

Chapter 5

Legislative Bargaining and Lobbying in Federations

5.1 Introduction

How does centralization of policy making affect lobbying for local public goods? So far, the theoretical literature on policy centralization has revealed two opposing effects. On the one hand, cost sharing of public goods among jurisdictions creates a common pool problem, which causes lobbying. Consequently, centralization may result in overprovision of local public goods (Persson and Tabellini 1994, Mazza and van Winden 2001). By contrast, other papers (Melo et al. 1993, Bardhan and Mookherjee 2000) argue that centralization increases the number of contesting lobby groups, which reduces the political cloud of each of them. Hence, centralization raises the marginal cost of obtaining policy favors, which dilutes the incentives to lobby.

A key assumption in most of the literature is that political centralization entails handing over decision making power to a single policy maker in the center (Persson and Tabellini 1994, Mazza and van Winden 2001), or that previously locally organized political parties merge across borders and then compete in a centralized election (Bardhan and Mookherjee 2000). However, both these centralized policy making settings do in practice not seem to fit well the institutional design of most federations; federal policies are typically

formulated by a committee consisting of regional delegates who are elected or appointed locally. A case in point is policy making in the European Union.

To shed more light on the effects of policy centralization in federations, this chapter presents a model where a committee of regional representatives decides on the provision of local public goods. We consider a two-stage Grossman and Helpman (1994) policy-making game, where in the first stage regional lobbies offer contributions to a local policy maker. In the second stage a committee of these local policy makers decides on public goods provision. A main result is that the common pool effect associated with centralization reduces lobbying expenditures. The intuition is that cost-sharing causes the local policy makers to become an ally of regional interest groups. Anticipating this, these interest groups are able to offer their policy maker a lower contribution in return for policy favors when compared to decentralized policy making. In addition, we endogenize lobby formation along the lines of Mitra (1999). We argue that centralization causes the number of lobbies to increase as the cost of lobbying falls. Hence, our model predicts that centralization will reduce lobby expenditures for each group and increases the number of lobbies.

There is a well established literature that studies the interaction between lobbying and legislative bargaining among politicians. This literature, however, does not explicitly deal with issues of centralization.¹ To name a few papers, in the spirit of Shepsle and Weingast (1981), Helpman and Persson (2001) introduce an agenda setter to derive legislative equilibria. One of their results is that lobbying efforts are concentrated on this agenda setter. Likewise, Grossman and Helpman (2001) show that majority voting causes lobbies to focus on the pivotal legislator. By contrast to the papers that stress financial contributions, Bennedsen and Feldmann (2002) consider information provision by lobby groups. In their paper, effort by lobbies signals the interest intensity of the policy maker, which increases her chances of being included in a coalition.

A few papers explicitly deal with issues concerning the effects of cen-

¹Various models of lobbying and legislative bargaining are surveyed in Grossman and Helpman (2001) and Persson and Tabellini (2000).

tralization on lobbying. In contrast to this chapter, these authors assume that centralized policy making is conducted by a single politician, so that in these papers there is no legislative bargaining. Redoano (2003) uses the citizen-candidate set-up by Besley and Coate (2001) to analyze the effects of centralization on lobbying in a representative democracy. In addition, she allows for endogenous lobby formation. One of her results is that centralization may increase the number and size of lobbies, since heterogeneous preferences in a federation make lobbying more necessary. Bordignon et al. (2003) analyze lobbying for public goods by a local and a foreign firm in two jurisdictions. Centralization of policy making internalizes the negative spillover effects of subsidizing the local firm. Among other things, they show that when merging markets enhances competition, this increases the incentives to lobby for local public goods.

The main motivation for introducing committee decision making as the post-centralization policy making setting is to analyze lobbying in the European Union. In the political science literature on European integration, for long the ‘functionalist’ approach has dominated (e.g. Haas 1958, 1964 and Lindberg and Scheingold 1970). According to this approach, the member states were envisioned to move towards ‘ever closer union’, which in the process would create truly European policy makers. By contrast, more recent ‘intergovernmentalist’ theorizing emphasizes that EU policies reflect power struggles between the member states (Moravcsik 1991). In this view there is no single European decision maker who dominates the political process.

In this chapter the policy outcome maximizes the joint welfare of the national policy makers. Clearly, the assumption that the joint surplus of all countries is maximized can be motivated by unanimity decision making. One may object that in the EU most policies that deal with local public goods have qualified majority voting. However, many experienced policy observers including Messerlin (2001) argue that consensus also is implicitly the rule in policy domains where there is qualified majority voting. The main reason is that member states anticipate that outvoting in qualified majority domains may cause a veto in unanimity domains. Arregui (2004) analyzes this issue empirically and shows that many EU policies reflect a cooperative outcome.

A more descriptive account of the cooperative nature of decision making in the European Council of Ministers is provided by Beyers and Dierickx (1998) and Beyers (1998).

To motivate further the assumption that lobbies predominantly approach national policy makers, case-studies show that in the EU this indeed is the case (see among others Lanzalaco 1993, Spence 1993, Van Schendelen 1993, 1998). For example, Mazey and Richardson (1993, p.211) note "...the growing importance of EC regulation has in many cases reinforced the dependency which exists at the national level between groups and 'their' ministries, since the latter are effectively *intermediaries* between groups and the EC in the final stages of Community decision-making"[original italics]. Spence (1993) in his account of the role of the British civil service in Brussels goes a step further and calls national officials 'lobbied lobbyists'. With respect to the largest public spending domain in the EU, Pappi and Henning (1999) analyze networks in the Common Agricultural Policy (CAP) – by many regarded as a supranational policy domain *pur-sang* – and conclude that national farmer's organizations spend by far the most resources on influencing domestic policy makers acting in Brussels.

5.2 Decentralized policy making

We consider m identical countries indexed by i , each populated by n groups indexed by j . To start, by assumption k of these groups are organized and belong to the set Λ , that is $k \in \Lambda$. The other $n - k$ groups are not organized. We assume that each group is small, so that functions of k can be differentiated. In the following we normalize n to 1, so that k can be read as the share of groups in society that is organized.

In each country a policy maker decides on the provision of local public goods g^j to group j . A group may be thought of as a region or a city, for which we assume that citizens have equal preferences. The utility from consuming public goods is described by a utility function $b(g)$ with properties $b_g > 0$, $b_{gg} < 0$, and $b(0) = 0$. In addition, there are no spill-overs from local public goods in other regions. The average and marginal cost of producing

a unit of g^j in terms of forgone private goods consumption is normalized to one. Production of local public goods is financed by a lump sum tax t that is equal for all citizens. Hence, utility of group j is given by:

$$V^j = b(g^j) + y - t \quad (5.1)$$

where y denotes income, so that the term $y - t$ represents the utility from private goods consumption. Given the concavity of $b(g)$ it follows that the socially optimal level of local public goods to group j satisfies the first-order condition:

$$b_g(g^j) = 1 \quad (5.2)$$

The equation above shows that in the social optimum the marginal benefits of local public goods to group j (LHS) equal the marginal cost to society (RHS). In the following, (5.2) serves as an efficiency benchmark against which to evaluate the political economy outcomes.

In our economy, organized groups have the option to offer a contribution schedule to the policy maker. The policy maker is assumed to maximize his own welfare V^p that is a weighted sum of social welfare V^s and the sum of political contributions $\sum C^{j \in \Lambda}(g^j, t)$ by the groups that are organized:

$$V^p = V^s + \alpha \sum_{j=1}^k C_i^j(g^j, t) \quad (5.3)$$

The parameter α measures the relative preference of the policy maker for the sum of contributions that she receives from the organized groups.

Solving the game backward, the second stage equilibrium describes the optimal provision of local public goods to each group j . To find this optimal level, we need to specify how the contributions are affected by changes in the allocation of local public goods. Following Bernheim and Whinston (1986) and Grossman and Helpman (1994), we avoid multiple equilibria by requiring contribution schedules to be ‘truthful’, that is, these schedules are assumed to reflect the marginal welfare gain (or loss) to group j from a change in the public goods allocation. The allocation affects each group through its own level of public good g^j and the tax t it has to

pay, where $t = \theta [kg^{j \in \Lambda} + (1 - k)g^{j \notin \Lambda}]$ and $\theta = 1/n$ is the identical population share of each group. A truthful contribution schedule is defined as $C^j(g^j, t) = \text{Max}(0, V^j(g^j, t) - \gamma^j)$, where γ^j is a scalar so that $V^j(g^j, t) - \gamma^j$ is the lump sum contribution to the policy maker. As we focus on positive contributions in equilibrium, in the neighborhood of such an equilibrium contributions take the form $C^{j*} = V^{j*} - \gamma^{j*}$. By making use of (5.1), truthful contribution schedules have properties:

$$\frac{\partial C^j(g^j, t)}{\partial g^j} = \frac{\partial V_i^j}{\partial g^j} = b_g - \theta > 0 \quad (5.4a)$$

$$\frac{\partial C^j(g^j, t)}{\partial g^{i \neq j}} = \frac{\partial V_i^j}{\partial g^{i \neq j}} = -\theta \quad (5.4b)$$

Using this, maximizing the policy maker's objective function (5.3) is the same as maximizing

$$V_i^p = (1 + \alpha) \sum_{j=1}^k V_i^{j \in \Lambda} + \sum_{j=k}^n V_i^{j \notin \Lambda}$$

In that case, the politically optimal local public goods supply satisfies the first-order condition:

$$b_g(g^{j \in \Lambda^*}) = 1 - \frac{\alpha(1 - k)}{1 + \alpha} \quad (5.5)$$

$$b_g(g^{j \notin \Lambda^*}) = 1 + k\alpha \quad (5.6)$$

When we compare (5.5) to the socially optimal allocation in (5.2), it is easy to see that there is overprovision of local public goods to organized groups when $k < 1$. In addition, when $k > 0$ the supply to unorganized groups is lower than the efficient level. Further, note that when all groups in society are organized ($k = 1$), the allocation of public goods is socially efficient. The intuition is that when all citizens are organized, increasing the public goods supply to group j raises the contributions of that group just as much as it reduces the combined contributions of all other groups. Hence, the policy maker has no incentive to raise the supply of public goods to group j above the efficient level. By totally differentiating the first-order conditions (5.5)

and (5.6) we have that:

$$\frac{dg_d^{j \in \Lambda^*}}{dk} = \frac{\alpha}{(1 + \alpha)b_{gg}} < 0 \quad (5.7a)$$

$$\frac{dg_d^{j \notin \Lambda^*}}{dk} = \frac{\alpha}{b_{gg}} < 0 \quad (5.7b)$$

so that public goods supply to both organized and unorganized groups declines when an additional group enters the lobbying game.

In the first stage, the contribution of each lobby binds the policy maker's participation constraint in the relation to that group, given the contribution schedules of the other groups. Suppose that one of the groups with size Δk were to decide whether to offer contributions to the policy maker. When this group contributes, in equilibrium the policy maker will obtain a utility level:

$$V^{p*} = \alpha(k + \Delta k)[V^{j \in \Lambda^*} - \gamma^{j*}] + V^{s*} \quad (5.8)$$

In the equation above, the first term on the RHS are total contributions and the second term the level of social welfare. The contribution of the group must make the policy maker indifferent between (5.8) and the utility level that results when the group does not make a contribution:

$$V^{p*a} = \alpha(k)[V^{j \in \Lambda^*a} - \gamma^{j*}] + V^{s*a} \quad (5.9)$$

where the superscript a denote the situation where the group abstains from lobbying. Writing the equality, solving for γ^{j*} , noting that Δk is very small so that we may differentiate V^j to k , and then substituting γ^{j*} in $C^{j*} = V^{j*} - \gamma^{j*}$ gives

$$C^{j*} = - \left[\frac{1 + \alpha}{\alpha} k V_k^{j \in \Lambda^*} + \frac{1}{\alpha} (1 - k) V_k^{j \notin \Lambda^*} \right] \quad (5.10)$$

This result shows that in equilibrium contributions reflect the weighted loss of welfare for the organized and the unorganized groups that results from the entry of the new group. To simplify this further, by using (5.1) and the envelope theorem (as the supply of public goods results from the maximized utility function of the policy maker), it follows that for each group $V_k^{j \in \Lambda^*} =$

$V_k^{j \notin \Lambda^*} = -\theta(g^{j \in \Lambda} - g^{j \notin \Lambda})$. Substitution then gives:

$$C^{j*} = \frac{1 + k\alpha}{\alpha} \Delta T$$

where $\Delta T = (g^{j \in \Lambda} - g^{j \notin \Lambda})$ is the tax increase that results from entry of an additional lobby group.

5.3 The effect of centralization on the size of lobbies

Following the set up in the previous section, we assume that there is a legislature consisting of m delegates that aims to maximize the sum of utility of the regions and the contributions to the policy makers:

$$V^{joint} = \sum_{i=1}^m V_i + \sum_{i=1}^m \sum_{j=1}^k C_i^j(g^j, t) \quad (5.11)$$

In the literature on the political economics of centralization (see e.g. Lockwood 2005), two motivations are given for this objective function. First, when side-payments are possible, it is in the interest of the legislature to maximize the joint surplus. Second, when all legislators are veto players, the committee will have an interest in maximizing the utility of each of its members, given the utility of the other members.

With centralized policy making, the costs of public goods supply to groups in region i are shared with the citizens in the other regions, which from the perspective of the organized groups changes the marginal tax costs to their members. Truthful contribution schedules of these organized groups have the properties:

$$\frac{\partial c^j(g^j, t)}{\partial g^j} = \frac{\partial V^j}{\partial g^j} = b_g - \frac{\theta}{m} > 0 \quad (5.12a)$$

$$\frac{\partial c^j(g^j, t)}{\partial g^{i \neq j}} = \frac{\partial V^j}{\partial g^{i \neq j}} = -\frac{\theta}{m} < 0 \quad (5.12b)$$

When we compare these contribution schedules to the decentralized case, the net marginal benefits of own public goods are larger, for the tax cost are shared with citizens in the other regions. Because of this, lobbies offer a more ‘aggressive’ truthful contribution schedule in which the rewards for an additional unit of public goods when compared to decentralized policy making are higher. By contrast, now that tax cost are shared, each lobby cares less for additional public good provision to each individual other group.

Using the truthful contribution schedules, the first-order conditions for the politically optimal supply in the second stage satisfies:

$$b_g^{j \in \Lambda} = 1 - \frac{\alpha(1 - \frac{1}{m} \sum_{i=1}^m k_i)}{(1 + \alpha)} \quad (5.13)$$

$$b_g^{j \notin \Lambda} = 1 + \alpha \frac{1}{m} \sum_{i=1}^m k_i \quad (5.14)$$

Clearly, comparing this result to (5.5) and (5.6) shows that with symmetry ($\sum_{i=1}^m k_i = mk_i$) centralization does not alter the equilibrium supply of local public goods. The intuition is that, as centralization does not alter the *share* of organized groups in society, the marginal political opportunity cost of providing a unit of g^j by the legislature equals that of a national policy maker.

In addition, when in one of the countries a larger share of society is organized in lobbies, centralization increases public goods supply in that country and reduces it in the other countries. Recall that in equilibrium all organized groups receive the same amount of public goods. Hence, when a country joins a federation in which a low fraction of citizens is organized in lobbies, this increases the share of unorganized citizens that can be exploited.²

Returning to the symmetric country case, making use of the truthfulness condition and using the same procedure as in the previous section, equilib-

²This result can also be found in Brou and Ruta (2003). However, they consider centralization with a single policy maker.

rium contributions with centralized policy making are:

$$C^{j*} = -\frac{1}{m} \left[\frac{1 + \alpha}{\alpha} k V_k^{j \in \Lambda^*} + \frac{1}{\alpha} (1 - k) V_k^{j \notin \Lambda^*} \right] \quad (5.15)$$

When we compare this result to (5.10) we find that equilibrium contributions with centralized policy making are a fraction $1/m$ of the contributions under decentralized policy making. The intuition is as follows. With centralized policy making, lobbies anticipate that the local policy maker will gain less from increased contributions from other local lobbies when it retreats from the lobby game. In addition, the increase in social welfare also is lower when the group retreats from the lobbying game. The reason is that when the share of organized groups in the other countries remains unchanged, defection of a group reduces the tax costs for lobbies and unorganized groups only by a fraction $1/m$ when compared to decentralized policy making. Hence, in the first stage of the game, each lobby realizes that the local policy maker gains less from it's defection. Concluding, because the tax costs of public goods are shared with citizens in other countries, centralization provides the opportunity for each lobby to reduce it's equilibrium contributions so as to still make the policy maker indifferent between accepting and not accepting the group's offer. For this reason, the policy maker will be willing to supply a higher public goods level to an organized group for a lower contribution and becomes an 'ally' in the struggle for directing centralized funds to the country.

Note that lobby contributions are declining in the number of countries m . The reason is that more countries means less power for the regional policy maker to change the tax cost to it's citizens. Each lobby group anticipates this by reducing it's contribution. This finding is close to one of the main results in the literature on checks and balances that says that increasing competition among policy makers reduces the rents from office (see for example Persson, Roland, and Tabellini 1997). More subtle, from the point of view of each lobby, centralization reduces the power of the other regional lobbies in shaping public policies. Regional public goods supply is now 'checked' through the legislative process in the center by lobbies in the other coun-

tries.³

Moreover, this result implies that enlarging existing unions reduces lobby expenditures. The reason is that enlargement weakens the political power of policy makers already within the union and of those in the new member states. In equilibrium this is anticipated by each lobby, which reduces contributions needed to make the policy maker accept the offer by the group.

Lastly, when m jurisdictions delegate policy making to a single policy maker in the center, as in Persson and Tabellini (1994) and Mazza and van Winden (2001), in our model there will be no effect of policy centralization on lobby expenditures. With a single policy maker, the centralized objective function again is equal to that with committee decision making (5.11): the single policy maker maximizes the weighted sum of social welfare and contributions from all groups. Each group's contribution schedule offered to the single policy maker in the center is truthful and, hence, at the margin has the same shape as the one offered to the domestic policy maker under decentralized policy making. Hence, the equilibrium supply of public goods with a single policy maker equals that of decentralized policy making and that of committee policy making.

However, with a single policy maker, the size of contributions that each lobby makes equals that of decentralized policy making and is therefore higher than with decision making by a committee of regional policy makers. To derive this result, with m countries, a lobby group must make the policy maker in the center indifferent between

$$V^{p^*}(k) = \alpha(mk + \Delta k)[V^{j \in \Lambda^* d} - \gamma^{j^*}] + V^{s^*}$$

and

$$V^{p^{*a}} = \alpha(mk)[V^{j \in \Lambda^*} - \gamma^{j^*}] + V^{s^{*a}}$$

³In a trade policy setting, Grossman and Helpman (1995) obtain a somewhat similar result. In their paper, coordination of trade policy pits domestic lobbies against foreign lobbies. The effect is that this increases the economic efficiency of trade policy. However, they do not consider the effects on lobbying expenditures but on trade policy outcomes.

Using $C^{j*} = V^{j*} - \gamma^{j*}$ it follows that

$$C^{j*} = - \left[\frac{1 + \alpha}{\alpha} m k V_k^{j \in \Lambda^*} + \frac{1}{\alpha} (1 - k) m V_k^{j \notin \Lambda^*} \right] \quad (5.16)$$

where $V_k^j = -\theta/m(g^{j \in \Lambda} - g^{j \notin \Lambda})$. Clearly, with m jurisdictions the policy maker will be less concerned about the tax effects on other groups because the tax base is higher. However, the change in public goods supply affects more groups and, hence, their welfare and contributions. In the linear setting of this model, these effects cancel out so that contributions are the same in centralized and decentralized policy making case. Our result differs from that of Persson and Tabellini (1994) and Mazza and van Winden (2001), as in these two papers centralization *induces* a common pool problem at the centralized level, which *creates* the incentive to lobby. In our chapter, the incentive to lobby is already present in the decentralized policy making case. As the fraction of organized groups does not change due to centralization, a single policy maker in the center does not alter the equilibrium level of contributions.

5.4 The effect of centralization on the number of lobbies

The previous section has shown that centralization reduces the cost of lobbying. So far we have treated the number of organized groups as exogenous, but clearly, when lobbying cost depend on the level of decision making, centralization alters the incentives to organize. Following Mitra (1999), this section extends the analysis by determining the number of lobbies endogenously.

Consider policy formation as a three stage game. The lobbying and policy making stage are identical to the two stages in the previous sections, but now they are preceded by a first stage in which members of a group decide to become engaged in lobbying. The equilibrium in this stage describes which share of the groups becomes organized. To avoid multiple equilibria, we introduce heterogeneity among groups. A natural way to do this is to

assume that fixed organization cost f^j differ between groups. Let the groups in country i be ranked in ascending order of these fixed costs, such that $f^1 < f^2 < \dots < f^n$, which means that, for a continuum of groups, $f_n > 0$. Members of a group engage in lobbying when the pay-off is larger than when the group remains unorganized. In the decentralized case, for group j this condition is fulfilled if

$$V^{j \in \Lambda^*} - C^{j^*} - f^j > V^{j \notin \Lambda^*} \quad (5.17)$$

It should be noted that the equilibrium values are affected by the number of groups that are organized. Given that $f_n > 0$, to find the interior solution we first show that the net benefits from becoming organized $NB(k) = V^{j \in \Lambda} - V^{j \notin \Lambda} - C^{j^*}$ are decreasing in the number of lobby groups ($NB_k \leq 0$) within the relevant interval. Differentiating the equilibrium contributions (5.15) with respect to k while treating the second-order derivatives as very small ($V_{kk}^j \approx 0$) and combining that with (5.17) gives:

$$\frac{dNB}{dk} = \frac{(m+1)\alpha + 1}{m\alpha} V_k^{j \in \Lambda} - \frac{m\alpha + 1}{m\alpha} V_k^{j \notin \Lambda} \quad (5.18)$$

Using the envelope theorem so that in equilibrium $V_k^{j \in \Lambda} = V_k^{j \notin \Lambda}$ (the tax increase that results from entry is equal for organized and unorganized groups) gives $dNB/dk = V_k^j/m < 0$. The intuition for this result is that entry of an additional group affects the tax costs for organized and unorganized groups equally. However, when more groups are organized, the costs of persuading the policy maker to increase the public goods supply to a group when it switches from unorganized to organized is higher, since more groups punish the policy maker with lower contributions for the resulting tax increase.

The next step is to analyze how centralization affects the equilibrium number of groups that organizes. When there are m countries, for the group that is indifferent between organizing and not organizing in each country it must hold that:

$$V^{j \in \Lambda} - V^{j \notin \Lambda} - C^{j^*} - f^j = 0$$

By totally differentiating this and noting that $C_m^{j*} < 0$, we find that:

$$\frac{dk}{dm} = \frac{C_m^{j*}}{NB_k - f_k} > 0 \quad (5.19)$$

Hence, the share of groups in each country that is organized in a lobby increases when more countries join a federation.⁴ The reason is that in larger federations the contributions that each of the lobbies needs to pay to his policy maker is lower while the gross benefits from organizing are unaltered. This increases the net benefits from lobbying, which in turn increases the equilibrium number of groups that becomes organized.

5.5 Concluding remarks

In this chapter we have studied the effects of policy centralization on lobbying. A main objective has been to contribute to the discussion on the effects of centralization of policy making in the European Union. With respect to spending on local public goods, the overall conclusion is that in the symmetric country case centralization does not alter public goods supply. How does this stand up to the EU experience? Among others, Vaubel (1994a, 1994b) shows that budgetary redistribution did increase in the first years of the establishment of the EU. However, this is often attributed to the initial economic bargain of establishing the EU itself. In this view, Germany gained from market integration, whereas France was ‘compensated’ for this by a large share of the Common Agricultural Policy funds and Italy and Greece through the Cohesion funds. Harrop (2004) shows that after these initial years, structural spending in the EU has remained constant as a share of GDP. Even stronger, Wildasin (1990) argues that the initial increase in centralized spending by the EU may have crowded out national spending, leaving total spending unaltered.

When analyzing the political effects of enlargement, we have argued that

⁴We assume that the fixed costs of lobbying are constant across institutional states. This may not be realistic in practice, as it is often argued that centralization raises the fixed cost of lobbying. This obviously reduces the incentive to form a lobby.

adding new member states may reduce lobby expenditures for each group and, hence, increase efficiency. However, the fall in costs may trigger new groups to organize, which may reduce overall efficiency in public goods supply. A major concern with respect to enlargement of the EU not discussed in the chapter is the loss of efficiency of the legislative process when policies are formulated on an intergovernmental basis. The reason is that taking up more members increases the transaction costs of policy making, for consensus among the member states is more difficult to achieve. However, Steunenberg (2001) notes that when taking up countries in Central Europe, these risks are limited, for policy preferences of these new member states are not further from the core than those of the present member states. In addition, when new member states are relatively poor, funds will shift, leaving present member states worse-off. Kandogan (2000) argues that this creates incentives for present members to change voting rules, so as to prevent new members from obtaining more public goods in the future. Heinemann (2003) shows that this is just what happened in the Treaty of Nice.

This chapter also adds insights to the political economics literature that studies how centralization affects the prevalence of corruption of policy makers (e.g. Bardhan and Mookherjee 2000). As informally argued by Prud'homme (1994), local policy makers are more exposed to powerful local lobbies. Hence, in the Madisonian tradition, centralization dilutes these local interest, and so reduces corruption. However, an argument against this stance is that centralization makes individual policy makers less accountable, which increases the prevalence of corruption. This last position is supported by Fisman and Gatti (2002), who in a cross-country study show that centralization is associated with higher levels of corruption. Possibly for this reason, in the current debate on institutional reform in developing countries, there seems to be a tendency in favor in promoting decentralized policy making.

This chapter contributes to this debate by separating the effects of centralization on lobbying. On the one hand, in our model centralization increases the willingness of local policy makers to lend an ear to special interest groups. Hence, one may argue that centralization increases the effectiveness of lobbying as the objectives of local policy makers become more intertwined with

those of their special interest groups. On the other hand, as special interest groups commit smaller funds to lobbying, one may conclude that the inefficiencies from rent seeking are less severe with centralized policy making. Further, as centralization reduces lobby costs, more groups in society will become engaged in lobbying, therefore increasing the role of special interests in society. However, the increased competition among these organized groups increases the efficiency in supply to each of them.