

EXECUTIVE SUMMARY

Fiscal Constitutions: An Empirical Approach

The overarching question posed by this dissertation is: *“why does the public debt grow, and why are fiscal (debt) crises repetitive and so widespread?”* A special focus in answering this question is given to a fiscal constitution, which contains a country-specific set of laws, rules and regulations, and guides decision making in the area of fiscal policy. By shaping incentives and limiting arbitrariness, the fiscal constitution determines the course of fiscal policy and fiscal outcomes in the long term. This dissertation does not give, however, an exhaustive response to the overarching question. Instead it asks much narrower questions, which are selected after reviewing and identifying the main weaknesses and gaps in the modern literature on fiscal constitutions.

Besides an introductory chapter that is instrumental in setting the stage for the discussion on fiscal constitution, this dissertation consists of four chapters including original contributions to the literature based on targeting self-contained questions.

Chapter 2 examines electoral systems and their impact on selected fiscal variables, such as vertical fiscal imbalance measured as a share of local expenditure covered through intergovernmental transfers and borrowings. It uses a quasi-experimental empirical setting and provides evidence that electoral systems influence fiscal imbalance. The empirical design employed in chapter 2 rests on a discontinuity in the application of electoral rules in Polish municipalities in the period 2002-2012. The results presented show that proportional systems lead to a larger vertical fiscal imbalance as compared to the majoritarian regimes. This result is important forasmuch as larger vertical fiscal imbalance leads to greater general government deficits and, consequently, to larger public debt.

Chapter 3 subscribes to the literature stream that attempts to answer the question regarding whether history matters. This chapter exploits a natural experiment, which was provided by Poland's partition in the 19th century. By means of spatial regression discontinuity, it is shown that municipalities from the former Prussian empire impose contemporarily higher property tax rates as compared to municipalities that were exposed to the Russian ruling. Higher property tax rates lead to larger own revenue and higher fiscal autonomy. As a consequence of it, there is a smaller vertical fiscal imbalance in the municipalities belonging to the former Prussian partition. Given the positive link between vertical fiscal imbalance and

general government deficits and debt, these results can shed some light on the overarching question: *“why does the public debt grow?”*

Chapter 4 analyzes judicial behavior overall and contrasts it with the judicial behavior in adjudicating fiscal cases. The analysis of the decision-making in the Polish Constitutional Tribunal seems to support the existence of some party alignment. It is to say that judicial behavior is influenced by the ideology, either because judges' preferences coincide with the interests of a specific party or because the judges are incentivized to show their loyalty to the nominating party. The fact that ideological bias is present also in fiscal cases might have important implications for public finance. Occasionally the majority of judges in the adjudicating benches are politically aligned with the petitioners, which in the Polish context are typically opposition parties. For that reason it might be harder for the governing party to pursue major reforms of public finance, such as fiscal consolidation and public debt reduction.

Chapter 5 provides an empirical assessment of federal fiscal constitutions and the interaction between constitutional arrangements. It demonstrates that federal fiscal constitutions differ in the degree of constitutionally guaranteed decentralization. More specifically, two types of fiscal constitutions can be distinguished: decentralized and integrated. An important contribution of this chapter is to show that fiscal constitutions vary in terms of coherence (or alignment) of institutional arrangements. Coherent (aligned) fiscal constitutions combine arrangements in a balanced manner or in a way that they “fit well.” together.

The thesis provides some preliminary evidence that the degree of decentralization of fiscal constitutions is hardly associated with economic and fiscal outcomes, but alignment (or coherence) of fiscal constitutions is correlated with selected outcomes. For instance, over the period 1980-2010, less coherent fiscal constitutions were correlated with higher debt and spending growth, and more economic and sovereign debt crises. Again, this finding contributes to answering the overarching question *“why does the public debt grow, and why are fiscal (debt) crises repetitive and so widespread?”*

Chapter 6 includes conclusions. However, it does not only summarize the main findings of the dissertation, but also sets a general agenda for future research on fiscal constitutions.