# The Politics of Fiscal Decentralization Revisited: a Typology and Comparative Evidence

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**Abstract :**

Although the practice of fiscal decentralization is worldwide and its implementation and effects vary from country to country, its political significance has been often neglected, or worse, treated as implicit to decentralization. This study considers the sources of politicization of fiscal decentralization, focusing on the determination and manipulation of intergovernmental transfers. It develops a new index of fiscal politicization and proposes an explanatory typology that takes into account subnational transfer dependency and the extent to which transfers are politically determined. This analysis renders a conceptual tool that captures nuanced facts about the intergovernmental level of conflict to a larger extent than conventional measures of fiscal decentralization do. We found that the effects of fiscal dependency are intertwined with political asymmetries derived from legislative overrepresentation of territorial units and intergovernmental bargaining strategies.

## Introduction

In both developed and developing countries, there has been a contemporary debate on the nature and merits of decentralization. The collapse of communism and the ‘crisis’ of the welfare state have rekindled serious thinking about the relationship between governance and the appropriate level of devolution of power away from the central state to lower levels of administrative and political authority. Moreover, the growing demand for public services and infrastructure in Third World countries has brought increasing calls for decentralization to develop taylor-made policies in congruence with varying national needs.1 However, and despite the fact that decentralization issues have been on the political front-burner in the last two decades, no single paradigm or theoretical model informs the study and practice of decentralization policies across nations.

On a very general level, decentralization is the transfer of responsibilities and revenue from national government to subnational offices.2 This definition suggests that power is being given away through a series of measures and steps meant to eliminate overload at the central level, in which case decentralization denotes a *process* rather than a final or pre-set goal. Despite most studies of decentralization accept a process-oriented perspective, there is no overarching agreement about its goals. This is basically due to the fact that students of decentralization oftentimes confound political and fiscal decentralization. In Europe, there has been a trend to encapsulate types of decentralization under the notion of regionalism and regionalization. Albeit useful to pin down the determinants of regional policy in a era of global political and economic change,3 this body of research uses indicators of political and fiscal decentralization interchangeably, diminishing their empirical usefulness. Also, frequent regime changes and a strong ‘centralist tradition’4 have been long-standing factors inflating the political nature of decentralization in Latin America and downplaying the significance of fiscal power relations. Borrowing from Bird,5 widely recognized as a leading student of fiscal decentralization, 'decentralization seems often to mean whatever the person using the term wants it to mean'.

To remedy this deficiency, I argue that it is important to distinguish between the distribution of political authority, namely the transfer of political power to subnational levels of government, and the organization of fiscal prerogatives, referring to where taxes are raised and public funds spent. The political significance of decentralization becomes apparent as it represents a necessary condition to advance democratization processes in countries with strong legacies of centralist and exclusionary politics. Strengthening local government through civil society participation and municipal elections constituted the dominant theme in the budding cottage industry of academic work on decentralization of the then transitioning democracies.6 Albeit valuable in emphasizing the participatory aspects of democracy, these literatures have seldom considered the determinants of such policies, virtually ignoring the role of institutions in uncovering the political logic of decisions by national authorities to decentralize.

Partly due to normative assumptions about local politics and some optimism stemming from ongoing episodes of democratization, the 'people can do it all' approach assumed that fiscal resources for effective local governance will flow once local actors will become politically invigorated. Central to all these arguments is the view of decentralization as promoting accountability and political efficacy,7 bolstering popular participation and local democracy. From a totally different theoretical perspective, this emphasis on the efficiency gains associated with the decentralization of local decisions to local governments is shared by normative economic theories of federalism. Guided by public choice theory, this body of scholarship put forth by Charles Tiebout, Wallace Oates, and more recently, Barry Weingast, sees decentralization as limiting the ability of government officials to supply local goods on political grounds. This superiority of decentralization, the argument goes, is due to the fact that the principal, *i.e*. central government, delegates administration and production rights to agents with superior local information. That is to say, more decentralization economizes on communication costs while also leading to a control loss on the part of the principal. Additionally, ordinary citizens can foreshadow their dissatisfaction with local policies by moving to an area where their preferences are fulfilled ('voting with their feet'), enhancing inter-jurisdictional competition. At this juncture, literatures on popular democracy, on the one hand, and international financial institutions, on the other, paradoxically converge.

While both logics linking decentralization to the 'small is beautiful' and 'voting with the feet' slogans are compelling, they fail to account for the fact that political leaders are, at the very least, as concerned about their power position as they are about public welfare. Despite the fact that both goals are not intrinsically contradictory, we will assume in this study that the former consideration would prevail over the latter. Politicians seek to place power where they can be more confident of controlling it, be it at the center or state level. Moreover, decentralized jurisdictions are less likely to attract high-caliber bureaucrats, since the rewards to local officials will be small in comparison to those at the central level.8 Accordingly, local bureaucrats oftentimes compensate for this income gap through rent-seeking practices and corruption. The latter practices are further exacerbated by the fact that subnational administrations are less susceptible to public and media scrutiny than the more powerful national office. And from the 'demand side', people living in the periphery of democratizing countries are often assimilated massively into the state payroll, intensifying long-standing loyalties with local politicians and diminishing the probability they will sort themselves into other jurisdictions. Therefore, the persistence of clientelism and patronage practices implies that poor citizens have strong incentives to stay in rather than opting for the ‘exit’ option.

This suggests that neither the civil society approach to decentralization nor normative public choice theories seem to capture the multifaceted nature of decentralization. In emphasizing the role of both vibrant societal actors and benevolent and foresighted actions of national authorities, these assumptions fall short of formulating the more mundane motives behind decentralizing changes. Brennan and Buchanan have forcefully shown that national politicians have every reason to restrain inter-jurisdictional competition if that furthers their own careers.9 Furthermore, some literatures on political economy establish that central governments are revenue maximizers that may wish to retain taxes for their own ends.10 Thus, as decision to decentralize fiscal power entails significant risks, considerations beyond notions of public interest do shape the mindsets of national politicians. This ‘Leviathan’ assumption about central government behavior suggests that national politicians support decentralization for the same reasons they support any other policy change.

## Why is Fiscal Decentralization Politically Important?

In fact, fiscal arrangements are one of the most politically contested aspects in multitiered systems. In Germany, which is the only federation where fiscal gaps among regions are ameliorated by transfers from richer *Länder* as well as federal government,11 ‘cooperative federalism’ has kindled resentment among richer *Länder* against ‘confiscatory’ levels of transfers. This unleashed a significant number of appeals to the federal Constitutional Court and self-serving lawsuits by said *Länder*, especially after reunification.12 There is additional evidence from cases in which small states play a king-making role. While asymmetries in population, size, and economic power are commonplace in decentralized systems, overrepresentation of states in national governing bodies is a major determinant of fiscal responsibilities and outcomes. Gibson and Calvo have shown that legislative overrepresentation in Argentina and Brazil produces federal spending distortions in favor of overrepresented territories.13 Patterns of federal spending reflect overrepresented states’ ability to reproduce their leverage in legislative chambers onto key congressional budgetary committees in the latter country, whereas Argentine national executive directs disproportionate federal funding to small-sized and state-dependent peripheral provinces because these render substantial political payoffs (*i.e.*, legislative support for hard-to-sell economic reforms) from relatively small investments of intergovernmental funds. In Belgium, increasing fiscal autonomy (including tax powers) is strongly associated with the necessity of promoting the visibility and influence of inchoate and recently established regional governments.14 Examples from other federations and rapidly decentralizing countries can be cited at length but the above illustrations suffice to show the extent to which fiscal and financial issues give rise to political struggle between central and regional authorities.

Yet, what makes fiscal decentralization particularly susceptible to political manipulation? As argued above, political decentralization is very much at the core of democratization processes, constituting a recurrent and unavoidable outcome. Oftentimes, local elected officials become standard-bearers of transitions processes,15 and any reversal to their prerogatives stirs public outcry and consternation. In contrast, the unfolding of fiscal reforms and the distribution of federal grants is far less subject to citizen scrutiny and tends to take place in ‘smoke-filled’ rooms.16 Particularly so in federations whose intergovernmental fiscal systems are extremely complex even to enlightened bureaucrats.17 However, the fact that elections of local officials have more profound symbolic undertones does not imply that the formulation and allocation of intergovernmental grants is something less of a *political* issue. On the contrary, and as this study attempts to show, when national politicians opt for reforming fiscal power- sharing relations they do so with an eye to territorial patterns of political and electoral support.

Adding to the above is the fact that fiscal arrangements are only rarely enshrined in laws of constitutional status.18 The ensuing rigidity stemming from constitutional mandates not only hinders governments' maneuvering space to respond to fiscal crises in different ways but also affects their ability to attune fiscal policy to changing political environments.19 Because processes of decentralization often entail significant redrawing of political boundaries and dynamics, renegotiation of agreements becomes necessary. Moreover, some scholars argue that insofar as it promotes different interpretations, constitutional ambiguity ensures the durability of the system.20 Yet, this study indicates that mutual trust among the different levels of governance is of essence and that Spain does not meet said requirement. Furthermore, the Achilles heel of the 'para-constitutional' nature of these intergovernmental agreements, however, lies in the strategic advantage of a few participants with strong bargaining positions. While this pattern occurs in other decentralized systems like Canada, intergovernmental relations in countries such as Argentina and Spain unfold in a framework of low institutionalization and their agenda is set by the political leadership of the governing parties in a largely unmediated manner.

The political nature of fiscal decentralization becomes also evident because there is no widespread agreement among policymakers on how to treat intergovernmental fiscal relations. On the one hand, central authorities offload fiscal functions to subnational governments at the face of budget constraints. However, recent experiences of countries experiencing macroeconomic crises like Argentina and Brazil indicate that central governments have sought to re-centralize by imposing fiscal restraints on state governors.21

## Conceptualizing the Politicization of Fiscal Decentralization: the Role of Transfers

If the crux of intergovernmental politics lies in the realm of fiscal relations, what aspects are most important in determining the trajectory of these relations? In this section, I investigate the thesis that transfers are a key component of political models of central-regional relations. In considering the effect of transfers on decentralization, it is important to refer to an important body of literature on local budgetary behavior indicating that central funding undermines regional/local fiscal autonomy.22 Autonomy, in this context, denotes the ability of subnational governments to raise tax locally to offset expenditures. More recently, however, it has been suggested that regional leaders may be less motivated to increase the tax burden in their jurisdictions because central government transfers minimize the costs of decentralized provision borne by local taxpayers, which can be financed by a 'common pool' of resources collected elsewhere in the economy.23 This view is reinforced by the presence of revenue-sharing arrangements, whereby every time a central government raises taxes to improve its own position, subnational governments receive a corresponding revenue benefit which they are normally free to spend.24

Intergovernmental transfers are the dominant source of revenue for most subnational governments in multitiered systems. Apart from federations like Canada, Switzerland and the United States, where emphasis is placed on local tax revenue mobilization, other countries have their subnational spending mostly financed by intergovernmental transfers.25 These transfers aim also to address fiscal gaps across regions, which are exacerbated by and stem from the insufficient revenuegenerating capacity of subnational levels of government to meet their expenditure responsibilities. Adding to the distorting impact of separating taxing and spending powers, namely the 'flypaper' effect,26 are policies of fiscal decentralization based on unfunded mandates,27 or, put simply, deficit-ridden central governments offload their imbalances onto state governments by increasing subnational expenditure without a parallel increase in revenues. These distortions do not only have fiscal significance but also pit the states and federal level against each other, buttressing the political significance of intergovernmental transfers.

More specifically, federal intergovernmental funds comprise general revenue and specific purpose (*i.e.*, conditional) transfers. The former, commonly known as coparticipation or revenue-sharing system, is oftentimes ruled by variables such as population density, developmental gaps, and state own tax collection or alternatively by fixed coefficients over which central and regional powers have limited leverage. In this case, transfers are allocated automatically and are not earmarked for any specific purpose. Hence, the extent of potential politicization of this type of transfers is nearly negligible because the three afore-mentioned variables have little variance in the short-term and fixed coefficients remain constant, let alone that revenue-sharing is unlikely to be affected by the policy choices and actions of recipient governments. In contrast, conditional transfers are subject to ongoing processes of intergovernmental negotiation, furnishing subnational-level leaders with a maneuvering margin of considerable proportions to extract additional resources from the central administration. By the same token, the center may attempt to manipulate transfers to force subnational authorities to pursue economic policies in tandem with national programs of fiscal adjustment, amounting to a re-centralization of fiscal policies. In Argentina, severe fiscal constraints compelled provincial governments to allow the National Treasury as well as international banks to withhold coparticipation (*i.e.*, unearmarked) income as a collateral for contracting loans. Thus, most provinces are deprived from using coparticipation monies during the first two weeks of the month. To mitigate said stringent conditions, provincial governors were allowed to redirect some of the earmarked (housing, highways, energy, etc.) funds to soothe mushrooming provincial fiscal deficits.28 Based on discretional criteria, this change has turned intergovernmental transfers into arenas of political manipulation. Comparable developments transpire in Spain, where Joint Agreements on Investment (*Convenios de Inversión*), the largest conditional intergovernmental transfer, are generally exploited by the central administration to adjust the expenditure priorities of the autonomous communities to national policies of economic stabilization.29

Focusing on intergovernmental transfers illuminates otherwise cryptic facts about the political nature of fiscal decentralization. As Bird and Vaillancourt argue, 'the design of intergovernmental transfers is always and everywhere an exercise not solely in normative economics but also in political economy'.30 This is so because looking into the relative shares of revenues and expenditures held by subnational governments (understood as the second-tier level and excluding the municipal level), as most studies on decentralization do, gives an incomplete picture of the real degrees of decentralization. A more nuanced and valid measure of regional fiscal autonomy, then, is the share of intergovernmental transfers in total subnational revenue, which taps the segment of subnational finance being determined by central government authorities. Although this indicator applies only to the apportionment between the central and the subnational governments (henceforth, primary distribution) and does not take into account the distribution among subnational governments (henceforth, secondary distribution), it is a useful starting point to establish the comparative context. Table 1 confirms that in countries Argentina and Spain there is an acute gap between the political sway of regions and their fiscal autonomy, when compared to a sample of federal and significantly decentralized unitary systems in their respective regions. To explain this disparity, I constructed the Index of Fiscal Politicization, in which the magnitude of intergovernmental transfers is weighed up by the level of subnational spending as a proportion of total government spending (see, Table 1, footnote). This index has no fixed range and its substance is more of heuristic than of econometric nature, but its high values denote higher potential for political conflict over fiscal decentralization and lower values otherwise. The rationale for this indicator lies on the stylized fact that high reliance on central government transfers on the revenue side of the equation combined with increasing subnational expenditure responsibilities exacerbates the zero-sum character of fiscal relations and their political 'corrosiveness'. Put differently, the higher the value of this index, the more intergovernmental bargaining will affect the inter-regional distribution of transfers.

**Table 1: Intergovernmental Fiscal Indicators**

Against this background, an important theoretical qualification to be introduced here is about the real political significance of decentralized spending. In this regard, the evidence presented above suggests that high levels of subnational spending are not tantamount to regional fiscal sovereignty. Whereas studies using subnational spending as a degree of fiscal decentralization are correct in pointing out that this is one of the best measures available without detailed study of each country,31 they fail to grasp that local expenditure is something of a 'double-edged sword'. On the one hand, it highlights the amount of government activity that subnational governments undertake, tapping into one of the main aspects of decentralization. On the other, mere expenditure decentralization funded through intergovernmental transfers renders local officials subservient to the priorities of the center, with the concomitant rent-seeking effects.32 In this context, it is worth emphasizing that while the classic public economics scholarship advocates that transfers are made by 'free-handed' central governments to internalize externalities (*i.e.*, interregional fiscal equalization), Rodden correctly argues that, both from an institutional political economy and more realistic perspectives, 'intergovernmental grants are not distributed by benevolent central planners, but rather by strategic politicians'.33 Hence, subnational governments get no 'free lunch' when local expenditure is financed with transfers that normally carry political, if not administrative, strings attached. The case of Argentina is very telling insofar as it is not only the most decentralized Latin American country in expenditure terms34 but, also, one of the front-runners in Table 1, matching the United States and approaching Switzerland, which have some of the highest levels of decentralized spending in the world. However, the extent of politicization, as measured by our index, is considerably much higher in Argentina, suggesting that transfers are prone to be hijacked by political interests.

What really matters, then, is the sphere over which state officials have autonomy. Ideally, local authorities can have more autonomy over tax bases of their own, but the 'common pool' dynamics illustrated above boosts their preference to externalize the founding source (*i.e.*, minimizing own revenue mobilization) to reduce accountability troubles in their electoral jurisdictions.35 Put differently, if the political costs of 'self-control' offset administrative and efficiency gains derived from own-revenue mobilization, local authorities will rather choose to maximize 'influence'. This sway can be materialized in the determination of the revenue-sharing allocation to be transferred to subnational governments and in the redistribution of transfers among them. With regards to the former, the determination of how much is to be distributed is usually a fixed proportion of central government total revenues, which is more heavily influenced by economic trends such as pro-cyclical effects than by political interferences.36 Furthermore, revenue-sharing arrangements are more commonly set on a tax-by-tax basis, with different coefficients of distribution among levels of government for each tax, rather on the entire pool of central government taxes, as found in Argentina, Brazil, Germany, India, Spain, and others. This scheme, however, is detrimental to subnational governments because it leads the central level over time to tend to increase those taxes which they do not have to share.37

## Types of Fiscal Decentralization: a Political Explanation

While state-level authorities have limited capacity to dictate the total volume of revenue-sharing, they have more influence on the primary and secondary distribution of earmarked transfers.38 In this regard, decentralization should be seen not only as a game being played between the central government and the regions but also as an issue subject to inter-state conflict. The rationale for this analytical strategy stems from the fact that, whereas federal transfers are important to all subnational units, the greater dependence of peripheral regions on the central government alters the parameters used to assess levels of decentralization. This dependency results from the greater share of said disadvantaged regions' budgets subsidized by intergovernmental transfers, compared to metropolitan areas. Thus, while the apportionment of federal transfers to individual metropolitan areas may exceed that for peripheral regions in absolute terms, the purse power granted to the latter is more significant in relative terms. Moreover, in countries traditionally seen as playgrounds of caudillos, dictators and strongmen like Argentina and Spain, centralist legacies transpire in the ongoing administrative and political hegemony of Buenos Aires and Madrid, respectively. In turn, this sway endows politically powerful regions with privileged access to fiscal resources, beyond their actual economic capability and despite the concomitant *de facto* separation of national political power from regional economic power.39

Consequently, we argue that the apportionment of federal transfers among subnational units is a most valid and sound indicator of real fiscal decentralization, providing a number of important insights into the political economy of multitiered polities. Furthermore, focusing on the secondary distribution of intergovernmental transfers allows us to knit together the fate of decentralization policies to the maintenance of state patronage. Despite the prevalent view, mostly from international financial institutions, of fiscal decentralization as a potent antidote against rent-seeking behavior, this policy arena renders substantial opportunities to reinforce established clientelist networks in the economically disadvantaged but politically relevant subnational units. In economic terms, this analytical divide between metropolitan and peripheral regions affects substantially the political economy of transfers because higher levels of development and economic prosperity in the former regions will boost their capacity to mobilize revenue locally. Thus, all else equal, transfers in said areas will amount to a smaller fraction of their public budget. However, the extent of peripheralization of transfers is also influenced by the leverage of political factors, as opposed to socio-demographic and economic ones, in the determination of the primary distribution of earmarked transfers. This argument is presented visually in Figure 1, which identifies four ideal-typical scenarios of fiscal decentralization.

**Figure 1: Types of Fiscal Decentralization**

The horizontal axis measures the extent to which the allocation of federal transfers is tilted to more transfer-dependent subnational units, composing a variable identified as *peripheralization of secondary distribution.* The vertical axis measures the extent to which the total amount of earmarked transfers is politically determined, namely whether the bargaining among politicians and the political ideology of the party in power federally are more decisive than fiscal criteria in said determination, identified as *political determination of grants.* On average, this typology shows that the equalizing and efficiency effects that fiscal decentralization policies aim to achieve are increased when the determination of transfers fits the lower right quadrant, which corresponds to the *cooperative decentralization* type. The afore-mentioned clause of the German *Grundgesetz* (Constitution) requiring ‘equivalence of living conditions’ implies that inter-regional welfare imperatives prevail over political considerations. Further, poor *Länder* are subsidized by an equalization scheme pursued through direct horizontal redistribution among *Länder*, without participation of the central government.40 Accordingly, constitutionally-determined outcomes prevail. In practice, this translates into what Börzel describes as ‘compensation-through-participation’, whereby all *Länder* share the adaptational costs through codetermination in fiscal decision-making.41 However, if the apportionment of transfers to peripheral regions is a function of the grantee’s ability to deliver votes or legislative support to central government’s policies, grants are more likely to be perceived as contractually established. This scenario, identified in the upper right quadrant as *cooptative decentralization*, is perhaps less desirable from a normatively-oriented fiscal federalism perspective, but it may be appealing to transfers-dependent regions. Note that Argentina has not only one of the world’s most malapportioned senates but also the most malapportioned lower chamber in Latin America.42 This overrepresentation renders poor peripheral units politically powerful because these can offer more ‘political bang for the buck’ to the national executive than underrepresented areas. Utility-maximizing central governments prefer to target transfers to disadvantaged regions rather than to more developed constituencies because they obtain substantial political payoffs from smaller investments in ‘political’ spending.43 The correlate of this standpoint is peripheral subnational governments’ keenness to secure a lavish flow of federal transfers, as their political survival hinges upon them to a larger extent than prosperous regions, where both economic clout and organizational resources are more readily available.44 Thus, this type of decentralization, which is based on institutional resources and their consequential biases, engenders a more predictable and reliable flow of transfer funds to said regions.

The upper left quadrant, however, indicates that political factors can twist transfers toward more developed, metropolitan regions. The rationale underlying this *collaborative*[45] type of fiscal decentralization is that central governments would reward highly populated, *i.e.* revenue-rich, subnational units, which are more ‘regionally assertive’,46 more likely to develop regionalist political forces and, thus, more prone to advance their region’s fiscal autonomy. Partly aimed at rewarding fiscal performance and partly due to the embryonic and evolving nature of fiscal federalism in Spain, the central government started first bilateral consultations and negotiation with Basques and Catalans, which virtually play a gate-keeper role47 and gradually incorporated all other regions in multilateral arrangements. This negotiation strategy stems to a large extent from the somewhat devolutionary centrifugal drift that characterized Spanish federalism since the beginning of democratization. Last, transfers can benefit more developed regions, inasmuch as these are ‘net-payers’ (due to the relatively high level of personal income tax generated in their jurisdiction), hence worthy of some sort of compensation for their fiscal contributions. This approach, which is widespread in the United States, shifts emphasis away from redistributive calculus and it prioritizes the removal of distortions in the allocation of federal transfers.48 Identified as *competitive decentralization* in the lower left quadrant, this policy rewards fiscal efforts of competent fiscal contributors and cuts back support for local tax administration in peripheral regions, where it is perceived to generate major revenue bottlenecks. In turn, this type of decentralization hinges on the development and protection of markets.49

In summary, considering that the territorial impact of federal transfers is gauged in relative terms, as suggested above, transfers that further peripheral subnational governments' spending power, relative to metropolitan regions, will bring about a type of decentralization that is qualitatively different from one resulting from an advantageous apportionment to metropolitan regions. The major policy-making implication of this crossroads of central government/peripheral areas' preferences is that a meaningful articulation of subnational interests is precluded, considering the underlying zero-sum game' character of said distribution of federal transfers. We argue that this competitive environment renders two major structural effects on fiscal decentralization; first, negotiations are based on bilateral bargaining that clearly dilutes the formation of subnational coalitions and, second, intergovernmental negotiation occurs mostly through *ad hoc* meetings between the executive levels of the governing parties, to the detriment of any meaningful parliamentary processes of scrutiny. These structural features hinder a redressing of the territorial balance of resources that fiscal decentralization policies are meant to achieve. These effects are more pervasive in Argentina than in Spain, where there has been a shift from confrontation and non-cooperation (between the central government and the autonomous communities, on the one hand, and among the latter, on the other) to a more cooperative approach based on an institutional framework that promotes multilateral cooperation.

## Conclusion

This article has shown that the design and working of intergovernmental transfers is a most appropriate analytical lens to uncover the political dynamics of fiscal decentralization. Further, we dealt with the sources of politicization of fiscal decentralization policies, suggesting that extant approaches fall short of revealing some ambiguous aspects of these policies. Particularly, the weakness of conventional measures of fiscal decentralization to capture nuanced facts about the inter-state level of conflict and the apparent, yet paradoxical, mutually reinforcing relationship between decentralization and the proliferation of patronage-ridden policy regimes in peripheral regions. What is more, the theory laid out in this chapter suggests that state patronage is not only a likely development but also that it is apparently a causally integral component of the overarching fiscal decentralization policies. In specific terms, the core question is what political features and/or institutional incentives of the system determine the afore-described manipulation of intergovernmental financing across subnational jurisdictions. Chief among these features and incentives are the legislative representation of territorial interests, partisan color of the national executive and governorships, presence of regional-party dominant systems, socio-demographic influences, and macroeconomic determinants. To conclude, as many of the issues discussed in this article loom large in the political economy of federal and decentralizing polities, subsequent iterations on the theoretical and methodological challenges taken up here would certainly enrich the comparative federalism agenda.

### Notes

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25 Fiscal relations in the EU obscure this characterization, insofar as its budget is financed mainly through upward-oriented grants from its member governments, as opposed to the typical pattern of top-down flows. The European regional policy is one of the few instances in which subnational governments are funded by the 'political center' through programs such as the European Fund for Regional Development.
26 Also known as 'fiscal illusion', this effect denotes an underestimation of the costs of locally provided services, resulting in increased demands for local government output. This 'inflation' of demands stems from the recipient's perception that said services are being paid for or heavily subsidized by residents of other localities; GROSSMAN (P. J.) (1990), 'The Impact of Federal and State Grants on Local Government Spending: A Test of the Fiscal Illusion Hypothesis', *Public Finance Quarterly*, vol. 18, n° 3, 1990, p. 313-314.
27 ROIN (J. A.), 'Reconceptualizing Unfunded Mandates and other Regulations', *Northwestern University Law Review*, vol. 93, 1999.
28 For instance, since the mid-1990s the central government has agreed to permit provincial governments to use nearly 50 percent of FONAVI (*Fondo Nacional de Viviendas*, National Housing Fund) funds to cover general expenditure needs (Personal communication with Senior Advisor, *Subsecreataria de Relaciones con Provincias, Ministerio de Economía,* Under Secretariat of Provincial Affairs, July 28, 2001). It is worth mentioning that FONAVI is the largest intergovernmental grant, accounting for roughly 20 percent of the total amount of sharable resources in Argentina.
29 MONASTERIO ESCUDERO (C.) and SUAREZ PANDIELO (J.), *Manual de hacienda autonómica y local*, Barcelona, Ariel Economía, 1998, p. 209.
30 BIRD (R. M.) and VAILLANCOURT (F.), *Fiscal Decentralization in Developing Countries*, Cambridge, Cambridge University Press, 1998, p. 30.

31 SCHNEIDER (A.), 'Decentralization: Conceptualization and Measurement', *Studies in Comparative International Development*, vol. 38, 2003, p. 32-56.

32 OATES (W. E.), 'Fiscal Decentralization and Economic Development', *National Tax Journal*, vol. 46, n° 2, 1993, p. 237-243.

33 RODDEN (J.), 'Reviving Leviathan: Fiscal Federalism and the Growth of Government', *International Organization*, vol. 57, 2003, p. 705-706.

34 Inter-American Development Bank, *Economic and Social Progress in Latin America, 1997 Report: Latin America after a Decade of Reforms*, Washington, DC, Inter-American Development Bank, 1997. However, as the World Bank's report by Burki, Perry and Dillinger claims, 'Argentina is arguably one of the most decentralized countries in the region but has essentially the same political and fiscal structure it had before the military intervened in 1976… In contrast, Colombia has radically increased the power and responsibilities of subnational units of government'. It is noteworthy that the index of fiscal politicization ranks Argentina much higher than Colombia, see BURKI (S. J.), PERRY (E. G.) and DILLINGER (W.), *Beyond the Center: Decentralizing the State*, Washington, DC, The World Bank, 1998, p. 11.

35 Likewise, some public choice scholars go as far as to argue that intergovernmental transfers undercut incentives for fiscal efforts, encouraging the formation of subnational cartels to avoid the discipline of tax competition, RODDEN (J.), *art. cit.*

36 Examples of revenue-sharing systems that determine transfers as a proportion of national current revenues may be found in developed and developing countries alike. These include Austria, Brazil, Colombia, India, Japan, Nigeria, Philippines and others, BIRD (R. M.) and VAILLANCOURT (F.), *op. cit.*, p. 30.

37 TER-MINASSIAN (T.) (ed.), *op. cit.*, p. 11-12.

38 PORTO (A.), 'El papel de los aportes del tesoro nacional en las finanzas provincials', in *Trabajos de investigación presentados en las decimonovenas jornadas de finanzas pública*, 17-19 September 1986, Facultad de Ciencias Económicas, Universidad de Cordoba.

39 In Argentina, the development of the Pampas region has, from the very beginning, enhanced the economic and administrative clout of city of Buenos Aires, whose ports gave it virtually unchallenged control over trade and customs revenues. The case of Spain bears resemblance in the standing of Madrid as the 'center', notwithstanding the economic strength of Catalonia.

40 SPAHN (P. B.) and FÖTTINGER (W.), *op. cit.*

41 BÖRZEL (T. A.), *States and Regions in the European Union: Institutional Adaptation in Germany and Spain*. Cambridge, Cambridge University Press, 2002.

42 SAMUELS (David) and SNYDER (R.), 'The Value of a Vote: Malapportionment in Comparative Perspective', *British Journal of Political Science*, vol. 31, 2001, p. 651-671.

43 This conjecture naturally assumes that national political power is more or less equally distributed among constituent units in a politically-decentralized system and that poor and unpopulated units are oftentimes overrepresented in national legislatures of federal systems; GIBSON (E. L.) and CALVO (E.), *op. cit.*

44 Federations furnish developed regions with channels to assert their economic sway whereby they may circumvent the central state. In Argentina, provinces are constitutionally entitled to establish international trade agreements without interference from the central administration. The Spanish case bears resemblance insofar as AC have access to EU-lead forums such as the Committee of Regions in Brussels. In both instances, better-off regions can exploit more effectively these institutional prerogatives. Organizationally speaking, metropolitan regions have normally a more developed (*i.e.*, more unionized and, thus, susceptible to exacerbate class conflict) workforce than peripheral regions, creating a more contested political environment; PRZEWORSKI (A.) and

SPRAGUE (J.), *Paper Stones: A History of Electoral Socialism*, Chicago, University of Chicago Press, 1986.
45 The term *collaborative* is used to denote a lower level of co-decision powers in the formulation and representation of subnational interests than in the more entrenched and institutionalized *cooperative* type. Borrowed from Painter, who couched the former term to portray the Australian intergovernmental policy process, the *collaborative* type involves the creation of joint schemes of administration and authoritative intergovernmental and consultative bodies. In this respect, collaboration is more affected by bilateral dynamics and thus can be seen as a preceding phase to full-fledged cooperation; PAINTER (M.), *Collaborative Federalism: Economic Reform in Australia in the 1990s*, Melbourne and Cambridge, Cambridge University Press, 1998.
46 VAN HOUTEN (P.), *Regional Assertiveness in Western Europe*, Ph.D. unpublished dissertation, The University of Chicago, 2000.
47 AJA (E.) (1999), *El estado autónomico: Federalismo y hechos diferenciales*, Madrid, Alianza, 1999, p. 214-215.
48 In the United States, approximately half of the categorical (*i.e.* earmarked) grants require matching funds from the state and local governments, regardless of fiscal capacity considerations. For instance, in 1993 the federal government had 593 grant programs, of which 15 were block (*i.e.* unconditional) and 578 categorical; STOTSKY (J. G.) and SUNLEY (E. M.), in TER-MINASSIAN (T.), *op. cit.*, p. 371.
49 WEINGAST (B. R.), *op. cit.*