Society, State, and Public Finance: Setting the Analytical Stage

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The essays that comprise this *Handbook* cover a wide variety of topics in the theory of public finance. As a field of systematic academic inquiry, public finance arose before economics or political economy. For instance, more than 90 chairs in public finance had been established in Europe before the first chair was established in political economy (Backhaus 2002, p. 615). The first scholars of public finance were the Cameralists, who emerged in central Europe in the 16th century. For a long time after its Cameralist founding, public finance was conceived as a multi-disciplinary field of study, and most certainly not simply a subset of economic theory. The object that public finance scholarship examined, the public household, was examined in a manner that sought to integrate the economic, political, legal, and administrative elements of public finance.

In the post-war period, a splintering of approaches has taken place, sufficiently so that it is meaningful to distinguish between the old public finance and the new, recognizing that new is not a synonym for better. The old public finance has not been replaced by the new. Both are practiced currently, and are competing for the affection and attention of scholars. If the old-style public finance is still called public finance, the new style is often called public economics instead. This distinction is found in contemporary texts and journals. For instance, there is a *Journal of Public Finance and Public Choice* and a *Public Finance Review*. There is also a *Journal of Public Economics* and a *Journal of Public Economic Theory*.

The distinction between what might be called old-style and new-style public finance was recognized clearly in Richard Goode's (1970) commentary on the theory of public finance. There, Goode compared the treatment of public finance in two different social science encyclopedias, written a generation apart. One of these was the *International Encyclopedia of the Social Sciences*, which was published in 1968. The other was the *Encyclopedia of the Social Sciences*, which had been published in 1930. While Goode duly noted the theoretical advances that had occurred in economics between 1930 and 1968, he also lamented the narrowing of the subject matter of public finance. Goode concluded his lamentation on the state of public finance by asserting that "a sophisticated and unified treatment of the economic, political, legal, and administrative elements of public finance is needed. Unification would represent a return to a tradition as old as that of the cameralists, but for modern readers sophistication can be attained only by rethinking old problems and using new techniques. There is much to be done and work for a variety of talents" (p. 34).

The difference that Goode noted maps nicely into the distinction we have advanced between an old-style public finance and a new-style, noting again that old and new refer simply to the times when those approaches arose and represent no judgment about relative merit or quality. As we do not embrace a Whig theory of history, we do not regard the new style of public finance as *ipso facto* superior to the old style. Indeed, there is much about the old-style that we regard as superior to the new. The essays in this *Handbook* generally affirm the orientation toward public finance that informed both Goode's appraisal and his assessment about the potential value of scholarly inquiry that sought more fully to integrate the economic, social, political, legal, and administrative aspects of public finance.

This opening essay is *not* a survey of the historical development of fiscal theory. It would take a very large book indeed to accomplish this. Our intention here is simply to provide some elementary historical orientation toward the two styles of public finance. We do this by referring to two main theoretical antinomies that run throughout the history of public finance, and to do so with reference to a few of the main historical contributors to the theory of public finance.

The first antinomy we explore is between conceptualizing the state as *intervening into* the economic order and the state as *participating within* the economic order. To do this we return briefly to consider the Cameralist origins of the theory of public finance, and to contrast the Cameralist approach with that of their classical British contemporaries, particularly Adam Smith. The second antinomy is between treating the state as some maximizing agent and treating the state as an institutional framework within which myriad individual agents interact. The primary historical figures who represent this second antinomy are the British economist Francis Edgeworth (1897) and the Swedish economist Knut Wicksell (1896). For Edgeworth, public finance was a choice-theoretic enterprise, with the policy choices of a state being assimilated to the market choices of an individual. In sharp contrast, Wicksell treated public finance as a catallactic enterprise, where the state provided an institutional framework within which individuals with differing values and preferences interacted. The extent to which those interactions proved generally beneficial to everyone, as against providing gains to some and losses to others, depended on the institutional framework within which political participants interacted with one another.

These two antinomies can in principle generate a four-fold description of analytical possibilities. A model of an interventionist state can in principle be developed within either a choice-theoretic or a catallactic framework. Similarly, a model of a participative state can be developed within either a choice-theoretic or a catallactic framework. For the most part, however, the interventionist state has been assimilated to a choice-theoretic framework, and with the participative state being assimilated to a catallactic framework. In the remainder of this opening essay, we will first illustrate the intervention-participation antinomy as it is found in the formulations of the Cameralists and the British Classicals. Then we use Edgeworth and Wicksell to illustrate the antinomy between the choice-theoretic and the catallactical approaches to public finance. We close this essay by briefly describing the essays that comprise this *Handbook*.

**The Cameralist Origins of Public Finance**

The cameralists emerged around 1500, and were mostly located in the German-speaking lands. By the time they had disappeared by the middle of the 19th century, they had amassed a collective bibliography of more than 14,000 items, according to Magdalene Humpert (1937). Joseph Schumpeter (1954, pp. 143-208) described the cameralists well when he referred to them as “Consultant

Administrators." They were both consultants and administrators. They were consultants to the various kings, princes, and other royal personages who ruled throughout those lands. Indeed, the term cameralist derives from camera or kammer, and refers to the room or chamber where the councellors to the king or prince gathered to do their work. The cameralists were not, however, anything like contemporary academic consultants. They were real-world administrators as well. They were engaged in such activities as managing mines and glass works. Many of the cameralists also held academic posts. The first chairs of cameral science were established in 1727, in Halle and Frankfurt on the Oder, and by the end of the 18th century 23 such chairs had been established (Backhaus 1993). The cameralists were partly economists, partly political scientists, partly public administrators, and partly lawyers. They approached their subject matter in a manner that used all of these talents and capacities.

The Peace of Westphalia in 1648 recognized more than 300 independent units of governance within the cameralist lands. Cameralism arose under conditions of high political fragmentation. A cameralist land faced different circumstances than the contemporaneous mercantist regimes. There was no concern within the cameralist lands about influencing terms of trade, about the use of colonies as instruments of policy, and about one's relative standing among the preponderant powers. All of these concerns were foreclosed by circumstance to those who ruled within the cameralist lands. The focal point of cameralist concern was on survival of the regime. Survival, in turn, required a military capacity. It also required economic development, which in turn required the acquisition of advanced technologies, the improvement of human capital within the population, the creation of new enterprises, and the growth of population with a view to creating human capital.

This concern about development took place within regimes that were both absolutist and severely constrained. The prince was the ruler of his lands. He did not have to worry about surviving periodic elections, and he could hope to pass his principality along to his eldest son. His ability to do this, however, varied directly with the extent of economic progress within his land. A prince whose land was supporting a growing population of energetic and enterprising subjects would both be wealthier and face better survival prospects than a prince of a land where the population was stagnant or declining, and whose subjects were dull and lethargic or else departing the country.

If one were to construct a model of the cameralist vision of the state, it would resemble a model of a business firm. The state's lands were potential sources of revenue. Forests could be harvested, game could be caught, and mines could be built and worked. The ruler would also sponsor an assortment of commercial enterprises, including such things as the operation of a glassworks or a brewery. Taxes occupied a secondary position as a source of revenue. They were a last resort option for public finance, and not the first source of revenue.

The cameralists' general predisposition against taxation as an instrument of public finance reflects an orientation that the state acts as a participant within the economic order. Individuals had their property and the state had its property. The state should be able to use its property to generate the revenues required to finance its activities. Or at least those enterprise revenues should support the major portion of state activity. Some of the cameralists argued that taxes should be earmarked for the support of the military, while all activities concerned with internal development should be financed from the prince's net commercial revenues. In any case, the state's enterprises were to be the primary source of revenue for the state. It was understood that the state would have significant expenses associated with its activities. These expenses, however, were not to become drains upon the private means of subjects. They were to be met from the lands and enterprises that constituted the state's property.

It is instructive to compare the approach to taxation taken by Johann Heinrich Gottlob von Justi (1771) and Adam Smith (1776), particularly with respect to the limits placed on the use of the power to tax. Smith, of course, is one of the premier figures of classical liberalism, and it is hardly surprising that his maxims of taxation are widely thought to serve as strong limits on the power to tax. Smith's four maxims of taxation have been stated repeatedly in public finance texts since he first articulated them in 1776. These are:

(1) Taxes should be levied in proportion to property.

(2) Taxes should be certain and not arbitrary.

(3) A tax should be convenient to pay.

(4) A tax should be economical to administer, for both the taxpayer and the state.

Justi (1771, pp. 549-65) similarly articulates maxims for taxation, though these maxims, unlike Smith's, have not been carried forward in the public finance literature. Justi's maxims actually go beyond Smith in limiting the power to tax. In addition to the limits articulated by Smith, Justi's maxims for taxation included requirements that taxes should never cause taxpayers to reduce their capital, harm their welfare, or violate their civil liberties.

While Justi placed even stronger limits on the power to tax than did Smith, even more notable is the sharp difference they accorded to taxation within the overall scheme of public finance. Smith regarded taxation as the primary source of public financing, and thought ideally that it should be the sole source of public finance. For instance, Smith preceded his presentation of tax maxims with an argument that the state should eliminate its property and the revenues derived therefrom. In sharp contrast, Justi preceded his discussion of tax maxims with a discussion of why taxation should be a last resort or secondary means of public finance. Indeed, Justi argued that ideally the state would not tax at all, and would derive all of its revenues from its enterprises. In sharp contrast, Smith argued that ideally the state would own no enterprises, and would derive all of its revenue from taxation.

This difference between Justi and Smith reflects one of the important orienting principles of the cameralists, namely, that the state acts as one participant among many within the society and its economic order. The cameralist advice on the use of state budgets and other policy instruments to promote the happiness of the state and its subjects took place within a presumption that the state itself was located inside the economic order and not outside it. Civil society and the state are nonseparable and co-emergent, and the state participates within the economy on the same terms as all other participants. The state finances its activities through market activities just as everyone else does; it acts within the market economy. By contrast, for Smith the state intervenes into civil society and its processes. Everyone else in society acts within the market, and the state then intervenes into the market by taxing various results of market activity.

Geoffrey Brennan and James Buchanan (1980) construe the state as a revenue-maximizing beast, a leviathan. While the leviathan of the Bible lived in the sea, it is easy enough to imagine it as living on the land. Smith's maxims for taxation are a recipe for living with the leviathan by doing such things as clipping the beast's nails and filing its teeth. A beast it will always be, and the objective of tax maxims should be to limit the damage the beast causes. Justi's maxims for about the primacy of enterprise revenues and taxation as a last resort measure represent a contrary intellectual orientation that would seek to domesticate the beast. Whether it is actually possible, or the extent to which it is possible to domesticate the beast is a different matter that has occupied a good number of scholars, fiscal and otherwise.

Cameralistic public finance was a choice-theoretic approach to public finance. The phenomena of public finance, state revenues and expenditures, arise out of a ruler's optimizing choices. It is quite different in modern democratic regimes. The phenomena of public finance do not arise from someone's optimizing choice, but rather arise through interaction among the many participants within the fiscal process. This interactive or catallactic approach to public finance leads often to quite different implications for public finance than the choice-theoretic approach (Wagner 1997, 2002). The dominant portion of contemporary public finance has maintained the choice-theoretic orientation toward public finance, as if fiscal phenomena are still generated through the same processes that were in place in mercantalistic and cameralistic times. This astonishing situation was noted in 1896 by Knut Wicksell (1958, p. 82), when he complained that the theory of public finance "seems to have retained the assumptions of its infancy, in the seventeenth and eighteenth centuries, when absolute power ruled almost all Europe."

**From Cameralist Origins to Contemporary Public Finance**

Cameralist public finance ended early in the 19th century, giving way to its closely related analytical cousin, Staatswissenschaften. Perhaps the best known treatise in the tradition of Staatswissenschaften is Adolf Wagner's (1883) two volume set. The contemporary relevance of this analytical tradition is probed, moreover, in a symposium that appeared in the September 2001 issue of the *European Journal of Law and Economics*. The tradition of staatswissenschaften fits clearly within the framework of the older style of public finance, as does the more widely known contribution of Knut Wicksell. The primary fault line that divides the older style from the newer style is the same fault line that Wicksell articulated, and concerns the political setting within which theorizing about public finance occurs. The newer-style public finance treats the political setting as one of old-style absolutisms where fiscal phenomena can be assimilated to some ruler’s maximizing or optimizing choices. This is the type of public finance to which Wicksell objected more than a century ago. The older style public finance, in its contemporary incarnation, deals seriously with Wicksell’s objection, by developing an interactive or catallactical approach to public finance. For contemporary times, the seminal articulation of the choice-theoretic orientation can be attributed to the British economist Francis Edgeworth (1897), while the seminal articulation of the catallactic orientation can be attributed to the Swedish economist Knut Wicksell (1896).

Cameralist public finance was choice-theoretic, in that it addressed the fiscal choices of some ruler. The cameralist regimes were autocratic. Fiscal programs were the choices of a ruler. It is reasonable to assimilate a theory of cameralist public finance to a model of the optimizing choices of a business firm. Indeed, the prince as a firm was a central part of the cameralist analytical framework. Edgeworthian public finance is likewise choice theoretic, only the ruler to which the formulations are addressed is some fictional being, at various times characterized as a social welfare function or a benevolent despot. Wicksellian public finance is catallactic and not choice-theoretic in its orientation toward fiscal phenomena. It also construes the state as one participant among many within the economic processes and activities of a society. In this construction of the state as a participant, the Wicksellian tradition contrasts markedly with the Edgeworthian tradition and its focus on the state as intervening into the economic process.

**The Edgeworthian, Choice-Theoretic Tradition.** This tradition treats public finance as the study of government intervention into the economy, typically to maximize some notion of social welfare. Edgeworth raised the question of how a government would impose taxes within a nation if it wanted to raise those taxes with a minimum amount of sacrifice to taxpayers. For a given amount of revenue to be raised, Edgeworth's ideal state would be one that imposed the least amount of sacrifice upon taxpayers in raising its revenue.

Taxes would reduce the disposable income of taxpayers, and the sacrifice that would be involved would depend on the utility that the taxpayer derived from that sacrificed income, in Edgeworth's utilitarian formulation. With taxpayer sacrifice being measured by lost utility, the total amount of sacrifices created by a particular level of taxation required an ability to sum sacrifices across taxpayers. If it is presumed that the relation between income and the utility provided by that income is identical for all taxpayers, and if it is further presumed that the marginal utility of income declines with income, a simple system of taxation arises, as a first approximation. The least sacrifice of utility comes from the highest income in society. Hence, taxation should take away the highest income first, if it is to minimize the total amount of sacrifice from taxation. What results is a tax that pares down incomes from the top until the required amount of revenue is raised.

To be sure, Edgeworth himself noted that this was only a first approximation, because the effort to impose such a punitive, 100 percent marginal rate of tax on high incomes would eliminate the incentive to earn those incomes, which in turn would make other people worse off. This insight was later formalized in what has become known as the theory of optimal taxation, inspired by Frank Ramsey (1927) and surveyed in James Mirrlees (1994). This theory fits within the Edgeworthian, choice-theoretic tradition, in that it construes the state as facing its own problem of utility maximization. In this case, the state is to maximize aggregate social utility, though its ability to do this is constrained by the recognition that high taxes will reduce the willingness of people to earn income. Where Edgeworth would apply a 100 percent rate of tax to the highest dollar of income in a society, the theory of optimal taxation would let that last dollar be free from tax.

Some of the details involved in these formulations will be addressed in some of the later essays. All we would note here is that this Edgeworthian, choice-theoretic approach to public finance treats the phenomena of public finance as arising from the maximizing choices of a benevolent entity, the state. The state stands outside the market economy and its participants. The people who participate in the market economy may write the first draft, so to speak, but it is the state that revises and perfects the manuscript.

**The Wicksellian, Catallactical Tradition.** Where the Edgeworthian, choice theoretic tradition is one where public finance is viewed as the means by which the state intervenes into the market economy to perfect its results, the Wicksellian, catallactical tradition views public finance as the study of how people participate through government to achieve their various ends. The state does not stand above the market economy and its participants. The same people who participate in the market economy participate in state governance as well.

Fiscal phenomena are not the product of some ruler's maximizing choices, but rather emerge through interaction among people. This interaction might be beneficial for everyone or nearly everyone, or it might be beneficial for only a few, and costly for many others. The state is treated as a nexus of contractual and exploitive relationships. The extent to which those relationships are contractual or exploitive depends, as some of the following essays will explore, on the constitutive structure of governance that is in place.

As a matter of general principle, political relationships are both contractual and exploitive. It is fine to say that taxes are the prices we pay for civilization. This doesn't mean, however, that the relationship between citizens and state is the same as the relationship between customers and the retail outlets they frequent. A customer can refuse to buy and, moreover, generally can return merchandise that turns out to be defective or otherwise unsatisfactory. There is no option to do this in politics. To say that civilization is being priced too highly and to withhold payment will only land the protester in prison. And there is certainly no point in asking for a refund by claiming that the state's offerings weren't as good as its advertisements claimed them to be.

To speak of a catallactical approach to public finance is not to claim that the phenomena of public finance arise through voluntary interaction among people. It is only to say that those phenomena arise through interaction among people, the very same people as who interact with one another within the market economy. Much of the phenomena of public finance surely arise through duress and not through genuine agreement. This aspect of duress was given particular stress in a good deal of the Italian scholarship on public finance, and which is surveyed in James Buchanan (1960).

The sometimes sharp differences between the older and newer styles of public finance is revealed in the dueling book reviews that accompanied the publication in 1934 of Antonio De Viti De Marco's treatise, *Principii di Economia Finanziaria*. De Viti's treatise was a major statement of the Italian tradition of public finance, a tradition that arose within an interactive framework. It was reviewed in the August 1934 issue of Economica by Fredric Benham, who asserted that De Viti's book "is probably the best treatise on the theory of public finance ever written." Benham laments that sorry state of public finance in England, which was dominated by the choice-theoretic orientation that Wicksell decried, could be improved greatly through a strong infusion of De Viti's orientation. Benham also noted the strong complementarity between the approaches taken by De Viti and Wicksell.

In sharp contrast, Henry C. Simons reviewed the English translation of De Viti that appeared in 1937, in the October 1937 issue of the *Journal of Political Economy*. Simons began by observing that "the Italian literature of public finance has long been held in high esteem; but its claims to distinction have rested mainly upon works which have been inaccessible to those of us who lacked facility with the language. The translations [both German and English translations were being reviewed by Simons] of De Viti's famous treatise are thus doubly welcome, for they will make possible a more informed consensus, both as to the merits of Italian economics and as to competence of the interpretation and appraisal which it has received in other countries."

After describing this initial sense of eager anticipation, Simons offered his judgment: "Careful reading . . . has left the reviewer with no little resentment toward the critics who induced him to search in this treatise for the profound analysis and penetrating insights which it does not contain. The *Principii* is revealed to him, not as a great book, but as a . . . monument to . . . confusion." Simons continued by asserting that "there is not a single section or chapter which the reviewer could conscientiously recommend to the competent student searching for genuine insights and understanding."

Simons concludes by taking on Benham's review three years earlier: "If his book is 'the best treatise on the theory of public finance ever written,' one hopes that it may be the last. . . . To say that it is distinguished among treatises in its field is to praise it justly and, at the same time, to comment bitterly on the quality of economic thought in one of its important branches. To call it a great book, however, is a disservice to the cause of higher standards and better orientation in economic inquiry."

That two reviewers, each so prominent in his time, can be so opposed in their appraisals can only testify to a sharp clash in the presumed domains of fiscal inquiry. De Viti and Benham shared an orientation toward the domain of public finance that was antagonistic with Simon's orientation. This clash of orientations toward public finance, moreover, took shape in the late 1800s and has been carried forward to this day

Within the Wicksellian, catallactical tradition, primacy of analytical attention is placed upon the institutions of governance, both market governance and, especially, political governance. This contrasts sharply with the Edgeworthian, choice-theoretic tradition where the primary analytical attention is placed upon prices and resource allocations. The essays in this *Handbook* are generally written from within a broadly Wicksellian or catallactical orientation toward public finance. The state is not treated as some exogenous force that perfects and corrects the outcomes of the market economy. The actual fiscal conduct of the state emerges through complex interactions among fiscal and political participants, and the precise character of those interactions is constrained and shaped by a governing institutional and constitutional framework.

**The Present Relevance of Past Formulations**

A choice-theoretic approach to public finance was suitable in cameralist and mercantilist times. A cameralist ruler could reasonably be described as seeking to use his fiscal means to promote his dynastic ends. For the cameralists it was historically accurate to ascribe the phenomena of public finance to the choices of the rulers. The state's revenues depended on the ruler's choices about how to operate his mines and forests and how to farm his lands. The extent to which state expenditures were directed to projects that might increase future productivity were likewise objects of choice for the ruler. Suppose two kingdoms were observed to undertake different expenditure programs. In the first kingdom expenditures were heavily oriented toward such investments as draining swamps and building roads that would be likely to increase future production. The budget in the second kingdom, however, did little about swamps and roads, and instead spent lavishly on amusements for the king and his court. It would be reasonable in this case to compare the budgetary choice of the two kingdoms, and to say that the first king had a lower time preference, or was otherwise more far-sighted than the second king. To the extent it is possible to make inferences about preferences from the observation of choices with respect to private choices, it would be possible to do the same thing with respect to state choices within the cameralist setting. To be sure, the conduct of cameralist rulers was relatively civilized, and nothing like the experience with dictators in the $20^{th}$ century. The conceptual construction of a benevolent despot perhaps finds historical validation in the cameralist period. That does not, however, render empirically valid the use of constructions based on benevolent despots in public finance today.

Whether budgets in a democratic regime are tilted toward amusements or capital projects would not be a source of information about some person's preferences. Budgets emerge out of interactions among participants, and those interactions are governed and shaped by a variety of procedural rules. The people who participate in a market make their various choices, but it makes no sense to speak of the market itself as making choices. The market simply registers and reflects the choices and interactions among the participants. It is the same with budgetary outcomes within a democracy. Furthermore, the same set of people can generate quite different budgetary outcomes, depending on the institutional framework within which the budgetary process proceeds. In this respect, there is an indefinite number of particular budgetary processes that can be imagined, and it is conceivable that a wide variety of budgetary outcomes could be generated, if the experiment were performed of having the same people engage in successive interactions across differing institutional frameworks. This consideration suggests immediately that a post-cameralist public finance would place particular importance and significance on the institutional framework within which fiscal outcomes emerge.

The cameralists were clearly agents for their royal principals. Principals who were unhappy with their cameralist agents would dismiss them, and could well imprison them for malfeasance. Justi, for instance, died while imprisoned for alleged financial mismanagement. While modern democracies are quite different from the cameralist absolutisms, such categories as principal, agent, and property are present now just as they were then. The cameralists spoke of subjects. We now speak of citizens. It is the citizens who are the principals in a democracy. The head of state was the principal in cameralist times, but is now the agent. The same relationship of agency exists in modern democracies as existed in cameralist times, only the substantive character of that relationship is different in many respects.

All agency relationships raise questions of how strongly the agent will promote the desires of the principals. Shopping centers, apartment complexes, and hotels all provide state-like services in a cameralist-like setting (see, for instance, McCallum 1970 and Foldvary 1994). What these organizations do is offer forms of tie-in sales, where private and public services are offered as a package. Apartments and hotels offer rooms to residents. The rental price, however, also finances the provision of an array of public services. Hotels will have subways that run vertically. Hotels usually sweep their streets daily. Hotels and apartment complexes typically provide a variety of parks and playgrounds. Walt Disney World in Florida offers the same kind of arrangement, only it covers 45 square miles of territory. All topics relating to property and agency within the conduct of government would fit naturally within a post-cameralist orientation toward public finance.

From the perspective of today, we would call the cameralists multidisciplinary, with the primary disciplines being economics, politics, law, and public administration. What is the relationship between public finance and these four disciplines? In the choice-theoretic approach to public finance, whose chief turn-of-the-century inspiration would be Edgeworth, public finance would be a proper subset of economics. Just as there is a *Journal of Economic Theory*, so there would be a *Journal of Public Economic Theory* to cover that subset of economic theory that dealt with the state. Public finance would look like economic theory, only it would have a specialized subset of subject matter. In this respect, it would be no different from, say, agricultural economics or housing economics. These are also specialized subsets of economics that are, nonetheless, not anything other than economics. In sharp contrast, a post-cameralist public finance would most surely not be a proper subset of economic theory. Suppose you were to draw a Venn diagram with intersecting circles denoting such fields of study as economics, politics, sociology, public administration, and law. Post-cameralist public finance would cut through all of those fields, and in its own right would be a genuinely multi-disciplinary field of study.

**The Essays to Follow**

The central concern of welfare economics is to explore the relationship between economic welfare and alternative forms for the economic organization of societies. With public finance being the treatment of government within the economic order, the concerns of welfare economics and public finance overlap one another. In Chapter 2, Russell Sobel examines welfare economics in relation to public finance. In particular, Sobel examines the efforts of fiscal scholars to examine the impact of fiscal practices and institutions on efficiency and equity. In the course of this examination, Sobel explores theories of public goods and externality, and considers the impact of government on the distribution of income and wealth.

In their treatment of “Fiscal Constitutionalism” in Chapter 3, Geoffrey Brennan and Giuseppe Eusepi develop a contrast between the constitutional approach to public finance and the orthodox approach. In large measure, this distinction accords pretty well with the distinction between the older and the newer styles of public finance noted above. The orthodox approach to public finance treats fiscal outcomes as reflecting the choices of some benevolent despot. The constitutional approach treats fiscal outcomes as phenomena that emerge out of interaction among a plethora of fiscal participants. The institutional framework within which fiscal outcomes emerge occupies center stage in the constitutional approach. Brennan and Eusepi contrast these two approaches to public finance across a number of fiscal institutions and practices.

Between the start of the twentieth century and the end, the share of national economic activity that flowed through government increased several times over. Where government's typically claimed less than ten percent of GDP at the start of the century, they generally occupied between 30 and 50 percent by the end of the century. In Chapter 4, Thomas Borcherding, Stephen Ferris, and Andrea Garzoni examine the growth of government since 1970. They find that the growth of government has not been so uniformly positive since 1970 as it was over the previous 70 years, and they account for this pattern of growth in terms of both economic variables that operate mainly on the demand side for government services and political variables that operate more on the supply side.

In their exploration of "Rules, Politics, and the Normative Analysis of Taxation" in Chapter 5, Walter Hettich and Stanley Winer contrast different approaches to the development of norms for taxation, and of the treatment of politics within the context of those norms. They distinguish between outcome-oriented rules and process-oriented rules. This distinction maps fairly well into the distinction that Brennan and Eusepi make between the orthodox approach and the constitutional approach in Chapter 3. Outcome-oriented norms are articulated outside of considerations pertaining to political processes, and represent statements about the character of the choices that might be made by some benevolent despot. Process-oriented norms recognize that taxes emerge out of political processes that are suffused with rivalry among interest groups, and seek to constrain the outcomes of those processes by eliminating particularly undesirable outcomes.

Tax revenues are used either to finance programs of public production or to provide transfer payments to recipients. This distinction between public production and transfer payments corresponds to the distinction between the allocative and the distributive branches in Richard Musgrave's (1959) presentation of the *Theory of Public Finance*. In Chapter 6, Randall Holcombe explores "Taxation, Production, and Redistribution" in terms of contrasting the implications of alternative approaches to public finance. Substantial differences result from replacing the presumption that fiscal outcomes are chosen by a benevolent despot with the presumption that those outcomes emerge from within a democratic political process. One famous illustration of benevolent despotism is the Ramsay model of excise taxation, where tax rates vary inversely with the elasticity of demand. Holcombe explains how a rule of uniform tax rates would economize on the various rent-seeking and rent-extraction activities that would exist under a regime of differential taxation, and which would be precluded by a requirement of uniform taxation. In this and in numerous other illustrations, standard propositions about public finance that have been developed within a political context of benevolent despotism are reversed in a democratic setting.

In Chapter 7, Fred Foldvary describes the generation of "Public Revenue from Land Rent." While it is easy to think that this would be just another form of taxation, Foldvary explains why this thought would be mistaken. The value of any piece of land depends on the value of the civic works that lie in proximity to that land. Such things as roads, parks, and schools increase the value of nearby land. Foldvary reports that a bridge across the Hudson River in New York increased adjacent land values by six times the cost of the bridge. The use of changes in land value as a means of financing government could be part of a program by which government participates within the economic process, as against intervening into that process through taxation.

Chapter 8, by Richard Wagner, examines "Debt, Money, and Public Finance." In principle, borrowing and creating money are distinct methods of public finance. They are confounded, however, within modern institutional arrangements. A government whose bonds are bought by citizens is borrowing, but a government whose bonds are bought by the central bank is creating money. While it is linguistically common to speak of governments as being indebted, this common usage is misleading for democratic states where government is simply an intermediary. Public borrowing within a democracy is a means by which state-based intermediation replaces market-based intermediation. This replacement might be universally beneficial or it might be beneficial to some but not to others, with the outcome depending on the institutional arrangements within which political and fiscal outcomes emerge.

The theory of corrective taxation treats instances where taxation seems to serve more a means of regulation than a source of revenue. In Chapter 9, Andy Barnett and Bruce Yandle examine "Regulation by Taxation." They note that the regulatory impact of such taxation often generates differential impacts among interest groups, in addition to generating revenue for governments. Indeed, they claim that such taxation fits the scenario of the Baptists and bootleggers, whereby both support restrictions on liquor sales, though for strongly different reasons. They illustrate their point empirically with reference to liquor taxation within the United States and environmental taxation within the member nations of the Organization for Economic Cooperation and Development.

In Chapter 10 on "Taxation, Black Markets, and other Unintended Consequences," Carla Marchese explores some of the many steps that exist between the establishment of a tax and the actual collection of revenue from that tax. The higher the rate of tax, the stronger will be the incentive to avoid or evade the tax. These efforts can take many particular forms, some legal and some not. This chapter explores tax enforcement and compliance from a variety of angles and perspectives.

In Chapter 11, Scott Hinds, Nicolas Sanchez, and David Schap explore "Public Enterprise: Retrospective Review and Prospective Theory." Prior to the development of public choice theorizing, the bulk of the literature on public enterprise was normative in character. That literature sought to set forth rules govern such things as when public enterprises should be created and what the pricing policies of those enterprises should look like. As public choice theorizing attained prominence, scholars began to realize that the actual conduct of public enterprises often bore little resemblance to the normative formulations. The authors describe this shift from a normative- to a positive-dominated agenda, and look forward to further developments of the positive-dominated agenda.

What is a public enterprise at one time might become a private enterprise later. Or it might have been a private enterprise before it was transformed into a public enterprise. In Chapter 12, William Peirce examines “Privatization, Nationalization, and Aspects of Transition.” There are many possible reasons why private enterprises might be nationalized, or why public enterprises might be privatized. At base, Peirce explains, the shift in organizational form should be explainable in terms of its ability to confer benefits on significant subsets of the population. For instance, a state might privatize to generate a temporary increase in revenue. Alternatively, a state might nationalize to maintain employment among the membership of an influential labor union.

In his wide ranging review of “Social Insurance” in Chapter 13, Heinz Grossekettler examines explanations for the development and growth of social insurance, describes the vast differences across nations, and considers future problems and projections. Social insurance is characterized as having been crafted out of a tension between two opposed sentiments. One is a desire for individual separateness or property. The other is a desire for peace or solidarity within some particular territory. The resolution of these opposing sentiments, moreover, differs greatly throughout the world. This resolution, furthermore, is not of the sort that brings to mind notions of stable equilibrium but rather brings to mind future turbulence.

The term “welfare state” is commonly used to cover both the social insurance programs that Grossekettler examines and programs of poor relief. To be sure, the distinction between social insurance and poor relief is muddied in practice. The metaphor of a safety net, for instance, has been used to characterize both social security types of programs and programs of poor relief. In Chapter 14, Richard Wagner explores “Redistribution, Poor Relief, and the Welfare State.” This essay begins with an examination of justifications that have been advanced for the state provision of poor relief, where the alternative to state provision is provision through privately organized charities. Arguments about justification are the province of fiscal philosophers, but the actual creation and operation of programs is the province of political realists. The remainder of this essay examines the problem of state competence in light of the possible clash between the fiscal philosophers and the political realists.

It would surely be hard to support inefficient public programs over efficient programs, at least without mocking linguistic meanings and conventions. Many economists have sought to bring economic principles to bear on the appraisal of the efficiency of public programs. In Chapter 15, Allan Schmid explores a wide variety of issues regarding “Economic Analysis and Efficiency in Public Expenditure.” Schmid notes at the outset that efficiency is not simply a matter of technique and calculation; computations of efficiency cannot be constructed that would serve unambiguously as judges of the content of political choices and actions. It is easy enough formally to say that one program is more efficient than another if it generates more output value for the same amount of input. But typically it is not easy to value output, or even to measure it. How, for instance, is a metric for the amount of education produced within public schools constructed? As Schmid notes, cost-benefit analysis may help to organize our thinking about public programs, but it cannot make our choices for us.

In Chapter 16 on “Local Public Finance,” Charles Blankart and Rainald Borck note that while local public finance can be traced back to the middle ages, the field began in earnest only with the publication in 1956 of a paper by Charles Tiebout. Most of the subsequent literature has been concerned in one fashion or another to look for parallels between a network of local governments to order collective activity and competitive markets to order private activity. There are several strands to the literature, all of which Blankart and Borck explore. On the one hand, competitive local governments are able to accommodate for fully differences in preferences across people. They can also promote experimentation and the generation of knowledge through their ability to serve as types of laboratory experiments of different approaches and policies. On the other hand, a multiplicity of local governments will typically generate externalities, which in turn will create problems of coordination, as well as prompting institutional innovations to deal with those problems.

Competition among local governments is a form of horizontal competition, with those governments competing to attract residents. Within federal systems of government, there is also vertical competition among governments, which arises from the simultaneous citizenship of people in multiple governments. Jean-Michel Josselin and Alain Marciano examine in Chapter 17 a plethora of issues concerning "Federalism and Subsidiarity, in National and International Contexts." The principle of subsidiarity supports the delegation of tasks to the lowest level at which they can be discharged responsibly and effectively. At first glance, subsidiarity might seem to be a principle that operates in favor of lower over higher levels of government within a federation. The practice of federalism, however, is not so neat, and in their examination of why this is so, Josselin and Marciano distinguish between federating a nation (as illustrated by the United States) and federating a set of nations (as illustrated by the European Union).

In Chapter 18 on "Fiscal Sociology: What For?" Jürgen Backhaus locates fiscal sociology as the contemporary continuation of the tradition of Staatswissenschaften. Economics and politics are thoroughly co-mingled in contemporary societies, and the disciplinary separation of analytical spheres calls also for efforts at unification. Backhaus explains how fiscal sociology can serve as the contemporary continuation of Staatswissenschaften, by promoting an integrative treatment of the economic, political, legal, and sociological aspects of public finance. He does this by generating an entire alphabet of concepts that fiscal sociology can illuminate.

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