The traditional discipline of public finance had originally been the core of political economy. Over the past three decades, however, it has been redefined by leading scholars as the new public finance or public economics. At the same time, economics as a scholarly discipline has experienced a precipitous decline in relevance, and this has prompted many university administrators to abolish programs in public finance. Recent awards of the Nobel Prize in economics went to James M. Buchanan and William Vickrey, both innovative professors of traditional public finance. Although not ignoring the accomplishments of the new public finance, this article focuses on the traditional message of public finance as a discipline that allows scholars to communicate with policy makers. The canons of taxation and the emphasis on focusing on the social question are identified as the main tenets of public finance proper.

OLD OR NEW PUBLIC FINANCE?
A PLEA FOR THE TRIED AND TRUE

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A plea for the tried and true makes sense only if the tested and tried has somehow been subject to challenge. In fact, there is a consensus in public finance now—even a name change in the subject matter has occurred—that "recent developments in and future prospects for public finance" have made the tested and tried public finance superfluous or perhaps a sideline of public finance.[1] Many other examples could be cited, such as the appearance of the *Journal of Public Economic Theory* and scores of similar lectures. In addition, a large number of survey works have cut out classical principles, knowledge, and empirical research in public finance, and this has often been hailed as progress. It is not inconceivable that forgetting acquired knowledge, the relevant techniques, and the appropriate legislation, including its interpreta-

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tion, can be progress if in fact the entity around which this revolved had always been evil. It would then have to be proposed that a less evil entity required different theories, applications, instruments, and their implementation. However, that effort has never been made in hailing the progress of the new public finance or public economics as it tends to be called now.

In many countries, such as in the Netherlands, public finance has disappeared as a scholarly discipline. It has been replaced in that particular case by public economics, and the supreme auditing institution (court of audit) recruits business economists and sociologists able to deal with accountancy. Also, the new fields of fiscal economics and fiscal law have arisen. Similarly, in Germany, even traditionally proud departments of economics have bled out, and new departments are being set up that teach business economics, particularly the economics of public business in many different variations, from budgeting to hospitals. These are traditional fields in public finance. This professionalization of traditionally public finance disciplines can be looked at in many different ways. My way to look at it is whether it makes sense to replace a traditional discipline that had its purpose, its methods, its journals, its modes of scholarly contact, and its encyclopedias and replace it with new developments that necessarily have to acquire talents who have to be trained differently and have to reestablish all those institutions I just mentioned.

This article is explicitly one-sided. It is a plea. I am therefore not discussing the new public finance at all because my readers will be very well aware of it. I am also not suggesting that the old public finance always led to benign results. As a matter of fact, it was such a thorough discipline, akin to game theory, that it lent itself to benign and less benign results. However, the discipline has always been solid enough to make it possible to weed out crooks. Nor am I claiming, as it has sometimes been suggested, that traditional public finance requires a strong and austere state. Rather, I am trying to show that the traditional principles of public finance could lead enlightened scholars to very benign welfare state legislation; as a matter of fact, that used to be the very heart of it. It is true that with my very heavy emphasis on public finance doctrine, I do create the impression that public finance is a matter of Europe (and Japan). Here, there is a slight possibility of misunderstanding, as the United States as a scholarly community established a strong public finance (mind you, not public economics) scholarly community as a consequence of the unfortunate policies in Europe during the 1930s. Where the scholars reach their insights, whether at home or in exile, there is not so much an effect on the result of their scholarly pursuit; it rather affects the zeal with which they try to pursue it. Hence, because America received this strong public finance tradition from the 1930s all the way through the 1970s and reaped its benefits later on, the American community of scholars, particularly deans, should be aware of what they would lose if the whole discipline were to be reduced to something much less significant and even perhaps hard to apply.

With this preface, I should now like to enter my plea for the tried and true. As a layman—who might, for instance, have to fund a university through tax payments—you might ask yourself what benefit you are doing to the community. When not least through the forceful intervention of Professor James M. Buchanan (b.1919) at a well-memorized occasion in Roanoke, Virginia, I was all of a sudden put into the environment of a land-grant university, and this very aspect of having to reach students with a particular objective was very much communicated to me, not least by the students. A land-grant university has three objectives—teaching, research, and extension—and the purpose of the land-grant university is to also enhance the extension of the scholarly work into the development of the community. Hence, when I started to teach public finance, it became clear to me that students wanted to have something that might have an extensive value to their future work in the community because they did not expect to remain students for the rest of their lives. These gentlemen students and southern ladies taught me that you have to address your instruction to a decision maker, who can then translate it into decisions that affect real people's lives. I was very much touched by this and went back to an approach when public finance was indeed taught that way. That is yet another reason why I want to suggest keeping public finance as one of the required courses, as well as keeping it as one of those disciplines that absolutely need to be funded by the National Science Foundation.

For those who ask what the purpose of public finance can be, my suggestion is to look at guideposts because this is a science with the purpose of policy. Centuries ago, those who asked for such a science to be established had a very precise purpose—an idea—and their specific circumstances before them, and so they conceived a vision. Let us then develop the science from the point of view of those who felt a need of the science of public finance, and let us put together, in an eclectic sense, what is needed to answer perfectly sensible questions of rulers that may not make perfect sense in the context of our models.

Once the new chairs in public finance had been established in the 19th century, more than 90 chairs had been founded on the European continent before the first chair in political economy was established at Oxford to study the matter; the problems that had to be seen in a coherent circumstantial set of events sometimes called for different solutions from those that could be developed in the more benign circumstances of Britain, the splendid island in isolation. In Europe, particularly where public finance was developed as a new discipline, doctrines of teaching had to be developed that would take into account disparate entities of statehood that still had to be ruled with sense under the circumstances. A science was called for that could accommodate empirical evidence and scientific knowledge that was not yet generally available and certainly not generalizable. The educative building proposed for the purpose always called for a precise description of the problems at hand, a survey of all the case studies that had been done, a survey of all the policy instruments available, and a survey of all the conceivable scenarios of policy making, most of which had typically failed. Because public finance was, at the time it was conceived, always a science that talked to a policy ruler, pointing out all the failed policies of the past was extremely important to accomplish the purpose, yet it was also important to prevent believing in the same fallacies and committing the same errors.

We can cite as our hero the political economist Johann Heinrich Gottlob von Justi (1717-1771), who can almost be called the prototype scholar of public finance under such conditions (von Justi 1760). He would always identify a ruler, whom he would talk to, and then gather assiduously, without being impeded, every conceivable fact that he could find to fit it into the system—of course, he had taken this method from Wolff (1679-1754). Now, the next step consists of finding the causes for public concern's problems; public concern identifies symptoms but never causes. At least, one should find triggers for such concern because those might point to policy instruments. Immediately, we discern hints to the attempts by Umpfenbach (1832-1907) and Wagner (1835-1917) to find general rules in describing the workings of ruleable states (Umpfenbach 1859-1860; Backhaus 1997a).

It is important to note that Wagner, in his attempt at finding laws for a state to be governed prudently, always presumed sensible rules of government that would prevail and prudent advisers who would help the governors, either popularly chosen or coming in through inheritance, to follow those general rules that had, historically and systematically, thus been understood scientifically. Here we have to cite first of all Wagner's law, which is the law of the increasing tasks of the state. Many economists have turned this into the increasing expenditures of the state. However, Wagner does not give any clue why that should be the case. Rather, Wagner saw the law of the increasing tasks of the state as an admonishment to the ruler to find increasing sources for state expenditure, notably those that would not burden the subjects. Hence, in a way, Wagner can even be called in as a witness for those efforts in some countries, such as Britain, that have embarked on large-scale privatization policies. In his law, those privatization legislations are clearly acts of government impressing the will of a government onto an economy to accomplish a particular economic style. Wagner's law, by the way, is even correct for countries that try to negate it. Those who turn to privatization invariably turn to regulation and thereby force the iron hand of government even more forcefully. Likewise, those who propose to engage in privatization typically turn to such instruments as public investment through new financial instruments, thereby increasing the future burden on the public purse.[2]

The more important aspect, to which Wagner's law should lead us, is the reason why the state has to engage in ever more encompassing tasks. This is shown when the state, in which the law was put to its purpose, faced its most extreme challenge, that of the class struggle. Two different notions had taken hold in the minds of leading citizens, as well as able scholars' minds. One was the notion of national unification, and the other was the notion of class struggle. By political ends, the notion of national unification prevailed, but an idea cannot be put down by fiat. Hence, the underlying cause of the competing notion of class struggle had to be addressed. This is where Wagner's law gets a totally different turn. Now, the state has to face the failures of the market. Hence, all those phenomena of the market that bring about these failures have to be properly understood. One cannot cure a failure if one has not understood the source of the predicament. Flight from the land, leaving not a good but at least a poor and secure life and going into the city, had destroyed the local community. Large numbers of people, particularly young people, went into the swelling cities, looking for a better life and for circumstances that somehow would fit their ambitions. That they did not find. It was Bismarck's (1815-1898) (advised and guided) ingenuity to understand this as a problem of insurance. Where the markets did not care to provide insurance, the state (guided by a preeminent investment banker by the name of Bleichröder [1822-1893]) had to step in. The idea of insurance for social predicaments was new. It was also new to suggest that the new social institutions should be brought about in such a way that they were only basic and could serve as the springboard for market-based arrangements.

It would perhaps be wrong to say that Bismarck fully understood the economic logic of what had been proposed to him. However, it would be equally wrong to say that he had not understood the political logic of what he was about to implement. Many different threads were necessary to weave the cloth of public finance. Bismarck was fortunate for having advice of the kind he did at that time. What is more important is the basic message, which Bismarck did not refuse to accept and modern scholars in public finance do refuse to accept: that there is such a thing as scientific public finance that can guide public policy. It has to be put on very sound footing. New institutions need to be devised that make it possible to find ever more purposes for the market. In the particular case of social policy at hand, with the uninsurable risks of life in the ever more rapidly developing economy, impetuous industrialization with new and threatening technologies had to be found. The then threatening technologies of the steam engine and the railroad, still to this very day under special legislation, filled the populace with grief and despair and had to be responded to with special policies. Today, we might laugh at this, but the fears of the population at a particular point in time certainly inform its investment behavior—how they invest in stocks, bonds, real estate, and, above all, their lives.

At the time, most of them invested in their children, many of whom perished in World War I.

Coming up, then, with a government program to create an investment scheme for the major uninsurable risks of life was a major push at what today would be called privatization. Because there was no insurer in place, the Prussian state with its (relative) majority vote pushed it forth in the federal council, and so it happened. No underwriting, no public tender, just a state-sponsored market-based social insurance system that would tackle these hitherto uninsurable four risks of life. From the point of view of public finance, as the theory then stood, this was absolutely new. Bismarck, who had brilliant advisers, had hit upon a formula that even his political instinct could not fully balance.[3]

From today's point of view, we should look at the four risks in detail. The four risks to be insured all relate to the fact that the newly arrived in the swelling cities had essentially only one asset, their ability to work for a wage. With no own land on which to eke out at least a subsistence, the loss of this ability to work necessarily had catastrophic consequences for workers and their dependents. The loss could occur because of work-related accidents, poor health, or early death with no provisions for dependents; inability to work due to old age; and, of course, unemployment. Bismarck's program covered the first three of these risks; unemployment insurance, which came later, covered the fourth.

When the new social institutions to cover these hitherto uninsurable risks of life were to be designed, two alternative options were discussed. On one hand, one can build new social institutions on old institutions and open those old institutions to the new circumstances of the market economy. Lujo Brentano (1844-1931) wanted to build on the old guild structure and to transform such workers guilds into institutions of self-help related to the trade unions (Backhaus 1997a). They were to perform the whole set of intricately related functions of individual and family support. Gustav von Schmoller (1838-1917), on the other hand, was afraid that the old institutions would not be able to perform the new functions and that accumulation of risk would further endanger those who were to be insured. He therefore pleaded for a market-like actuarial insurance approach with the state as the reinsurer of last resort. Coverage was to be limited, providing a base on which private insurers could then build so as to provide insurance policies for those workers and craftsmen who started to accumulate wealth through industrialization. Prince Bismarck carried out the essentials of von Schmoller's approach.

von Schmoller, however, emphasized another aspect as well. On the occasion of his introduction as rector of the University of Berlin, he used his inaugural lecture "On the Idea of Justice in Political Economy" (von Schmoller 1881) to point out that public policy, particularly the creation of new social institutions, could only be successful if these institutions were considered just by the standards of the population for which they had been created. Justice as an empirical concept was differently conceived of in different countries by different peoples, and it was, in principle, possible to establish justice in a particular people and apply it to the creation of new social institutions. By establishing the notion of justice as an empirical social scientific concept, he distinguished himself from philosophical, theological, legal, or other approaches to provide for a political and constitutional safeguard to protect the new social institutions.

After the crushing defeat of the German empire, with which all these reform policies of building new social institutions had to be identified, the generation of von Schmoller's students, including Heinrich Herkner (1856-1932) and Werner Sombart (1863-1941), set out to deal with "the economic consequences of the peace" from the point of view of public finance (Sombart [1916] 1927). The framework of new social institutions was actually extended, unemployment insurance was added, but the actuarial principle fell victim to the regime of reparations under which Germany operated; the formation of new insurance funds was impossible in view of the demands for reparations, and the old funds had long been used up in war finance. Opting for a pay-as-you-go system to fund social security, war victims and veterans, orphans, widows, and the retired was a fiscal necessity, not a matter of political expediency as in the United States under President Franklin Roosevelt (1882-1945). There, on the other side of the Atlantic Ocean, Congress mistrusted the president and did not want to deal him a large and ever-growing fund that the executive might mishandle for its own political ambitions.

As a consequence of the provisions contained in the Treaty of Versailles, the revenues of the great state institutions (including the railroads) were no longer at the disposal of the government. Hence, the public economy after 1919 had to function in reverse gear. Where before profits had been made through participation in the market, now losses had to be shown. Where before insurance funds had operated strictly according to actuarial principles, now cross-subsidization had to be resorted to. This system, initially a measure of despair, was in fact an anticipation of the new era of public finance that, after Abba P. Lerner (1903-1982), came to be known as functional finance. Lerner (1943) drew the conclusion from Keynes's (1883-1946) teachings that the public budget could be put at the disposal of economic policy, notably macroeconomic policy, to develop stabilization policies with respect not only to the national economies but ultimately also to the global economy (Keynes 1936).[4]

German public finance had one last intellectual peak at the end of the 1920s, when, under the direction of Wilhelm Röpke (1899-1968), an employment program was designed with purely fiscal instruments, which was immediately put into effect after the stemming of the reparations payments as a consequence of the Lausanne Conference in 1932.

The successful policies, launched by the last two democratically legitimized governments, bore their fruit with small delay, but the harvest could be reaped, initially with reluctance, by the National Socialist government (Backhaus 1999a). This resulted in a twin tragedy. On one hand, reducing unemployment has to this day been credited to the National Socialists, although these policies had been laid out by the preceding democratic governments (Backhaus 2001b). Second, the obvious success of the employment measures, which had been erroneously ascribed to the National Socialists, led to a taboo. There is no serious study that looks at why these programs were actually successful. The first fault (that of not understanding the historical circumstance) led to the second fault, not touching the taboo area of National Socialist policies with respect to labor markets. Because these policies initially were not National Socialist, an important lesson was lost on the profession that could have studied the theory and the measures based on the theory well before 1936. This case shows in a particularly crass form that public finance as a scholarly discipline is always subject to political influence; we should have surmised as much; yet the consequence is that scholars in public finance should not be allowed to pursue their models without consequences. Scholarship in public finance carries a particular political ethic and responsibility. You do not have to agree with his solutions, but it was James M. Buchanan again who reminded us, remorselessly, of this particular ethical responsibility of public finance scholars.

If you introduce your topic with a historical survey, it is becoming to leave about half a century between your historical observations and the situation as it presents itself at present. Hence, I am not looking at the development of public finance after the Federal Republic had been founded. The last really interesting approach to integrate public finance and public finance administration into economic theory probably came from Freiherr von Stackelberg (1905-1946), who presented his approach to fellow scholars during the waning days of World War II. He was interested in the economic order after the war, as he was convinced that the war had been lost (Backhaus 1996). At the time, it was considered high treason to promulgate such thoughts, and in fact von Stackelberg had not only thought about removing the Hitler regime, but in all likelihood he had participated in the attempt of July 20, 1944. He was one of those rare economic theoreticians ready to take his economic insights and translate them into economic policy measures that he thought to be relevant, with respect to a specific economic purpose: In his case, he was interested in promoting competition. Instead of having an anti-trust authority that would permit, forbid, or fine, he proposed a rigorous tax scheme that is much more radical than commissioner Monti might ever conceive of; as a matter of fact, he should not because it would render his entire commission unemployed. However, von Stackelberg's scheme, which is different from the current policies of the European Commission, would provide the order of the law (*Rechtsstaat*) so as to allow markets to function. After this very broad and general survey, let us now look at our topic in more detail.

1. THE OLD AND TRADITIONAL DISCIPLINE OF PUBLIC FINANCE

As we look at classical public finance—after all, this is what I am pleading for—the best way is to start with Wolff's general system (von Wolff 1754), and then we can immediately proceed to Johann Heinrich Gottlob von Justi. In true public choice tradition, one has to look at the background and the circumstances to understand the purpose of the core ideas of this man to give them their proper place. Adam Smith (1723-1790) only a little later tried to explain the causes of the wealth of nations (Smith 1776), whereas von Justi (1760) was interested in the core idea of the state (*Grundfeste*), which would explain the might but also the welfare of the states. The might of the state consists of the abilities of its inhabitants, what today is called human capital. Yet von Justi was interested in not only the wealth but also the ability to create wealth and to make it possible to enable others to create wealth. Friedrich List (1789-1846) used the expression of productive forces. What von Justi described as the welfare of the state (*Glückseligkeit des Staates*) can only be accomplished if the citizens can be enabled to reach such a bliss point themselves, and hence it is the purpose of the state to create the conditions for this to happen. In the case of von Justi, the state's happiness is obviously greater when a larger number of people can be made happy. This is perfectly logical. After all, he was interested in the ability to produce and create wealth and welfare and to be able to accumulate both.

Given the circumstances, von Justi founded public finance as a science in the context of a state-oriented general science, with heavy emphasis on bookkeeping in the Cameralistic tradition. This is important. The Venetians developed bookkeeping to make it possible for democracy to function in a state that disposed of substantial resources, in addition to risk-laden activities, whereas the Cameralists (who have their name because they had access to the chambers of the prince) developed a system of thought that could be taught, which was also fitted into administrative procedures. In a sense, this is not very different from contemporary business economics. In business economics, it is clear what the purpose is. The consultant talks to the chief executive officer and the board.

Likewise, the Cameralist would talk to the prince and, to maximize the bottom line, would deal with the question of how the sustainability (*Macht*) and welfare (*Glückseligkeit*) of the state could be enhanced and furthered. The discipline, then, had a clear function: There was the consultant, and there was the consultee (i.e., the prince)—in any event, an identifiable regime. It could just very well have been a republic because at the time, there were republics soliciting this advice. It is important that the purpose is not diffuse—it is the maintenance and sustainability of the might of the state and the welfare of the people that goes along with it—but this is a far cry from today's welfare economics. Welfare economics is embedded in Cameralist economics, but the difference is that the welfare of the people is not assumed as something that is to be given by some elite; it is enhanced through a conversation between the adviser and the policy maker (the prince or, in republican circumstances, the governor). Schumpeter (1883-1950) was right in calling the Cameralists the consultant administrators because in a Habermas-type fashion, the adviser became part of the analysis (Schumpeter [1912] 1934). Because the consultee had to be convinced—and this can only be done on the basis of an analysis that produces suggestions that make sense, and that sense had to be enough for the consultee to be able to translate the advice into reasonable policy—the advice could be easily measured in terms of its success as far as the implementation was concerned. In this sense, a scholarly discipline of public finance in the Cameralist tradition can never be irrelevant.

With broad brushes, classical public finance can be characterized by three points. On one hand, it is built on principles that von Wolff (1754) originally presented in his general system of natural law. The German term for this is *Rechtsschöpfung*, and this means that you find general principles in a broad literature. Wicksell (1851-1926) did the same thing when he derived his principle of just taxation. It was by no means tongue-in-cheek when he presented his inquiries into the theory of public finance (*Finanztheoretische Untersuchungen*) (Wicksell 1869) as a series of case studies in fiscal conflicts in the Swedish kingdom and then derived from this a general principle (Wicksell 1869, 1958). He was very much in line with von Schmoller's approach, who even went further in trying to distill the idea of justice in political economy (Hansen 1996). The point is that a particular people live by principles that have developed over time. These principles are not necessarily generalizable principles of statehood, but they are certainly general as far as a particular populace is concerned. From these general principles, you can derive somewhat attenuated principles that hold more generally over public entities that have experience with taxation but that are also democratically constituted. This is an important point to note. Modern public finance does not function for political entities that have not been democratically conceived. Only functional public finance and public economics can conceivably be applied in those instances, but modern public finance, dealt on the traditional principles of public finance, cannot be applied to undemocratic societies. This is important because *consensus* is the key word in classical public finance. Also, classical public finance always has had a penal code of public financial activity; in particular, Wolff mentioned contributions (i.e., taxes that are imposed and for which citizens do not receive any valuable activity, deeds, or services of relevance). This is in violation of the principle of equivalence. Hence, we should now look at those principles.

THE PRINCIPLES

The classical principles in public finance can be differently grouped and expressed, but taken together they all amount to the same system of rules. Most authors, even in modern principles textbooks, stipulate about a handful of these principles. von Justi (1760) postulated six of them to form the normative core of public finance. He started with the principle, which he emphasized as the most important one, of the ability of the citizen to pay a tax. Citizens must be able to assume a burden without being compromised in their ability to enhance the welfare (*Glückseligkeit*) of the state. It is obvious that this is an objective criterion. Only so much can be taken by taxation that the economic process is not impeded at all. Hence, according to von Justi, the tax should not incite any tax resistance. We note how big the difference is between von Justi's principled formulation and the current versions of the principle of ability to pay. Instead of measuring objectively whether tax resistance exists as a social phenomenon and whether it is further incited through specific measures of taxation, today it is generally taught that the ability of citizens to pay a tax depends on their income and wealth; the principle is used as an almost self-evident argument for redistribution. And this is done, although it was established beyond any doubt well over a century ago that redistribution in whichever direction cannot be established as a sensible political goal of taxation by way of an argument that meets scholarly standards (Stuart 1958).

The second principle von Justi (1760) established is that of equity and fair proportions. In modern public economics, the principle of equal treatment before the law, particularly before the tax authorities, has been turned into one of equity as fairness and serves as the moral underpinning and argument for the redistribution of life chances. An example can be found in the public health services. Again, according to established scientific criteria, a basis for these policies cannot be established (Backhaus 1992).

von Justi's (1760) third principle concerns welfare and civic liberty. Each and every measure of the state must be shown to enhance the welfare of the citizenry, and it must not infringe on civil liberties. Only such measures of the state can therefore be recommended, which unequivocally increase the chances of the citizens to meaningfully conduct their affairs. Today, with respect to welfare maximization, the much weaker Kaldor-Hicks criterion with its potential improvements is taken as a measuring rod or yardstick of public policy, and the problem of individual liberties and areas of inalienable freedom has totally disappeared. In most textbooks, we look in vain for an explicit discussion of civic liberty with respect to taxation.[5]

von Justi's (1760) fourth principle requires each measure of the state, notably those that entail burdens, to be established in tune with or according to the nature of the state in question and the form of its government. This seems nebulous, but an example may serve to clarify what he means. A city-state with regular markets has different measures of taxation at its disposal than a territorial state with a substantial subsistence economy. (Many of the successor states of the former Soviet Union or most sub-Saharan African countries fit the latter type.) The hint contained in this principle is particularly fascinating as it seems to be regularly ignored by the team of the World Bank. A republic with constitutional rule by the clergy such as the Islamic Republic of the Iran obviously needs other measures than, for instance, the city-state of Singapore; the same science of political economy and taxation must be able to take into account the institutional and constitutional circumstances and to suggest equivalent but different measures for taxation and sustainable development. However, today we often meet the hidden assumption that more or less the same programs can be applied to all countries alike, and the same indicators can be used worldwide to trigger different parts of one and the same program package.

von Justi's (1760) fifth principle requires certainty and a broad legal and constitutional basis of every state measure, particularly with respect to taxation. Certainty of the law in most textbooks is mentioned indeed, but none of the textbooks I have consulted discusses in a systematic way how the economic models explained can be implemented as measures of taxation that withstand the test of an administrative procedure.[6]

von Justi's (1760) sixth and last principle refers to the implementation of all state measures, particularly those of taxation. The tax has to be levied in the easiest and most convenient way available from the point of view of the citizens. The examples show that von Justi wanted to minimize what today we call costs of transactions. When today we try to establish the extent of the excess burden of state measures, notably the excess burden of taxation, those costs of transactions are regularly overlooked. However, they constitute an important part of the research program in fiscal sociology (Backhaus 2001a).

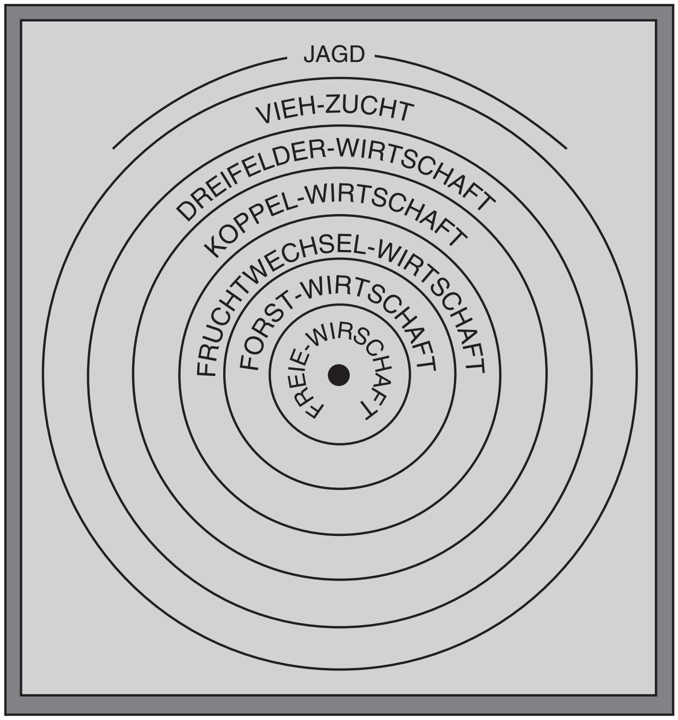
CONSENSUS

All six principles taken together show clearly that von Justi tried to put together entire packages of public measures that the prince could successfully suggest to the general estates, the traditional feudal parliament without which no taxation could be passed. Everything that constituted an additional burden had to be agreed to by these assemblies of lords. We see clearly the same principle of just taxation, which Wicksell (1869) established as the result of his empirical studies on the fiscal history of the Swedish kingdom. It was this principle of consensus (not unanimity) that James M. Buchanan put at the center of his reorientation of public finance, which he based on the classical Italian texts and, notably, the work of Wicksell.

von Justi (1760) postulated the principle more generally for economic policy, not just public finance. Contrary to the Kaldor-Hicks criterion, in von Justi's formulation, the implication is clearly that the state as an entrepreneur can find "new combinations" (Schumpeter 1934)—new combinations that he suggests to the citizens and that they will gladly appreciate if they are advantageous from their point of view. Hence, the state is not seen as a Leviathan but rather as an entrepreneur that acts in the interests of his citizens. Is this a realistic perspective? From the point of view of economic history, we can state as a matter of fact that even in 1918 in the German empire, which was a confederation of states, there were some principalities that raised no taxes at all yet at the same time offered substantial public works and services that were all supported with the profits of market-based entrepreneurial operations. Even the Prussian state received about half of its revenues from its state enterprises. During the early years of the German Federal Republic, public enterprises played a substantial role, notably in reconstruction. Once these tasks had been largely accomplished, they tended to be privatized, such as the VW corporation.

From the point of view of the principle of consensus, entrepreneurial activity of the state, if the state is not granted any privileges, is particularly significant because the state as an entrepreneur does not claim anything from its citizens that these citizens do not want to give voluntarily. When there is no coercion and when everything is done out of free will, there is obviously no resistance and no economic loss due to this resistance; hence, there cannot be an excess burden on the basis of those measures that von Justi (1760) had in mind.[7]

By putting von Justi into the proper context within the history of thought in public finance, we can arrive at a conclusion that is, from the point of view of economic policy, rather unusual. The state as an entrepreneur can very well be seen as an integral part of the market economy, and this also can be the case in this age of globalization. Likewise, given recent controversy and the activities of commissioner Monti, state enterprises can claim their proper place in the common markets of the European Union, as it had been provided for in the Treaty of Rome. Yet the condition must always be that state enter-



prises are given no preference over others, whether this competition already exists or whether it is only by contention. This argument for state entrepreneurship follows consensus-based welfare economics not just from the interest of the treasurer, however legitimate these interests might be.

THE PROHIBITION OF CONTRIBUTIONS

The third critical element of classical public finance, on the face of it, looks so utopian that I have left it for the conclusion. von Wolff (1754) was explicit in deriving the prohibition of contributions from natural law; this means that all those levies for which citizens do not receive an equivalent are illegal and void. If citizens have to choose between the demands of a state and those of a criminal organization, and they decide on the latter (Nerré 2001) because they expect better protection from the gang than from the state, then precisely that case has occurred against which von Wolff had adamantly warned. von Justi (1760) repeated this warning in his set of basic principles. How should a state be fiscally provided for if it cannot levy any taxes for which the citizens receive nothing in return?

The answer to this question is by no means trivial, but there are numerous historical examples. We can turn to the populist economist Henry George (1839-1897) or the Nobel Prize winner William Vickrey (1914-1996), who both in their different ways have argued for incentive-compatible forms of taxation (George 1888; Vickrey 1994). A somewhat more exotic example, which is not very well known, may drive home the point more forcefully. In 1898, the later admiralty council Dr. Wilhelm Schrameier (1859-1926) was suddenly confronted with the task of designing a constitution for the protectorate of Xingdao that should have allowed for (1) the protectorate to serve as a base to access the Chinese internal market; (2) the building of an infrastructure, an administration, and public health services, including a university; and (3) a plan for the entire protectorate to be handed over to China after the end of a lease of 99 years. The task was one of sustainable development. He therefore divided the time horizon in three equal parts of 33 years and designed a city map and zoning for the practically uninhabited place, which, from the point of view of geography and maritime demands, was a particularly favorable bay. The city map with the zoning system allowed for an assessment of the land rents. Public areas remained untaxed. By taxing away the land rent yet leaving all improvements tax free (i.e., all the buildings and other infrastructure investments could bear their fruits without any taxes levied on them), Schrameier was able to lay the foundations of what shortly thereafter was to be called the pearl of East Asia. In 1914, the pearl was considered so valuable that the Japanese invaded China and took the protectorate from the mainland as it had defenses only toward the sea. (Because it was to be turned over to the Chinese, there was no attempt at fortifying it against the mainland.) Not a single tax penny had been allocated in the imperial German household for the civilian construction of the city, which the parliament would probably never have approved anyway. Today, the city boasts several million inhabitants, yet the buildings constructed under Schrameier's tax scheme, seemingly built for eternity, have even survived the tempests of the Cultural Revolution (Backhaus 1997b).

Much less exotic examples can be found in the numerous projects that William Vickrey had theoretically devised and practically proposed, which are designed in such a way that politicians, aiming at reelection, can successfully pursue and put into practice (Vickrey 1994).

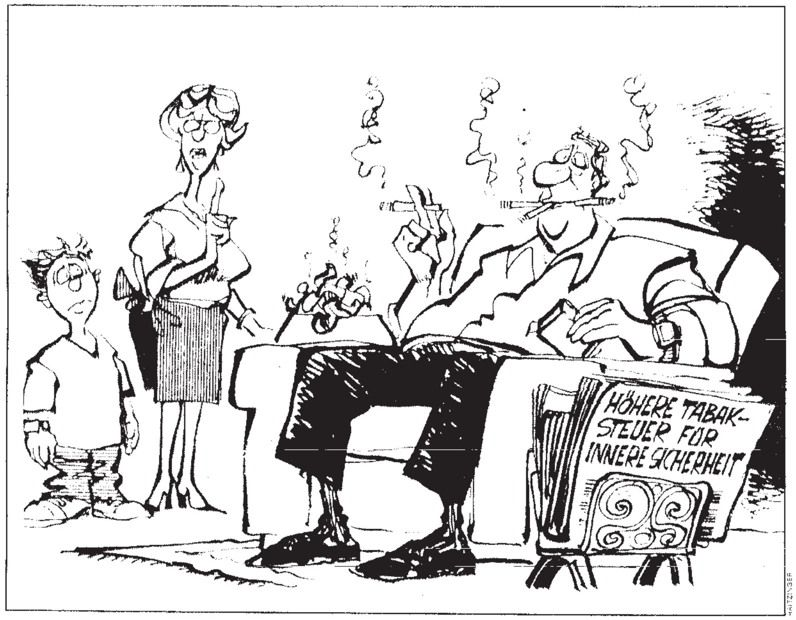
A BASIC POINT ON ECONOMICS

Economics is the science of choices. Citizens, out of their free will, make choices, and they do not behave like the elegant figures in Heinrich von Kleist's puppet theater. For economic and fiscal policy, this implies that citizens have to be presented with alternatives from which they can meaningfully choose. They have to be presented with choices that they gladly opt for. This article will close with a brief discussion of three such options.

2. THE PHENOMENON OF FASHIONS IN PUBLIC FINANCE THEORY AND POLITICS

Fritz Neumark (1900-1991), for a long time the senior of public finance in Germany and longtime editor of its foremost journal, *Finanzarchiv*, was one of those budgetary experts who helped in translating the deficit-based reemployment policies of 1932 into budgetary measures. In 1933, he was forced to emigrate from Germany and moved to Turkey, which had extended an invitation to German scholars to build the new university at the Bosporus, the Marmara University. He also helped bring about fiscal reforms there; even in the 1980s, he enjoyed a stupendous public reputation in Turkey. This realist, who emphasized practical results and applications in a much-noted essay in the international social science journal *Kyklos*, pointed to a problem that can plague a discipline that, by its purpose and function, is close to political decision taking.

He talked of the fashions in public finance politics that can sway and infect an entire scholarly discipline (Neumark 1975). In many parts of life, little may be objected to the phenomenon of fashions. We



are happily surprised when, due to the caprices of fashion, people we have grown used to suddenly surprise us by appearing in different costumes; small disadvantages may be adroitly compensated, and as we grow older we are reminded of happy times when the fashion cycle repeats itself. Fashions do not only make life more varied and interesting, but due to the cycle in which they tend to appear, they even create a semblance of continuity.

In politics, however, fashions do not necessarily meet with positive reactions. When, confronted by a budgetary crisis, the minister of finance wants to increase the tobacco excise, we are reminded of Popitz's law, and the appearance has an haut goût of déjà vu. One cannot suppress a certain distaste, and the cartoonist makes the point clearly. (Headline: "Increase in Tobacco Excise to Bolster Security Expenditures.") The recurring topic has a very long history. During the Seven Years War, which almost led to the bankruptcy of the Prussian state, Frederick II (1717-1786) had to increase the coffee excise. A poster shown in the streets of Berlin depicted the king as an old woman with long fingers trying to snatch away coffee beans from a coffee grinder. One day, people gathered in the street to look at the poster as the king rode by. Embarrassed, the citizens gave way, but the king is supposed to have said, "Put the poster higher up, so it can be better seen."

Today, the classical excise tax is sometimes called an eco-tax. Although it is well known that an eco-tax can only be effective inasmuch as it is ineffective as an excise in raising revenues, only taxes without revenues can be effective eco-taxes. And when, on top of this, the classical excise is even hailed as a measure of labor market policy (which is to yield the double dividend of an improvement in the environment coupled with a positive employment effect) and is seriously suggested in political discourse, citizens have a right to turn away from traditional politicians and claim to be tired of politics (Backhaus 1998a). It is easy to show that the double dividend rests on a very specific modeling approach with very specific assumptions that cannot be reaped in present-day Germany with its present-day institutions.

From the point of view of public finance, you have to ask whether, instead of turning to models, it would not be better to use a classical form of legitimizing taxes. I am thinking of the agreement of the taxed. Even if the expert in public finance in the council of economic advisers is willing to go along with this political game, the simple citizen who has to pay the eco-tax at the gas station knows full well that the so-called eco-tax is nothing but a classical excise tax. Citizens may not know the term *excise tax*, but they know how it works because it has already been around for several centuries. With good reasons, von Wolff (1754) criticized the excise tax from the point of view of natural law principles; today, we can put forth essentially the same argument by pointing to the welfare loss that excise taxes cause.

In fact, fashion cycles in public finance have a long tradition. Since Teutophilos (ca. 1685) proffered the excise tax as a recently discovered nugget hole, ministers of finance have rediscovered the nugget hole with ever-new names but always the same principles. Most of the eco-tax and the tobacco tax are classical excises. Another recent comeback of an old nugget hole are the so-called privatization windfalls that some states such as Bavaria and Baden-Wuerttemberg have recently earned and disposed of. Selling mines, stocks in public utilities, or real estate can hardly be hailed as a profit-making activity. We are talking now about pure liquidations, which are extraordinary state revenues that should not be used, according to classical principles, for the ordinary budget but only for the extraordinary budget for either reducing the public debt or infrastructure investments. In fact, what is hailed here as an extraordinary operation of privatization should be an ordinary restructuring procedure. For every public enterprise that cannot earn profits in excess of the current bond rate, the assets should be disposed of with the possible side effect that a private entrepreneur might do better.

In this vein, privatizations had already been suggested by von Cölln (1753-1804), who in this way interpreted Adam Smith's teachings against the then current Prussian fiscal policies. The state should retreat from public enterprise and leave it to the private initiative. In this way, the first large wave of privatizations was initiated after Napoléon (1769-1821) had both politically and economically weakened Prussia, and new ideas were much in demand. The state bankruptcy as a consequence of the Treaty of Tilsit did not happen, however, because the Prussian sea trade corporation skillfully managed the substantial and unfunded Prussian public debt, notably in the London market. To avoid an open bankruptcy of Prussia, the extent of the debt had been kept secret, and after about a generation of skillful management, new issue and repurchase, and the launching and later sale of new public enterprises (notably in new technologies), the debt had been totally paid off. The sea trading corporation even built positive assets. It needs to be emphasized that these practices were totally at variance with the views of the leading theorists of the time. Wilhelm von Humboldt (1767-1835), who put his stamp on the new Prussian state, was interested in defining the limits to which the state could be effective. It cannot be denied that this basic approach can also lead to ideologically caused mistakes when effective and beneficial state activities are dismissed on a priori grounds.[8]

Sometimes intellectual fashions can be used to create new areas of freedom for scholarship. This is, of course, particularly important when scholarship is under siege. After Hans Grimm (1875-1959) published his book *People Without Space* (*Volk ohne Raum*) (Grimm 1926), a book written in Southwest Africa that argued for the need of colonization there, a whole new scholarly discipline dealing with space and location developed and received politically motivated support in the 1930s. Economists recalled the roots of mathematical economics, notably von Thünen's (1783-1850) location theory (von Thünen 1842), and the Institute of World Economics with its research emphasis on space theory (i.e., location theory) created an area of free and unfettered research, where von Lösch (1906-1945), who had returned homesick from Harvard, could work out his path-breaking contributions.

CLASSICAL PRINCIPLES AND MODERN EXPERIENCE

Having first discussed the classical principles with respect to government, but notably with respect to taxation, it now makes sense to look at 300 years of experience and to see how they stand up in the light of three centuries. After all, the principles had not just been revealed; rather, von Wolff had carefully distilled them from natural law, and von Justi had transposed them into a system of public finance that could be taught. The method of derivation was, however, not pure deduction as it had been before, when Luther (1483-1546) dismissingly said about the natural law, "*de iure naturae multa fabulamor*" (Luther 1883). In von Wolff's case, there is not just the construed, the hypothetical, the possible, and the derived; rather, the whole work tries to integrate all those empirical facts of law that the author could put his hands on. It is the concreteness and empirical validity of his explications that explains why von Wolff, after a quarter of a millennium even today, is an important source at the tribunal at The Hague.

The six principles. From an empirical point of view, the first principle seems to be almost self-evident. A measure of public finance must be feasible; otherwise, it cannot fulfill a function except in talk shows. The limits of feasibility, however, have been drastically extended as a consequence of progress in making administrative procedures more efficient, in developing new instruments in every market in which the government plays a role, and in terms of the international interconnectedness where new techniques (e.g., market instruments) can be pushed to their great effect. In fact, public finance in administration is hardly up to the task of modern government. The procedures that are necessary to follow the rule of law rarely have been upgraded and are often cumbersome. We can see that the first principle, which Stiglitz (b.1942) pointedly put in last place from the point of view of modern financial practice, is particularly important because it requires the public finance institutions to upgrade their practices to modern possibilities and the modern state of the art (Stiglitz 2000). This refers to the Internal Revenue Service, but it also refers to the cooperation between certified public accountants and the revenue service, as well as the services of controllers, fiscal courts, courts of audit, specialized colleges where civil servants are being trained, and, to that extent, also the universities.

The second principle—that of equality—certainly found a solid position in occidental constitutions, especially after the French revolution with its call for liberty, equality, and fraternity. Far beyond its original area of application, the principle is now universally being applied, even to an extent inside the family. The connected principle of proportionality also belongs to the solid core of principles in European public administration and constitutional law (Backhaus 2001b). We cannot think of modern open societies that are market based without these twin principles being in force. The market is a system of communication that can only work on the principle of equality of access, and a legal system that is formed around the market has to incorporate the same principle of equality of access (to the court, to administrative procedures, and the like). The classical principle has been vindicated, we might say, by the logic of the market.

Looking in hindsight, the third principle also had an unbelievable predictive power. The warranty of individual liberty is now universally taken for granted, and trying to insist on it leads to the resistance of many a powerful apparatus. Yet the connection between individual civil liberties and the activities of the state in the individual spheres of income and wealth is not necessarily well understood—notably on both sides of the Atlantic and especially after the September 11, 2001, terrorist attacks on the World Trade Center and the Pentagon. Hence, when the state exceeds its limits and violates individual liberties, even in the pursuit of noble purposes, the necessary welfare loss may be large but is never fully accounted for. Another example taken from recent German history may illustrate the point. The parties negotiating the reunification treaty always claimed that those properties expropriated by the Russian military administration immediately after 1945 (largely real estate and industrial property, where much of the real estate concerns agricultural and forestry property) could not be restituted because of objections from the former Soviet Union, then guaranteeing power. This is not just a matter of whether the families expropriated under archaic circumstances after 1945 are now being prevented from disposing of their property and thus have their individual freedoms violated. The negative economic consequences go much beyond this because the old and legitimate owners can no longer build on the specific bond that they have with their inherited property, they cannot bring the long lines of credit that they have built up in the West back to the former properties, and they cannot bring back the know-how they have taken to the West. In addition, the new technologies and goodwill accumulated in the West are withheld from the orphaned factories, farms, and other ventures. This is particularly true after mid-1990s because the large orphanage, the German *Treuhand*, has finished its task of finding new parents. The result of this is easily grasped by any visitor in the new federal states, where inner-city areas remain unused; large, impressive buildings decay; and the state forestry services run large deficits, despite the fact that returning the forests to their legitimate owner would not only relieve the state of a burden but would also make sense from a business and ecological point of view (Backhaus 2002). Hence, we note that the principle of protecting individual liberty has much more complex indications from a purely economic point of view than generally meets the eye.

The fourth principle likewise remains fresh and modern. Every measure of the state has to be in synchrony with its structure because otherwise there may be friction. In the European Union, we have member states with largely differing constitutional structures. Any common initiative cannot be readily legislated; it can only be formulated in principle, and then the principles need to be translated into measures commensurate with the structure, the legal institutions, and history of the specific member state in question. This means that, in principle, the commission cannot regulate directly, nor can the council of ministers. Everything has to be implemented, and there is plenty of room for disagreement about the quality, intensity, and form of implementation, as well as about the European zeal with which it is pursued in any particular member state. Here, traditional principles of public finance can be readily applied and generalized into more encompassing principles of harmonization. The new subdiscipline of constitutional public finance can help in showing how different legal principles and different legal institutions, given the same purpose as agreed on a European level, can be put into effect in an efficient and expeditious manner (Backhaus 1998b).

The principle of legal certainty, the fifth principle, likewise has been validated from an economic point of view. Its importance extends by far beyond the sphere of public finance proper. When legal certainty is lacking, economic progress cannot take place. One only has to look at those countries undergoing processes of economic transition: In those states that succeed in building up reliable legal institutions and guaranteeing the rule of law (*Rechtsstaat*), not only economic life but also civic life is developing, sometimes in large leaps. On the other hand, when the rule of law cannot be established, we see retrogression at sometimes more primitive stages of development (e.g., a reversion to an agrarian subsistence economy). The rule of law is also a matter of competition among legal regimes. In the United States, the share in the social product that is used for the legal sector is almost twice as high as what is needed in Western European states, and it would be hard to suggest that the degree of legal certainty and the quality of legal services are commensurately higher in the United States than they are in, for instance, France. Future research will have to focus on isolating those transactions costs that are responsible for these substantial differences. Those legal systems that can render services at lower cost will have to prevail. This type of research will require cooperation between economists working in the areas of public finance, law, and economics and lawyers working in comparative law and empirical legal research.

Finally, the principle of efficiency, the sixth principle, is now quite generally a principle of social organization that is generally accepted. However, this acceptance does not mean that it is widely realized. Although those corporations that are market oriented have to develop forms of organization that compete with each other (otherwise, the corporations cannot survive), this is not the case for the organizational forms of public administrations and enterprises, and this has a peculiar result: Because X-inefficiency is not eliminated during processes of organizational evolution, it tends to accumulate in public organizations, and there is increasingly a pent-up need for organizational reform that cannot find a ready release in decisive political and organizational action. Future research will have to focus on the development of processes that, in a self-regulating way, allow for public organizations to reform themselves in much the same way as private organizations do.

The social question. The second big and modern area of public finance, the social question, has undergone a very similar intellectual development, as have the classical principles or canons of taxation. Originally derived from the postulates of natural law but elaborated in a scholarly fashion over the centuries, they have developed their political function and received an empirical underpinning that has turned what was originally a legal and political postulate into a research program with its constitutive scholarly disciplines and respective social institutions that correspond to the research program. When Prince Bismarck posed the social question, economists at the German Association for Social Policy organized their research projects to come up with reasonable answers, which resulted in the new social institutions and in a further elaboration of what could be expected from the state. In fact, the functions or tasks of government increased manifold (see von Schmoller 1978, particularly bk. II, chap. 8).

Of course, even in preindustrial times, the state had a social function, and many institutions such as municipal foundations still exist in European cities, which have continued their work since medieval times. However, the social question Bismarck referred to could not be dealt with by means of those traditional institutions. The new state was in danger of falling apart not because of external aggression but rather because of the conflict that Marx (1818-1883) described as class struggle. A growing proletariat that reproduced itself according to the iron law of wages was pitted against an upper class that became smaller and smaller in proportion yet accumulated more and more of the nation's wealth. It was the great achievement of the creators of the new social institutions to reverse this process. It has to be kept in mind that the new social institutions did not just evolve. They were the product of theoretical work, empirical research, and political action, all three working hand in hand. In this way, the life chances of the working class and the small middle class were much improved as a consequence of conscientious social policy based on economic research. Today, we are confronted with a very similar problem—not on a national but rather on a global plane. Neither the European Union nor the United States can close its borders, but it is equally impossible for them to open their own social institutions to a sustained stream of immigrants. It is equally impossible to lock those immigrants out from social services because that would create an underclass and break up the communities. The social question, hence, is back on the political agenda, and again it is the task of the social scientist to provide an answer in the way described above.

The challenge posed by the open economies. Globalization, however, poses new questions and offers new challenges in the very research area of public finance. I am referring to public goods or social goods, as Musgrave (b.1910) prefers to call them. These goods meet two criteria. On one hand, consumption of the same good by one consumer or one group of consumers does not rival the consumption of the same good of some other consumer or group of consumers. Public goods are nonrivalrous. Second, they also have the characteristic that nobody can be excluded from consuming such a good. This means that economists have to come up with a response in terms of organizational design: Those who cannot be excluded from consumption will be hard to persuade to pay for the production. In this sense, the public finance theorist is challenged to come up with schemes that allow for the participation of every beneficiary in both production and consumption. This can be done by making consumption in the future conditional on assuming a share of production in the present. Or one can take a complementary private good and use it for financing the production of the public good, or else one can structure the groups of consumers to organize their self-interest and make it the agent of efficient production.

Creative organizational design is needed because the traditional form of organizing production by national states, provinces, or local entities will no longer suffice in the globalized economy. Increasingly, these public goods extend over entire parts of the world, and often they require substantial resources to be provided. We can think, for example, of the means of modern communication, including the transfer of the written word, the transfer of other data, and the modern traffic of people and commodities. We can also think of ecological issues, climate change, the diversity of species, the protection against specific and lethal forms of radiation, and the like. And finally, the most important factor of production, if it is sufficiently available, has elements of a public good. I am referring to human capital. Human capital is currently produced in different states to very different degrees and by very different groups; in fact, the production of human capital is concentrated in only very few regions of the world—entire subcontinents contribute little or nothing to the production of human capital. However, we can recall von Justi and his felicitous citizens. The more educated citizens in the world are, the happier they will be because with the improvement in their education, we also have a concomitant improvement in their health state and their life expectancies. Well-educated and happy citizens produce more than they can consume and thereby shoulder a larger share in the costs of providing global public goods.

The tried and true—two theoretical arguments. One could mistakenly think that my plea for the tried and true is just the expression of a deep-seated anti-modern conservatism. The opposite would be closer to the truth. There are two theoretical arguments for the tried and true. The first has been proposed by Friedrich August von Hayek (1899-1992), the Nobel Prize winner. He offered an evolutionary approach to social theory, which looks at institutions from the point of view of how they can deal with information. Each institution such as a family, a group, a corporation, an administration, or an institute such as the civil code or a tax code all absorb information over the course of time, information that results from the vicissitudes in the circumstances with which a particular institution is confronted. Organizations confronted with these vicissitudes develop strategies for survival. This is also true for social institutions, such as the German Civil Code (Backhaus 1999b), which is so durable because it has survived the most diverse environments and provided answers to very different legal and social conflicts. The social institution involves, of course, not just the civil code but all those systematically working with it—the commentators, the professors, the lawyers, the attorneys, and the general public as its user. These conflicts first posed themselves during the Empire and its sometimes stormy development, which also included deep crises; the war economy; the conditions posed by the revolution of 1918; the period of the democratic government with such specific influences as occupation, coup d'état, hyperinflation, and mass unemployment, including a deep economic crisis; the national socialist dictatorship; the second war economy; the postwar economy without a currency; the reconstruction of the German Federal Republic; and the reconstruction of the Democratic Republic—all still with the same civil code. From this follows that this particular social institution, the civil code, is attractive to countries in transition because while adopting it, they adopt an entire legal tradition that is necessary for a market economy and provides an interesting alternative to their own limited legal tradition because the entire process of learning embedded in the code and its commentaries can be taken over without having to repeat and incur the costs of learning.

The same is true for tax codes and entire tax systems. Intricate issues of applying tax codes have to be resolved in such a way that both parties, the revenue service and the taxee, can somehow live with it. The solutions become the common knowledge of public accountants and can be taught in tax courses; they become part of business life. Every basic change implies that this entire process is to start off afresh, and a new equilibrium has to be found. In this sense, the advantages from change must be very clear, and it must always be shown that the advantage from change is larger than the loss of experience that has to be rebuilt after the change. These costs of change, as a rule, are hard to ascertain and therefore tend to be underestimated.

A different issue is specific to the results of research in the social sciences. Leland B. Yeager (b.1924) has pointed to this issue (Yeager 1981). In the natural sciences, the result of research has a natural counterpart in technology. The technological achievements can be reproduced and, in this sense, become part of the common cultural heritage; they cannot be forgotten. You can always reconstruct a machine, as long as you have a prototype or at least the blueprint. Social institutions, on the other hand, particularly if they are based on theory (e.g., the International Monetary Fund, which is based on the theoretical work of John Maynard Keynes [1883-1946]), can only be sensibly steered and used if that theoretical foundation is present as common knowledge. In this sense, we need to build our work on those old theories as we have done in this article, so that we understand how old institutions are intended to function. If you are irritated by Cameralist bookkeeping, and you look at this system from the point of view of modern theories of corporate controlling, then you totally misunderstand its purpose, which consists of showing how political results have been achieved with specific budgets. After all, the purpose of government is not to maximize the net asset value of the state. Only if you understand the basic theory underlying Cameralist bookkeeping and hence its principles can you systematically and sensibly use this particular instrument of management (Mühlhaupt and Eisele 1994).

From this point of view, the purpose of our teaching in public finance also has to consist of communicating the functions and purposes of those institutions in which our students will later work; it is necessary to equip them with that collective knowledge that these institutions need so that they can function and learn and, on the basis of this learning, increase their efficiency and effectiveness. If such an increase in the effectiveness and efficiency of institutions and the economy in the public sector and in the nongovernmental sector can be accomplished, then we will earn the trust of those state legislators who have to vote for the funds for state universities.

THREE PRACTICAL PROPOSALS

The preceding text contains the germs of many practical policy proposals. I want to mention only three. For any state and its resources, it is true that there should be incentives for the use of these resources and disincentives for a misuse or underutilization. If the state forestry service is not able to adequately contribute to the state budget, then privatization is called for. The same is true, mutatis mutandis, for all public assets that are used to compete in the market. Second, if real estate or property is inadequately used and if this hinders the development of inner-city growth, then taxation can be billed on the possible and not just the realized profit, and property values can be assessed accordingly. Tax arrears can be entered as mortgages, and in this way distress sales and a transition in property will revitalize the local economy. The disincentive effect of this procedure will lead to the beneficial result that ideal investors will take action so that they will not lose their property. This will attract investment into the distressed area, and a positive impulse for the development of the economy of this state will result.

Above all, one should emphasize the well-being of those citizens who live in the state; people who have been unemployed for long should receive an attractive offer to renounce their unemployment benefits and receive, instead, the net present value of the expected future benefits as the starting capital of their own enterprise. Combining this with incentive taxation of real estate and systematic privatization of poorly functioning government services will result in a triple effect of boosting economic development. These are just three practical suggestions that follow from the tried and true tradition in public finance.

NOTES

1. James M. Poterba, invited lecture at the Southern Economic Association meetings, November 2001. James M. Poterba is the Mitsui Professor of Economics (Massachusetts Institute of Technology) and a research associate at the National Bureau of Economic Research. He thanks leading researchers in public finance for helping him with this survey.

2. To accelerate public investments, many new federal states enter into leasing arrangements—the leaser finances the investment and the state leases it, thereby committing future budgets.

3. Unannounced, he entered the crown council and announced, against the wish of the emperor, that the final program stage could not be implemented. This led to his dismissal.

4. Current calls for the so-called Tobin tax are a late intellectual outgrowth of this approach to public economic management through taxation.

5. Hence, Buchanan's suggestion to discuss regulatory burdens in terms of a liberty tax has likewise gone largely unnoticed.

6. In his currently dominating textbook, Stiglitz (2000) requires "administrative feasibility," but he does not discuss administrative procedures used by the Internal Revenue Service or other authorities of taxation, procedures of a tax court, or important institutions such as courts of audit. However, courts of audit can be systematically discussed with modern economic theory (see Backhaus 1994).

7. Again, this aspect is an important line of research in empirical fiscal sociology. When the state meets no resistance, the citizen has chances to expand its economic, social, and political activities.

8. Whether the closure of the University of Erfurt by Humboldt in 1816 has to be counted among such mistakes should be looked at in light of the careful report by von Schmoller's student Wilhelm Stieda (1852-1933). About a century later, Stieda looked at the case and largely supported Humboldt's actions (Stieda 1934).

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