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**Institutional Aspects of Regional Policy: The Impact of Centralized vs. Decentralized Responsibilities in the Field of Regional Policy on Economic Efficiency and Interregional Cohesion**

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**Institutional Aspects of Regional Policy:  
The Impact of Centralized vs. Decentralized Responsibilities  
in the Field of Regional Policy on  
Economic Efficiency and Interregional Cohesion**

*Paper (Draft Version, July 2003) prepared for the*

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*by*

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***Abstract***

There are many studies on evaluating the impact of different instruments of regional policy on cohesion and economic efficiency, but only few investigations so far into the institutional framework of these instruments. One institutional aspect has become more and more relevant in public discussions: In federations (e. g. in the EU), we have a tendency of centralization in many fields of public policy, also in regional policy. Therefore, there have been made proposals in order to decentralize regional policy. The possible more central or more decentral arrangements of regional policy are located between two polar cases: At one pole, we have an arrangement where only the central level of government is responsible for regional policy; neither any subcentral unit of

government, nor the regions which are to be supported have any influence for deciding on regional policy instruments, and only the central government has to finance regional policy with its own resources. At the other pole, we find an arrangement where mainly the subcentral units of government and the less developed regions themselves are deciding on regional policy and are responsible for financing. The paper is evaluating the consequences of a decentralization in the field of regional policy, in the sense that the current allocation of responsibilities is changed in the direction of the described decentral arrangement of regional policy.

The paper comes to the result that there are only a few arguments to legitimate the central (European) competences in the field of regional policy. In any case, subsidy-control should remain a task of the EU level. As – at least in the case of Germany – the European system of regional policy has some advantages, as compared to the national system, a decentralization may not be favourable. With regard to the responsibility of financing regional policy, a decentralization would be better than the present state. But this does not mean that the more central units of government should no longer be responsible for shifting resources to the poorer regions. Change should take place in the sense that the supported regions are getting more leeway in deciding how to make the best use of these resources. But such a decentralized system will only work under several conditions.

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## **1. Introduction**

In recent years, there has been an ongoing debate on regional policy in Europe and the present member states of the EU. The main reason for this debate is the EU's eastern enlargement, which will lead to an increase in regional divergence within the EU. More or less all the regions in the accession countries have, up to now, a GDP per capita which is significant below the European average, what will make them eligible for European regional policy measures after the enlargement has taken place. The GDP per capita in the regions of the accession countries is also lower than the GDP per capita in the majority of regions within the existing EU which are supported today by European regional policy measures. After the enlargement, according to the *existing* rules of European regional policy, these regions will drop out of the system of EU regional policy – although their economic development problems will not have changed (for details see Rosenfeld and Kronthaler 2002). There are different proposals in order to help the regions in question after the EU enlargement (see e.g. Rosenfeld 2001; Akademie für Raumforschung und Landesplanung 2003). Some scholars and politicians are suggesting that the EU should expand its budget for regional policy and give not only support to the regions in the accession countries, but also to the regions which are supported today by the EU. Others are proposing that regional policy should be re-nationalized, at least for the existing member states.

Such a re-nationalization of regional policy is also favoured by the critics of an expanding – or even: overwhelming – EU level of government and is in accordance with general ideas of decentralization in the present system of EU administration, and also in national-subnational fiscal relations within the EU member states. In market economies, according to the principle of subsidiarity, the responsibilities for public activities should be in general allocated to the lower levels of government, as far as it has not been proven that an assignment of responsibilities to a higher level could lead to an increase in economic welfare.

As we have today, in fact, at the EU level, als well as in the EU member states, comparatively centralized arrangements of regional policy institutions, the paper is dealing with the question whether a more decentralized system in this field of public policy could lead to gains in economic welfare. Up to now, this question has not been discussed comprehensively. Many studies are evaluating the impact of different *instruments* of regional policy on interregional cohesion and economic efficiency. But

there are only few investigations so far into the *institutional framework* of these instruments.

The (dis-) advantages of a centralized system of regional policy have to be compared to a decentralized system. The possibilities of a decentralization are depending on the institutional settings of the EU-member states. As there are great differences in the public sector institutions among the EU member states, the paper is focussing on the situation of just one country: Germany. The German public sector has often been described as a “centralized federation”, the state level and the local level are in general dominated by the federal level of government. Like in other countries, Germany has established its own national system of regional policy, which is also dominated by the federal level. There have been many proposals to decentralize the German public sector, and some of these proposals have included the national competences for regional policy, (see e.g. Reform der Finanzverfassung 1998) but – so far – , as for the regional policy of the EU, there has been no detailed analysis of the benefits and the costs of such a reform.

After a short operationalization of the subject of this paper (see section 2), the general possibilities of a central vs. decentral arrangement in the field of regional policy are described (section 3). Section 4 is giving an overview on the present state of allocation of competences in the field of regional policy. Afterwards, it is discussed for different categories of competences, which costs and which benefits would arise if the present allocation of competences is changed in direction of a more decentralized system (section 5). The final section (6) is asking for the political implications of this discussion.

## **2. Operationalizing Regional Policy**

In economic theory, as well as in public discussions, there is often some confusion on the meaning of “regional policy”. Some scholars and politicians are identifying regional policy with all kinds of policy measures *of a region* which are oriented at economic growth. But in this view, there would be no difference between regional policy and economic growth policy in general. Therefore, in this paper, regional policy is defined as economic policy *for regions by policymakers from a higher level of government*. “Regional policy is always a policy ‘from above’” (Artobolevskiy 1997, p. 3), what means that a minimum degree of centralization is always necessary for regional policy. Other important features of regional policy are that

- “regional policy exists only when regions/areas receive unequal levels of support or rights from the state”(Artobolevskiy 1997, p. 3), what means that regional policy always includes an element of interregional redistribution,
- regional policy is trying to promote or stimulate private economic activities in certain regions (“supported regions”); regional policy is not aiming at only alimentating or compensating those regions which are economically lagging behind.<sup>1</sup>

The targets of regional policy are either growth- or equalization-oriented (cf. e.g. Eckey 1978). This means, that some concepts of regional policy are aiming at supporting the economic growth centers of an economy, in order to strengthen national economic growth. Or regional policy wants to shift resources and growth potentials from the growth centers to the less developed regions, in order to making them – in the long run – independent from outside support.

On the EU level, today, the so-called *structural funds* (the European Regional Development Fund, ERDF; the European Social Fund, ESF; the European Agricultural Guidance and Guarantee Fund, EAGGF) are the main instruments of regional policy. In Germany, the most important program of national regional policy is the federal-state-program „Improving the Regional Structure of the Economy“ (“*GRW-program*”<sup>2</sup>). Both the EU and the German programs are oriented on equalization and want to stimulate economic activities in the less developed regions.

### ***3. General Possibilities of Allocating Competences between Central and Decentral Units of Government in the Field of Regional Policy***

In each field of public policy, there are several possibilities of constructing intergovernmental relations (IGR). The responsibilities for regional policy could either be allocated to the central or to the decentral units of government. But – as had been discussed before, and differently to other sectors of public policy – at least some competences for regional policy measures have always to be allocated to a more central governmental level, which is able to give unequal levels of support to the less central units of government. As Figure 1 illustrates, the competences for deciding on the general targets of regional policy and for deciding on the supported regions have always to be reserved to the more central levels. “More central” does of course not mean necessarily the most central level of government, but only a level which is more central than the regions to be supported. Therefore, in a system of totally decentralized

competences for regional policy, the competences for deciding on the general targets of regional policy and for deciding on the supported regions have to be allocated to a middle level of government.

The responsibilities for deciding on the admitted set of instruments, deciding on the targets and instruments for specific regions, and for financing regional policy could be allocated to either level of government. In a totally decentralized system, the competences in question would be allocated to the governmental bodies of the supported regions.

Figure 1: Possibilities for IGR in the Field of Regional Policy.

level of gov.	deciding on				financing
	general targets	supported regions	set of instruments	targets and instruments for individual regions	
central	X	X	X	X	X
middle	O	O			
supported region			O	O	O

X = totally centralized arrangement

O = totally decentralized arrangement

In this paper's section 5, it will be discussed what are the consequences of changing the present allocation of competences in the field of regional policy in direction to a totally decentralized arrangement, as it is described in Figure 1.

#### ***4. The Present Allocation of Competences in the Field of European-German Regional Policy***

Figure 2 is showing the present allocation of competences for regional policy in the systems of the EU structural funds and the German GRW-program. In both systems, the decisions on the general targets of regional policy, on the supported regions, and on the admitted set of instruments are reserved to the EU level and the national (federal) level<sup>3</sup>, respectively.

The competence for deciding on the targets and on regional policy instruments for individual supported regions is a "joint responsibility", what means, that the subnational and the national level (in the case of the German GRW-program) or the subnational, national and the EU-level (in the case of the EU structural funds) are sharing the



responsibilities for this kind of decision. The subnational level, in Germany the state or “Lander” level, is responsible for developing so-called “operational programs” (in the context of the EU regional policy) and so-called “regional support programs”(in the context of the GRW-program); but these programs have to be approved by the EU level and by the German federal level, respectively.

The responsibility for financing is also a “joint responsibility”. The EU level is giving matching (special purpose) grants in aid to the Lander level. The federal level is also responsible for financing matching (special purpose) grants in aid to the Lander level. And in some cases, also the supported regions<sup>4</sup> are involved in (co-)financing regional policy measures which are intended to raise their potential for economic growth. This is true especially for financing expenditures for public infrastructure.

Figure 2: The Status Quo of IGR for European-German Regional Policy.

level of gov.	deciding on				financing
	general targets	supported regions	set of instruments	targets and instruments for individual regions	
EU	X	X	X	✕	✕
national	X	X	X	✕	✕
subnational				✕	✕
supported region					✕

X = responsibility of only one level

✕ = joint responsibility of more than one level

## 5. *The Incidence of a More Decentralized Allocation of Competences*

### 5.1 *Deciding on the General Targets of Regional Policy*

Are the political decision-makers on the higher levels of government more inclined to spend money for less developed regions than the decision-makers at the lower levels? Is regional policy for regions that are lagging behind a kind of a “merit good” (Musgrave), in the sense that it is necessary to force the decision-makers at the lower levels of government to help the less developed regions? (If this is the case, some critics of regional policy in general would, of course, always prefer a decentral arrangement of regional policy, in order to minimize the public intervention in the “natural” interregional allocation of growth and welfare which results from the market process.)

From the view of economic theory, the answer to this question depends on the political and economic structure of the jurisdictions at the more central resp. more decentral level of government. If we look at a jurisdiction L at the subnational (or: middle) level of government, the decision of the politicians from L for a growth- versus equalization-oriented regional policy will depend on

- the economic position of L, as compared to other jurisdictions at the same level of government (the higher the position, the more will the politicians tend to a equalization-oriented regional policy; they will tend to decide on a growth-oriented version of regional policy, if the economic performance of L as a whole is weaker than the performance of other jurisdictions at the same level of government. In the result of this decision, L as a whole may improve its performance, but at the price of increasing regional disparities within L),
- the degree of competition between L and its neighbouring jurisdictions (if there is not much competition, e.g. because of an existing fiscal equalizing system, the tendency for a equalization-oriented regional policy within the jurisdiction L will increase),
- the regional disparities within L (if the disparities are already relatively strong, the politicians will have a tendency for a equalization-oriented regional policy),
- the conditions on the „political market“ within L (if the politicians are elected in certain districts or delegated by the parliaments of certain subregions, they will have a stronger tendency to support the economic progress of their election-regions than if they are elected according to the rules of proportional representation. Public benefits for certain regions may be used by politicians to get more support by voters for their own policy in general or for the EU-level in general),

In general, the same arguments will also influence the decisions of politicians at the more central levels of government. But at a higher level of government (within a larger jurisdiction), the regional disparities will in general be greater than at a lower level. In addition, the degree of competition between jurisdictions will in general be higher at the lower than at a higher level of government. This leads to the conclusion that the more central units of government will have a stronger tendency towards equalization-oriented regional policy than the more decentral units. But it is impossible, from a theoretical point of view, to predict how large a jurisdiction must be for tending in this direction. Also another mechanism may work in the same direction. Ethnical minorities which are concentrated in some less developed subregions of L might find it easier to get support

for their subregions at the more central levels of government; the majority of voters in L could tend to neglect these subregions because of traditional prejudices against the minorities.

With a look at the present practice of regional policy, both the EU and the German federal level have decided for equalization-oriented arrangements of regional policy. Therefore, if the competences of the EU in the field of regional policy were shifted to the national level of government, for Germany, there would be no change in the general target of regional policy. A shift towards the subnational (in Germany: Lander-) level of government could lead to different results, but as – at the moment – most German Lander have no institutions for subnational regional policy of their own, we have not enough evidence for predicting what really will happen. According to the theoretical considerations, there could be expected a change into the direction of a more growth-oriented policy, but only if some other institutions like the system of fiscal equalization would be changed, too.

## ***5.2 Deciding on the Regions to be Supported***

In the following subsections of this paper, we will only look at the equalization-oriented kind of regional policy which is dominating in practice. If the politicians have decided for such a policy, in order to reduce interregional disparities, it is necessary to identify those regions which are to be supported by regional policy measures. If – as has been explained in subsection 5.1 – there is a higher tendency for the actors at the higher levels of government to equalization-oriented regional policy than for those at the lower levels, one could expect that the more centralized the decision on the regions to be supported is, the greater will be the number of such regions.

In the real world, the EU support for German regions is including (at the moment) mainly the so-called „Objective-1-Regions“, the so-called „Objective-2-Regions“, and the “Interreg-Regions”<sup>5</sup>. The German GRW-program is including so-called A-, B-, C-, and D-Regions, where the A-Regions are getting the highest, and the D-Regions the lowest level of support. The A- and B-Regions are located in East Germany, while the C- and D-Regions are regions within the poorer states of West Germany. The Objective-1-Regions are – at the moment – all regions in East Germany<sup>6</sup>. Objective-2-Regions are located in the more prosperous German states Baden-Württemberg, Bavaria, Hestia, Northrhine-Westfalia and Hamburg, as well as in the less prosperous West-German states Rhineland-Palatinate, Lower Saxony, Schleswig-Holstein, Bremen

and West-Berlin (cf. Entscheidung der Kommission 2000). The regions to be supported under the GRW-program are – at the moment – also all regions in East Germany and some regions in the West. As far as Germany is concerned, the Interreg-Regions are mainly the counties and cities alongside the German borderline. Interreg is designed in order to stimulate cross-border, transnational and interregional cooperation, especially for those regions which share external border with the accession countries.

A shift of competences from the EU to the German federal level of government would have two consequences: If the federal level will not re-adjust its federal regional policy, all the Objective-2-Regions in West-Germany will lose their support, and also the Interreg-Regions will lose their special support by the EU. Some of the regions which are supported by the EU (those which get support under Objective 1) are also GRW-regions. For them, their status as supported regions will not change at all (although probably the contents and the amount of support money will change).

The politicians of the present Objective-2-Regions may see the support of their regions by the EU as a contribution to improve their regional economic growth potentials. It is not realistic to assume that the federal level or the Lander level will replace the support from the EU level. From the view of economic theory, it is not easy to legitimate the EU support under Objective 2. Most of the Objective-2-Regions are situated in those German Lander which have, in general, no development problems. The Lander in question should be able to start their own, state-funded regional policy programs. The existence of a regional policy program for depressed areas in wealthier sub-national regions could be an incentive for the decisionmakers in those regions to neglect their depressed areas.

With regard to the border regions, we may expect that the federal level would establish special programs for them, if the EU programs should run out. In former times, there had been national German programs for border regions, e. g. for the regions along the inner German border („Zonenrandförderung“). But the set of regional policy measures could change. The Interreg-Program is aiming at measures in order to overcome the existing borderlines in Europe. The federal level might have a tendency to give help to the border regions only in order to stimulate their economic development, without taking into account the economic situation on the other side of the border.

It is not quite clear how the Lander level would react if the Lander would become responsible for defining the supported regions. As has been explained in the beginning of the chapter, the Lander will have less interest in equalization-oriented policy

measures than the central government. A decentralization from the federal to the Lander level in the case of the GRW-program would necessarily mean that for the East German Lander, regional policy for the whole territory has to come to an end, because the East German Lander as a whole are today supported by the GRW-program.

### ***5.3 Deciding on the Admitted Set of Instruments***

From the view of economic theory, we have no clues to answer the question whether a more central level of government is tending to favour other instruments for regional policy than a more decentral level of government. Sometimes it is suggested that at the lower level, we will find a stronger tendency to favour subsidies in order to protect and preserve the current pattern of regional industry. However, this assumption has not yet been proven.

On the EU-level, the instruments for regional policy are regulated in special orders by the EU commission on the structural funds. More or less the same regulations on regional policy instruments have been installed for the Objective-1-Regions, the Objective-2-Regions, and the Interreg-Regions. The EU regional policy is including a broad range of instruments. With regard to subsidies to private companies, the EU commission has established some general subsidy-rules, which have to be followed not only in the system of European regional policy, but also in the systems of regional policy at the other levels of the public sector. These subsidy-rules are limiting the subsidies to certain regions and are defining maximum rates of subsidies for private investment.

In the German federal system of regional policy, quite in contrast to the EU regional policy, only some few instruments are included: subsidies to private firms for private investment or for consultations by external experts or for training of employees or for research and development measures; grants in aid to local governments for “infrastructure for private firms”. A decentralization in the sense that the EU would give up its responsibilities in the field of regional policy would therefore lead to a shrinking set of instruments which could be used for supporting the regions which have development problems. From the view of regional economics, a more complex set of instruments is better able to meet with the complexity of regional development problems. This means, that without the present set of instruments which are allowed within the EU system of regional policy, the regional development problems of some

regions may not be dealt with adequately, so that their economic performance could be worsened.

From a theoretical point of view, it is not easy to explain why a national system of regional policy is narrower than the European. With regard to the German system, this may be explained by the institution of joint federal-state-commissions which have been installed for ruling the GRW-program. In such a commission, there is always a strong tendency for “minimizing the costs of agreement” (cf. Scharpf, Reissert, Schnabel 1976).

At least at present, a decentralization in the sense that the regional policy by the EU would come to an end, would lead to increasing development problems of the supported regions.

A further decentralization of the competences in question (to the Lander-level or even to the level of the supported regions) could – in theory – lead to more diversity in the range of instruments for regional policy. But at present, there is no evidence on the possible instruments the Lander or the regions would use if they would become responsible for deciding on the admitted set of instruments. From looking at other fields of public policy, one could expect that the Lander will tend to come to some kind of harmonization of their regional policy instruments, in order to limit interjurisdictional competition. The reason for this behavior may be seen in the typical German version of federalism, which is often called „executive federalism“, what means that the Lander are mainly governmental units which have to carry out what the federal level has decided.

A direct shift of competences to the regions to be supported could lead to different results: The policymakers in the supported regions could have a tendency for favoring subsidies to private firms, because of a stronger influence of pressure groups and private firms on policymakers at the lower levels of government, as compared with the higher levels. Consequently, the politicians at the more decentral level could tend to more inefficient decisions and perhaps to the support of regions with certain industries, which have no great future. As has been pointed out before, these assumptions have not yet been proven. But the regions, in contrast to the Lander level, could tend towards a greater variety in the set of instruments.

A decentralization in the field of subsidy-rules could lead to losses in efficiency. If the supported regions could decide on their own on the rates of subsidies for private investment, it could be expected that the competition for investors among the supported

regions leads to a race in direction of higher and higher subsidies. Only the wealthier regions would be able to take part in this race. And a relocation of firms from one supported region to another supported region is making no sense. Therefore, the supported regions should obey to subsidy-rules which are made by jurisdictions on the higher levels of government. But it is not easy to decide whether the EU-level or the national level of government should be responsible for the subsidy-rules.

#### ***5.4 Deciding on the Development-Targets for Implementing a Specific Set of Instruments in Specific Regions***

At present, in Germany, the Lander are responsible for setting up „operational programs“ (in the case of EU regional policy) and „regional support programs“ (in the case of German national regional policy), in which they have to specify the development-targets for the supported regions. The EU and the federal level in Germany<sup>7</sup>, respectively, have to agree to these programs and plans.

A more decentral allocation of competences could imply that the EU and the federal level would give up their present responsibilities in favour of the Lander level and / or that the supported regions could decide on their own about their future development.

It may be supposed that the actors in the regions to be supported have – because of asymmetrical information – better information on their regional problems and specific shortages than actors on the higher levels of government. But this argument of a higher diagnostic capacity of decentral units of government in the field of regional policy has not been proven so far. It may also be, that the actors on the decentral level of government have a tendency to favor inefficient measures, if they themselves have direct advantages from this measures. Such negative results are depending on the incentive structure. If the actors on the lower level of government have to co-finance the regional policy measures with their own resources, it may be expected that they are more oriented on efficiency. In contrast, if – as it is the case at present – the supported regions will get more money from the higher levels of government, if their situation has not improved in recent years, the actors at the regional level will tend to inefficiency (supporting firms that have no chance to survive, in the long run; subsidies for firms with a great influence on the regional labour market).

Have the plans of the Lander to be approved by the higher levels of government? It would be more important that the Lander should be forced to evaluate and legitimate their development strategies *ex post*. If the strategies of the Lander have not been able

to stimulate economic development, the decision makers at the Lander level must be responsible for explaining why the strategies did not work and what they are willing to do in the future in order to overcome the present problems.

### **5.5 Financing Regional Policy**

As has been explained before, regional policy is always a policy of a more central level of government in order to help some regions or jurisdictions at a lower level of government to improve their economic performance. This makes it necessary that a jurisdiction at a higher level of government is transferring some kind of resources to the supported regions: Either fiscal resources (grants in aid) or the exception from some legal standards (e.g. from the general ban of subsidies to the private sector) or the right to make such exceptions. In the real world, grants in aid are the dominant resources to be transferred. Therefore, in this section, the other kinds of transfers will not be discussed.

From the viewpoint of economic theory, those jurisdiction should be responsible for financing the grants in aid which have the competences for deciding on the general targets of regional policy, on the regions to be supported, on the admitted set of instruments and on the development-targets for implementing a specific set of instruments in specific regions. According to the principle of „connexity“ – as one element of OLSONs „principle of fiscal equivalence“ – only in this case, an efficient allocation of resources may be possible. If more than one jurisdiction is involved in the competences in question, all these jurisdictions should take part in financing the grants in aid. In the result we will find a kind of „mixed funding of public activities“ („Mischfinanzierung“). But such an arrangement will always lead to losses in economic efficiency. Additional losses of efficiency will take place if the grants in aid to the regions to be supported have the character of special purpose grants in aid, what is the case in the field of grants in aid for local public infrastructure:

- (a) Losses in Efficiency because of Mixed Funding of Public Activities (cf. Rosenfeld 1999 a; Rosenfeld 1999 b; Lichtblau 1999; Rosenfeld 2000; Rosenfeld 2002)

In the case of mixed funding and sharing of competences between different levels of government, the politicians have the possibility to act not in the way which their voters had wanted. The reason for this possibility is that such deviations may easily be explained to the voters with the decisions of the other levels of government. If the politicians at each level are acting this way, at last no one is feeling responsible for



wrong decisions. The voters are not able to find out who was responsible, because of the intransparency of intergovernmental decision making processes.

Apart from these problems, mixed funding is also inefficient because it leads to higher costs of bureaucracy, because administrative bodies are not only necessary at one, but at several levels of government (cf. e.g. Olbrich 1987).

The problems of a mixed funding of public activities are leading to the proposal that the mixed funding *and* the sharing of competences between different levels of government should better be stopped. A disentanglement of responsibilities would lead to more efficiency in regional policy. One way in this direction could be to give the competence for deciding on the development-targets for implementing a specific set of instruments in specific regions to the regions themselves.

(b) Losses in Efficiency because of Special Purpose Grants in Aid to the Localities

The potential recipients of grants have a tendency for applying for grant programs, even if there is no need for a special purpose grant. With the help of the grants, the policy makers at the decentral level of government are able to expand their budgets. “Cheap money from higher levels of government” is always a good argument for such expansion strategies – which will lead to losses in economic development. This is especially true in the case of matching grants in aid: The supported regions are not only applying for funds they do not need, they also have to spend their own money for less relevant activities.

Another aspect is that the policy makers at the decentral level may try to deceive the giver of the grants. If they try to adjust the description of projects (which may be important for the economic development of the supported regions) so that the descriptions are “well fitting” the criteria which are the conditions for getting the grants, it is not possible for the higher levels of government to direct the decisions of politicians in the supported regions. In this case, special purpose grants are making no sense at all.

Finally, if there are no grants in aid for an activity which may be of greatest importance for regional development, the decision makers in the supported regions will tend to wait till perhaps someday there will be a suitable grants in aid program. In the result, relevant infrastructure is still missing in the supported regions.

A solution could be to change the current grant programs into general grants in aid – only with the condition that the supported regions have to use the money they get

for improving their economic performance. Of course, the regions have to prove the effectiveness of their decisions.

## **6. Conclusions**

From the theoretical point of view, there are only a few arguments to legitimate the central (European) competences in the field of regional policy. Subsidy-control should remain a task of the EU level. As – at least in the case of Germany – the European system of regional policy has some advantages, as compared to the national system, a decentralization may not be favourable (as long as the German system is not ready to change). With regard to the responsibility to financing regional policy, a decentralization would be better than the present state. But decentralizing in the field of financing could not mean that the more central units of government should no longer be responsible for shifting resources to the poorer regions. The change should take place in the sense that the supported regions are getting more leeway in deciding how to make use of these resources. This will enable the decision makers in the supported regions to take the best measures for the development of their regions; but such a system will only work under some conditions:

- the decision makers of the supported regions must have strong incentives to spend money for programs which will lead, in the long run, to make their regions independent from support,
- the decision makers have to know which instruments and programs are most appropriate for this goal; at the moment, regional economic theory is not able for giving enough clues (specified for individual regional conditions) in order to facilitate this task; this means, that regional economic theory has to be improved as a precondition for decentralization in the field of regional policy,
- the decision makers have to account for their decisions, and the central level must have the right to cut further transfers to a region if the decision makers of a supported region are not able to explain why their region has made no progress (in direction to become independent from support from outside).

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## *Footnotes*

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- <sup>1</sup> The system of general revenue sharing (the fiscal equalization system) has the task of only alimentating the poorer regions.
- <sup>2</sup> „GRW“ means „Gemeinschaftsaufgabe ‚Verbesserung der Regionalen Wirtschaftsstruktur“, the German term for „Federal-state program ‚Improving the Regional Structure of the Economy“.
- <sup>3</sup> „Federal“ means in this case that a joint commission of federal and state governments is responsible for the planning process, and both the German parliament and the German upper house („parliament of the states“) have to approve the plans.
- <sup>4</sup> Respectively: the localities or the local level of government in the supported regions.
- <sup>5</sup> Interreg is (at present) one out of four “community initiatives”. The other three are “Urban”, “Leader” and “Equal”. From the view of regional policy, Interreg is the most important of these “initiatives”, therefore, only Interreg will be discussed.
- <sup>6</sup> Not including West-Berlin.
- <sup>7</sup> The federal-state planning commission for regional policy is responsible for this task.