6 Functional, overlapping and competing jurisdictions (FOCJ): a complement and alternative to today’s federalism

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I. Introduction
Traditional types of federalism and decentralization exhibit many important advantages over centralization, but they also face some serious problems. In this contribution we develop a new concept of functional federalism which exploits the advantages of decentralization, but which at the same time avoids the inherent problems. Our concept, called FOCJ as the acronym of functional, overlapping and competing jurisdictions, is well suited to improve policies in industrial as well as developing countries. This new kind of competitive federalism we put forward may seem radical in various respects, but we shall show that the concept has been successful in the past as well as the present. Thus, we believe that it constitutes an idea worthy of serious consideration. The remainder of this chapter is organized as follows. In the next section we discuss the advantages and problems of traditional federalism. The third section specifies the concept of FOCJ, and discusses its main beneficial effects. The fourth section puts it into theoretical perspective. The fifth section shows that some aspects of FOCJ have existed throughout European history and continue to do so today. Furthermore, the relationship to US special districts and in particular to functional communities in Switzerland is emphasized. While the sixth section discusses how FOCJ can be institutionalized in Europe, the seventh section focuses on the relevance of FOCJ for developing countries. The last section concludes.

II. Advantages and problems of federalism
The economic theory of federalism yields one clear and overriding result: a federal (that is, decentralized) state is superior to a centralized one in the sense that it fulfills the demands of the citizens more effectively. A federal constitution that endows the federal subunits (provinces, Länder, states or cantons as well as municipalities, cities or communities) with sufficient decision making rights and taxing power has three major advantages over a unitary state:

1. More flexible politics In all societies, citizens differ widely in their demand for services provided by the state. These differences in demand are not only the result of heterogeneous tastes due to differences in tradition, culture, language and so on, but also of unequal economic conditions. The latter are caused by, for example, leads or lags in the general business cycle and, of course, special structural conditions such as differences in infrastructure, unemployment, the concentration of particular industries and so on. These differences in the demand for public services must be met by differentiated supply policies if citizens’ preferences are to be fulfilled. Federal subunits are best able to meet this challenge. While the politicians in charge are better endowed with information about the local requirements, they have the incentives to provide these services according to the preferences of the citizens because they are directly accountable for local policy and their re-election depends on the satisfaction of the voters they represent (1). In contrast, centralized states tend to produce unitary policies which are less capable of responding to differences in local demands.

2. More efficient provision of public services The efficiency of the public sector is extremely important due to the very large size of today’s public sector in terms of government expenditure as a share of national income, public servants as a share of the total workforce, the dependence of a substantial portion of the population on income redistributed by government (for example, in the form of subsidies, social security and old-age pensions) and, of course, the many resources that go into tax collection. In federally organized states, efficiency is enhanced by at least three mechanisms. First, individuals and firms which are not satisfied with the balance between the supply and cost of public services may move to jurisdictions where this balance is more favorable. Such exit and entry thus establishes competition among the various local suppliers of public services, giving them a strong incentive to be efficient. The exodity mechanism does not depend on the full mobility of individuals or firms (there are, of course, costs of moving): it suffices if some such mobility is induced (in analogy to the marginal traders leading to equilibrium prices on normal goods markets). Indeed, spatial competition between jurisdictions in a federal system mimics competition among firms for the supply of private goods and services (Tiebout 1956). Second, decentralization enhances efficiency by decreasing the cost of information for the citizens. As the voters can compare politics and policy outcomes in their own jurisdictions with those variables in other jurisdictions, it becomes easier for them to assess the performance of their governments and politicians. Such comparisons lead to ‘yardstick competition’ among local governments (see Salmon 1987, and Ch. 2 in this volume; Besley and Case 1995) which enables the incentives of the governments to cater for the preferences of
the citizens. Third, there is not only horizontal competition among governments of the same level, but also vertical competition among governments of different levels which fortifies the governments' incentives to provide their services efficiently (Breton 1996, and Ch. 3 in this volume).

3. More innovation In a federal system, innovations in the supply of public goods or taxation can be implemented first in those local units where the conditions are ideal for success. Moreover, a particular local unit finds it less risky to undertake innovations in the supply of public goods or taxation because the effects are limited and can be observed and controlled. If the innovation is unsuccessful, not much is lost. However, if it proves to be successful, it will be quickly adopted by other jurisdictions and eventually the entire nation. For this Hayekian process to take place, the innovators must reap at least some of the benefits. This is much more the case when the innovation starts from a clearly defined local jurisdiction where the success (or failure) can be clearly attributed to the respective politicians and governments.

In spite of these heavy advantages, federalism is not an ideal system. However, there is no ideal system. Following the well-established ‘comparative analysis of institutions’, it is fruitless to judge any existing system or a new proposal by comparing it with a theoretical optimum. Rather, a comparison must be made with actual systems existing in reality. In the case of federalism, it is appropriate to compare it with a centralized state. From this point of view, it has often been argued that a federal constitution is faced with four major problems:

1. Spillover effects Spatial positive and negative externalities produce systematic distortions in the allocation of publicly supplied goods and services. ‘Fiscal equivalence’ (Olson 1969; Oates 1972) is not secured: some benefits of local public supply go to citizens of other jurisdictions who have not paid the corresponding tax cost (which induces under-supply); some costs are carried by citizens outside a particular jurisdiction (which induces oversupply). This cause for the distorted allocation of public services cannot be neglected. In reality, it can often be observed that such spillovers are substantial and part of the fiscal crises of cities can be attributed to this factor. As an example, the cultural institutions (for example, the opera house) whose costs are carried by the local taxpayers but whose benefits are enjoyed by many people living and paying taxes outside the city. Acknowledging that such positive and negative spillovers may be serious under many circumstances, we hereby propose a solution: the size of the jurisdiction should correspond to the ‘geography of the problems’.

2. Smallness In traditional federalism, jurisdictions are often too small to exploit economies of scale. Think, for example, of nuclear power plants or universities, which normally require heavy capital investments for a local jurisdiction (city, communities) to run efficiently. In our proposal for a new federalism, we are trying to confront the problem directly. We envisage flexible (functional) jurisdictions which are able to adjust to the lowest cost size.

3. Need for coordination It is often claimed that federalism makes cooperation difficult or impossible. However, this is only part of the real problem. In federal states, cooperation among the various national subunits emerges endogenously because it is obviously advantageous for all actors concerned. Moreover, it should be noted that coordination problems also exist within unitary states, in particular among the various national ministries whose competencies and interests overlap. Thus, a unitary state is neither a necessary nor sufficient condition for effective cooperation.

4. Redistribution of income This argument says that when a local unit tries to tax the rich in order to support the poor, the rich will leave and the poor will enter. The redistribution policy therefore cannot be maintained in a federalist state, but is only feasible in a unitary state. This argument has some truth in it. However, empirical evidence shows that federalist structures admit a substantial amount of income redistribution (see, for example, Gold 1991; Ashworth et al. 2002). One example is Switzerland where the (partly very small) 26 cantons together with about 3000 communities levy more than 80 per cent of total income and capital taxes. Although each canton is free to set its own tax schedule, all cantons rely on progressive taxes and engage heavily in income redistribution (see Kirchhöfer and Pommerhunte 1996; Feld 2000). Moreover, quite a large amount of redistribution exists between rich and poor cantons. Nevertheless, the problem of redistribution in a decentralized governmental system has to be taken seriously. In our proposal for a new kind of federalism, we argue that this is one of the functions for which the national state is sometimes an appropriate jurisdiction.

III. FOCJ: beyond traditional federalism

The federal units proposed here are named FOCJ due to their four essential characteristics: they are

- functional (F), that is, the new political units extend over areas defined by the tasks to be fulfilled;
- overlapping (O), that is, in line with the many different tasks (functions), there are corresponding governmental units extending over different geographical areas;
• competing (C), that is, individuals and/or communities may choose to which governmental unit they want to belong, and they have political rights to express their preferences directly via initiatives and referenda; and
• jurisdictions (J), that is, the units established are governmental, they have enforcement power and can, in particular, levy taxes.

These functional, overlapping, and competing jurisdictions form a federal system of governments that is not dictated from above, but emerges from below as a response to citizens’ preferences. For this to become reality, a fifth freedom has to be enacted, which in some ways is the political counterpart to the four well-known economic freedoms as established by the European Union. It simply has to permit the formation and continued existence of FOCI. Such a fifth freedom requires a constitutional decision (see, for example, Frey 1983; Mueller 1996) which ensures that the emergence of FOCI is not blocked by existing jurisdictions such as direct competitors or higher-level governments. In the European Union, this would mean that every citizen and community would have the right to directly appeal to the European Court if barriers to the competition between governments are established. A European Union directive must be enacted to give the lowest political units (communities) a measure of independence so that they can engage in forming FOCI. The citizens must be given the right to establish FOCI by popular referenda, and political entrepreneurs must be supported and controlled by the institution of popular initiatives. The FOCI themselves must have the right to levy taxes to finance the public services they provide.

The concept of FOCI is based on theoretical propositions advanced in the economic theory of federalism. It nevertheless leads to a governmental system that is completely different from the one suggested in that literature. While the economic theory of federalism (see Oates 1991), or the various contributions on federalism in the Fall 1997 issue of the Journal of Economic Perspectives analyses the behavior of given political units at the different levels of government, FOCI emerge in response to the ‘geography of problems’.  

FOCI with their four main elements are now compared with existing federal institutions and theoretical concepts, pointing out both similarities and differences and the beneficial effects of FOCI.

The main characteristics

Functions A particular public service which only benefits a certain geographical area should be financed by the people living in this area, that is, there should be no spillovers. Under this rule, the different political units can cater for differences in the populations’ preferences or, more precisely, to their demands. To minimize cost, these units have to exploit economies of scale in production. As these may strongly differ between functions (for example, between schools, police, hospitals, power plants and defence) there is an additional reason for single-function (or linked-function) governmental units of different sizes. While this idea is central to ‘fiscal equivalence’ as proposed by Olson (1969) and Oates (1972), the endogeneity of the size of governmental units constitutes an essential part of FOCI. Moreover, fiscal equivalence theory has been little concerned with decision making within functional units. The supply process is either left unspecified or it is assumed that the mobility of persons (and of firms, a fact rarely mentioned) automatically induces these units to cater for individual preferences. This criticism also applies to a closely related concept of fiscal federalism, namely ‘voting with one’s feet’ (Tiebout 1956). This preference-revealing mechanism makes comparatively efficient suppliers grow in size, and the others shrink. According to this model of federalism, the political jurisdictions are exogenously given, are multipurpose, and do not overlap, while the political supply process is left unspecified. In contrast, we emphasize the need to explicitly study the political supply process. In line with Apple and Zelenitz (1981), exit and entry is considered insufficient to eliminate rent extraction by governments. Individuals must have the possibility of ‘raising voice’ in the form of voting. Buchanan’s ‘clubs’ (see Buchanan 1965; Sandler and Tschirhart 1989) are similar to FOCI because their size is determined endogenously by club members’ benefits and costs.

Overlap FOCI may overlap in two respects: (i) two or more FOCI catering for the same function may geographically intersect (for example, a multitude of schools: FOCI may exist in the same geographical area); (ii) FOCI catering for different functions may overlap. The two types of overlap may coexist; however, a constitutional decision can be taken to restrict FOCI of specific functions to the second type because this alleviates free-riding problems (see also Vanberg 2000). An individual or a political community normally belongs to various FOCI at the same time, FOCI need not be physically contiguous, and they need not have a monopoly over a certain area of land. In this respect the concept of FOCI is similar to Buchanan-type clubs which may intersect, but it differs completely from archaic nationalism with its fighting over pieces of land. It also breaks with the notion of federalist theory that units at the same level may not overlap.

Competition In FOCI, two mechanisms guarantee that empowered politicians conform closely to their members’ preferences: while the possibility for individuals and communities to exit mimics market competition (Hirschman 1970), their right to vote establishes political competition (see Mueller 2003). It should be noted that migration is only one means of exit. Often, membership in a particular FOCUS (we define a FOCUS to be the singular of FOCI)
can be discontinued without changing one's location. Exit is not restricted to individuals or firms, as said before, political communities as a whole, or parts of them may also exercise this option. Moreover, exit may be total or only partial. In the latter case, an individual or community only participates in a restricted set of FOCUS activities. This enlarged set of exit options makes 'voting with one's feet' a real constraint for politicians.

'Secession', that is, exit of jurisdictions such as states or regions, has been recognized in the literature as an effective mechanism for restricting the power of central states (for example, Zarkovic Bookman 1992; Drize 1993; Backhaus and Doering 2004). Secession has been suggested as an important ingredient for a future European constitution (Buchanan 1991; European Constitutional Group 1993). The right to secede stands in stark contrast to the prevailing concepts of nation states and federations where this is strictly forbidden and often prevented by force, as is illustrated, for example, by the American Civil War, 1861–65, by the Swiss Sondertuntskrieg 1847, or more recently by the wars in Katanga (1960–63), Biafra (1967–70), Bangladesh (1970–71), and in the past decade in the former Yugoslavia.

For FOCUS to establish competition between governments, exit should be as unrestrained as possible. In contrast, entry need not necessarily be free. As for individuals in Buchanan-type clubs, jurisdictions may be asked to pay a price if they want to join a particular FOCUS and benefit from its public goods. The existing member of the particular FOCUS have to democratically decide on the entry prices. ‘Free’ mobility in the sense of a disregard for the cost imposed on others is overcome by internalizing the external cost of movement. In addition, FOCUS do not have to restrict entry by administrative and legal means such as zoning laws. Explicit, openly declared entry fees substitute for implicit restrictions resulting in high land prices and hoarding rents. The commonly raised concern that pricing could be exploitative and mobility strongly curtailed is unwarranted as FOCUS are subject to competitive pressure. Moreover, the possibility of imposing an explicit entry fee gives incentives to FOCUS governments to cater for the preferences not only of actual, but also of prospective members.

However, the exit option does not suffice to induce governments to act efficiently. Thus, competition needs to be enhanced by political institutions. The citizens should directly elect the persons managing the FOCUS, and should be given the right to initiate popular referenda on specific issues. These democratic institutions are known to raise efficiency in the sense of fulfilling individual preferences (for elections, see Downs 1957 and Mueller 2003; for referenda, see Frey 1994; Frey and Stutzer 2001; Feld and Kirchgässner 2001 and Feld and Matsusaka 2003).

Jurisdiction A FOCUS is a democratic governmental unit with authority over its citizens, including the power to tax. According to the two types of overlap, two forms of membership can be distinguished. First, the lowest political unit (normally the community) is a member, and all corresponding citizens automatically become citizens of the FOCUS to which their community belongs. In that case, an individual can only exit via mobility. Second, individuals may freely choose whether they want to belong to a particular FOCUS, but while they are its citizen, they are subject to its authority. Such FOCUS may be non-voluntary in the sense that one must belong to a FOCUS providing for a certain function, for example, to a school FOCUS, and must pay the corresponding taxes (an analogy here is health insurance which in many countries is obligatory but where individuals are allowed to choose an insurance company). The citizens of such a school FOCUS may then decide that everyone must pay taxes in order to finance a particular school, irrespective of whether one has children. With respect to FOCUS providing functions with significant redistributive effects, a minimal amount of regulation by the central government may be in order so that, for example, citizens without children do not join ‘school FOCUS’ which in effect do not offer any schooling but have correspondingly low (or zero) taxes. In this respect, Buchanan-type clubs differ from FOCUS, because they are always voluntary while membership in a FOCUS can be obligatory.

FOCUS as jurisdictions provide particular services but do not necessarily produce them themselves if contracting out to a public or private enterprise is advantageous. It is noteworthy that present-day outsourcing by communities does not automatically lead to FOCUS. The former is restricted to production, while FOCUS typically concentrate on provision and are democratically controlled. FOCUS also differ from existing functional and overlapping institutions such as the various kinds of specific administration unions (or Zweckverbände as they are aptly called in German-speaking countries). These institutions normally do not have the legal status of governments but are purely administrative units. The same applies to the many types of corporations which usually have no power to tax but have to rely on charges.

Beneficial effects of FOCUS
Due to its four essential characteristics, FOCUS compare favourably to traditional forms of federalism. One aspect concerns the governments' incentives and ability to satisfy heterogeneous preferences of individuals. As a consequence of the concentration on one functional area, the citizens of a particular FOCUS have better information on its activity, and are in a better position to compare its performance with that of other governments. As many benefits and costs extend over a quite limited geographic area, we envisage FOCUS to be often small which is also helpful for voters' evaluations. The exit option opened by the existence of overlapping jurisdictions is not only an important
means to make one’s preferences known to governmental suppliers but it also strengthens the citizens’ incentives to be informed about politics (see Eichenberger and Senna 1996).

On the other hand, FOCI are able to provide public services at low cost because they are formed in order to minimize interjurisdictional spillovers and to exploit economies of scale. When the benefits of a specific activity indivisibly extend over large areas, and there are decreasing costs, the corresponding optimal FOCUS may cover many communities, several nations, or even Europe as a whole. An example may be defence against outward aggression where the appropriate FOCUS may most likely extend over the whole of Europe (even beyond the European Union). That such adjustment to efficient size is indeed undertaken in reality is shown by the Swiss experience. Communities decided by referendum whether they wanted to join the new Canton of Jura established in 1978, and in 1993 communities in the Laufental opted to belong to the Canton of Basel-Land instead of Berne. Communities also frequently change districts (the federal level below cantons) by referendum vote, which suggests that voters perceive the new size of jurisdictions and the new bundle of services to be more efficient. The same holds for American special districts.

The specialization in one or a few functions further contributes to cost efficiency due to the advantages of specialization. As FOCI levy their own taxes to finance their activity, it pays to be economical. In contrast, in API (all-purpose jurisdictions) financed from outside lacking such fiscal equivalence, politicians have an incentive to lobby for ever-increasing funds, thereby pushing up government expenditures. The incentive to economize in a FOCUS induces its managers to contract out whenever production cost can thereby be reduced. While FOCI are more market oriented than API, they reduce the size of the public sector. However, they differ from today’s one-shot privatization, which usually does not impact on the government’s basic incentives and thus is often reversed by re-regulation and de-privatization. In contrast, in a system of FOCI privatization emerges endogenously and is sustainable, as the politicians’ incentives are fundamentally changed.

The threat of dissatisfied citizens or communities exiting the FOCUS, and the benefit of new citizens and communities joining, gives an incentive to take individual preferences into account and to provide public services efficiently. Quite another advantage of FOCI is that they open up the politicians’ cartel (classe politique) to functionally competent outsiders. While in API people with broad and non-specialized knowledge tend to become politicians, in FOCI those with a well-grounded knowledge in a particular functional area (for example, education or refuse collection) are successful.

FOCI not only make it possible for the citizens to change from one supplier to another, but they also increase the mobility of politicians. In transborder

FOCI, politicians will be allowed to supply their services in several countries. This is in stark contrast to current regulations, which prevent politicians from doing so. In FOCI, it is also more likely than in traditional territorial units that foreigners and institutional providers are allowed to enter the political market (on the favourable effects of open markets for politics, see Eichenberger and Frey 2002; Eichenberger 2003). While many people reject the idea of allowing policy consulting firms and foreigners to run directly for office in general-purpose units, they are quite favorable to the idea when it is applied to the politics of FOCI. Examples are FOCI that concentrate on the supply of fresh water and sewage systems, which could be governed by international firms specializing in water resource management.

The right to form FOCI helps to address issues raised by fundamentalist sentiments. Political movements focused on a single issue (for example, ethnicity, religion, environment and so on) are not forced to take over governments in toto but can concentrate on those functions they are really interested in. An ethnic group need not disassociate itself from the state they live in as a whole but may establish FOCI which cater for their particular preferences. South Tyroleans, for example, unhappy with the language domination imposed by the Italian state, need not leave Italy in order to have their demands for cultural autonomy fulfilled, but may establish corresponding FOCI. Such partial exit (for example, only with respect to ethnic issues) does not lead to trade barriers often following the establishment of newly formed all-purpose political jurisdictions. FOCI thus meet the criterion of market preserving federalism (see Qian and Weingast 1997).

A federal web composed of FOCI undoubtedly affects the role of nation states. They will certainly lose functions they presently do not fulfil according to the population’s preferences, or which they produce at higher cost than FOCI designed to exploit cost advantages. On the other hand, the scheme does not purport to do away with nations but allows for multinational as well as small-scale alternatives where they are desired by the citizens. Nation states subsist in so far as they provide functions efficiently according to the voters’ preferences.

IV. FOCI in perspective

Our proposal is purely process oriented. It is neither necessary nor possible to determine at the European and at the national levels all the functions which should be provided by FOCI and how these entities should be organized. The internal organization of a particular FOCUS lies solely in the competence of the communities and individuals who decide to establish such a jurisdiction. Nevertheless, it is possible to specify the conditions for FOCI to emerge and to fulfil their tasks effectively. Thus, our approach follows the logic of constitutional economics, which aims to design beneficial decision
processes without closely defining the outcomes (Buchanan and Tullock 1962; Mueller 1996).

One condition is crucial for FOCI to work properly: economic and political competition must be guaranteed. Thus, economic markets in FOCI have to be open; in particular, the four freedoms referring to the free movement of goods, services, and capital, and the free mobility of individuals have to be secured. At the same time, the political markets of FOCI have to be competitive, that is, human rights and fundamental democratic rights have to be guaranteed. This includes the right for citizens to make use of the instruments of direct democracy.

Not only traditional governments, but also the governing bodies of FOCI, pursue their own interests and tend to undermine competition and to build cartels or even monopolies. Therefore, the rules have to be monitored by a 'competition supervisory board'. This body also has to fix rules for determining the ceiling on entry and exit fees. If they are too high, mobility is hampered. However, such prices for mobility prove effective in preventing individuals from exploiting the redistributive policies in FOCI. Regulative measures may also be necessary to enable FOCI to supply public services effectively (see also Vanberg 2000), as has been discussed above for the case of school FOCI. In such cases, it may be advantageous to declare membership in a FOCUS to be obligatory, and to fix minimum service levels. The competition supervisory board must be given the competencies to step in if such regulations are violated. This board has to be empowered in a constitutional decision at the national (or, even better, international) level. However, it would be a mistake to delegate the monitoring of competition among FOCI to the national bureaucracies which are interested in restricting FOCI. Rather, an independent agency seems appropriate. A possible solution could be a constitutional court (in the European Union, the European Court of Justice). Even though such institutions tend to favour national at the expense of regional and local interests, their decisions tend to be less biased than those of national political institutions.

In light of the stiff resistance functional jurisdictions will meet, they can emerge successfully only if two conditions are met:

1. To establish and to operate FOCI must be a constitutionally guaranteed right—the 'fifth freedom', as we would like to call it. The newly founded political units must be allowed to operate as jurisdictions with (restricted) enforcement rights. The power to tax in order to finance a clearly specified service is the key to efficiency. However, this right of FOCI will be disputed by other political units with which FOCI will compete for the same tax base.

   Principally, the communities (as the lowest level political units) as well

   as individuals should be allowed to form FOCI. However, depending upon the function to be fulfilled, membership may be restricted to the former. It is, for example, highly possible that individuals form a FOCUS which provides a special type of schooling; for other services, especially for those with stronger public good appeal, for example, waste water treatment or local police, communities or parts of them are the 'natural' agent. It is important to note that the decision to which of these two classes a function belongs can be left to the local level itself. This decision should not be transferred to the European level.

2. Existing political units may not hinder the formation of FOCI. Most importantly, the higher-level political units have to appropriately reduce the taxes of those citizens who become members of a FOCUS or of various FOCI providing governmental services. The competition supervisory board has to force the existing units to openly declare the cost, that is, the tax prices of the various services they provide. These 'tax price lists' can then serve to fairly rebalance the tax rate of the citizens who receive services from newly emerging FOCI instead of from traditional political units. The existing governments' tendency to underrate the cost in order to minimize tax reductions to FOCI members can be broken simply by demanding that the tax prices for a specific service serve not only to compensate exiting citizens, but also to tax former and newly entering service recipients. This rule makes the market for politics contestable. The potential existence of FOCI is enough to compel all levels of government to give an account of the real cost of their services. However, it need not be said that existing political units will use all possible measures to impede the new competitors. Thus, the competition supervisory board does not have an easy job. Again, the constitutional court seems to be the appropriate institution to undertake this task. It could rely on the competencies of the audit office (or the court of accounts or Rechnungshof) to control the calculations of the tax prices. This latter institution has the necessary knowledge which has so far been wasted, as audit offices are typically only allowed to formulate non-binding recommendations which are most often ignored by the political decision makers.

V. FOCI in the future and in the past

Future opportunities

There is a wide range of functional issues to which FOCI could profitably be applied. A practical example is the policing of Lake Constance (which borders on two German Länder, two Swiss cantons and one Austrian Land) which involves the regulation of traffic, environmental protection, the suppression of criminal activities and the prevention of accidents. Formally, the various local
police departments are not allowed to directly collaborate with one another, not even to exchange information. Rather, they must advise the police ministries of the Länder and cantons, which then have to notify the respective central governments which then interact with one another. Obviously, such a formal procedure is in most cases vastly inefficient and unnecessarily time consuming. In actual fact, the problems are dealt with by direct contact among the local police commissioners and officers. However, this is outside the law and depends, to a substantial extent, on purely personal relationships (which may be good or bad). A FOCUS committed to policing the lake would allow a pragmatic, problem-oriented approach within the law—and would, moreover, be in the best spirit of Europe.

FOCJ are not restricted to such small-scale functional issues but are relevant for all levels of government and major issues. An example would be Alsace which, while remaining a part of France in other respects, might partially exit by joining, say, the German social security or school system (with German as the main language), or might join a university FOCUS involving the Swiss University of Basle and the German universities of Freiburg and Karlsruhe. Actually, the first steps for establishing such a university FOCUS are under way. But these efforts contrast with the idea of regions as set out in the Maastricht Treaty (or elsewhere), not least because one of the participants (the University of Basle) is not part of the European Union. Another example refers to Corsica which according to Drize’s (1993) suggestion should form an independent region of Europe because of its dissatisfaction with France. However, most likely the Corsicans are only partially dissatisfied with France. This suggests that one or several FOCUS provide a better solution in this case; they may, for example, especially focus on ethnic or language boundaries or on Corsica’s economic problems as an island. This would make it possible for the Corsicans to exit France only partially instead of totally. Quite generally, tourism and transport issues, in particular railroads, are important areas for FOCUS. It should be noted that, despite the membership of various countries in the (then) European Community, railroad policy was not coordinated to exploit possible economies of scale; a FOCUS may constitute an appropriate organization to overcome such shortcomings.

Contemporary and historical forerunners
The original European Community started out as a FOCUS designed to establish free trade in Europe, and was from the very beginning in competition with other trade areas, in particular North America, Japan and the European Free Trade Association (EFTA). Due to its economic success, it has attracted almost all European countries. But entry has not been free, the nations determined to enter had to pay a price. They have (with partial exceptions) to accept the acquis communautaire as well as to pay their share to the Union’s outlays which to a large extent serve redistributive purposes. In several respects these exist FOCUS-like units within Europe with respect to law enforcement, education, environment, transport, culture or sports, though they have been prevented from becoming autonomous jurisdictions with taxing power.

Most of these functional units are not contiguous with the area of the European Union. Some are smaller (for example, those organized along ethnic or language functions), and some are larger. Several East European countries and Switzerland, which are not EU members, are certainly fully involved in, for example, European culture, education or crime. FOCUS of the nature understood in this chapter may therefore build upon already existing structures, and are in the best of European traditions.

There are two countries in which functional, overlapping and competing jurisdictions exist, that is, the United States and Switzerland (though they do not in all cases meet the full requirements of FOCUS specified above).

United States Single-purpose governments in the form of ‘special districts’ play a significant role in the American federalist system (ACIR 1982, 1987; Foster 1996; Nuun and Schoedel 1997). Their number has increased considerably, between 1967 and 1972 by 30.4 per cent, and between 1972 and 1984 by 19.7 per cent, in both cases more quickly than other types of jurisdiction (Zax 1988). There are both autonomous and democratically organized as well as dependent special districts (for example, for fire prevention or recreation and parks). Empirical research suggests that the former type is significantly more efficient (Mehay 1984). In contrast to all-purpose jurisdictions, functionally specialized units are able to exploit economies of scale. While, in school districts, increasing size leads to lower cost of production, in all-purpose communities there is no size effect as they fulfill many functions with decreasing economies of scale, and their citizens lose control over politicians (Zax 1989).

Our theoretical hypothesis of the opposition of existing jurisdictions to the formation of special districts is well borne out. In order not to threaten the monopoly power of existing municipality statutes, 18 states prohibit new municipalities within a specified distance from existing municipalities (ACIR 1982, Zax 1988); in various states there is a minimum population size required, and various other administrative restrictions have been introduced (see, for example, Nelson 1990). Empirical studies reveal that these barriers imposed by local agency formation commissions (LAFCOs) tend to reduce the relative efficiency of the local administration (Di Lorenzo 1981; Deno and Mehay 1985), and tend to push the local government expenditures upwards in those municipalities which have introduced LAFCOs (Martin and Wagner 1978).
Many Swiss cantons have a structure of overlapping and competing functional jurisdictions which share many features of FOCl. In the canton of Zurich (with a population of 1.2 million), there are 171 geographical communities which in themselves are composed of three to six independently managed, direct democratically organized communities devoted to specific functions and levying their own taxes on personal income: in addition to general-purpose communities, there are communities that exclusively provide for elementary schools and others specializing in junior high schools, and there are the communities of three different churches. All these governmental units have widely differing rates of income taxes. Moreover, there are a vast number of "civil communities" (Zivilgemeinden) providing water, electricity, TV antennas and so on, which are "direct-democratic" but finance themselves by user charges. These communities often overlap with neighbouring political communities. In addition there are 174 functional units (Zweckverbände), whose members are not individual citizens but communities. These Zweckverbände are responsible, for example, for waste water and purification plants, cemeteries, hospitals and regional planning. The Zurich canton is not the only Swiss canton with various types of functional communities. A similar structure exists, for example, in the Glarus or Thurgau cantons (for the latter, see Casella and Frey 1992). Various efforts have been made to suppress this diversity of functional communities, usually initiated by the cantonal bureaucracy and politicians. However, most of these attempts were thwarted because the population is largely satisfied with the public supply provided. The example of Switzerland—which is generally considered to be a well-organized and -administered country—demonstrates that a multiplicity of functional jurisdictions under democratic control is not a theorist's wishful thinking but has worked well in reality.

Decentralized, overlapping political units have also been an important feature of European history. The competition between jurisdictions in the Holy Roman Empire of German Nations, especially in today's Italy and Germany, was intensive. Many of these jurisdictions were small. Many scholars attribute the rise of Europe to this diversity and competition of governmental units which fostered technical, economic and artistic innovation (see, for example, Hayek 1960; Jones 1981; Weede 1993; and Baumol and Baumol 1994, who also give a lively account of how the musical genius of Wolfgang Amadeus Mozart benefited from this system of government). While the Chinese were more advanced in many very respects, their superiority ended with the establishment of a centralized Chinese Empire (Rosenberg and Birdzell 1986; Pak 1995). The unification of Italy and Germany in the nineteenth century, which has often been praised as a major advance, partially ended this stimulating competition between governments and led to deadly struggles between nation states. Some smaller states escaped unification; Liechtenstein, Luxembourg, Monaco, San Marino and Switzerland stayed politically independent, and at the same time grew rich.

The above-mentioned governmental units were not FOCl in the sense outlined in this contribution but they shared the characteristic of competing among themselves for labour and capital (including artistic capital). However, history also reveals examples of jurisdictions close to FOCl, most importantly in multicultural and plural societies (Coakley 2003; Kyriacou 2004). For instance, the problems connected with Poland's strong ethnic and religious diversity (Catholics, Protestants and Jews) were at least partly overcome by jurisdictions organized according to these features, and not on geographical lines (see, for example, Rhode 1960; Haarmann 1991). The highly successful Hanse prospered from the twelfth to the sixteenth century, and comprised among others Lübeck, Bremen, Köln (today Germany), Stettin and Danzig (today Poland), Kaliningrad (today Russia), Riga, Reval and Dorpat (today Baltic republics) and Groningen and Deventer (today the Netherlands); furthermore, London (England), Bruges and Antwerp (today Belgium) and Novgorod (today Russia) were Hansekomore or associated members. It was clearly a functional governmental unit providing for trade rules and facilities and was not geographically contiguous.

VI. FOCl and Europe
In its present form, EU enlargement solves some old problems, but also creates many new ones. With progressing enlargement, the economic and institutional disparities grow among the member countries, as well as between the existing members and the new neighboring countries at the shifting outer borders. The envisaged integration of Turkey, for instance, would make Georgia, Armenia, Iran, Iraq and Syria neighbors of the EU.

For several reasons, it will prove impossible to fully integrate all the present neighboring countries and, a fortiori, the new neighbors, without changing the whole concept and institutions of the EU:

1. Decreasing potential for full integration. The increasing economic and institutional gap at the outer borders makes it unlikely that border countries can, in due time, meet the formal requirements regulating the entry into the EU, which stipulate that acceding states must have a stable democracy and a functioning market economy, follow the rule of law, observe appropriate standards of human rights and protect minorities, and most importantly must agree to the obligations of EU membership which include adherence to the aims of political and economic union. This means that they have to fully accept the "acquis communautaire." This legal corpus of the EU has now reached a considerable size, involving more than 16,000 pages of text.
The concept of FOCI suggests a totally different approach. Countries which want to be integrated more closely with the EU should have the option of forming FOCI with some or all EU member states. Thus, they would get the possibility of partial entry rather than the all-or-nothing decision to accept the whole acquis communautaire in one go. These FOCI should not be imposed from above, but should emerge as the result of the voluntary negotiations between the new partners. To the extent that the partially integrated countries develop (partly as a result of the existence of these flexible partnerships), an increasing number of such FOCI with different members and functions will arise so that an even closer integration can take place. With FOCI, variable geometry is a desirable feature of integration rather than a shortcoming. It goes far beyond the proposal for a multispeed integration of some 'chosen' countries into a 'core Europe' (as recently proposed by the former German foreign minister Joachim Fischer), or the special cases of the treaties of Schengen and of the Economic and Monetary Union (EMU), which not all EU member countries need to join.

Flexible widening and deepening

FOCI allow for differentiated, tailor-made integration. Thus, they are in stark contrast with the acquis communautaire, which stands for equalized integration. With FOCI, countries and regions can establish cooperation in those matters in which it is really important that they cooperate, and they are not forced into cooperation with respect to those matters where they would rather act alone. However, for three reasons FOCI do not lead to less integration than the acquis communautaire. First, FOCI decrease the price of integration for the citizens and thus increase the demand for integration, as they make integration more efficient and enhance citizens' democratic influence. Second, thanks to FOCI, integration of partner countries is no longer a question of 'all or nothing'. The countries which are not able to quickly incorporate the acquis communautaire can be integrated better with FOCI than without. Third, a FOCUS may aim at stronger integration with respect to its specific function than the acquis.

Of course, differentiated integration is not a totally new concept. Today's standard procedure of integration of new member countries also entails some differentiation, as the countries are granted different adaptation periods. These, however, are only looked at as temporary exceptions and unwelcome deviations from the current acquis. They neither allow for stronger integration with respect to certain functions, nor do they give the new entrants the right to search for different degrees of integration with a special selection of today's members. Partial integration has also been institutionalized in the European Economic Area (EEA) with Norway, Iceland, and Liechtenstein, or with Switzerland via bilateral treaties. However, the concept of FOCI goes for
beyond a partial integration via treaties. It provides for a common government composed of all the members. The extended rights of political co-determination strengthen identification and provide the basis for solidarity among the members.

**Multilevel integration**

Transborder FOCI can emerge at all levels of government. With respect to European integration, three kinds of FOCI may be identified:

1. **FOCI formed by all the EU member and some non-member states** The EU and its neighbors have a common interest in fighting transnational mafia-type activities. Today, this problem is approached in a purely technocratic way via EUROPOL and INTERPOL, often with very limited success. A police FOCUS comprising the affected nations would bring about a more efficient anti-mafia policy because governance and taxation would be matched. The FOCUS would make it possible to deploy police resources in the areas where they could most effectively be used. In contrast, the EU does not have any joint police forces, not even for special purposes. Such a police FOCUS would thus go beyond the integration now existing in the EU.

2. **FOCI formed by some EU member and non-member states** An example is the reciprocal acceptance of technical norms for goods and services. With present arrangements, trade between the EU member and non-member states is severely hindered, as the norms differ and the countries do not accept each other's norms—that is, the 'Cassis de Dijon' principle is only valid within the EU. However, it is impossible to apply this important principle to non-EU members, as there are always some member countries in which some influential special-interest groups stand to lose from freer trade, and thus object to liberalizing trade. Under the regime suggested here, those members of the EU could partially integrate their economies with selected neighboring countries by establishing a joint FOCUS for the reciprocal acceptance of norms. Such a FOCUS would most probably not only represent a treaty stipulating the reciprocal acceptance of norms, but it would also have an institutional structure, which guarantees that the norms of the EU partner countries satisfy some reasonable standards and that the norms are followed by the producers. Thus, such a FOCUS would be an institution which comes close to a special government for the setting, controlling and reciprocal acceptance of norms. This allows all the FOCUS members to exploit their international comparative advantage, and thus to experience a welfare gain, even if full integration according to the *aquis communautaire* is impossible.

3. **FOCI formed by communities and regions of some EU member and non-member states** This is a new form of cross-border cooperation. A pertinent example refers to local environmental degradation, say water pollution. One or several communities of, for example, Finland, Estonia, and Russia, may form an environmental FOCUS. The government of the FOCUS would be elected by the citizens of all the communities involved. The FOCUS would be responsible for water quality in the area, would set the standards best meeting the preferences of all the citizens and would impose the taxes necessary to reach these goals. The Russian communities can therewith adopt an environmental standard higher than that generally obtained in the rest of their nation. Such an institutional arrangement is also advantageous for the respective Finnish and Estonian communities because of the negative spillovers connected with Russian emissions.

Obviously, FOCI not only facilitate the integration of new countries, but they also make it possible for the current members to flexibly deepen integration. Therefore, the general rules of full integration into the EU can be relaxed to some extent, as the countries that want to integrate more closely have an effective institutional tool for doing so (which differs sharply from existing instruments such as the regions as envisaged in the INTERREG programmes, see, for example, European Commission 2001; Jensen and Richardson 2001).

**Meeting the challenges**

By making use of the concept of FOCI, the three main challenges faced when enlarging the EU can be successfully addressed.

1. **Outer-border problems** The use of FOCI allows a differentiated expansion of the EU instead of an abrupt rupture when it comes to non-EU countries. This can be achieved in two ways: first, a country which is not yet able to accept the *aquis*, would nevertheless be able to enter the EU partially, that is, with respect to only some functions. Thus, integration of potential member countries is accelerated and facilitated. Such partial enlargement will have much further-reaching geographical implications than the all-or-nothing approach. Second, the institutional development of partially integrated countries will be accelerated. EU transborder FOCI are ideal vehicles for the transfer of democratic culture to neighboring countries, as their citizens come in contact with, and become accustomed to, well-functioning democratic institutions.

2. **Income redistribution** FOCI reduce the number of problems connected with redistribution by two means. First, the demand for receiving subsidies by current members of the EU will be reduced because with FOCI it is feasible to cooperate mainly with respect to those functions which yield
particularly high benefits of cooperation. The applicant countries are not forced to compromise on functions from which they do not profit much, or even lose, when accepting the *acquis communautaire*. Therefore they need less compensation.

Second, it is likely that the full entry of some or all neighbouring countries will be blocked by those members which would lose from a new targeting of redistributive flows. With FOCIJ, instead, particular neighbouring countries and the EU could establish a redistribution FOCUS acceptable to all existing EU members.

3. EU decision making structure and democracy deficit The existing EU members which do not agree with the partial admission of one or several neighbouring countries can opt out instead of having to use their veto power. Thus, the current decision-making mechanisms in the EU need not be changed. However, FOCIJ can help to overcome the democracy deficit of the EU because they are based on effective democratic principles.

VII. FOCIJ and developing countries

The concept of FOCIJ is not only suited for industrial countries. It can also be fruitfully applied to developing countries whose problems are mainly due to inadequate institutions.

**Too much and too little government**

Economic growth in many developing countries is hampered by excessive government. The state tends to interfere in, and minutely regulate, almost all activities. The government sector, which is often very large, employs a high proportion of the population outside agriculture. The administration tends to be more bureaucratic than in industrial countries. Rent-seeking distortions are rampant and waste is pervasive. This combination of interventionism and bureaucracy stifles investment and innovation in the private sector, making over-government a reality.

At the same time, however, many governments do not adequately fulfil the functions necessary for rapid economic growth. Most importantly, property rights are only insufficiently secured. Investors are faced with a high degree of uncertainty and are, therefore, reluctant to commit themselves to long-term investments. Instead of concentrating on productive endeavours, investors devote their resources to finding substitutes for the deficient property rights.

But governments in developing countries are also inadequate in a second, quite different sense. They are far from meeting the wishes of the citizens; many are either strongly paternalistic or even dictatorial. While the preferences of the city dwellers — in particular of the capital — are at least taken into account in so far as to avoid an uprising, the preferences of the peasantry are almost totally disregarded. While some Third World countries are officially federal, central governments regularly neglect local problems and demands. Often, it even actively destroys well-working production and distribution arrangements, in particular in self-governing units.

Thus, developing countries are faced with a paradoxical situation: at the same time there is 'over-government' (that is, interventionism), and 'under-government' (that is, too little consideration for fragmented local problems). The concept of FOCIJ can overcome this unproductive situation as it allows for a large number of jurisdictions that are based on grassroots local democracy to check government and prevent it from evolving into an oppressive and intervening bureaucracy. Of course, the concept of FOCIJ deviates strongly from existing development plans. It is worth observing that a large part of the economic literature on development does not address the government structure. The failures of government are duly noted but no remedies are proposed. To just hope that the future will bring 'better politicians' is unfounded optimism. Government will only improve if the underlying institutional conditions are changed. This is exactly what FOCIJ do. These jurisdictions are formed according to the geography of problems, that is, by the citizens seeking to cope with issues with which they are confronted.

The local power to impose taxes as an essential ingredient to FOCIJ will also prove decisive for developing countries. Whenever the central government allocates funds (as it is the rule in today's federal developing countries) the lower-level units become dependent on it and have biased incentives so that most of the advantages of decentralization are lost. Under these circumstances, decentralization is not necessarily beneficial. In a system with important central allocations, the lower-level units are liable to become fiscally irresponsible. They tend to borrow too much on the (normally correct) assumption that they will be bailed out by the central government if they run into trouble. In contrast, if FOCIJ have the power to levy their own taxes, the population would have to carry the cost of bad politics, therefore, governments have an incentive to observe the budget constraint and to behave fiscally responsibly.

**Benefits of FOCIJ for developing countries**

FCOIJ produce major advantages over the existing form of government in developing countries:

1. They break the central government’s effort to monopolize politics which would otherwise stifle economic development and oppress the citizens.

FCOIJ shift the power to initiatives from below. Effective, local governments become viable because they have authority over particular government functions, and may raise taxes to finance the respective expenditures.
2. FOCJ make it possible to combine various forms of political rules. They blend not only federalism with democracy, that is exit and voice, but also modern and traditional styles of governing such as meetings by village elders. Time-proven local ways of public decision making are not eliminated, but are used and fostered in those areas in which they prove to be effective.

3. FOCJ solve the 'fundamental organizational dilemma' between an open polity and decentralized development at the local level: 'one of the necessary (though far from sufficient) conditions of a development state is a large degree of insulation that the development-minded decision makers can have against the ravages of short-run pork barrel politics and their inability to use the discipline of the market ... against the inevitable follies of group predation' (Bardhan 1993, p. 46). Indeed, FOCJ provide such insulation by the establishment of new, growth-oriented development units which are, however, disciplined by economic and political competition.

4. FOCJ deal with another ‘fundamental dilemma of government’ (Montignola et al. 1995, pp. 54–5). The state has to be strong enough to enforce legal rules, especially property rights which are prerequisites for economic development. At the same time, government institutions have to be ‘weak’ in the sense of not exploiting the citizens by, for example, expropriation or excessive taxation. FOCJ are able to convey credible limits against such exploitation because each FOCUS is self-financed and may go bankrupt if its members choose the exit option. In a system of FOCJ, individuals and firms do not face a monopolistic and therefore oppressive state but may resort to substitutes.

5. There is an emphasis on local public production and efficient polycentric organization. This aspect has been much neglected in the literature.

6. The fiscal decentralization induced by FOCJ reduces the volatility in macro-economic variables (for instance, in budget deficits and income growth).

7. The concept of FOCJ overcomes the fruitless contradiction of 'government versus market' which was typical of many of the writings on developing countries. FOCJ mark a radical departure from much of the earlier literature on developing countries that emphasized the need for a strong, well-organized central state and bureaucracy to steer and support economic growth. They depart from the more recent exclusive emphasis on private property and free market as the key to successful development. In both cases local governments needed for economic growth are neglected.

Arguments against FOCJ in developing countries
Some people consider the claim that FOCJ are also advantageous to developing countries too optimistic and naively neglect the specific conditions reigning there. The following three related assertions are discussed below:

1. FOCJ will not work in developing countries which are neither federalistic nor democratic The pre-colonial political system in most developing countries was characterized by various forms of self-government, though they, of course, did not meet the criteria of democracy with which we are familiar. Vestiges remain even today, but this traditional way of governing was on the whole destroyed by the authoritarian colonial rule. Post-colonial governments wanted to centralize as much power as possible in their hands, and consequently destroyed traditional local rule.

2. FOCJ are unsuitable for developing countries This 'culturalist position' maintains that individuals in developing regions are basically different from Westerners and, therefore, need a different form of government, arguably a more authoritarian one. A popular version of this belief is that people in developing countries lack the discipline and initiative to form FOCJ. However, the economic approach to human behaviour suggests the opposite causation. The lack of observed discipline and initiative is the consequence, and not the cause, of unfavourable institutional settings.

Three types of empirical observations strongly support the economic view: (i) Empirical evidence shows that to the extent self-government could be preserved, it often functions well and is even able to solve difficult common property resource problems (Wade 1988; Ostrom 1990; Ostrom et al. 1993). (ii) When individuals in developing countries rely on the rest sub limits imposed upon them by government bureaucracies, they become active and venturesome. While this applies to all developing countries, it has been particularly impressively demonstrated for Peru by de Soto (1989), who shows that people who are passive within the confines of the highly regulated and imbalanced official sector become enterprising and energetic once they act in the unofficial or shadow economy. (iii) Even experiences with an extreme form of democracy, popular referenda, are positive provided they are devoted to substantive issues and not simply plebiscites to support the authoritarian or dictatorial rules (Rourke et al. 1992). If citizens in developing countries are taken seriously, they participate in political affairs (for Africa, for example, Chazan 1994; for Mexico, see Opperweier and Welland 1994).

3. FOCJ worsen inequality Many people believe that central governments promote inequality while federal systems make the rich richer and the poor poorer. Central governments are at best formally committed to an 'equal' provision of public services but in actual fact, there are huge differences in the services provided across the country - Ostrom et al. (1993, p. 211) even speak of a myth of equality'. Typically the population in the capital is grossly favoured, in particular by highly subsidized food, while the much poorer inhabitants in the rural areas are taxed. FOCJ
redress such imbalances because they are based on decentralized decision-making and subsequently allow regional and local development of the natural and human resources to be made available.

VIII. Conclusions
Our concept of functional, overlapping and competing jurisdictions provides a radical alternative to today’s policy in industrial and developing countries. However, the idea of FOCI is not driven by any particular ideology (except for the normative position that politics should function according to the citizens’ preferences), and it does not suggest perfect, simple or ready-made solutions. Nor does it require an all-or-nothing decision. It may sometimes appear surprising and perhaps even shocking, but it may be introduced on a step-by-step basis. The beneficial features of the concept already become evident even when it is only applied with regard to some functions and a few members. This does not mean that FOCI emerge all by themselves. Even if political competition works well to the advantage of citizens, established politicians who see their power reduced will make an effort to block or at least undermine the concept. It is, therefore, necessary to openly and seriously discuss the proposal in order to make the advantages generally known and accepted by the population. In democratic societies the citizens then have the means to make FOCI become a reality by rewriting the constitutions such that FOCI may emerge.

Notes
1. It could be argued that locally elected politicians in central states also face incentives to cater to the local preferences. However, in many countries, the members of the national parliament are only partly, or not at all, elected in local districts. In the federal Republic of Germany, for instance, a substantial share of the members of the Bundestag are not elected by winning a particular precinct but because they are placed on a list which is controlled by the party they belong to. Moreover, in national parliament, a local delegate’s accountability is low as he/she is only one of several hundred parliamentarians.
2. The concept of FOCI is extensively discussed in Frey and Eichenberger (1999). Similar ideas have already been found in Montagnoli (1974), Burstein (1985) and Wehner (1992).
3. According to Stashen (1994, p. 24), in the first half of the nineteenth century, average income was higher in strongly decentralized Germany than in strongly centralized France, which may at least partly be attributed to the difference in the degree of centralization.
4. See Cameron (1998); Dehousse (1998); Laurent and Moret (1998); Wagner and Heiko (1998).

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Functional, overlapping and competing jurisdictions


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