



# Switzerland—a paradigm for Europe?

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Learning from the Swiss experience, this article argues that federalism and direct democracy are effective mechanisms for dealing with the diversity of interests, languages, cultures and religions in Europe. These institutions only partly harmonize economic, social and cultural politics. By far more important is that federalism and referenda foster *competition* between the various interests, but do so within a well-defined basic constitutional design so that competition produces beneficial effects. Federalism is not an alternative to referenda but rather a prerequisite for the effective working of a direct democracy. In small communities, the information cost of voters deciding on issues or judging representatives' performance are much lower than in a large jurisdiction. The more fiscal equivalence is guaranteed, the better the benefits of publicly supplied goods can be acknowledged and the corresponding costs be attributed to the relevant political programmes or actors. Thus, while federalism provides for cheaper information, referenda enable citizens to use this knowledge effectively in the political process. The interdependence of federalism and referenda also works the other way around: referenda improve the working of federalism. Besides the possibility of voting with their feet, citizens may also vote directly. This represents a double incentive for politicians to take their citizens' preferences into account; otherwise, they may lose their tax base to another jurisdiction or may be forced by referenda and initiatives to meet the demands of the voters.

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## Two model institutions

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Switzerland is the country of cheese, chocolate, the Alps, and perhaps of the Red Cross. More recently, it has also been associated with banks and

money laundering, and the younger generation might think of it as the producer of the Swatch.

We propose that Switzerland has something else to contribute to the world: something that is both an idea and reality, namely, the *constitution* of a modern *democracy*. Swiss society is politically organized around two essential features: federalism and direct democracy. Switzerland is composed of federal subunits, 23 cantons (some of which are divided into half-cantons) and 3019 political

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communes, which make a peaceful life of many diverse interests possible within one national political unit. The subunits can, to a larger extent than in any other country, act as independent decision-makers; most importantly, they have the power to determine their own tax rates with respect to the income of persons and firms. Direct democracy enables the citizens to express their views by referenda and initiatives, which exist in the form of obligatory referenda for constitutional changes, optional ones for laws (50 000 signatures, or roughly 1% of the voting body are needed), and popular initiatives (100 000 signatures needed). They serve as an effective barrier against the dangers of an unresponsive and sometimes self-seeking 'political class'.

Switzerland is generally recognized as a well-functioning, peaceful and prosperous country. As a consequence, one may at least state that the institutions of federalism and direct democracy have not prevented it from achieving that position. We wish to go much further: decentralization and extensive participation by the citizens have been a major factor in creating the favourable conditions for Switzerland. This was indeed not always the case. It may come as a surprise to some readers that, during the Middle Ages and in more recent times Switzerland was among the poorest countries in Europe and was plagued by regular famines, which induced many citizens to emigrate in order to evade the economic misery. The Swiss constitution of 1848, strongly revised in 1874, started a long-term increase in real living standards, placing Switzerland today among the richest countries in terms of per capita income. The direction of migration also changed dramatically. Instead of a continuous outflow of people, Switzerland has experienced a massive inflow of foreign workers benefiting from the high wages and favourable social conditions.

This in no way suggests that Switzerland is a paradise. We are well, and often painfully, aware of the many weaknesses and shortcomings of Switzerland as a whole, and of Swiss political life in particular. Nevertheless, we wish to argue that federalism and direct democracy are excellent institutions for producing socially, politically and economically beneficial outcomes. The future European Constitution which is yet to be designed should seriously consider these institutions. Switzerland provides a real-life experiment

revealing both the great strengths and also the limits of decentralized, direct-democratic decision-making. The size of the European Union and Switzerland vastly differ but federalism and direct democracy also work in large political units. It may even be claimed that they reveal their strength the larger and more diverse is the political unit.

Federalism and direct democracy offer a much needed alternative to the present road chosen by the European Union, which to most observers is far from satisfactory. The much discussed 'democratic deficit' cannot be overcome by relying more on the huge and amorphous European Parliament. Even less capable of accurately dealing with this deficit is the European High Court, which is divorced from democratic rules of selection and legitimacy. Discussions about the future European Constitution almost always restrict federalism to the member nations while neglecting the underlying levels (regions, provinces, districts, communes). The European regions envisaged are more the result of administrative directives and subsidies than the outgrowth of the citizens' needs and demands.

The next section provides an outline of what economists expect from federalism and confronts the theoretical expectations with the Swiss experience. The third section is devoted to direct democracy, while in the fourth section we present the conclusions that might be drawn for a future European Constitution learning from the 'Swiss case'.

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## Federalism

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Federalism is the central institutional provision allowing for competition within the political arena. Competition is as important to politics as it is to the market. Not only monopolistic firms derive rents by selling their goods above the market price but also governments with monopoly power may provide their services at higher tax prices than competitive governments would. Although it is not argued here that politicians and bureaucrats always and exclusively seek to maximize their own utility to the extent of actively exploiting the citizens and taxpayers, taking governments to be completely responsive to the population's wishes is not realistic either. Rather, political units may

be thought of as clubs that only exist as long as the club committee advances the interests of its members. Just as members who do not see their preferences fulfilled by the club withdraw from it, so too may unsatisfied citizens leave a jurisdiction. This 'exit' possibility provides a safeguard against politicians' taking unfair advantage of their discretionary power.

A decentralization of decision-making thus enables the citizens to 'vote with their feet'. That people or whole communes may indeed break away peacefully is demonstrated by the Swiss experience. Peaceful secession, with a constitutionally guaranteed right to secede, stands in stark contrast to the prevailing concepts of most nation states where it is strictly forbidden and often also prevented by force. Sad illustrations are the presently ongoing conflicts in former Yugoslavia and the former USSR, or the wars in Bangladesh (1970–71), Biafra (1967–70), Katanga (1960–63) and of course, the American Civil War (1861–65). Switzerland, having experienced a civil war itself, the 'Sonderbundskrieg' in 1847, nowadays is able to solve such conflicts peacefully. In 1978 a group of citizens residing in one particular area of Switzerland, the Jura, decided to form their own polity, i.e. to establish a new canton. As the withdrawal of some members from the club can have adverse effects on the remaining members, the other Swiss cantons had to decide by a referendum whether they approved of the new federal structure. The new canton was created with a majority of 82.3% of the votes on 24 September 1978. Another case is the Laufental, a region between the cantons Berne and Basel-Land, where in 1993 some of its communes opted to belong no longer to the canton Berne but to join the canton Basel-Land. The transfer of the Bernese districts into another canton was again approved in a national referendum by 75.2% of the votes.

Recognizing the benefits offered by federalism, it is surprising that many European countries do not employ the institutions of federal competition at all, prominent examples being France, Great Britain, the Netherlands and Sweden. Others, such as Germany, Austria or Switzerland, have introduced competition between autonomous local governments to a limited extent. However, the potential of federalism as a mechanism to enlarge the citizens' possibilities and to create a vigorous competition between governmental units has so far

not been rationally designed by any country. The principle of 'fiscal equivalence' applies only partly. Fiscal federalism would mean that the size of a political decision making unit depends on the spatial effects of the benefits and cost of a publicly supplied good. Each public function (e.g. education, police, fire protection or, if not privately supplied, refuse collection) could be allocated to a particular political unit whose geographic extension varied according to the specific supply conditions. The Swiss canton of Thurgau, for instance, uses this concept; hence, several hundreds of such functional jurisdictions exist, each with corresponding taxes.<sup>1</sup>

Federal competition may lead to an increase in economic spillovers.<sup>2</sup> Many economists, therefore, argue that centralized regulation must be introduced to correct market failures such as the underprovision of public goods and of redistribution. Taking the trade-off between political efficiency—i.e. the responsiveness of the political representatives induced by federal competition—and economic efficiency—that is, the optimal provision of public goods and redistribution by centralizing and harmonizing certain policies—seriously, means comparing the costs that arise if one aspect is neglected. A recent study for Switzerland, presents compelling empirical evidence that federal competition does not inhibit redistribution. Even though taxes vary enormously between Swiss cantons—from the highest tax rate in the canton of Wallis with 155.5 index points to the lowest in the canton of Zug with 59.1 index points (compared with the Swiss average of all cantons indexed at 100 in 1993)—the rich and high income recipients do not move to the low taxation cantons to a large extent as the costs of mobility are high. Thus, all cantonal governments are successfully able to redistribute income.<sup>3</sup> On the other hand, if some centralization proves to be efficient for 'economy of scale' reasons, a government deviating from the citizens' wishes may also be disciplined by other means, such as increasing the democratic rights and therefore the control possibilities of the citizens (a point to which we shall return below).

As the discretionary powers—and thus the rents of politicians and bureaucrats—are higher, the more a government resembles a monopolist, governments do not tend to favour federal competition. The incentive to centralize and not to delegate power to lower levels may lead

to economic inefficiencies because tasks are not assigned to the level where they can best be undertaken.<sup>4</sup> As the interests of political representatives diverge from the citizens' preferences once politicians are in power, safeguards against an increasing centralization must be taken at the constitutional level. In Switzerland, any amendment to the constitution requires not only the agreement of the voters but also the cantons. This double majority provision was adopted in 1848 and indeed proved to be a safeguard for cantonal prerogatives. In Swiss history there have been six obligatory referenda that the people approved and the cantons rejected, the last one being in 1983 when the cantons prevented the establishment of an energy policy at the federal level. Whenever the cantons deviated from the citizens' opinion, a change of the constitution would have implied a further transfer of power to the central government.

The decentralization of decision-making, and the institution of citizens directly deciding an issue, are closely connected. On the one hand, federalism is a prerequisite for an effective direct democracy, i.e. their relationship may be characterized as complementary; on the other hand, both political arrangements fulfil the same function. Both are a means to create incentives for the politicians to take citizens' preferences into account and may therefore be considered as substitutive mechanisms. While the substitution argument has a long tradition, the complementarity argument has only recently been introduced into the politico-economic debate in the context of the breakdown of the German Democratic Republic. The sudden exit option opening up in 1989 did not supersede other forms of protest, but contrarily, people in the German Democratic Republic interpreted it as a sign of weakness and therefore felt encouraged to 'voice' their dissatisfaction publicly.

Comparing the performance of different jurisdictions becomes easier the smaller the communities are, as the costs of being informed are lower. The impact of public programs and the related tax burdens may be attributed to the responsible representative more easily. This visibility of benefits and cost of policies allows the casting of an informed vote representing one's preferences, which in turn makes initiatives and referenda most effective.

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## Direct democracy

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By the end of 1994, Switzerland had held a total of 420 nationwide referenda covering virtually every aspect of politics. Interestingly, the first nationwide referendum was 'initiated by a foreigner': it was Napoleon who asked the citizens to decide about his design for a Swiss constitution in 1802. He, however, took precautions so that the result would correspond to his favoured outcome. Any abstention was considered an affirmative vote which led to the acceptance of the constitution with 92 500 votes against, 72 500 in favour and 167 000 abstentions!

'Regular' referenda were instituted at the federal level by the first Swiss constitution, in 1848, which declared referenda obligatory for all proposed amendments to the constitution. The first referendum was held on 14 January 1866 treating subjects such as taxation, religious liberty and the prohibition of lotteries. In the constitution of 1874, the optional legislative referendum was introduced, and in 1891, the Swiss adopted the constitutional initiative by which citizens could propose and decide about amendments to the constitution. The first nationwide initiative was approved by the citizens in 1893 leading to a prohibition of the 'slaughtering of cattle by bleeding'. A very important initiative then was to follow in 1900, trying to break the monopoly power of the parties in government. As in most countries at the time, the Swiss elected their representatives according to the plurality principle (which is still used in most English speaking countries today). The plurality principle, however, creates barriers to entry for new, small parties, thereby favouring large parties' incumbents. The latter would be, of course, against any changes of the election rule. Allowing for proportional representation would have increased the chances of smaller parties entering the political arena significantly and was, therefore, against the interests of the ruling party, the Radical Democrats.

Opposition was so strong during the first trial that the 'outsiders' had to reinstate the initiative twice, in 1910 and 1918, before the change to proportional election of the parliament (National Council) was accepted by the people. The approval was remarkable, as it was the first time in Swiss democratic history that the citizens' opinion did not correspond with the parliament's

recommendation. In the following election, the Radical Democrats lost about 40% of the votes while the Social Democrats and the Rural Party won substantial shares. This example demonstrates that initiatives enable outsiders to propose issues for democratic decision that many elected officials might have preferred to exclude from the agenda, thus taking the agenda-setting monopoly away from the politicians.

Recent Swiss history shows that the political elite's opinion differs from the voters' preferences when the uncertainty about the economic consequences of a decision is relatively high and strong value judgements are involved. The two most recent examples are two referenda on Switzerland joining international agreements or organizations: the United Nations in 1986 and the European Economic Area in 1992. Both proposals were rejected by the citizens even though all major parties, all interest groups including both employers and trade unions, a vast majority of the members of parliament and the government strongly supported them. While a clear majority, 76% of the voters, rejected the referendum on Switzerland joining the United Nations, only a small majority, 50.3% of the citizens, voted against Switzerland becoming part of the European Economic Area.

As citizens' preferences deviate from their representatives' opinions in important instances, we should expect people to value direct democratic rights highly. This indeed seems to be the case, not only where initiatives and referenda are regularly used but also where representative decision-making is dominant. In a survey in March 1990, the Swiss indicated that direct democracy was the most important institution in politics, more important than federalism or the constitution. A national survey (Gallup) in the USA in 1987 revealed similar results. When confronted with the following statement 'Citizens ought to be able to vote directly on important issues and policies instead of having their representatives voting on them', 76% of the population agreed while 18% preferred representatives to decide alone and 6% were indifferent (Reference 5, p. 80). Even more surprising is that some authors report majorities for direct democratic decision-making in countries where referenda do not exist (anymore).<sup>6</sup>

While many states in the USA changed from a representative system to direct-democratic institutions during the 20th century, no case is

known where the initiative once installed has been abolished again (for a survey, see Reference 7). Popular initiatives are held in 23 states, facultative referenda in 25 states, and obligatory referenda on changes of the constitution in all but one state (Delaware) of the USA today. In California, referenda on subnational issues regularly take place. While the total number of issues to be decided about in California is comparable with the number of referenda held in Switzerland (taking the difference in size into account) the voting mechanisms in the two jurisdictions are quite different. Swiss citizens are normally called to the polls four times a year where they are asked to cast their vote on two national propositions, on average, and a number of cantonal and communal issues. Very rarely are voters confronted with more than ten issues at a time. In California, on the other hand, voters only decide about ballot issues every other year, which induces the critics of direct democracy to point out the 'overload' and the 'overstrain' of the citizens.<sup>8</sup> Indeed, an individual cannot make a reasonable decision when confronted with a situation as described by *The Economist*<sup>9</sup> (13 February 1993, p. 19): 'Last November any Los Angelano voter was allotted ten minutes in the ballot booth to make over forty different electoral choices, varying from statewide propositions to local judgeships; in 1990 the total was over 100.'

Switzerland is a semi-direct democracy, combining representative elements with the direct participation of the citizens. While a parliament and a bureaucracy are indispensable to provide information, work out the details, and assess the consequences of the various political issues at hand, the citizens are needed to supplement the technical expertise of the representatives by their human competence. The judgement of the people also seems to be asked in representative systems when especially controversial and important problems have to be solved.<sup>10</sup> Recently, the question of joining the European Union led to referenda in Austria and in all Scandinavian countries and, earlier, the United Kingdom. Referenda on the Maastricht treaty were held in Denmark, France and Ireland. The example of Norway shows that such referenda are not purely a formal exercise. They are crucially important in order to establish a democratic legitimacy for the European Union. The intensive democratic discussion induced by the two referenda in Denmark stands in stark

contrast to the indifference about the issue in Germany, where the population had no say and therefore did not get involved in the democratic process. In these instances, compatibility with the citizens' preferences was valued higher than any technocratic brilliance, even though the ballot issues included very complex matters. Thus, the citizen's intellectual capability cannot be the standard to measure whether a political issue should be referred to the parliament or decided by the citizens themselves. Rather, the correct standard is how far a decision is considered a value judgement.<sup>11</sup>

It is often argued that pressure groups take advantage of the extensive rights possessed by the citizens in direct democracies. Compared with the unorganized taxpayers, it is the pressure groups who have got the financial and human resources to mobilize supporters of their interests, to be agenda-setters by starting initiatives and engage in referendum propaganda before an issue is decided at the polls. It cannot be denied that well-organized and financially potent groups wield relatively more power than the poor and the unorganized. This, however, is true in any political system. The important question then, is under which institutional arrangements do organizational and financial advantages play a more important role, or whether what *The Economist*<sup>12</sup> said (13 October 1990, p. 20) really applies: 'Because initiatives can pass with so little informed consent, they attract special interests like bees to honey'. Empirical evidence contradicts this statement in so far as it was the pressure groups who most intensively fought against adopting direct democratic institutions in American states (especially in Minnesota, New Jersey and Rhode Island). In the 1980s the pressure groups supported the 'National Center for Initiative Review' in order to stop a further spread of the initiative and the referendum (Reference 5, p. 204). While pressure groups may use other means of influence such as direct lobbying of the representatives, these channels are not easily accessible for unorganized interests.

Citizens seem to be well aware of the advantages of direct-democratic decision-making. It enables them not only to have their preferences better met but also to trust the 'system' more than in a representative democracy, because they themselves are part of the game. Taxpayers exhibit a higher tax morale in communities where institutional

options for political participation exist. In Switzerland, in some cantons, referenda and initiatives can be taken on virtually all issues, whereas others grant these options only for special issues and under restrained conditions or rely completely on the institutions of representative democracy. Empirical evidence suggests that the more directly democratic are decisions, the less tax cheating takes place. Compared with the mean of all cantons, almost 8 percentage points (that is, about SWF 1600 per taxpayer and per year) less income is concealed in cantons with a high degree of direct political influence. In contrast, in cantons with little participation possibilities and therefore low tax morale, the mean income undeclared exceeded the mean of all cantons by SWF 1500. That direct democracy is much valued by citizens is further corroborated by the fact that people are prepared to pay more for being able to live in a commune where decisions are taken by initiatives and referenda. The price of land, for example, is *ceteris paribus* significantly higher in direct democratic communes than in representative systems.<sup>13</sup>

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### Conclusions for a future European constitution

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The experience of Switzerland reveals that federalism and direct democracy can work (despite gloomy predictions) and that it is consistent with, and actually strongly supports, a higher level of individual and collective satisfaction. The experience also shows that citizens may express and have their demands best fulfilled when federalism and direct democracy are closely integrated.

It would be naive to transfer the example of Switzerland directly to the European Community. Yet we stress that the basic features of federalism and direct democracy, suitably adjusted, can well be applied to the European case. It is often argued that these institutions may be good for a small country such as Switzerland but not for a large political unit now embracing almost the whole of Western Europe.

However, size is a weak argument. It should be noted that it is not accidental that very large democratic nations such as the United States, Australia and Canada are decentralized federal states, and that popular referenda have been

regularly used in such large units as California, where 1098 referenda have taken place between 1884 and 1990, and Australia where 45 referenda have been held between 1906 and 1990.

Federalism in a future Europe, we suggest, should not be restricted to the interaction of nations but should extend down to lower levels. Most importantly, all communities in Europe should have the constitutional right to form new jurisdictions with other communities (even if they belong to another nation) in order to better fulfil functional tasks. Nothing should prevent a particular unit from belonging to various such functional jurisdictions. A community may also choose to join another jurisdiction if it expects to be better served. The possibility to exit and enter jurisdictions freely, establishes competition between different suppliers of public services and tends to improve quality and decrease costs. Of course, each jurisdiction must have the right to raise its own taxes to finance the respective public services demanded and approved by their constituents. These new political units can be called FOCJs, the acronym of Functional, Overlapping, Competing Jurisdictions.<sup>14</sup>

FOCJs are based on the theoretical propositions advanced by the economic theory of federalism discussed above. They, nevertheless, form a governmental system completely different from the one so far suggested in the literature. While, traditionally, the behaviour of existing political units at different levels of government is discussed, FOCJs emerge in response to the 'geography of problems'. An example would be a community in Alsace forming a jurisdiction with a German community on the other side of the Rhine to provide fire protection or medical care. At the same time, it could participate in a jurisdiction with other French communities to supply elementary school services and be part of a jurisdiction composed of communities from various nations dealing with environmental problems and transportation. While the idea of FOCJs certainly departs from conventional thinking about the organization of states (and is only partially realized even in Switzerland) it is in the best European tradition.

Popular referenda could be introduced at various levels within the European Union. As mentioned earlier, when it comes to the decision of entering the European Union, many countries that otherwise do not use, or even abhor, referenda, take this step

only with the consent of the people. Popular referenda, including initiatives could, however, also be introduced at the lower political levels, in the states and in the communities. The future European Constitution should actively encourage the direct democratic participation of the citizens at these levels in order to counteract the inevitable tendency for increasing centralization as a result of the transfer of tasks to the level of the Union.<sup>15</sup>

Allowing for direct democracy differs from the proposals advanced for a future European constitution by other scholars. The 'European Constitutional Group'<sup>16</sup> focuses on the example of the American constitution and presents proposals in a constructivist tradition with respect to the houses of parliament and the respective voting weights of the various countries. The recent proposal from politicians (Hernan report of the European Parliament,<sup>17</sup> 1994) also concentrates on the organization of the parliament and, to a large extent, accepts the status quo. Competitive federalism from below is not elaborated on even though the 'subsidiarity principle' is often criticized as an empty concept.<sup>18,19</sup> We argue that even if subsidiarity were taken seriously, it would not lead to a real federal structure because many members of the European Union are essentially unitary states without federal subunits with significant competences. Exit or secession, although suggested as an important ingredient of a European constitution<sup>16,20</sup> is not formally regulated and exceptions to specific aspects of agreements reached are only reluctantly granted (as in the Maastricht Treaty concerning the European Monetary Union and the Protocol on Social Policy, or in the Schengen Treaty concerning the free movement of persons). Whether differential degrees of functional European integration are labelled variable geometry, multi-track, multi-speed, two-tier, hard core, or concentric circles models, it always evokes fierce opposition.

Federalism and direct democracy could well be combined at the level of the European Union as a whole. The forthcoming European Constitution should specify for what issues the citizens of the EU must be asked for their consent via an EU-wide popular referendum. In order to protect the interests of the smaller countries and to prohibit the dominance of the large member states (especially of the now largest nation, Germany), it should be stipulated that a proposition is only accepted if it meets two majorities: more than half



of the voters in the EU plus more than half of the member countries agree. Such a double majority (which is effectively practised in Switzerland) represents part of a constitutional system of checks and balances, which prohibits excesses both within the electorate and within the 'political class'.

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