

Theory of Public Finance in a Federal State

The last few decades have seen a substantial increase in the mobility of capital and population between the individual jurisdictions of long-established federal states (such as Canada, Germany, and the United States) and among the formerly independent member countries of the European Union. This book examines the consequences of this development for government policy. Its central question is whether the assignment of government functions to the individual jurisdictions in a federal state can ensure an optimal allocation of resources and a fair distribution of income. The analysis thereby gives a new answer to the old question about the optimal degree of fiscal decentralization in a federal state. It shows that fiscal decentralization is a viable method to disclose the preferences of currently living and future generations for local public goods, to limit the size of government, and to avoid excessive public debt finance. The allocative branch of the government benefits from this decentralization, although it is difficult to obtain an income distribution much different from that induced by the market.

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