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**Conference Paper**

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50th Congress of the European Regional Science Association: "Sustainable Regional Growth and Development in the Creative Knowledge Economy", 19-23 August 2010, Jönköping, Sweden

**Provided in Cooperation with:**

European Regional Science Association (ERSA)

*Suggested Citation:* Friedrich, Peter (2010) : Legal European company forms to realize FOCJ: Functional Overlapping Competing Jurisdictions, 50th Congress of the European Regional Science Association: "Sustainable Regional Growth and Development in the Creative Knowledge Economy", 19-23 August 2010, Jönköping, Sweden, European Regional Science Association (ERSA), Louvain-la-Neuve

This Version is available at:

<https://hdl.handle.net/10419/119116>

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# Legal European Company Forms to Realize FOCJ –Functional Overlapping Competitive Jurisdictions<sup>1</sup>

Peter Friedrich

## I. Introduction

Recently a special form of jurisdiction has been advocated, particularly by Bruno Frey (1997, 1999, 2001, and 2006) and Reiner Eichenberger (Frey, Eichenberger 1995, 1996, 1999, 2000, 2006), to perform public-sector tasks. They recommend – **functional, overlapping, competing jurisdictions** – known by the acronym FOCJ<sup>2</sup> – to supply citizens, firms and public economic units with specific public services. An individual FOCJ may sometimes be termed a **FOCUS**. Individual jurisdictions can compete for members and users. The FOCJ may be supranational and operate within the European Union. They should supplement the federal structure (Friedrich, Fladung 2006) of a state, which could be, for example, the European Union, the Polish Government, and Polish municipalities (counties and towns) or could be the European Union, federal government, state governments and municipalities (counties and towns). If they are to have a European-wide mandate, they would require an appropriate legal environment that enables them to operate successfully. This article analyses whether they could be a tool for cross-border public management and cooperation. We discuss the following questions:

- What are the features of FOCJ?
- How can we model them to integrate them in economic theory?
- What difficulties arise for cross-border FOCJ?
- Which European forms of legal entity exist for cross-border FOCJ?
- How can FOCJ be combined with other forms of public cross-border management?

## II. Features of FOCJ

FOCJ should, according to Frey (1997), have the following **properties** (c.f. Weigel 2008):

- FOCJ may perform various functions or tasks; their size depends on the kind of functions they are responsible for

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<sup>1</sup> This paper is written with support from the Ministry of Science and Education foundation project No SF0180037s08 “The path dependent model of the innovation system: development and implementation in the case of a small country”(University of Tartu)

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<sup>2</sup> In literature the FOCJ are referred to as a FOCUS in the singular.

- They can overlap in their operations as due to their functions (e.g. schools), there might be several of them acting in one region and supplying the same services
- The FOCJ compete for members who might be citizens or municipalities. The FOCJ should have a democratic structure, clearly showing decision-making bodies such as assemblies of members and with published procedures like majority decision making rules.
- The FOCJ should have a “taxing power” and the power to fix fees and contributions of the members.

FOCJ can have obligatory or free **membership**. The tasks of the FOCJ would have to be at least partly funded by their members. Members may leave one of the FOCJ and participate in another. If there is no obligatory membership, members can quit. Economic implications concerning the procurement, production, marketing and finance (Friedrich, Fladung 2006) are not often discussed although there have been many historical examples of FOCJ<sup>3</sup>. There is little literature on their decision making procedures (Nowotny, pp. 132) and features of their chosen management methods. To compensate, findings from studies of economic units with similar characteristics may be applied. Therefore, we can investigate studies of cooperatives, associations, public special-purpose associations, clubs and many non-profit institutions. The literature on clubs discusses the club size, special club goods, club rules (Buchanan 1965 ).The literature on multiple-decision makers in a council and public choice approaches (Shughart, Razzolini 2001) can provide useful hints. The literature on the **application of FOCJ** is not rich. Examples are mentioned such as Swiss school municipalities and some contributions deal with business promotion (Detig, St., Feng, X., Friedrich, P. 2002), FOCJ in regional competition (Friedrich 2002), population policy (Friedrich, Popescu 2006), technology cooperation (Bartholomae, Popescu 2008), health organisations (Friedrich 2006), and forestry (Spindler 2008).

FOCJ may differ considerably according to their internal structures and tasks, and they vary particularly in terms of their membership. One should consider **four kinds of FOCJ**:

- **FOCJ- type I** with citizens as members, e.g. municipalities without territories. Citizens living in various municipalities establish a FOCUS to provide services.
- **FOCJ-type II** with governments as members, e.g. municipalities, counties, states, national states, European Union) also to provide services.

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<sup>3</sup> E.g. leagues of cities (Hansa), defence alliances (NATO), ecclesiastical orders (augustines), colonial companies (East India company), chambers of commerce, functional municipalities Switzerland (Spindler 1998; Spindler 2008a) and USA (Mehay 1984), in some countries personal jurisdictions such as churches, social insurance, etc.

- **FOCJ-type III** comprising municipalities, other governments, other subjects of public law and of private law (firms, etc.).
- **FOCJ-type IV** with members who are natural persons, and /or private and public legal persons (e.g. citizens, associations, chambers, churches, municipalities, private and public firms).

**Cross-border FOCJ** would have members in several EU member countries. Within a national member state cross-border FOCJ can exist if members belonging to different sub-states join FOCJ.

In literature the authors (see Frey 2006) deal mostly with the **first type-I FOCJ**. Forming these FOCJ makes major constitutional changes necessary. Therefore, these types of FOCJ are really utopian but also strongly recommended (Frey 2000). Examples of type I FOCJ exist in Switzerland and the USA. Establishing them is difficult **within member states** of the **European Union**. Even member states of a national federation such as the Länder of the Federal Republic of Germany (FRG) heavily restrict membership. If a municipality wishes to join Type II FOCJ the Länder allow an internal state cross border FOCJ of municipalities only with special permission from the respective state (Land). Normally a state contract – between Länder or between EU member states – is necessary (Detig, St., Feng, X., Friedrich, P. 2002). Within one state (Land), **type II FOCJ** are possible for municipalities that form FOCJ in public law. In some German Länder and in other EU member states private legal persons can also participate in, **type III or type IV FOCJ** in public law. In private law, forms II to IV can be possible if the legal structure matches the FOCJ features mentioned above.

In Poland and Germany (Detig, St., Feng, X., Friedrich, P. 2002; Leitenstorfer A, Török A. 2008) similar legal forms of private and public law are available at least to form FOCJ of types I to III. There are **capital oriented forms of private law**: the joint stock company (Spółka akcyjna (S.A.)), the limited liability company (Ltd) (Spółka z ograniczoną odpowiedzialnością (sp. z o.o.)), the limited stock partnership (Spółka komandytowo akcyjna (S.K.A.)), and state-owned enterprises (przedsiębiorstwach państwowych). The three first forms exist in Germany too. Especially with the **joint stock company** it is not easy to construct FOCJ which match FOCJ characteristics. A joint stock company can concentrate on a function, there can be several joint stock companies supplying the same service in a territory, members can leave and join through trade of shares, but the membership is not really tied to receiving services from that company. Although the finance and decision-making power is very restricted as most decisions are taken by the board of directors. Mainly decisions changing ownership structures are within the remit of the general assembly. It can decide about new capital raised from owners and other key issues. The normal prices for services are fixed by the board of directors perhaps in cooperation with the supervisory board. Only actions according to private

laws on the basis of contracts are possible. An ownership structure closer to the FOCJ structure is that of the **limited liability company** and the **limited stock partnership company** where, at least internally, a company contract and statutes can provide a structure which matches the features of FOCJ. The members can decide on fees, contributions to finance, etc. And influence the decisions and policies of directors. Again the members and their FOCJ have only legal options provided by private law. The **state-owned companies of Polish law** are more suited to a form of company law to deal with the former “people-owned” socialist firms. They are not appropriate to form a typical FOCJ structure.

Moreover, legal forms of co-operatives established by natural or legal persons (spółdzielni europejskiej), of association (stowarzyszenie), and of a private foundation (fundacja prywatna) are available. The **co-operative** is a legal form that comes very near to the FOCJ requirements. It can have natural persons, persons of private law and of public law as members. Its activities are mainly intended to promote the members themselves. Services to non-members are possible. Leaving and joining the cooperative is possible according to rules fixed in the statutes. Rules for financial contributions of members are set out in the statutes and the influence of the general assembly of members on pricing can be assured. This company form can permit meeting the requirements of FOCJ, but it can only be applied for activities under private law. The **association** does however allow creation of FOCJ structure if the founding members agree to a statute that matches the requirements of the FOCJ. If the association wants to achieve tax privileges it normally cannot benefit the members in terms of income increases. The association can comprise private and public members as well. The members can leave or join they are free to use the services of the association. Financial commitments can be formulated as necessary. Again there is the limitation to actions of private law. The **foundation of private law** is not member oriented; it represents financial and real resources dedicated to promote some private tasks. Normally, it is not suitable for FOCJ.

In Poland there are also company forms of public law, which are: the public corporation (person oriented governments, special purpose associations, associations of public law), public law institutions (środki specjalne), and public foundations (e.g. Fundusze celowe). Then there are public entities that are not legally independent such as the legal dependent agency (jednostki budżetowe) and legal dependent funds (gospodarstwa pomocnicze). The legally dependent forms cannot be used as FOCJ –which must have their own legal personality. The public law institution and public foundations do not possess the membership structure needed to form FOCJ. Special purpose associations are appropriate for FOCJ mainly if they concentrate on members of public law such as municipalities or on private members, as far as the laws allow their engagement as members, such as private firms or public firms of private law. Here the actions belong to the sphere of public law. The membership structure,

the financial obligations of the association and its members, the options to join and to leave the public corporation coincides with the FOCJ requirements, especially with those of Type-II, and as in some German states with type-III and type IV.

Although no constitutional provision for type-I FOCJ, e.g. a municipality without territory, is provided, legal forms to establish FOCJ do exist in European countries, e.g. Poland and Germany.

**Figure 1: Existing national legal forms for FOCJ**

Legal Form	Function	Com- peting	Democ- ratic	Public Mem- bers	Private Mem- bers	Power to finance	Public law	Private law	FOC J
Joint stock company	X	X	-	X	X	O		X	O
limited liability company (Ltd)	X	X	O	X	X	O		X	O
Limited stock partnership	X	X	O	X	X	O		X	O
state-owned companies of Polish law	X	O	-	X	O	-		X	-
Enterprise run by a natural person	X	-	-	-	-	-		X	-
Civil partnerships Civil code	X	O	O	O	X	O		X	O
Civil partnerships Commercial code	X	O	O	O	X	O		X	O
Limited partnership	X	O	-	O	X	O		X	-
Polish partnership	X	O	O	-	X	O		X	-
Co-operatives	X	X	X	X	X	X		X	X
Association	X	X	X	X	X	O		X	X
Foundation of private law	X	-	-	O	X	-		X	-
special purpose associations	X	X	X	X	O	X	X		X
Personal governments	X	O	X	O	X	X	X		O
public law institution	X	O	-	X	-	-		X	-
public foundations	X	-	-	X	O	-	X		-
legal dependent agency	X	O	-	X	-	-		X	-
legal dependent funds	X	-	O	X	-	O		X	-
Territorial governments	O	-	X	-	X	O	X		-

X strong relation or appropriate, O weak relation or difficult to realise, - no relation or inadequate, **Source:** author's compilation

Turning to cross-border FOCJ between member states of the European Union, the national member states do not like to allow a citizen to be under the authority of a municipality located in another state and at the same time in its

own state. This is true for Type-I FOCJ but also for some other FOCJ. Therefore, cross border FOCJ of public law need special contracts between the member countries of the EU. FOCJ of private law are possible, but difficult to form. An example of a FOCUS in public law is the **European Union** itself after the Lisbon treaty was ratified. It covers the basic features of FOCJ.

### **III. Cross-Border FOCJ**

Within the European Union the need for public **cross-border co-operation** has developed for several reasons:

- The public sector and its public economic units are themselves partners in the EU common markets. They deliver services of public interest and other services and goods by public offices or public enterprises.
- Sometimes there are cross-border dependencies in production, in procurement, in delivery and because of the common financial markets also in public finance and also in public revenues.
- Industrial structures and clusters develop across borders with public agencies, public offices and public agencies involved.
- Functional regions, e.g. labour markets extend across borders.
- Transportation infrastructure in transportation, water provision, electricity and energy provision is becoming more international
- Personal and cultural infrastructure also develop across borders
- European cross-border regions develop that compete with other regions
- Bilingual cultural regions not following national borders gain importance as in medieval times
- Safety issues, social service problems, health problems are on the agenda for cross-border solutions
- Leisure and tourist regions integrate across borders
- External cross-border effects operate.

Cross-border FOCJ might be a tool to address such problems. However, as there is no European legislation for a **type I, FOCJ** are difficult to form. A type-I European regulation or a respective directive is hard to achieve. About 27 member states have to agree and each of them has to change their constitution to allow at least for a new type of municipality. Public law legislation in particular, is a task of the member states – as long it does not interfere with the common market or counteract EU policies. A type-I is dominantly under the power of the national states where the public sector is shaped rather differently and the need for such an institutional reform will not be felt everywhere. There are two ways to form the other types of FOCJ. One is to apply the legal company forms which are available in the framework of national law as discussed above or the other is to apply European forms of company law.

The national ones could use the **co-operative** with domestic public members and members who come from abroad. However, the law of the country of the FOCJ has to be considered. The stipulations there may not benefit the members from abroad and they may face unfavourable conditions at home. This is also the case with an **association**. Here the national laws may be even more restrictive. Sometimes donations are not allowed to an association that is situated in another country. One would then have to consider capital-oriented legal forms of companies, such as the limited liability company with FOCJ-style statutes. The owners of these companies are indigenous or from abroad and represent municipalities or other public or private legal persons thus creating type-II or type-III FOCJ. The other two firm types may serve as well. However, these forms are restricted to private law activities and the owners are subject to the national law system of FOCJ location and if they are from abroad, additionally their national law system, for example with respect to taxation. Therefore these kinds of FOCJ encounter the following difficulties:

- There are **27 legal systems** with different conditions determining the establishment, merger, purchase, and closure of firms in the common market area - making cooperation and operation rather complicated in different markets and regions. This concerns the FOCJ according to their task and their regions of operation.
- It is difficult to change the **location** of a firm and also of FOCJ of private law from one country to another, as in one country the firm has to undergo a liquidation procedure and then be re-established in the other country.
- **Different legal and organizational requirements** have to be met with respect to capital size, reserves, guarantees, decision making, monitoring, auditing, accountancy, assessment of assets, taxation, social standards, etc. This makes management of FOCJ producing and selling cross-border within the countries of the European Union very difficult and hinders competition.
- Severe **transaction costs** are caused that make cooperation and FOCJ less attractive
- The **workers codetermination** is different in the member countries. This causes difficulties within the FOCJ and influences the regional distribution of production, and investment, and movements of FOCJ among member countries.
- The **publicity conditions** are different. The conditions to apply competition laws differ. Further difficulties arise for taxation and to determine the legal location of decision making, management and production whether in the centre of a FOCUS or in FOCJ subsidiaries.
- As management has become very powerful within companies in EU. The EU hierarchy wants to strengthen the position of firm owners and of stakeholders in firms. Therefore, more equal **corporate governance** is going to be introduced within the common market. The corporation forms and laws may become more equalized but only in the long run.



- To create a new legal individual form for **FOCJ of type-II by contracts** between neighbouring EU member states is costly, takes a long time and bears many legal and political risks.

To reduce the respective difficulties one may embrace the European legal company forms that are created to enable cross-border cooperation among economic units of EU-member countries, including the countries of the European Economic Area such as Norway, Iceland and Lichtenstein as well. We therefore analyse whether there are any opportunities to develop FOCJ on the basis of the following **existing European legal company** forms:

- European Company – Societas Europaea (SE)
- European Economic Interest Grouping (EEIG),
- European Cooperative Society – Societas Cooperativa Europea (SCE)
- European Grouping of Territorial Cooperation (EGTC)

Suggested and included in the **legislation procedure** are the following forms:

- European Private Company - Societas Privata Europaea\_(SPE) European mutual society (ME)
- European Association (EA)
- European Foundation (EFS)

The European private company is expected to be decided on this year. At present three kinds of European companies of private law and one of public law exist.

**Figure 2: Existing European companies**

	Poland, Companies Existing	Germany Companies existing	Europe, companies existing 2010
European Company SE	0	131	348 (since 2004)
European Economic Interest Grouping EEIG	1	301	1687 (since 1989)
European Cooperative Society SCE	0	1	7 (since 2008)
European Grouping of Territorial Cooperation EGTC	0 <sup>4</sup>	0 <sup>5</sup>	5 (since 2008)

**Source:** Libertas Europäisches Institut 2010

<sup>4</sup> One is in Poland/Germany in preparation: Oderland NadOdrze (DE,PL).

<sup>5</sup> 3 more are in Germany in preparation

Since 2004, the supranational **European stock company**<sup>6</sup> (SE) has existed in the EU (European Commission 2010). The regulations concern **the establishment, capital, and organization** of the company. Other matters are subject to national legislation. About 40 % of the European stock company law is European regulation, 60% are national stipulations, e.g. Polish state laws. The member states, e.g. Poland, formulated national laws to realize the European company. Therefore many country specific solutions still exist, e.g. the one or two tier management and workers participation. It is important that owners can come from different countries – at least two member countries. The number of European stock companies in Europe (figure 2) is increasing. The management can be more effective because of **reducing the mix** of different national company forms. It may be enough to have one SE and branches in other countries. **Changing location** and merging becomes easier as firms can transform, merge and establish holdings. However, the company form is only appropriate for **large firms** and those firms where a high degree of worker participation already exists.

The SE is partly restricted to **multiple country firms** with the exception of the transformation of a national company. An SE is expensive and it needs a higher **minimum capital** level, especially compared to a Polish joint stock company. However, the European SE promotes **large scale co-operation**. It can be used for production, sales and project activities. Also a public enterprise in the form of a joint stock company can be involved. A public body may participate in a SE. Competition exists if there are different SEs supplying the kind of service needed or if an SE competes with others to deliver services to member owners. However, European procurement laws (Schwintowski 2007; Kluth 2009), may require tenders and auctions that may preclude a municipality from buying through its own FOCJ, because the use of FOCJ may not be considered an in-house business. A solution might be to use yardstick competition<sup>7</sup> showing that the FOCJ supply is the cheapest and most economic purchase, thus avoiding the need for a tender.

A **European Economic Interest Grouping (EEIG)** (Zahorka 2001, Friedrich 2008) is a person oriented type of legal company form of private law. The **European basic regulation** is the same in all EU Member States. An EEIG<sup>8</sup> consists of at least of **two members** from separate EU countries. The members can be companies or **legal bodies of a member state** or natural persons. **A public body** can join an EEIG. They operate in many **sectors**: the craft sector, research and development, consultancy, personnel exchange and staff development, tourism, agriculture, forestry and the food industry, aquaculture, social services, sports promotion of business, promotion of EEIG

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<sup>6</sup> There are **two European laws**. A regulation on the statute of a European Company SE(2157/2001) (European Union 2001), and a directive on workers codetermination (2001/88/EG of 2001) European Union 2001a).

<sup>7</sup> The public buyer decides and proves that buying from his own firm or FOCJ he belonged too - his in-house solution - is better than alternative market offers.

<sup>8</sup> c.f. Council Regulation (EEC) No 2137/85, European Union (1985).

project planning and realization. The **objective of the grouping** must be to encourage co-operation between the partners and thus increase and improve their economic results. Therefore, many objectives are possible. They can range from profit attainment, to improved service provision, to realization of projects and improved planning. The statutes or the founding contract can contain a **minimum of regulations** or it may comprise a collection of stipulations determining FOCJ structure. The withdrawal of members, the selling of membership and the rights of new partners as well as leaving conditions can be fixed. The **members are the sovereign organ** of the EEIG. Their voting power may be related to the number of participants, their shares, or other indicators, etc. However, no one should be assigned a majority of votes. The members supervise the company. The EEIG, like FOCJ, has a **management organ**. The members are bound by the acts of the managers in relation to third parties. Managers' powers can be specified and restricted and additional organs can be established. The EEIG needs no **start-up capital**. The group cannot issue bonds, shares etc. Equity capital can be increased through member capital or the creation of reserves during the operation of the company. Debt finance through loans and the like using banks and an insurance company is possible. The **financing of operations** serve membership fees, resources submitted by members, member's current accounts and money from projects, sales and equipment provided by members. Guarantees can be provided on the basis of the assets of the EEIG, and through guarantees from other institutions. Members have to guarantee the debts. The EEIG is taxed according to the **taxation** prevailing in the member state of location. Profits or losses are passed to the members who declare personal income tax or corporation income tax. An EEIG is subject to VAT. Contributions by members that just share the costs of the EEIG are exempted. Because of the flexibility of an EEIG, FOCJ structures can be created. However, there must be competition. This can be arranged by competing FOCJ in one country or another country where municipalities, etc. are members (Type II to Type IV FOCJ). A more severe problem is again whether a public member can use the FOCJ without arranging a tender or auction. As the FOCJ is of private law origin there are doubts whether an in-house business can be assumed. Until now services of special purpose associations are accepted as in-house businesses. There is again the hope that yardstick competition showing that the FOCJ supply is the cheapest and most economic purchase is accepted to prevent the need to go to tender. However, no case on that matter has yet come before the European court. The EEIG is used for public cross-border public co-operation but not in a FOCJ framework. For some services a FOCJ situation and institutional structure may be used.

Another European legal company form appropriate for cross-border FOCJ operation seems to be the **European Cooperative Society (SCE)**<sup>9</sup>, which is a

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<sup>9</sup> Council Regulation (EC) No 1435/2003 of July 2003 (European Union 2003).

legal person of private law with European wide basic regulation. A SCE can be founded by: 5 natural and legal persons of **private and public law** that are residents of different member-countries or are subject to the law of two different member-countries. The main purpose of an SCE is to serve the needs of the members or to promote their economic or social activities by delivering goods or providing services. There can be also investor members who do not use the services. There can be **three organs** (two-tier, dualistic system) a management board, a supervisory board and a general assembly. The statutes can consider the FOCJ needs of membership changes, voting, etc. The SCE can be financed by **own capital** payment of capital shares from members, reserves and profits. It can be financed through sales and through short term and long term **debts**. The SCE can be active in banking and insurance business. An SCE can **relocate** to another member state without having to be wound up and re-register. Competition can prevail between cooperatives acting as cross-border FOCJ or against other service providers. Although FOCJ structures can be created cross-border, there remains again the problem of tender and in-house business. This problem has not yet been solved.

A legal form of public law is the **European Grouping of Territorial Cooperation (EGTC)**<sup>10</sup>. The European Grouping of Territorial Cooperation (EGTC) is a new community legal instrument at the service of public entities willing to develop projects and activities of common interest in the field of territorial cooperation. (Interact 2008). **Four main models of EGTC** are possible: EGTC in order to implement territorial cooperation programs (European Territorial Cooperation programs). EGTC for implementing co-financed projects in the field of territorial cooperation under the Structural Funds (ERDF, ESF, Cohesion Fund), EGTC for the purpose of carrying out other EU-funded territorial cooperation actions, and EGTC in order to implement territorial cooperation actions outside of any EU funding. For purposes of FOCJ the fourth alternative is important.

An EGTC must be composed of **members from at least two Member States** belonging to the following categories: local and regional authorities, other public entities or public-equivalent bodies, associations of public entities and, finally, member states (national level). **Bodies governed by public law**<sup>11</sup> are also eligible for participation in an EGTC<sup>11</sup>. **Associations** can become members of an EGTC even if they are private-law based, as long as they fulfil the criteria applicable to bodies governed by public law. **Public enterprises of**

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<sup>10</sup> Regulation (EC) No 1082/2006 of the European Parliament and of the Council of 5 July 2006 (European Union 2006).

<sup>11</sup> A “body governed by public law” means any body: established for the specific purpose of meeting needs in the general interest, not having an industrial or commercial character, having legal personality and financed, for the most part, by the State, regional or local authorities, or other bodies governed by public law; or subject to management supervision by those bodies<sup>11</sup>; or having an administrative, managerial or supervisory board, more than half of whose members are appointed by the State, regional or local authorities, or by other bodies governed by public law (Interact 2008, p.13).

**public** law may fit and those of private law that are dominantly owned by public owner and acting in the general interest. Therefore, type-II and partly III or type IV, FOCJ are possible. **The establishment of an EGTC** should not be a goal in itself **but a means to reach other goals**, such as long-term strategic developments, management of public services, program management, etc. The EGTC can be used as an **instrument for integrated territorial (multi-level) governance** in coherent areas split by borders. The **objective and tasks** of an EGTC are laid down by its members in the convention.

An EGTC can be established to manage a specific action or project (**'uni-functional EGTC'**), or it may function as a cooperation platform with several missions/tasks (**'multi-functional EGTC'**), including coordinating a joint development and/or solving common problems arising in the cooperation area. **Services of general interest** that are a competence of all EGTC members, e.g. managing public facility equipment for the implementation of a service of general interest (transport, health, education, etc.) are not purely commercial but imply a payment by the end-users for the services provided by the EGTC – although often the price does not cover the real costs of the services but only part of them, the rest would be covered by the members of the EGTC. An EGTC shall have at least the following organs: an **assembly**, which is made up of representatives of its members; a **director**, who represents the EGTC and acts on its behalf. The statutes may provide for **additional organs**. Managing its own budget enables the EGTC to hire its **own staff and acquire property**.

Contributions by the members dedicated to the EGTC in terms of assets or money donations occur upon **establishment**. Then there is current finance by members, by sales and debts, grants of the EU or other public bodies. The **annual budget** should contain a component for running costs and, if necessary, an operational component (project-related budget). It is not compulsory that all members participate financially. **In-kind contributions** by a member may also be considered, for example provision of staff, office space or equipment. In terms of share of contributions, there is no set rule. Various **agreements on contributions** may be reached perhaps including: equal contributions by all members; a split of financial contributions between each member state; a split of contributions among members on each side of the border; or contributions could be calculated on the basis of the population in each member's territory. The EGTC is established by working out a convention on name, members, objectives etc. which has to be accepted by the members. The convention serves as the **basis** for the statutes comprising organs, decision rules, voting procedures, financial contribution of members, etc. Managing its own budget enables the EGTC to hire its **own staff and acquire property**.

Therefore, a FOCJ structure can be created and the FOCJ can deliver services to its members. As it is of public law, and services are supplied under public law and especially if all members are public bodies, it is easier to nominate it an in-house business as no tenders are necessary by the receivers. If there is

competition among the FOCJ and other private suppliers, there will be a doubt how special purpose associations will be treated in future. On the one hand the EGTC is a European law form, which is promoted by the EU and on the other hand such cross border activities are regulated by EU. Special purpose associations on the national level often deal with services of a regional character where Europe-wide competition is not so important. Of legal interest are strategies to use the EGTC as a public member in FOCJ of private law, (e.g. EEIGs or SCEs). Between them a Public Private Partnership (PPP) is established. Although the legal circumstances are difficult the EGTC could be used as a cross-border FOCJ. In the coming years, other European legal forms mentioned above may become available as well.

Other possibilities such as bilateral or plurilateral agreements and treaties (i.e. öffentlich rechtlicher Zweckverband Euregio Rhein-Waal and Ems-Dollart, Benelux Convention of 1989) can be used as well as could formal agreements on cross-border cooperation, such as local working communities and cross-border purpose associations (Interact 2008, pp.108). They may lead to cross-border public law FOCJ of type II; however, they have to fit into both national law systems. The Madrid Outline Convention of 1980 (European Union 1980) and its Additional Protocols (1980, 1995, and 1998) (Interact 2008) merely provide a framework of cross-border cooperation in the EU. This framework has to be filled in by treaties or by using European forms of company law.

#### **IV. Theory of Cross-Border FOCJ**

The cross border members of FOCJ have to decide, which resources should be dedicated to the FOCJ. For the sake of simplicity, we address type-II FOCJ in the form of EGTCs or special purpose associations as part of a cross-border treaty or agreement that has municipalities of two EU member states as members. The founding members and the resources brought in must be determined. Such resources might be expressed in monetary terms (financial means, real estates, existing buildings, infrastructure, etc.) and named as  $x$ .  $x_i$  shows the resources brought in by municipality  $i$  and  $\sum x_j$  ( $j=1, \dots, n$ ) shows the total amount of resources  $X$  dedicated by municipalities to the FOCUS.  $X_R$  depicts the total resources of the FOCUS without those of the municipality  $i$ . The possible number of towns is indicated by  $n$ . The town  $i$  expects advantages from cross-border activities by the FOCUS and expects higher advantages from its engagement in the FOCUS if the share of its resources in the FOCUS increases<sup>12</sup>. These advantages are expressed by the parameter  $c_i$ . These advantages might depend on the kind of service, the commercial gain, the kind of town, its geographical position, transportation situation, its size, economic

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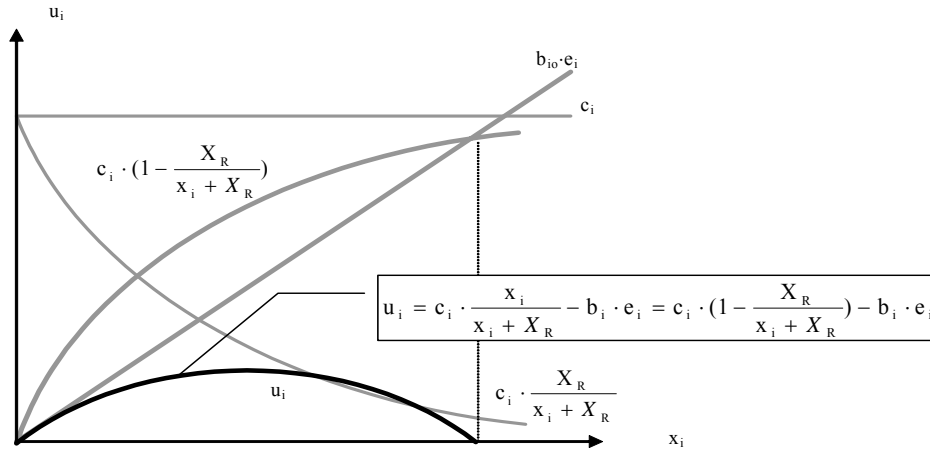
<sup>12</sup> There might be time savings, better use of existing capacities, quality increases, a broadened service program, more tourism, and utility gains for citizens, etc.

structure, languages spoken, nationality, etc. The dedication of resources by a town to the FOCUS shows also some negative effects<sup>13</sup> captured by the parameter  $b_i$ <sup>14</sup>.

We obtain a utility function of town  $i$  (c.f. figure 3):

- (1)  $u_i = c_i \cdot (x_i / \sum x_j) - b_i \cdot x_i$ ; (2)  $X_R = X - x_i$ ;  
(3)  $u_i = c_i \cdot (x_i / (x_i + X_R)) - b_i \cdot x_i = c_i \cdot (1 - X_R / (x_i + X_R)) - b_i \cdot x_i$ .

**Figure 3: Utility development of town  $i$**



In case of  $n$  candidates the uncertainty about the strategies chosen by other communities' increases. Therefore, we assume that the municipalities retreat to a simpler autonomous strategy that means that one municipality maximizes utility under the assumption that the others do not react, that means  $X_R$  (see equation (2)) the offers of the other partners remain constant. The solution found refers to an approach devised by Cornes and Hartley (2001). The utility function (1), (3) becomes maximized<sup>15</sup>:

The optimum share of resources in the FOCUS turns out (c.f. figure 4) to be:

(4)  $x_i / X = 1 - (b_i / c_i) \cdot X$

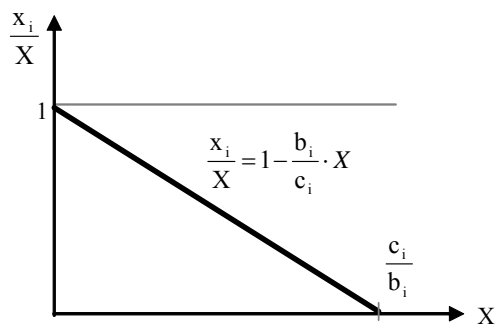
The optimal solution that leads to the optimal number of communities and the adequate volume of  $X$  is determined by the establishing managers where the sums of the values of the optimal shares add up to one (c.f. figure 4). To participate in FOCUS the cost/benefit ratio must be smaller than the average of the sum of other members of the FOCUS.

**Figure 4: Solution of FOCUS formation**

<sup>13</sup> Such as loss of centrality of the town, movement of buyers to places abroad, higher transportation times and other unfavourable effects on achievement of municipal goals.

<sup>14</sup> Other forms of  $b_i$  can be treated as well (Friedrich 2002, pp. 248-250).

<sup>15</sup> (4)  $du_i / dx_i = c_i (x_i / (x_i + X_R)^2) - b_i = 0$ ; (5)  $x_i = \sqrt{(c_i / b_i) \cdot X_R - X_R}$ ;  
(6)  $x_i = \sqrt{(c_i / b_i) \cdot (X - x_i) - (X - x_i)}$ ; (7)  $X = (c_i / b_i) \cdot (1 - (x_i / X))$ .



Many times favourable benefit/cost relations develop for neighbouring municipalities that are going to form a FOCUS and thus delegate part of their competences to the FOCUS. Competition among existing FOCJ can be considered in extended models. Municipalities, which do not like to join FOCJ, have low  $c$  parameters. They have a high preference for self-produced services and accept high opportunity costs.

There is also a model available to show the determination of the current contribution the members have to pay to receive the type-II FOCUS services. The members of a FOCUS have to cover a share of the operating costs of the FOCUS<sup>16</sup>. For the sake of simplicity we assume that current costs are to be covered by the members. The members have to pay a contribution that is equal to the costs per service unit. The usage of the services of the FOCUS also depends on the contribution to be paid. If the costs are high less usage is made of the capacities of the FOCUS services.<sup>17</sup> An added up demand curve of all members exists for the services of the relevant FOCUS depending on the level of cost contribution per service unit the municipalities have to pay. The FOCUS possesses a management that shows a utility function related to the production and labour input of the relevant FOCUS.

If the rule of cost coverage is stipulated and the management has the right to fix or to suggest the contribution rate, on the basis of costs the following results are obtained. The model comprises a modification of a fee determination model (Friedrich 1998; Friedrich, Kaltschütz, Nam 2004).

It comprises:

- A utility function  $U$  of the public firm's management depending on output  $X$  and labour input  $L$ .

$$(1) \quad U = U(X, L), \quad \partial U / \partial X = U'_X, \quad \partial U / \partial L = U'_L$$

- A restriction concerning the production function. There is one fixed factor  $A$  and there are two variable production factors,  $L =$  labour and  $C =$  materials.

$$(2) \quad X = f(L, C)$$

<sup>16</sup> Some costs, e.g. interest payments, normal amount of teacher services, etc. might be paid by the central state.

<sup>17</sup> If the costs are high less usage is made of the capacities of the FOCJ services. There might still be some uncomfortable substitution possibilities for the municipalities.



$$\begin{aligned} \partial f / \partial L = f'_L > 0 \quad \partial f / \partial C = f'_C > 0 \\ \partial f'_L / \partial L = f''_{LL} \leq 0 \quad \partial f'_C / \partial C = f''_{CC} \leq 0 \end{aligned}$$

$$\partial f'_C / \partial L = f''_{CL} = f''_{LC} = \partial f'_L / \partial C > 0$$

- A demand function showing the relationship between price P (contribution) and volume X of output sold

$$(3) \quad P = P(X), \quad \partial P / \partial X = P' < 0$$

- The cost function demonstrating fixed cost  $K_A$  and two types of variable cost. The factor price of labour is w and that of materials is i, hence

$$(4) \quad K = K_A + wL + iC$$

- The towns should cover the variable costs  $K_v$ , they need not to pay for  $K_A$

$$(5) \quad K_v = wL + iC$$

- A restriction that contribution revenue is equal to total variable cost is introduced. We assume a self-financing FOCUS

$$(6) \quad P(X) X = g \cdot (wL + iC)$$

- Utility maximization of management under the restrictions mentioned above leads to the following Lagrange equation<sup>18</sup>

$$(7) \quad \Lambda = U(X; L) + \lambda(P(X) X - wL + iC), \text{ where } X = f(L, C)$$

The first-order conditions reflect two optimality conditions. One concerns the equivalence of the relation of marginal utilities of marginal factor-inputs to the proportion of respective marginal profits caused by the contribution (8) and the other refers to the contribution rate under cost coverage (9). Consequently

$$(U_X' \cdot f'_L + U_L') / U_X' \cdot f'_C = ((P' \cdot f'_L \cdot X + P \cdot f'_L - w) / (P' \cdot f'_C \cdot X + P \cdot f'_C - i)) \quad (8)$$

$$\text{and } P = ((wL + iC) / X) \quad (9)$$

The optimal contribution rate from the point of view of FOCUS-Management is shown by figure 5 at point B. Here the management of the FOCUS has a high influence on the contribution and the towns (members) are depending to a high degree on the type of management that manages the FOCUS. If it is only interested in X that means U(X) than it realizes cost minimization with a low contribution rate and no X-inefficiency according to Leibenstein<sup>19</sup>.

This approach opens an analytic framework for the analysis of FOCJ-behaviour. Typical conditions can be considered as well. The possibility of members opting-out encourages the FOCJ managements to exercise cost control. Some municipalities do not use FOCJ if the contribution rate become too high. Moreover, if towns can leave the FOCJ maximum restrictions can be introduced

<sup>18</sup> The following first-order conditions for the utility maximization are delivered

$$\delta \Lambda / \delta \lambda = P(X) X - (wL + iC) = 0$$

$$\delta \Lambda / \delta X = U_X' + \lambda(\partial P / \partial X \cdot X + P) = 0$$

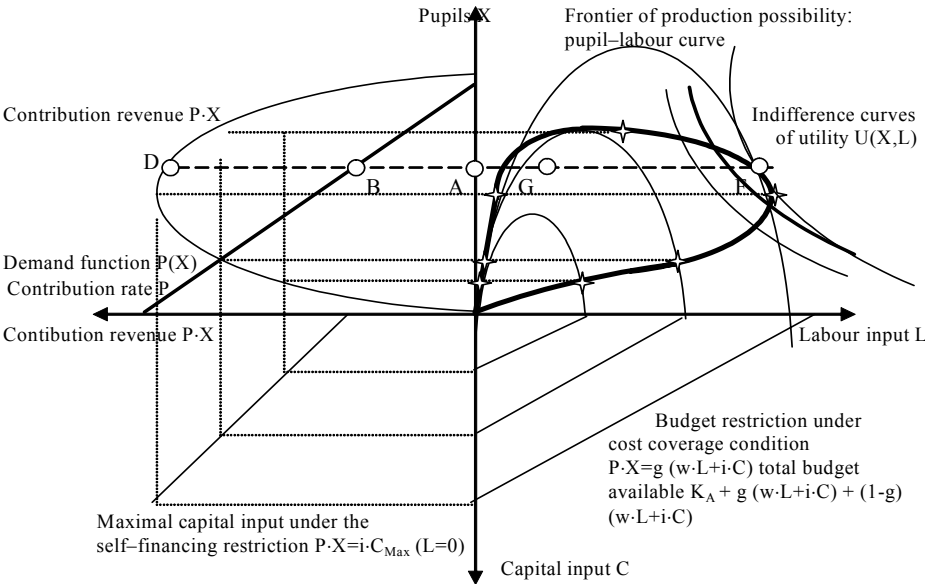
$$\delta \Lambda / \delta L = U_X' \cdot f'_L + U_L' + \lambda(P' \cdot f'_L \cdot X + P \cdot f'_L - w) = 0$$

$$\delta \Lambda / \delta C = U_X' \cdot f'_C + \lambda(P' \cdot f'_C \cdot X + P \cdot f'_C - i) = 0$$

<sup>19</sup> Several types of managers can be considered: those that evaluate pupils education and labour input positively (type I); those that are only interested in education (type II); or those that want to maximise labour (type III). Type I and III are Leibenstein X-inefficient, but produce more than under profit maximization (hidden).

that show a contribution rate and a related utility level at which the towns leave the FOCJ. There is a pressure to lower costs involved.

**Figure 5: Determination of contribution rate for FOCUS**

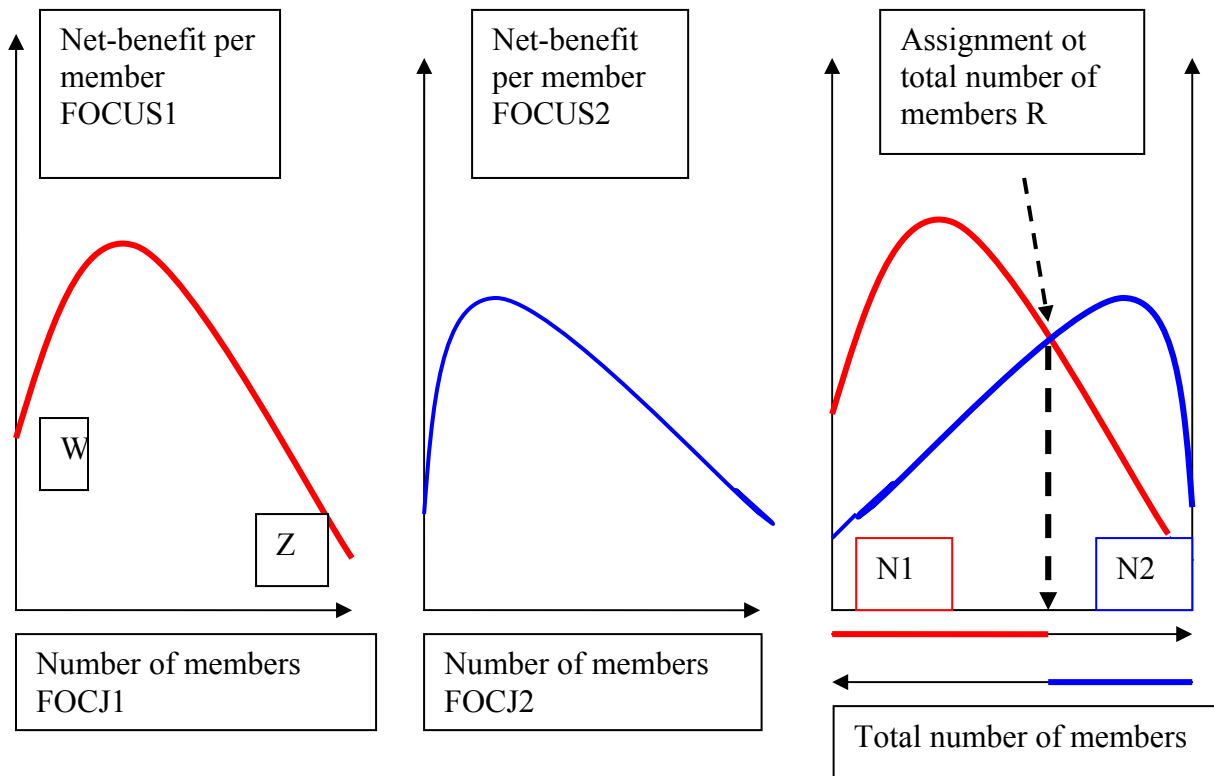


Horizontal competition among FOCJ can be introduced if towns are allowed to purchase from suppliers - FOCJ or other suppliers— which could include FOCJ that they are not members of — and if they are allowed to be a member of several FOCJ (similar Friedrich 2002).

There is also a model (Friedrich 2006, pp. 150) that shows the distribution of members between two or more already established FOCJ. There might be FOCUS1 located in one EU member state and FOCUS2 in another EU member state. A net-benefit to a member results from the service and the contribution paid. This net-benefit depends on the number of members in the FOCUS. It might increase and decrease with the number of members. For a FOCUS1 this development is reflected in curve WZ in figure 6 in the left-hand section. The middle section shows the curve TU – the development of net-benefit if the number of members varies for FOCUS 2. Left of assignment R it makes no sense for possible members of FOCJ to stay with FOCJ2. The same is true for possible members of FOCUS1 right of point R. Therefore the size of FOCUS1 turns out to be  $N_1$  and that of FOCUS2 is  $N_2$ .

A theory of cross-border FOCJ management can be built up according to competition in procurement, finance, marketing, and member treatment referring to those kinds of models for different forms of competition and to management theories of corporations. The features of cross-border conditions reflect the parameters and restrictions such as minimum capital requirements, taxation

**Figure 6: Distribution of FOCJ members**



**Source:** Friedrich 2006, pp. 150

conditions, legal kinds of members allowed, scope of management decision making decision spaces of management, quality requirements of services , requirements of qualities, staffing conditions, location and investment conditions, production functions, time horizons, etc.

## V. Advantages and Disadvantages of Cross border FOCJ

### Advantages:

(1) FOCJ can combine the efforts of members in different EU-member states to produce services through using synergy effects caused by common use of knowledge, management skills, capacities information, scale effects, integration of spillovers, etc.

(2) Cross-border clustering is supported by appropriate FOCJ. Some kinds of infrastructure services can be promoted across borders, such as energy provision, passenger transportation, schools, theatre, agriculture, and environmental improvements.

(3) The supply of services can be more differentiated; innovations and adaptations are to be expected because of different national legal and cultural conditions.

(4) Compensation possibilities between municipalities increase, and in the case of type-II, III and IV FOCJ can grow, especially within common border regions.

(5) FOCJ for regional competition may change market forms in regional competition and integrate cross-border regions.

(6) FOCJ in the form of public law can use different and extended instruments of action.

(7) Cross-border co-operation in special fields is feasible without having to narrow links to political negotiations, log rolling and political exchange in other fields and with other governments, e.g. central governments.

(8) EGTC-FOCJ help to develop and finance cross-border projects.

(9) The FOCJ is able to have a highly-skilled management that is able to negotiate with EU, higher level governments, and even consider European procurement laws and to organize production plans, capacity plans, and facility management systems.

(10) There is financial support from the European Union for and through EGTC and EEIV.

(11) The possibility of leaving the FOCJ promote efficient production and cost consideration in cross-border management.

(12) Opportunities to receive services from suppliers outside the FOCJ increase the tendency to higher efficiency within the FOCJ.

(13) The autonomy of municipalities against central governments is more protected. They can organize political influence through the FOCJ, organization, they co-ordinate and they have an agent that acts in their interest.

(14) New fields of cross-border cooperation are opened. Democratic cross-border management develops within FOCJ.

(15) Some European legal forms as well as national legal forms are available to form FOCJ, from types-II to IV. Cross-border FOCJ are possible as EEIGs, SCEs, and SEs. Also with difficulties, some national legal forms serve the purpose as well, especially cooperatives, associations and special purpose associations.

(16) In the framework of treaties among member states and agreements, special purpose associations are applied, and could be used for cross-border FOCJ.

**Disadvantages:**

(1) There is no legal form for type-I FOCJ, especially for cross-border FOCJ. They could be developed by treaties between EU-member states, but this is unlikely because the appropriate public law-form does not exist within the national law systems. A European directive to create a type-I FOCJ legislation is unlikely and would need at least 10 years to be developed and ratified.

(2)The European procurement and tender rules hinder some FOCJ. The in-house business problem creates uncertainties for FOCJ.

The European legal forms available can be used to form FOCJ-structured legal persons. However, the European Association would be a more adequate form when it becomes available in the future.

(3) Transaction costs to create and operate a FOCUS might compensate for efficiency gains because of entering and leaving members, of complicated rules, of different management cultures, of information, publicity costs, and of monitoring costs

(4) Some authors fear a loss of solidarity.

(5) The structure of FOCJ shows rigidities, as rules of equal treatment, and many rights and obligations of members have to be considered.

(6) Sometimes the establishment of several FOCJ to cause competition leads to multiple material infrastructure, e.g. transportation and energy lines, waterlines etc. That increases capacity costs. The right of way and transmission must be solved for the different competing FOCJ. This is, as was illustrated in the field of electricity provision, a rather problematic task.

(7) There is a loss in flexibility of parameters of political and economic actions. To apply coordinated actions and parameters becomes more difficult as some of the parameters are fixed by the FOCJ and not available for other political measures and strategies, e.g. in local income distribution policy.

(8) The dependencies in the framework of intergovernmental relations or from central-governments or the political dependence from them sometimes hinder realization of efficiency gains from cross-border FOCJ.

(9) To find rules determining decisions within FOCJ is not easy under these conditions. It is also difficult with some European legal forms such as the EEIC as none of the partners is allowed to have more than 50 % of the votes.

(10) The FOCJ may overlap competing regions, which leads to conflicts with municipalities.

(11) There is a lack of management theory relating to FOCJ, particularly with respect to goals analysis and determination, phases of management, levels of management, tools of management and management styles. The analysis of plans, competition solutions, internal and external market forms, contributions, finance, procurement, production and marketing is also in a very early stage, as is specific investment theory too. The inclusion of cross-border FOCJ in the very few existing approaches is possible.

(10) A general scheme for FOCJ cross-border evaluation or for utility analysis does not yet exist.

## **VI. Conclusions**

(1) Cross-border management gains in importance in the EU.

(2) FOCJ is a new management tool that can be used in some cross-border corporation situations.

(3) It is yet not applicable in its utopian form of type-I FOCJ. There are legal options available for the other three types. The European legal company forms in particular offer the possibility of realization in cross-border management.

(4) FOCJ exist on the national, regional and local levels in many forms.

(5) An intensive research program is necessary to identify in which sectors cross-border FOCJ are applicable and appropriate management tools.

(6) A special theory of FOCJ, of cross-border FOCJ and of international cross-border management offers a rich field of research.

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### Abstract

**Functional, overlapping, competing jurisdictions** – known by the acronym FOCJ – are to supply citizens, firms and public economic units with specific public services. This article analyses whether they could be a tool for cross-border public management and cooperation. FOCJ may differ considerably according to their internal structures and tasks, and they vary particularly in terms of their membership. One should consider four kinds of FOCJ) with citizens as members (type I), purely public bodies as members (type II), public bodies and firms as members (type III), citizens and persons of private and those of public law as members (type IV). FOCJ is a new public management tool that can be used in some cross-border corporation situations. It is yet not applicable in its utopian form of type-I FOCJ. There are legal options available for the other three types. FOCJ exist on the national, regional and local levels in many forms. The European legal company forms in particular offer the possibility of realization of FOCJ in cross-border management. EGTC-FOCJ help to develop and finance cross-border projects. Approaches of a special theory of FOCJ, of cross-border FOCJ and of international cross-border management are offered.