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SUBSIDIARITY

SUBSIDIARITY, GOVERNANCE, AND EU ECONOMIC POLICY

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For reasons largely related to ensuring long-run national security and political stability, the nations of western and central Europe, and perhaps soon the new democracies of eastern Europe as well, have banded together to form an economic federation: the European Union. Recognizing that economic interdependency is often the best deterrent to destabilizing political or military interventions, the Union's member nations have, since the initial 1951 Treaty of Paris, moved steadily forward to a fully integrated European economy.

To ensure the efficient performance of this wider economy, uniform rules of commerce, fiscal harmonization, and integrated public infrastructures will be required. Deciding and then enforcing these union-wide regulations and fiscal policies will require supranational political and judicial institutions. Economic unions necessarily lead to political unions of some form, and political unions require clearly articulated, and perhaps constitutionally protected, principles of policy assignment and governance. Who should be responsible for economic policy (assignment), and how should policies be decided (governance)?

The European Union's guiding principle for assignment, now constitutionally grounded in the Maastricht Treaty for the European Union, is subsidiarity, the allocation of policy responsibility to the lowest level of government at which the objectives of that policy can be successfully achieved. The Union's principles of governance are still evolving, having swung pendulum-like from an early period of unanimous rule under the 1957 Treaty of Rome to a period of *de facto* executive control following the adoption in 1986 of the

Single European Act. Today, the Union is searching for a middle ground stressing governance through co-decision-making between two majority rule legislatures, the Council of Ministers and the European Parliament.

The Objectives of Federal Constitutions: Constitutions establish the rules for collective decision-making: who is allowed to participate, what is to be decided, and how policy decisions are to be reached and enforced. The unique contribution of a *federal* constitution is to allow for multiple tiers of governments, each with a domain of policy responsibilities. In setting the number and layers of governments and in drawing their exclusive and mutual responsibilities, three objectives for government are commonly mentioned: to guarantee personal, political, and economic rights; to encourage political participation; and to promote the efficient allocation of economic resources.

Protecting Rights: Personal, political, and economic rights define the domains of individual liberty. Liberties may be either "negative" or "positive." Negative liberty ensures that individuals are free from interference of others in certain choices and actions; positive liberty guarantees each individual an ability to make certain choices or to perform certain actions. Religious rights, voting rights, the right to speak freely, and property rights guard matching negative liberties. A right to minimal subsistence and shelter, to education, or to health care provide protection for corresponding positive liberties. Governments in turn protect rights. A citizen Bill of Rights joined with a credible and independent judiciary is perhaps the most important institutional guarantor of individual rights and thus liberties. Separation of powers between branches of the central government joined with credible checks and balances across those branches offers



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further protection. Federalism is a possible third line of defense; see Rapaczynski (1986).

Encouraging Political Participation: Political participation is how ordinary citizens influence or attempt to influence political outcomes. The lack of such influence constitutes a “democratic deficit.” Jeremy Bentham and James Mill saw political participation as a way to ensure that governments maximize aggregate citizen utility or welfare. Jean-Paul Rousseau and John Stuart Mill stressed how participation helps to protect citizen liberties; active political participation in a democratic society ensures no one individual or group is master over any other. Aristotle and Alexis de Tocqueville noted political participation’s important contribution to encouraging communitarian values. By giving an important role in policymaking to subnational governments, particularly local governments, the federal form of governance encourages political participation; see Dahl and Tufte (1973).

Promoting Economic Efficiency: Economic efficiency requires that no reallocation of union resources can make one person or group within the union better off without hurting another person or group. Competitive markets and free trade will move a union a long way towards economic efficiency, but unencumbered markets alone cannot guarantee economic efficiency. Markets fail for a variety of reasons: public goods, spillovers, increasing returns to scale, asymmetric information. In each of these instances, efficiency requires cooperation to overcome the market failure, but the cooperative provision of a good or service often creates strong incentives to conceal true benefits and to free-ride. “Let the other fellow contribute – I don’t really want that service anyway!” The federal form with its possibility for competition between lower tier governments offers a unique means for solving the problems of information revelation and free-riding. National defense and union-wide transit and communication networks are probably best supplied at the highest level of government. Here the federal form of governance has no particular advantage. But for most other public services, competitive state and local governments are more efficient, and thus the federal form of governance can be preferred; see Oates (1999).

The Structure and Performance of Federal Constitutions: Federal constitutions are defined along three dimensions: (1) The *number* of member states included within the union; (2) The *assign-*

ment of policy responsibilities between member states and the union government; and (3) The *representation* of member jurisdictions to, and rules of governance for, the union-wide government. From the Treaty of Paris to the Treaty of Nice, each European Union treaty has made an explicit choice along these three dimensions of a federal constitution. Choices along these dimensions define one of three generic federal constitutional forms, with each constitution likely to have different performance properties against the objectives of rights protection, political participation, and economic efficiency.

Decentralized Federalism: Decentralized federalism combines Charles Tiebout’s (1956) model of competitive governments with Ronald Coase’s (1960) model of efficient bargaining. The number of subnational or member governments requires that each union member be sufficiently large so as to be able to provide congestible »local« public goods efficiently. Very small or economically inefficient candidate nations should not be allowed to join the union as separate member states. Typical examples of congestible public goods, where more users eventually reduce the benefits enjoyed by previous users, include education, police and fire protection, health care, local roadways, parks, and local environmental quality such as trash collection, clean water, public sanitation. The efficient size of government for the most congestible local public goods is no smaller than 20,000 residents and probably no larger than one million residents. Current and proposed member nations in the European Union clearly meet this constraint.

Assignment under decentralized federalism allocates all policy responsibilities, at least initially, to these subnational or member governments. Member governments may then jointly decide to reassign some or all of their policy responsibilities to a union government.

Governance rules will be required for all policy decisions reassigned to the central government. The decision-making body will be a union-wide legislature with at least one representative from each member government. Unanimity will be the required voting rule in the union legislature under decentralized federalism.

As a protector of individual rights, the performance of decentralized federalism is uncertain. If

individuals are mobile across member governments, if new member governments can be created by citizens of the union, and if member governments have full responsibilities for rights enforcement and policies within their borders, then individual rights to personal freedoms, political rights, and property rights are likely to be well protected. Any citizen who feels abused can relocate to another, presumably safer member state, or perhaps to a newly created member state. But to guarantee mobility and to protect or create states, a strong central government at the union level will still be needed. If free mobility, new government formation, and member independence cannot be guaranteed by the overarching union government, then subnational member governments may become a source of oppression through “tyranny by a majority.” U.S. Southern states before the Civil War is one telling example and so too is the recent history of Serbian oppression of Muslim citizens of Yugoslavia.

Decentralized federalism may also fail to ensure positive liberties. If protecting positive liberties requires the taxation of the more able to subsidize the less able – say to provide a subsistence income, basic shelter, or minimal education and health care – then a decentralized network of fiscally competitive member governments is not likely to succeed when economic resources are mobile. The redistribution required for the protection of positive economic rights can be achieved, if at all, only through the efforts of the union-wide government. But under decentralized federalism, union government policies require the unanimous consent of all member states. Positive liberties are likely to be denied, but now through “tyranny by a minority.” The U.S. effort to redistribute income and public services through state governments provides strong evidence on the point; see Feldstein and Wrobel (1998).

The likely performance of decentralized federalism in fostering political participation is more encouraging. Available evidence reviewed by Dahl and Tufte (1973) from within country comparisons of political influence and political effort shows that citizens in smaller governments make a greater effort to understand, and have more success in understanding political issues. Further, citizen effort to influence government is two to three times higher for subnational than for national governments. Political effectiveness or influence also increases as the size of government declines;

Finifter (1970) shows a significant negative correlation between an index of political power and the size of government. Finally, locally elected legislatures are likely to be the most responsive to citizen preferences (Cain, et al. 1987).

Finally, like the protection of rights, the potential for decentralized federalism to efficiently provide government services is uncertain. Five conditions must hold for a decentralized public economy to be economically efficient: 1) Publicly provided goods, services, and regulatory activities must be available at a positive, but minimal average cost; 2) There must be a perfectly elastic supply of competitive governments; 3) Households and businesses must be fully informed about the fiscal and regulatory policies of each government; 4) There must be free and easy mobility of households and businesses across the member governments; and 5) There can be no significant intergovernmental externalities or spillovers. When any one of these five conditions is violated, union-wide provision of government services or regulations must be considered.

In decentralized federalism, central government policymaking is done through unanimous agreements among the member states. For successful agreements to occur, five conditions must be met here as well: 1) There must be no, or very small, resource costs associated with the bargaining process; 2) Preferences over outcomes must be common knowledge; 3) Bargaining agents from the member states must accurately represent the economic interests of their constituents; 4) All agreements must be enforceable; and 5) The parties to the agreement must agree to a division of the bargaining surplus. To expect union-wide decision-making to meet these five conditions, particularly as the size of the union grows much beyond four or five members, seems to us to be very optimistic; see Inman and Rubinfeld (1997a).

The assignment and governance structures of decentralized federalism will encourage political participation but, except in very small and homogenous unions, such constitutions are likely to perform poorly against the other constitutional objectives of rights protection and economic efficiency. There are alternatives.

Centralized Federalism: Centralized federalism combines all member governments into a single union-wide government. All policy responsibilities

There are three generic types of federal constitutions: decentralized, centralized, and democratic federalism

Decentralized federalism promotes political participation

are assigned, at least initially, to this one central government. The central government is governed by a president or a small executive council elected by all citizens of the union. If the elected president wishes, policy responsibilities may be reassigned to member country governments, whose own executives may be elected locally or appointed by the centrally elected president or council.

Centralized federalism combines all member governments into a single union-wide government

Centralized federalism is likely to offer only fragile protection for individual rights. Open and competitive elections of the union executive will protect individual rights and liberties, but when the majority electing the executive forms a stable political “monopoly,” either because of fixed and aligned economic interests or ethnic allegiances, then minority rights are significantly at risk. The fate of Blacks in the U.S. South before the Voting Rights Act of 1965 or that of Jews in Nazi Germany illustrates the potential risks to basic liberties with stable majority-controlled central governments.

Nor is centralized federalism likely to enhance the goal of political participation. All policy responsibilities are assigned to the central government. Smaller member governments are arguably the more participatory, yet they run the risk of becoming no more than administrative agencies of the central government. Nor is political participation at the union level of governance likely to be very great, limited as it is to the election of a single executive or oligarchy.

The goal likely to be best encouraged by centralized federalism is economic efficiency. Here a democratically elected executive sets policies for the nation as whole. For these policies to be efficient, however, the executive must first reveal citizen preferences, and then choose efficient policies after citizens’ preferences are known. The burden for finding an efficient resource allocation falls to the election process. If elections are open so that any citizen can run for the presidency, then policies chosen by the president will be efficient in two-candidate elections; see Besley and Coate (1997). The intuition is straightforward. In two-candidate elections, citizens vote truthfully. Thus, any efficient candidate can propose a policy which a majority of voters prefer and which defeats any policy proposed by an inefficient candidate. Open elections with informed voters are essential, however.

In the end, the overall performance of centralized federalism will be at best mixed. Competitive

democratic elections of the union-wide executive are likely to foster overall rights protection, but monopoly control of the executive raises a significant risk of rights abuses. Political participation is likely to be discouraged; a “democratic deficit” results. The one virtue of centralized federalism is its potential for efficient resource allocations when elections are open and voters are informed.

Democratic Federalism: Democratic federalism offers a promising middle ground, joining the ability of decentralized federalism to protect rights and promote participation with the economic efficiency advantages of centralized federalism. As in decentralized federalism, member states in the economic union must be of sufficient size so as to provide congestible public services efficiently. Constitutional assignment allocates policy responsibilities to member states or to the union level of government by a principle of subsidiarity – that is, member governments are allocated those policies which benefit local populations and which have no significant positive or negative spillovers onto non-residents. For goods with significant economies of scale in production or consumption, for taxes which alter the spatial allocation of economic resources, and for services and regulations with economic spillovers, allocation by the union government is preferred. Finally, governance within democratic federalism gives each member state a clear voice in the central government through direct representation in a locally elected union-wide assembly. Decisions in the union legislature are made by simple majority, or perhaps supermajority, rule.

Assignment of important taxing and policy responsibilities to the lower-tier member states will make an important contribution to ensuring personal, political, and economic liberties. For example, assigning significant taxing powers to subnational governments controls unwanted taking of private property by government; see Weingast (1995). Assigning member governments responsibility for police functions ensures that local residents can monitor and discipline any abuses of police powers and provides possible protection against armed interventions by other local or even national interests; see Rapaczynski (1986). Education too can be assigned locally to ensure political rights and freedom of speech. The union government can then be given responsibility for ensuring minimal economic subsistence, access to clean and safe shelters, lit-

Democratic federalism combines the advantages of both other forms

eracy, and basic health services; see Sen (1988). Finally, a representative legislature run by majority rule checks tyranny by a stable minority, while wide representation of local interests minimizes the risks to rights arising from a stable majority; see Madison's Federalist 10 (1787).

Political participation is likely to benefit from the introduction of democratic federalism, but again only if member state governments are given significant policy responsibilities. Furthermore, the union legislature must allow for significant representation of member state interests in its deliberations.

The efficiency performance of democratic federalism also rests fundamentally on the constitutional rules of assignment and governance. Efficient assignment limits central government responsibilities to those activities which entail significant externalities across the member states. Efficient governance must solve the inherent policy instability found in any majority-rule legislature but must do so in a way which retains an alignment of member states' benefits and costs from union policies. There is a significant risk that legislators from member countries, when faced with the problem of policy instability, will find a legislative norm of deference – more commonly characterized as “I'll-scratch-your-back-if-you'll-scratch-mine” – as the only feasible way to make decisions. Under this norm, locally beneficial but centrally inefficient government policies will be approved. If assignment cannot be easily enforced, then local projects funded from the union-wide tax base become part of the union-wide budget. That will be an inefficient budget. Failing effective assignment, strong governance in the form of strong union-wide political parties within the legislature or a strong union-wide executive with veto powers will be needed; see Inman and Fitts (1990). Enforceable assignment and strong governance are essential for economic efficiency under democratic federalism. With appropriate rules of assignment and governance, however, democratic federalism goes a long way towards meeting each of the three objectives for a federal constitution.

The European Union's Search for a Federal Constitution: Beginning with the 1951 Treaty of Paris between France, West Germany, Italy, Belgium, Luxembourg, and the Netherlands establishing the European Coal and Steel Community, to the 1957 signing in Rome of the European Economic

Community Treaty (EEC Treaty of Rome), to the Luxembourg Compromise in 1966, to the entrance of Denmark (1973), Ireland (1973), United Kingdom (1973), Greece (1981), Portugal (1986), Spain (1986), and then finally Austria (1995), Finland (1995), and Sweden (1995) into the Community, the nations of western and central Europe have been moving steadily towards an integrated economic and political union. The central driving force both historically and to this day has been the desire of France and Germany to avoid military conflict on the continent. Integrated economies are seen as one crucial means for ensuring political stability in a wider Europe.

Governing the initial steps towards this economic union was a federal constitution best described as *decentralized federalism*. The Treaty of Rome created a variety of supranational institutions akin to a central government, the most prominent of which are the European Commission serving as an executive civil service, the European Parliament serving as an elected (since 1979) legislature but originally with consultative powers only, the Council of Ministers whose final *unanimous* approval was required for all EU decisions, and the European Court of Justice to make rulings on matters of treaty enforcement. Under the Treaty of Rome, the center of power lay with the Council of Ministers composed of one representative from each member state and guided, since 1974, by a complementary body of heads of state called the European Council. Beginning in 1966, the Treaty required a formal change in Council voting procedures, moving the decision-making rule from unanimity to qualified majority. However, a threat by France to withdraw from the Council of Ministers if qualified majority took effect led the Council to adopt the Luxembourg Compromise to continue a rule of unanimity on all matters of “vital national interest.” While not formally part of the EEC Treaty, the Compromise stood as a binding constraint on Council decisions until the passage of the Single European Act in 1986. Prior to 1986, however, only unanimous agreements could become Community policies.

The Treaty of Rome also assigned policy responsibilities to the Council, foremost of which was to create a common market. This the Council did through its power to remove intercountry tariffs and through the promotion of economic competition between firms in member countries. The

With appropriate rules of assignment and governance, democratic federalism is best suited for a federal constitution

The EU's quest for a constitution has gone through several stages

Council also assumed responsibility for a Common Agricultural Policy and adopted a variety of price support policies “to ensure a fair standard of living for the agricultural community.” In all instances these policies were approved by a unanimous vote of Council members. Also assigned to the Council were transportation policies and social policies. Because of significant disagreements among member countries in these policy areas, however, unanimity was not achieved and little could be accomplished towards the overall goal of economic integration.

Born in part from the frustration over the slow pace of integration and a growing appreciation of the advantages such reforms might have in combating Europe's declining economic fortunes (known as “Eurosclerosis”), the then ten members of the Union put aside the Luxembourg Compromise and the principles of *decentralized federalism* and adopted in 1986 the Single European Act (SEA) and a new institutional structure closely approximating that which we have called centralized federalism. The rule of unanimity was replaced by a »consultation procedure« and a commitment to allow qualified majorities to make substantive policy decisions. Proposals would come from the European Commission as before. Now, however, only a qualified 71 percent majority of the Council of Ministers was needed for a policy to become law. Still the Commission's proposals could be only accepted or rejected; unanimity was required for the Council to amend the Commission proposals. The use of a qualified majority meant no one country could block a policy, while the consultation procedure gave strong agenda-setting powers to the Commission. Together these two reforms moved policymaking into the hands of a single central executive.

The consultation procedure applied to all policy areas covered by the original Treaty of Rome (agriculture, transportation, social policy, environmental policy, regional and fiscal policies) except for those policies concerned with the completion of the internal market (competition policy, free movement of goods, labor, and capital). For these policy assignments, the SEA recommended a second innovation to Union decision-making called the “cooperation procedure,” where policies approved by the Council go to the (now locally elected) European Parliament to be accepted, rejected, or amended by simple majority rule. The cooperation

procedure raised the Parliament to the role of a conditional agenda-setter, where an alliance between the Commission and Parliament (a frequent outcome) could force the Council to make decisions on their terms (Tsebelis 1994). Parliament, however, had no original agenda-setting powers under cooperation. Thus, the pivotal institution for policy innovation under the SEA became the European Commission, an executive cabinet appointed by member nations.

The appointed Commission's influence reached its peak in the late 1980's, no more clearly evident than in its 1988 decision to establish a committee under the direction of the Commission President Jacques Delors to explore the feasibility of a European Monetary Union (EMU) as a complement to the increasingly integrated European marketplace. At this time, the European Commission stood as the dominant voice in Union policymaking. Paradoxically perhaps, the approval of the Commission's crowning achievement, the EMU, would begin the significant erosion of its powers and the evolution towards democratic federalism under the Treaty of Maastricht.

The Maastricht Treaty of 1991 created the Economic and Monetary Union, charged to encourage the free flow of goods, labor, and capital and to establish a common monetary policy for all member states through the introduction of a single European currency and a single European Central Bank. Whatever the economic benefits of a Monetary Union, they come at a cost. Member countries sacrifice their ability to use expansionary monetary policy to offset the adverse employment effects of negative economic shocks. If economic shocks affect all or most of the Union's countries similarly, then the EMU's common monetary policy can serve the same role as country-specific expansionary monetary policies during times of deep recessions. But if economic shocks are asymmetric across the potential members of the EMU, as recent experience seems to indicate, then the loss of country-specific monetary policy imposes potentially large costs on members during economic downturns. The costs are likely to be largest in the larger countries of the Union, where domestic monetary policy is most likely to have expansionary benefits during recessions. One response would have been to allow these member countries to run decentralized, country-specific deficit fiscal policies. But Maastricht, as amended by the Pact for

Stability and Growth, denied member countries this policy option. Concerned that economic spillovers from high deficit countries could threaten promised price stability, the Stability Pact imposes a tight 3 percent of GDP limit on country budget deficits.

Facing constraints on their use of countercyclical deficit policies, the member countries introduced yet another revision to EU political institutions. The co-decision procedure, first introduced in the Maastricht Treaty but amended and strengthened by the 1997 Treaty of Amsterdam, elevated the locally elected European Parliament to a legislative coequal with the Council of Ministers. The co-decision procedure now gives the Parliament joint say along with the Council of Ministers over the final specification of EU fiscal and regulatory policies. Policies first rejected or amended by Parliament but once again approved by the Council, perhaps in another amended form, must be returned to the Parliament for reconsideration. Disagreements between the Council of Ministers and Parliament are to be resolved through a Conciliation Committee composed of members from both bodies. The net effect of the co-decision procedure is to create two equally powerful legislative bodies, each capable of blocking the preferred outcomes of the other. Negotiations between a broadly elected Parliament and a country appointed Council have now fully replaced the non-elected European Commission as the focal point of EU policy-making. In its current form, the Union's decision-making structure closely resembles that of the United States: an institutionally weak executive, a state (country-specific) Senate and a district (region-specific) House. The EU constitution is today best characterized as democratic federalism.

Whither EU Policy Under EU Federalism? As the Union expands, there will surely be adjustments to its rules of decision-making, but there now appears a core commitment to the institutional structure of Maastricht and Amsterdam: a weak executive with agenda-setting but no veto powers and two coequal legislative chambers. In response to Union expansion, the 2001 Treaty of Nice proposed changes in the voting rules within the Council of Ministers and an expansion of membership for the European Parliament, but the constitutional structure for legislative action – Commission agenda-setting and legislative co-decision – remains unquestioned. With this structure for EU democra-

tic federalism now firmly in place, what are the prospects for EU policymaking? Here the Union can learn important lessons from the recent U.S. budget and regulatory histories. Decentralized legislatures, unless checked by nationally (or, in the case of the Union, supranationally) elected executives with veto powers or stable national (or, for the Union, supranational) legislative political parties, will typically approve inefficient public budgets and government regulations. Decentralized legislative decision-making is inherently unstable, cycling from one majority, or qualified majority, coalition to another with no equilibrium policy guaranteed. If any policy decisions are to be made, further institutional structure beyond majority-rule will be required. These can be imposed from the outside, as in the case of a “take-or-leave-it” agenda-setting executive, or may arise from within the legislature itself, as in the case of legislative political parties with the ability to discipline members who fail to vote the party position.

U.S. congressional and state legislatures have discovered a third, and unfortunately very inefficient, way to avoid cycling in a “I’ll-scratch-your-back-if-you’ll-scratch-mine” norm of deference among legislators. Under this norm of voting, legislators informally agree to defer to others’ favorite budget items or regulations if deference to their favorite choices is granted in return. The result is typically many very inefficient projects and regulations. Everyone consumes from the Union tax base paying only their very small share of costs but, when their project is “local,” enjoying all the benefits. The best analog to this norm of budgeting is the behavior of a large group ordering lunch after agreeing to share the check. Since each person pays only a fraction of the cost of their own lunch, the incentive is to order too much food. To solve this “shared lunch” or “common pool” problem, either separate checks are required (subsidiarity and assignment) or someone needs to assume control over what people order (governance). There is strong evidence that “common pool” budgeting is pervasive in the decentralized legislatures of the United States (Gilligan and Matsusaka, 2001) and that the resulting budgets and regulations are economically inefficient (Inman and Fitts (1990) and Inman and Rubinfeld (1997b)).

Having adopted democratic federalism, the challenge for the Union is to now find a workable middle road between the indecisions of legislative

Today's decision-making structure of the EU may be characterized as democratic federalism

cycling and the inefficiencies of common pool budgeting. Again the U.S. experience is instructive. Occasionally we have solved our common pool problems with a strong elected executive with veto and agenda powers – Ronald Reagan comes to mind – or stable party control over legislative politics – for example, (southern) Democratic control of Congress from 1954 to 1968.

It is unlikely the EU constitution will be revised to allow for the election of a single, institutionally powerful Union president. Thus supranational political parties within the Council of Ministers and the European Parliament will be needed. Within the Council, at least presently, this seems unlikely, too. There is, however, some recent evidence suggesting that Members of Parliament (MEP's) do vote along Parliamentary party lines, collecting around the positions preferred by the liberal Party of European Socialists (PES) and the center to conservative European People's Party (EPP). One must interpret such results with great care, however. Knowing that members vote with other Parliamentary party members may simply mean that members separately choose party labels and votes according to an exogenously specified ideological position, and not because the party is strong enough to control votes; see Krehbiel (1993). Careful empirical work by Kreppel (2002) and Hix (2002) establish very clearly that when local or national party interests are at stake, MEP's vote locally and not with their supranational EP parties. At the moment, EU legislatures lack strong party control of member voting behaviors. Inefficient common pool policymaking remains very much a risk for EU democratic federalism.

There are two institutional hurdles within the current structure of EU federalism which may slow the tendency of Union legislatures to adopt inefficient public policies. The first is judicial enforcement of the principle of subsidiarity to deny inefficient Union projects and regulations. In our own research on U.S. federalism, we have outlined how the judiciary might apply the logic of subsidiarity to control U.S. legislative excesses; see Inman and Rubinfeld (1997b). Bermann (1994) has addressed this same question for the EU. Like us, he concludes that court enforcement should be limited to procedural matters only: When adopting policies, did the legislature weigh a possible violation of subsidiarity? A substantive evaluation of whether a policy does, or does not, meet the standards of subsidiari-

ty seems to us, and to Bermann, well beyond the competency of the U.S. Supreme Court or the Union's Court of Justice. Judicial enforcement of procedural violations can be a check on policy inefficiencies, but it will be at best a low hurdle.

The Treaty of Nice offers a second moderating institution against policy inefficiencies. In an effort to placate the current large members of the Union, Nice increases the qualified majority necessary for policy passage in the Council; the resulting smaller "blocking percentage" strengthens the hand of the large members in Council decision-making. At the same time, in an effort to placate the many smaller members of the Union, Nice also requires any approved policy to win the support of an absolute majority of the nations in the Union. In an expanded 27 member Union, 14 small countries will be able to block legislation even when a qualified majority has approved a policy. These two changes together increase the ability of the Council to veto – that is, block – deviations from the policy status quo; see Tsebelis and Yatağan (2002). Thus really inefficient policies favored by Parliament can, *if* Council incentives are appropriate, be checked by the Council. To be effective, Council members must collectively favor Union-wide economic efficiency, however, and this very much remains an open question.

Today, the EU stands at a crossroad. For good reasons – rights protection and political participation – Union members have made a constitutional commitment to democratic federalism. Economic efficiency, however, remains in doubt. Admitting twelve new members in 2005, whatever the benefits for European political stability, will create added pressure for inefficient fiscal transfers, industry subsidies, and locally beneficial regulations. In light of the Union's current legislative performance, it seems unlikely that supranational political parties with a Union-wide electoral mandate will arise within the Council and Parliament to efficiently manage public policies.

The task then is to strengthen those EU institutions of assignment and governance that best promote efficiency. Articulating the principle of subsidiarity and requiring all policies to be measured against this standard, with the Court of Justice as the enforcer, is a good first step. A valuable second step has been the decision in the Treaty of Nice to strengthen institutionally the hand of the Council of Ministers over that of the European Parliament.

The EU's democratic federalism ensures rights protection and political participation, but not efficiency

But when all this is said and done, the best safeguard against legislative inefficiencies will be, as it has been for U.S. federalism, an informed electorate willing to defeat all politicians and political parties that fail to find and embrace the efficient common ground.

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