety information, and to reasons of diplomacy and relations between countries, which often lead governments to ignore the public opinion. Therefore this is an area where the government has a large amount of leeway in its decisions. While citizens accept a lower level of accountability in this policy area at the national level, it is likely that they would find it less acceptable at the EU level.

The analysis based on legitimacy therefore adds to the analysis based on fiscal federalism the conclusion that there should be greater centralisation at EU level of the aspects of foreign and defence policy that are most directly related with ensuring security within the EU, and where problems of accountability are lower. This should be combined with the conclusion from first and second generation fiscal federalism, that the areas where heterogeneity of foreign policy does not cause a problem should be centralised to benefit from economies of scale. This implies that the Member States should centralise at EU level the areas where they have similar approaches, especially to deal with concrete security problems.

Education and Research

The literature on traditional fiscal federalism is divided. Some authors defend that these policies should be at EU level, due to the existence of economies of scale, as Member States can pool their research capacities and human capital, and avoid the duplication of research (Hoeller et al, 1996). On the contrary, others argue that these policies should remain at the national level due to heterogeneity, as EU countries have very different approaches in their educational systems (Alesina et al, 2001).

Concerning second generation fiscal federalism, Persson, Rolland and Tabellini (1996) argue that, since educational systems are inefficient and badly organised in European countries, harmonization, by increasing the competition between the countries, could increase efficiency. Moreover, several aspects of policies can help tackle another EU-wide market failure: the insufficient mobility of the workers between EU countries. Programmes such as the existing Erasmus (which finances university students who want to spend one year of their studies in another Member State) are particularly useful in this respect.

This paper argues that it is necessary to differentiate between primary and secondary education on the one hand, and university education and research on the other hand. The former should, according to fiscal federalism principles, remain national, as it does not involve significant economies of scale or externalities but does involve large heterogeneity. The latter on the contrary should be at least partly centralised at the EU level, as it involves large economies of scale, and no large heterogeneity problems.

The analysis based on legitimacy strengthens this conclusion. There is very wide support for EU action on “scientific and technologic research”, with 70% of the population thinking that the EU should be active in this field. On the contrary, there is very low support for EU action in "the education system", with only 29% of the population thinking that the EU should have any involvement in this area. This may be due to the fact that people want to keep at the national level the policies that touch them most directly, such as the education system, while at the same time they support to transfer to the EU level policies where they feel that cooperation between the Member States can lead to more efficient results.

In what concerns normative justifiability, research policy is directly related to the Single Market in two ways. One is that research and development is an integral part of companies' activities, and therefore to have a single market it is necessary to have a regulatory environment that allows EU-wide research. The other is that research at EU level fosters the mobility of researchers, and the mobility of workers is needed for the Single Market. On the contrary, primary and secondary education has no direct relation with the Single Market.

Concerning accountability, if parts of primary and secondary education were to be transferred to the EU level, it is likely that this would lead to people following more attentively the policymaking at EU level, as these are areas that touch people directly. It is therefore likely that accountability would be high.

Concerning research policy, this is an area where governments often delegate part of the decision-making to an independent agency, as decisions on which research to support can be made more efficiently if they are impartial and independent. When that is the case, having an independent agency at EU level or at national level should lead to the same degree of accountability. When that is not case, it is possible that accountability is lower at the EU level, as people typically do not follow how research policy is conducted at the EU level, and there is a risk that this policy could fall prey to vested interests.

In conclusion, concerning primary and secondary education, a legitimacy analysis confirms the conclusions from standard fiscal federalism that these policies should not be centralized. Concerning research, the analysis confirms the case for a degree of centralisation at the EU level, as long accountability of EU level research policies is improved, and the policies are focused mainly on supporting economic integration by allowing companies to undertake cross-border research.

Common Market and External Trade

Fiscal federalism supports the EU deep free trade area, known as Single Market, as unifying the Member States' markets leads to large economies of scale: a bigger market can be considerably more efficient, namely as it makes it possible to benefit from comparative advantage and greater competition between firms. External trade will be considered as part of the same policy field, because having a Single Market requires having a single trade policy.

Second generation fiscal federalism confirms this conclusion: as markets are often over-regulated at the national level, EU level deregulation brings improvements in efficiency.

The definition of normative justifiability used in this paper clearly supports these policies, as they are at the core of economic integration. Unfortunately the Eurobarometer "subsidiarity question" does not include these policies, so there is no measure of their popular support. Accountability is lower at the EU level than if markets remained closed: these areas are complex to understand and not much followed by public scrutiny, and they are areas where the EU, and in particular the Commission, has very wide powers. Nonetheless, it is argued that these problems are small in relation to the large benefits originated by the Single Market, so the best solution is to continue integration in this area while ensuring that accountability problems are minimized.

Competition Policy

Traditional fiscal federalism makes a very strong case for competition policy at EU level. Given the existence of a Single Market, the externalities caused by different competition policies would be very large; a single market requires a single competition policy. Moreover, heterogeneity is low, as there is a growing consensus regarding the optimal type of competition policy. Second generation fiscal federalism finds that the risks of regulatory capture are similar at EU and at national level.

From the point of view of normative justifiability, competition policy directly supports the Single Market, which itself is clearly supported by the definition of normative justifiability used in this paper. Public support for competition policy at EU level is considerably high at 54%. In what concerns accountability, competition policy is one of the most transparent policies at EU level, as the Commission follows pre-determined rules and is required to explain all its decisions based on those rules.

Social Security, Employment, Taxation and Health

Traditional fiscal federalism would argue in favour of centralising redistribution policies due to externalities – different levels of social security could lead to individuals moving to where the tax system is most favourable leading to distortions and harmful tax competition. However, this problem is not very relevant in the EU, as mobility is very low. Moreover, the problem of heterogeneity is so large that it is best to keep those policies at a national level.

Second generation fiscal federalism also advises to keep those policies at the national level, since under the current political system in the EU it would be difficult to have centralised decision-making on this issue, as all funding at EU level is subject to negotiations whereby each country focuses on getting back as much funding as possible from the EU.

Social policy is not directly related to either the Single Market or ensuring peace and security in Europe. This excludes only the aspects of social security that are related to the mobility of workers, such as social security arrangements for mobile population regarding the possibility to transfer pensions from one country to the other, for example.

Moreover, public opinion is very largely opposed to transferring welfare policies to the EU level. According to the Eurobarometer survey, only 27% of the population support having some aspects of health and social policies at EU level. The estimate falls to 25% for taxation

policies, 23% for policies regarding pensions. This may reflect a wish to retain control over policies that touch citizens most directly. It may also be related to the fact that citizens are generally not comfortable with the thought of transferring too much of their tax money to the EU level.

As in the case of education, it is suggested that accountability would be high at EU level, as these areas are well-followed by citizens, since they touch people's daily lives; but on the other hand, these are areas where a very high level of accountability is demanded, and even more if they were at EU level.

The analysis based on legitimacy therefore strengthens the case for keeping these policies at the national level, except when they are directly related to the cross-border mobility of workers.

Cohesion policy

Cohesion policy, which consists of transfers to the poorer regions of the EU to help them catch up with the rest of the Union, must by definition be done at the EU level, so the question addressed by fiscal federalism is not at what level this policy should be done, but how much, if any, of the EU resources should be dedicated to it.

Traditional fiscal federalism generally justifies cohesion policy as being necessary for the Single Market. Therefore, since the Single Market is justified by fiscal federalism. However, cohesion policy should also be seen as meeting an EU-wide equity goal: that of allowing poorer countries to catch up with the average, so that all Member States attain the same level of prosperity.

Insofar as cohesion policy is seen as a necessary condition for the successful Single Market, it would have normative justifiability; that is not the case for the solidarity goal. Public opinion is divided, with 57% supporting the existence of an EU cohesion policy. In great part this reflects the fact that some countries receive funding, while others are net payers. This shows that Europeans do not feel much solidarity towards citizens of other Member States.

Therefore a legitimacy analysis completes standard fiscal federalism analysis with the conclusion that cohesion policy is more legitimate if it is directly focused towards improving the Single Market.

Environment policy

Traditional fiscal federalism defends the centralization of environment policies, due to the existence of large negative externalities among the Member States. These externalities are constituted not only of environmental effects themselves but also of distortions to the single Market caused by different environmental standards. However, there is large heterogeneity in the preferences towards levels of environment protection (for example, while in some EU countries the environment is one of the main concerns of the population, in others it is seen as a more secondary issue).

There is a very high level of public support for environmental policies at EU level, at 64%. This is possibly due to a perception that environment is an international issue as pollution doesn't stop at the borders. Concerning accountability, environment is an area of

policymaking that is generally understood by people and followed by the media, so it is likely that the same would happen at EU level. Concerning normative justifiability, environment policies are related to the Single Market only insofar as they relate to environmental regulations that, if they would be different, could hamper the Single Market. For example, harmonization at EU level on the types of chemicals allowed in products is justifiable under this definition, but regulations on protection of animal species are not.

The legitimacy analysis therefore completes the standard analysis by suggesting that environmental policies should only be transferred to the EU level if they are directly related to the Single Market.

Agriculture

Traditional fiscal federalism advises that these policies should be kept at the national level as there is no case for centralizing them: there are no externalities or economies of scale involved, and on the contrary there is a large heterogeneity problem, as preferences on how to sustain the countryside vary widely among countries. Second generation fiscal federalism adds that there is a significant case of political failure involved in EU-level agricultural policy, as it has been captured by vested interests – offering a further reason to keep these policies at the national level.

EU policies on agriculture are not normatively justifiable; the Single Market would only justify regulatory policies such as those used for goods and services, but not the extensive programme of funding and supporting of agriculture that is currently in place at EU level. Public opinion is mixed at 49% – this could reflect the fact that some countries benefit from funding while others are net payers. Accountability is clearly a problem at EU level, as the policy has been captured by lobbies. In this case the legitimacy analysis confirms the clear conclusion of the fiscal federalism that there is no case for funding of agriculture at EU level.

Home Affairs

The term “justice, liberty and freedom” is used at EU level to cover policies relating to the safety of citizens, immigration and the justice system. Traditional fiscal federalism says that, due to the opening of the borders between the Member States, several safety issues now have such large externalities between countries that they have become effectively common to all Member States (they have become “EU public goods”). Examples are international crime, immigration and protection of the common borders of the EU. Those policies should therefore be centralised.

On the contrary, there is no case for centralizing the policies that only impact on the national or local level, such as most elements of the justice system – they have by definition no externalities with other countries and there would be large heterogeneity problems.

Concerning normative justifiability, the opening of the borders between the Member States is related to the movement of workers, which itself can be seen as part of the Single Market. These issues could also be seen as related to the objective of peace within the EU territory. Therefore they derive their legitimacy from both sources.

Concerning public opinion, the Eurobarometer poll does not include a question relating to home affairs in general, and instead asks about individual policies: fighting terrorism, fighting

crime and immigration. Public opinion is very supportive of policies to fight terrorism at the EU level, at 79%. This is most probably due to a perception that this problem can only be tackled effectively at an international level. Support is lower but still positive for fighting crime (59%) and immigration (57%).

Concerning accountability, these policies are among the most publicised at the EU level, as the Commission is aware of the fact that they include some of its most popular activities. Therefore there is a certain level of awareness of EU activities in this field, which makes them more accountable. However, this does not apply to all the aspects of the policies.

CONCLUSION

The combination of fiscal federalism with an analysis based on the concept of legitimacy has given several new insights, which complete the conclusions from standard fiscal federalism. In particular, it has shown why certain policies where fiscal federalism makes a strong case for centralisation at EU level have largely been kept national.

For example, research policy is an area where fiscal federalism strongly advocates centralisation, due to large potential economies of scale. However, the legitimacy analysis shows that the centralisation of those policies could lead to countries no longer being able to promote their national research in the fields where they do not have a comparative advantage. This would pose a problem for the legitimacy of the policies, given that citizens are generally concerned about promoting national research. Moreover, research is only linked to the core objectives of the EU (as defined in this paper) insofar as it relates to allowing companies to undertake R&D freely throughout the EU.

Another example is foreign policy, and particularly defence policy. This is an area where it would be efficient to centralise policies, due to large economies of scale. However, a legitimacy analysis helps to explain why this policy has remained at the national level: under this paper's definition of normative justifiability, foreign policy is only indirectly related to the goals of the EU.

This analysis has also given insights on what makes some areas legitimate at EU level as opposed to others. In particular, it has shown that legitimacy is lower if the policy involves transferring large amounts of money to the EU level. There are a number of reasons for this: firstly, public opinion is opposed to a large amount of tax money going outside the country; secondly, funding at EU level is more at risk of capture by lobbies (as can be seen in the case of agriculture); thirdly, the most important policies for the good functioning of the Single Market are regulatory as opposed to relying on funding. This could explain why the EU budget remains relatively small despite the growing powers of the EU on the regulatory front. It can also be concluded that, when a policy is transferred to the EU level, the EU should be given more powers on the regulatory aspects and less on the funding aspects. Legitimacy is also lower if the policy touches people directly. Examples are education or health policies; public opinion is widely opposed to their transfer to the EU level.

Fiscal federalism has so far amalgamated issues related to legitimacy with its condition of heterogeneity. However, the two concepts are very different: heterogeneity reflects differences in tastes and traditions which make it difficult to implement the policy in practice and to satisfy everyone; this is different from whether it is legitimate to give up national sovereignty in a certain area or not. For example, in the case of research policy, heterogeneity

is not a problem (because the Member States undertake similar types of research) but legitimacy is a problem (because people are keen on having successful research at the national level, and research is an essential part of a country's economic activity).

This paper has also offered a way to operationalise the concept of legitimacy, as to include it in an economic analysis. This was done by identifying, in the political science literature, three concepts that make it possible to apply, in a relatively objective way, this very subjective concept.

The literature on fiscal federalism has so far not taken centre stage in the debate on the Future of the EU. This is partly due to the fact that these theories had so far appeared to be out of touch with the reality of the EU, as they ignored political considerations. It is argued that the "European version" of fiscal federalism proposed in this paper can contribute towards bridging the gap between the academic work and the policy debate on the EU competences.

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