The Impact of Collective and Competitive Veto Points on Redistribution in the Global Age.

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February 4, 2002

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Abstract:

This study examines the determinants of redistribution in advanced market economies by simultaneously assessing the impact of domestic political institutions and globalization. A distinction is made between “collective” veto points and “competitive” veto points, demonstrating that not all veto points have restrictive effects. It is shown that redistribution is significantly and positively affected by collective veto points, while the opposite is true for competitive veto points, indicating that not all veto points are created equal. In addition to veto points, the effects of “globalization” are also assessed revealing that globalization is exerting little reform pressures on the welfare with strong evidence indicating that more globalization buoys welfare expenditures. While current disbursements and social transfers are positively influenced by globalization, civilian general government consumption is negatively affected and its impact is strongly mediated by competitive veto points indicating that domestic political institutions continue to fundamentally shape policy trajectories.
The Impact of Collective and Competitive Veto Points on Redistribution in the Global Age.

Redistribution of incomes, achieved mainly through taxation and transfer payments, is one of the most central functions of the modern state. This function was traditionally understood to be in the domain of “domestic politics”. With the purported rise of “globalization”, however, many observers believe that redistribution is affected in ways that threatens the modern welfare state and its institutions. The purpose of this paper is to assess these claims in conjunction with a specific emphasis on how the configuration of domestic political institutions, more specifically, the nature of “veto points”, affect redistribution by mediating, and adding to, the effects of globalization.

The current scholarly debate on the character and effects of veto points as well as the consequences of globalization has created two intriguing puzzles: first, do more veto points, measured by the number of parties, mean that it is more difficult to change the status quo? George Tsebelis (1995, 1999, 2001), Hallerberg and Basinger, (1998), Basinger and Hallerberg (2001), Hallerberg (2001), Huber, Ragin and Stephens, (1993) suggest that indeed, more veto points, operationalized by the number of parties, means more difficulty in changing the status quo, while Weingast (1979), Roubini and Sachs (1989), Tabellini (2000), and Crepaz, (1998, 2000, forthcoming) argue that more parties tend to change the status quo towards a direction of “expansion”, or “less reduction” than when fewer parties are present. Similarly, Swank (2001, 2002) presents a thorough theoretical and empirical account of the positive effects of what he calls, “electoral
inclusiveness” (a standardized score of the degree of proportional representation and number of effective legislative parties) and “dispersion of policy-making authority” (a standardized score of the degree of federalism, bicameralism and referendums) on various measures of welfare effort. Both of these measures, while very similar, are not as encompassing as the concepts of “collective” and “competitive” veto points introduced here.

The second puzzle is a more familiar one. It refers to the question of whether “globalization” will lead to a “neoliberal” convergence, i.e. to a retrenchment of the welfare state, to a dismantling of the institutions which distinguish organized market economies, and perhaps even to a breakdown of state sovereignty (Strange, 1995: Ohmae 1995; Cable, 1995; and many others) or whether globalization will have either the opposite effect, or no effect on the institutions of organized market societies, the welfare state, or even the sovereignty of the state. (Cameron, 1978, Katzenstein, 1985, Rodrik 1996, 1997; Swank 1998, 2000, 2001, Garrett 1998, Garrett and Mitchell 2000, Hall 2001, Rhodes 2001 and many others).

The reason why both puzzles need to be examined in order to establish a more complete model of the factors that drive redistribution is straightforward: not only are domestic institutions affecting these crucial functions of the state, but there is growing evidence that “globalization” is also having a measurable effect. Thus, in order to more completely understand what explains redistribution, it is crucial that the forces of globalization are examined in tandem with domestic political institutions, providing a more complete analysis of the predictors of taxation and redistribution than has hitherto
been achieved. In addition, further alternative hypotheses will be introduced and tested later.

While it may seem that the literature on veto points is a novel research project, the idea behind this concept has been around for a long time. In Federalist No. 47, James Madison speculates that, “… the preservation of liberty requires that the three great departments of power should be separate and distinct”. Madison turns to “the oracle that is always consulted and cited on this subject, the celebrated Montesquieu”. (1982, [1788] 244). Of course, Montesquieu’s conception of “separation of powers” is today described as “mixed government”, meaning that powers are functionally the same and separated vertically between the monarchy, aristocracy and “the people” (different status), while the authors of the Federalist paper adopted a functionally different and horizontal separation of powers with no differences of status.

One of the earlier systematic studies of “veto points”, which employed the Madisonian conception of veto points, was Ellen Immergut’s (1992) comparative study of national health insurance policies in Switzerland, France and Sweden, which was soon followed by empirical research by Huber, Ragin, and Stephens (1993, 722) who argued that welfare state expansion will be adversely affected by constitutional structures that “disperse political power and offer multiple points of influence on the making and implementation of policy”. Later, George Tsebelis (1995, 1999) and Tsebelis and Chang (2001) developed and tested the ideas of veto points in more detail. Swank (2001, 2002) also found strong empirical evidence that his “political dispersion index” tended to have restrictive effects on policy trajectories.
Central to the idea of “veto points” and separation of powers is the deliberate design to restrain government. This is certainly the case as far as constitutional features are concerned, such as presidentialism, federalism or bicameralism. However, all of the authors mentioned above, have at times used the concept of “number of parties” as a proxy of veto points, arguing that the more parties are represented in a parliament or government, the more difficult it is to change the status quo. This article will take exception to these claims and will argue that there are two different kinds of veto points: collective and competitive veto points and that they lead to systematically different outcomes. In other words: not all veto points are created equal and have equal effects.

In addition to the configuration of veto points, we will also take the impact of “globalization” seriously. There is no doubt, that the world is becoming increasingly interconnected. In this study, globalization will be operationalized as a composite indicator consisting of trade, foreign direct investments and capital mobility.

This study will proceed as follows: first, the theory of veto points will be critically assessed and a difference between collective and competitive veto points will be established; secondly, the central arguments on how globalization should affect redistribution will be examined; third, the research design, the variables and hypotheses will be developed, followed by a summary of the findings and of the implications of the findings.

Restraining and enabling institutions
Fundamental to the theory of veto points is that the more of them exist, the more difficult it is to change policy, or in Tsebelis’ (1999, 593) useful definition: “a veto player is an individual or collective actor whose agreement is necessary for a change of the status quo”. Thus, this theory predicts that the larger the number of veto players, the higher policy stability. Tsebelis (1995) also provided a very useful distinction between partisan veto points (such as the number of parties) and institutional veto points (such as federalism and bicameralism).

Typical examples of veto points are, for instance, the type of executive-legislative relations such as presidentialism or parliamentarism. Obviously, a president who is constitutionally protected by votes of no confidence from the parliament, such as the American president, represents an additional “veto player” vis-à-vis Congress which consists of two equally strong houses both which can be understood to be a “veto point”. The election debacle of November 2000 and the controversial decision of the Supreme Court in Bush vs. Gore, clearly demonstrated that the US Supreme Court might also be thought of as a “veto point”. On the other hand, the British Parliament and its mechanism of “fusion” between executive and legislative power, and parliamentary systems with single-member district electoral system in general, constitute only one veto point since the Prime Minister emerges out of the majority party in Parliament reducing “institutional competition”. In addition, the degree of federalism represents levels of veto points as well as whether countries are unicameral, bicameral, or have very weak upper houses, such as the United Kingdom. One may even speculate on the degree to which the mass media has become a “check” on policy.
In the literature on veto points, the number of political parties has played a central role. Tsebelis (1995, 1999), Tsebelis and Chang (2001), Hallerberg and Basinger (1998, 2001), Hallerberg (2001), Bawn (1999) and others, find that the more parties are present in governments, the more difficult it is to change the status quo. Each party is understood to represent a “veto point” and the more there are, the more unlikely it is that change in policy will result, in other words, neither an expansionary nor restrictive effect should be observed. Tsebelis (1995, 1999) also examined the ideological distance between the parties, arguing the further the parties are apart, the more unlikely it is for them to change the political status quo. The jury is still out on this hypothesis: while Tsebelis finds evidence of the ideological distance hypothesis, Hallerberg and Basinger (2001) do not find that ideological distance matters.

Applying the thesis that more parties means more veto points, and thus a low capacity to change the status quo, to welfare state spending, we expect to find that the most generous welfare states should also be the ones with the lowest number of parties. However, this is not the case. The assertion that more parties mean more veto points, i.e. very low capacity to change the status quo, is at odds with the observation that high welfare spending, “decommodification”, and many other measures of an extensive welfare state, is associated with multi-party or oversized coalitions. If more parties means more veto points, the welfare state should be quite minimal in multi-party systems and extensive in systems with single party, bare majority cabinets.

Tsebelis’ (1999, 592) explanation is that “… oversized coalitions will be locked into the previous policy pattern (whatever that pattern happens to be)”. Thus, his claim implies a path dependency argument. However, if his assertion is correct, we should
observe, for instance, less spending, lower budget deficits, and lower transfer payments in multi-party coalitions or in oversized coalitions. Why? Since such party systems consist of many veto points, according to the “locking in” thesis, such government largesse should have never occurred in the first place because the agreement of many parties is supposedly inimical to the expansion of the welfare state. However, more government spending has occurred precisely in such party systems.

Bo Rothstein (1998) and Esping-Andersen (2000) find that welfare spending in the early 1960’s was very similar in all OECD countries, but began to dramatically diverge among the OECD countries leading to the intriguing variation in government spending observable today. According to the “locking in” argument of Tsebelis, today’s big spenders should be those with the fewest parties in government such as the United Kingdom, the United States, and Japan – an assertion that is inconsistent with empirical facts. Thus, the “locking in” argument cannot explain the dynamic change from a time where all OECD countries indicated similar spending levels in the 1960s to a “fanning out” into the intriguing, tremendous variation in spending levels observable today.

A casual look at the top three “big spenders” of general government spending in the 2001 forecast by the Economist (August 4th, 2001) are Sweden (52%, 3.3), Denmark (50%, 4.5), and France (50%, 3.4), while the three “stingiest” were Australia (32%, 2.2), Ireland, (30%, 2.8), and the United States (29%, 2.4); the parentheses also include the

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1 Rothstein (1998, 18) argues that, “In the 1990s, the large European countries spend about 50 percent more [public spending] than the United States, while the Scandinavian countries spend about twice as much as the United States. This was, however, not always the case. In the 1960s, the difference between these countries in total public spending was much smaller – the level in the United States was about 28 percent compared to a mean of 29 percent for the Scandinavian countries.” Similarly, Esping-Andersen (2000, p. 4) makes the point that “… the decisive period in which the basic components of post-war welfare regimes were put in place, was… during the 1960s and 1970s. […] The essential differences between the Nordic, social democratic, the Continental European, and the Anglo-Saxon liberal welfare states were affirmed in these years”. If it were true that policies are “locked into the previous level”, then such dynamic change should not occur.
average number of parliamentary parties from 1946 to 1996 demonstrating the “big spenders” also tend to have on average more parliamentary parties.

One may still argue that the number of parliamentary parties follows a different dynamic than parties in government. However, using the fifteen countries of this study and the time period from 1973 to 1995, a pooled cross sectional/time series analysis of government outlays as the dependent variable and the number of parties in government as a predictor, yields a highly significant (p<.01) positive relationship, clearly indicating that more governmental parties (not parliamentary parties and independently of their partisan coloration) have a significant expanding effect on government outlays. Apparently, the conception that more parties means more veto points, which results in less capacity to change the status quo, is inconsistent with the path dependency argument and with empirical observations. In addition, significant evidence has been amassed by other scholars which indicates that more parties (driven mostly by proportional representation, pace Duverger) lead to larger “government growth”, higher inflation, and higher budget deficits and has generally “expansionary” tendencies” (Roubini and Sachs, 1986, 1989; Tabellini, 2000; Tabellini and Persson 2000; Crepaz, 1998, 2000, 2001; Swank 2001, 2002).

This study argues that not all veto points are created equal. Some, such as political parties, tend to have expansionary effects, while institutional vetoes, such as federalism and bicameralism, in which separate agencies are empowered by vetoes, tend to inhibit

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2 The Scandinavian minority governments present the well known coding problems since many of them are actually single party governments, but in order to pass bills, they engage in coalition building on an issue by issue basis, thus, coding them as “single party government” is not a valid operationalization. Still, this study employs the more “conservative” approach and counts only actual parties in government including the Scandinavian minority governments. The Beck/Katz (1995) method of panel corrected standard errors with a lagged dependent variable was employed. The coefficient was .27, with a standard error of .087; N=345; R-squared: .96.
policy making. The difference lies in the “setting” in which these veto points occur. In multiparty coalitions, which are based on collective responsibility, on day-to-day interaction, in which the actors interact with each other on a face-to-face basis, sometimes in different roles, we should observe “expansionary” effects.

Such effects are driven by rational motives of the coalition partners who have parochial interests combined with a tremendous power to potentially topple the government. Such a setting encourages log-rolling, with the effect that even though it might be in the interest of the coalition as a whole to reduce government growth, from the perspective of an individual party, it is not rational to engage in less spending while the other coalition members increase spending. Thus, the actors are caught in a classic collective action problem. This has been clearly understood by scholars who study budget deficits (Roubini and Sachs, 1989a/b; Alesina and Drazen, 1991).

From an institutional perspective and again examining government spending, Tabellini (2000, 13) concludes that “… social security and welfare spending is larger in proportional systems than in countries ruled by majoritarian elections”. Milesi-Ferretti, Perotti, and Rostagno (1999) have found a similar relationship. In the American politics context, Barry Weingast (1979) argued that where simple majorities are less likely to form, all-inclusive coalitions pass higher spending bills. A classic example of the expansionary tendencies during non-concurrent majorities in the USA is the dramatic rise of the US budget deficit under Ronald Reagan, where he and Tip O’Neill agreed on a

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3 Tabellini is examining the role of electoral systems on government spending rather than the number of parties. However, there is a very well established relation between the electoral system and the number of parties, widely known as Duverger’s law. The more proportional the electoral system, the higher the number of parties – thus, Tabellini’s finding provides strong direct evidence that PR systems are more redistributive than SMD systems. By extension, Tabellini provides indirect evidence that social security and welfare spending tend to occur in systems with a higher number of government parties.
plan that the House of Representatives will not block the president’s legislative program to increase defense spending and to support a tax cut, as long as Reagan agreed not to veto the Democratic budget, which maintained spending increases for social programs. Thus, a budget was passed that both, cut taxes and increased spending, with a hitherto unprecedented rise in the US budget deficit (Manuel and Cammisa, 1999).

This study argues that collective veto points, of which parties are an important element, does not mean less of a capacity to change the status quo; it argues that collective veto points have more of a capacity of changing the status quo towards an “expansionary” direction, particularly when examining government growth. Since parties in coalition governments share political responsibility, they might be called “collective” veto players. In the words of Robert Goodin (1996, 331) “…where there is a formal coalition, collective agency has been created, and all parties to it will be judged… by its successes and failures” (emphasis added).

When “competitive veto points” are examined a different hypothesis emerges, one that is consistent with Tsebelis and many others observers. In competitive veto points, power is diffused by means of institutional separation such as federalism and bicameralism, where different political actors compete through separate institutions with mutual veto powers. Such institutions should have a tendency to restrain government, sometimes to the extent of leading to deadlock, immobilism and even shutdowns of government. Swank (2001, 2002) and Crepaz (1998, 2001) found empirical evidence for the restrictive effects of such institutions.

Thus, it is important to distinguish two types of veto points: “collective veto points” so named because the actors share collective authority and responsibility and
interact with each other “personally”. It is hypothesized that such veto points should have expansionary effects. Competitive veto points, are so named because the actors represent separate agencies with mutual veto powers, which compete against each other. Such veto points should have restraining effects on government. This study will employ Lijphart’s (1984, 1999) well known distinction of “executives–parties dimension” and “federal–unitary dimension” and will use these empirical measures to capture the concepts of collective and competitive veto points.

Globalization and the sovereignty of policy making

Besides the nature of veto points, there is another strong contender which helps explain variations in the state’s capacity to redistribute incomes: a contender which has given rise to a whole new cottage industry of political economy: that contender is called “globalization” referring to the dramatic growth of trade, deregulation of capital controls, impressive rises in foreign direct investments, the increasing effectiveness of international organizations such as the WTO working zealously to reducing the role of tariff and non-tariff barriers, dramatic migration shifts, and, last but not least, the terrific advances in modern technology, such as in the fields of transportation, communication, and information. These technological advances reduce transaction costs to such an extent that moving the means of production to other parts of the world becomes a viable alternative and making products that were hitherto not tradable are now ready to be bought and sold.
Aside from examining whether globalization is really a new phenomenon, the reason why globalization is studied so intensely is because theories on the effects of globalization on the viability of the modern state, yield a variety of opposing, yet plausible hypotheses. There are those who argue that the state will no longer be a viable institution since its capacity to tax and redistribute incomes will be adversely affected as holders of mobile assets (owners of capital, professionals, highly skilled workers) will take advantage of low transaction costs and move their assets to wherever accumulation of profits is the most frictionless, i.e. where the lowest wages, lowest taxes, and generally, the least regulation are to be found. In order to contain this migration of productive capital, politicians will have to induce mobile asset holders to stay put by providing tax incentives, subsidies, cutbacks in welfare-state provisions, and other such means. Tax competition between countries will lead to shifts of the tax burden from mobile (capital) to immobile (labor) asset holders allowing firms to exploit existing differences between national tax systems and undermining the redistributive capacity of the state.

In fact, countries will have to compete against each other for attracting capital by offering lower wages and taxes, leading to a “race to the bottom”, i.e. a situation in which welfare states are minimal and in which markets reign over politics. The relationship between political incumbents and business will become even more nuanced: the credible exit option of business puts tremendous pressure on governments to induce capital to

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4 Some authors, such as Paul Krugman (1995) and Vincent Cable (1995) argue that in the late 19th century our world was already remarkably integrated. On the other hand, there is a new “backlash” literature developing that takes a very critical view of globalization, arguing that the level of world market integration is exaggerated and that local politics, cultures, and institutions, will continue to put an idiosyncratic stamp on political outcomes (Hirst and Thompson, 1996; Streeck, 1996; Gourevitch, 1996; Boyer and Drache, 1996; Berger and Dore, 1996; and many others).
stay, making the position of business even more “privileged”. Realizing that significantly extending the scope of social provision, public consumption, and tax burdens will undercut the confidence of business in a profitable rate of return on investment, governments cannot afford to continue providing “generous” welfare schemes. The end-effect of this “competitive deregulation”, so the argument goes, is a dismantling of the welfare state, its political institutions and the social insurance schemes that have protected its populations. Globalization, thus puts into much sharper relief the familiar “structural dependence of the state on capital” argument, pioneered by Michal Kalecki (1943) and extended in the 1970s and 80s by neo-marxists such as Habermas (1975) and Offe (1984), and Lindblom (1977).

If these claims are correct, governments operate in “significantly shriveled policy spaces” (Prakash, 2001, 544). However, as plausible as this view is, there is another, equally plausible view, that argues precisely the opposite: as a result of globalization, there is even more need of a protective welfare state, precisely because markets, and their unequal distributive effects, will be even more prominent. This view sees the need for government to be even more interventionist to compensate for the increased insecurity and inequality wrought by international market integration (Garrett, 1998). This same view is consistent with a whole slew of scholarly works in comparative political economy which has argued for a long time that small, open economies have embedded their markets in corporatist and welfarist institutions in order to protect themselves from the ups and downs of international market forces (Cameron, 1978; Katzenstein, 1985; Ruggie, 1983; Rodrik, 1996; Swank, 2001, Garrett, 1998, and many others).
The two competing theories on the viability of the state in the age of globalization laid out above make for an intriguing puzzle in need of resolution but they also represent somewhat of a caricature. In an enlightening comparison of liberal market economies and organized market economies, Peter Hall (2001) argues that many theorists on globalization assume that firms are essentially similar across nations. In fact, this is not the case; some kinds of activities can be more efficiently pursued in the low regulation environment of liberal market economies, while other activities may be more efficiently pursued where there are plentiful mechanisms for non-market coordination. Soskice (1994) demonstrated that innovation patterns were systematically different depending on whether they originated in liberal market economies or organized market economies.

Moreover, firms are not only induced by low wages, instead, they may compete for quality as well as price. In such a case, firms may find a comparative institutional advantage in countries that provide a highly trained and educated workforce, which allows the firm to compete at cutting edge level of quality. In the words of Peter Hall (2001, 71) they are engaging in “institutional arbitrage” that is exploiting the differences in institutional arrangements that lead to differences in the quality of the labor force as when American car manufacturers decide to locate their plants in Germany or in Austria.

Finally, the logic of mobile capital to go wherever allocative efficiency is maximized may only apply to liberal market economies in the first place. In organized market economies, the business community may resist deregulation “in order to preserve the institutional infrastructures supporting the kind of non-market coordination on which they rely for competitive advantages” (Hall, 2001, 71). In fact, Wood (1997) and Swenson (1989) found that international pressures actually serve to unite labor and
capital to protect the institutional advantages under which they both prosper, making organized market economies a viable alternative to more anarchic liberal market economies.

Besides institutional differences, there may be variations in “cultural capital” that might give various nations a comparative advantage. A very important, but mostly forgotten concept of “vulnerability dependence” was introduced by Keohane and Nye (1977) referring to the ability of a country as a whole to adjust to exogenous shocks. Vulnerability dependence is sociopolitical as it refers to behavior and, thus, is deeply rooted in national culture. Depending on variations in this cultural capital, the same exogenous shocks may be absorbed in one country with only some grumbling of the citizenry, while in others it may lead to industrial disputes or more serious political violence. This “cultural capital” may prove to be an important national resource.

Similarly, different levels of “work ethic” may lead to higher monitoring costs of workers at the workplace in some countries than in others. Monitoring costs may be so high in some countries that investors decide to locate their production facilities to areas in which they can rely on a culture of hard work rather than spending money on video cameras, software monitoring computer use or the old fashioned “capo” or other ways of overseeing worker performance. Ricardo’s “comparative advantage” and Heckscher-Ohlin’s “factor endowment theorem” may be complemented by a “theory of comparative cultural advantage” in the near future. This is perhaps overstating the importance of

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5 As an example, during the 1973/74 oil crisis, the Austrian government simply created another month of winter school holidays for its teachers and pupils, and more importantly, imposed that motorists choose one day of not using their car. A sticker, indicating the weekday in which the car was not to be used, had to be displayed in the windshield of the car for police to enforce the law. The Austrian population accepted this solution without much grumbling. Such a solution would be unthinkable in the United States. Centuries of strong feudalism and powerful monarchical regimes have created an attitude that sees the state not as an obstacle to people’s goals but as a facilitator. This might be a reason why trust and confidence in government tends to be higher in countries that experienced feudalism as opposed to those which did not.
“culture” when it comes to investment decisions large companies make. However, Peter Gourevitch (1996, 258) is doubtful for “neoliberal convergence” to take place, since among many other factors, he argues that, “Cultural traditions are powerful: countries have different traditions in networking, personal relationships, conceptions of authority, models of organizations and individuals”.

One of the most intriguing observations regarding the effects of globalization on the state’s capacity to independently create policies, is the dramatic incoherence of empirical findings in this matter. Garrett’s useful distinction of the literature into advocates of the *efficiency hypothesis*, who argue that social democratic welfare policies will no longer be feasible in a global world and of advocates of the *compensation hypothesis* who argue that precisely because global markets are expanding it is necessary to have even more interventionist states, reveals a remarkable puzzle needing further examination. This will be the task of the empirical section next.

Research design, data, and hypotheses

The spatio-temporal parameters of this study are the following: fifteen OECD countries will be examined. N=15 (Austria, Australia, Belgium, Canada, Denmark, Finland, France, Germany, Italy, Japan, Netherlands, Norway, Sweden, The United Kingdom, and the United States) and the time period will range from 1973 to 1995 (t=23).

Three dependent variables measuring different aspects of redistribution will be utilized in this study, moving from the general to more specific forms of redistribution:
first, current disbursements as a percentage share of GDP will be examined. Current disbursements refer to expenditures such as public administration, law enforcement, public health, transfers, grant-in-aid payments from the central to local governments (in order to support for education for example), and public works. It includes expenditures on law enforcement and some defense related expenditures, but does not include military expenditures that are part of government capital formation.

Second, civilian general government consumption will be utilized as a second dependent variable. This measures total government consumption of goods and services net of military spending as a percentage of GDP, for instance it includes goods such as airplanes and paper clips, and services such as school teaching and police protection purchased by all levels of government. However, it does not include government transfers such as social security and unemployment benefits. Government consumption, besides transfers, is the main component of welfare state spending as it includes wages paid to workers in the public sector. To employ workers which are hard to place otherwise in the public sector has been a preferred strategy of the Scandinavian welfare states. Such a strategy of “active labor market policies” affords and “indirect” access to health care and education, as opposed to the direct use of transfer payments and may be politically more contentious than outright transfer payments (Iversen and Cusack, 2000).

Our third distributive measure are government transfers which are sums of money specific groups receive as outright grants from the government, such as social security benefits, unemployment compensation, paid maternity leave, and the like. All our three dependent variables are operationalized as a percentage share of GDP. (For detailed operationalization and sources of variables see appendix).
The three core theoretical predictor variables are “collective” and “competitive” veto points, and “globalization” the latter of which is operationalized as a composite measure consisting of trade (imports and exports as a percentage of GDP), inflow and outflow of Foreign Direct Investment as a percent of GDP and capital mobility based on the data collected by Dennis Quinn (1997). These three measures were standardized, added up, and standardized again to create a composite measure called “globalization”. Both, the aggregate globalization measure, as well as the three disaggregated elements will be used in the empirical analysis.

Collective and competitive veto points are operationalized as the first and second dimension of democracy by Arend Lijphart (1999), standardized for the sample of 15 countries used in this study. Lijphart’s two dimensions of democracy aptly capture the concepts of “competitive” and “collective” veto points as operationalized in this study. Lijphart’s five elements that fall under the rubric of “collective” veto points are (consensual elements are cited first): executive power-sharing in broad multi-party coalitions vs. single party, bare majority cabinets; executive legislative balance of power vs. dominant executives; multi-party systems vs. two party systems; an electoral system of proportional representation vs. single-member district system, and finally: an interest group representation system that is corporatist vs. one that is pluralist.

Thus, “collective veto points” have a consensual as well as a majoritarian polarity. It is the configuration of these five elements of institutions contained in this concept of “collective” veto points in which we should expect to find an “expansionary” policy process because this is the arena in which political power is shared, where there is joint responsibility, where the actors meet each other face to face, oftentimes in different roles
and in different functions. The nature of this form of interaction has a tendency to lead to higher cooperation (Axelrod, 1980). It is immaterial that this form of cooperation might often be detrimental to the interest of the whole government as such (as when coalition parties refuse to cut their part of budget and impose on other governmental parties to go first which is essentially a collective action problem) – the point is that this set of institutions has a “built-in” tendency to expand the growth of government, or at least reduce it less than other “competitive” veto points. Thus, it is expected that the more consensual collective veto points are, the higher the redistributive effects, the more majoritarian they are, the less the redistributive effects. We expect a similar relationship to hold with our two tax measures, business and personal income taxes. Therefore, the predictions for this category of “collective” veto points is the opposite of what the “traditional” literature on veto points postulates, i.e. the more veto points there are the more difficult it is to change the status quo.

With regard to “competitive” veto points, however, the predictions are consistent with the literature on veto points. Since competitive veto points in this study are defined as separate agencies with mutual vetoes the more of these agencies there are, the more difficult it is to change the status quo. Competitive veto points are defined as (the consensual element is mentioned first again): federalism vs. unitary government; equally strong legislatures vs. unicameral legislatures; rigid constitutions vs. flexible constitutions; presence of judicial review vs. absence of judicial review; and independent central banks vs. dependent central banks. Does more consensus in this category of competitive veto points also mean more redistribution and taxation? No it does not. In competitive veto points, more consensus means more dispersion of political power by
means of separate agencies endowed with mutual veto powers. Thus, the theoretical predictions of the effects of “competitive” veto points are consistent with the claims made by Tsebelis (1999), Hallerberg and Basinger (1997) and others.

Since “collective” and “competitive” veto points are clusters of five constitutional elements each, we have decided to also display disaggregated results. However, since all of these elements are correlated with each other we cannot employ all five of the measure simultaneously for reasons of multicollinearity. We have chosen “corporatism” and “federalism” for the collective and competitive veto points respectively. Corporatism very much represents the informal nature of relationships between capital and labor and the ethic of “shared responsibility” that is typical for social partnerships. In addition to the more traditional “economic logic” of corporatism, i.e. the trading of moderate wage increases for full employment, or the indexing of wages to productivity, and the “institutional logic of corporatism”, i.e. its capacity to “internalize externalities” (Olson, 1986; Jankowski, 1993), various scholars have recently (re)discovered the “moral logic” of corporatism. Visser and Hemerijck (1997) have argued that corporatist arrangements are similar to Putnam’s (1993) idea of “social capital” where norms of reciprocity, trust, and sense of duty and responsibility to other social partners are cultivated.\(^6\) Thus, corporatism represents a crucial element in our syndrome of collective veto points.

Disaggregating competitive veto points, we selected “federalism” as a prototype of dispersion of political power. The effect of federalism (and, of course of the idea of “competitive veto points”) is the slowing down of policy change. For the theoretical

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\(^6\) It is of course true that corporatism has always consisted of much more than just an “economic logic”; the guilds of the 12th century were not only rent-seeking organizations, but also mutual aid associations. Corporatism and Catholicism have always had a natural affinity with each other. The strong corporatism in Austria is built upon the *Katholische Sozialelehre* which was always critical of the fragmenting effect of liberalism and capitalism.
reasons laid out above we would expect federalism to restrict policy change as groups at lower levels of government might successfully restrain the attempts by the central government to retrench the welfare state.

In addition to these three core predictor variables, other theoretically relevant control variables are also introduced: given that the dependent variables measure the redistributive and extractive capacity of the state, the ideological stance of government parties must be examined. Many scholars have argued that “parties do matter” when it comes to taxes and welfare state spending (Kirschen, 1964; Korpi, 1983; Castles, 1982, and many others). It is hypothesized that the higher the proportion of left votes in general elections, the higher the extractive and redistributive capacity of the state, ceteris paribus.7

In addition, the state of the economy needs to be taken into consideration also. Unemployment will be introduced as a control variable since it affects directly transfer payments and puts strong pressure on taxes. It is hypothesized that higher unemployment will positively affect transfer payments and civilian government consumption. In addition, the extent to which governments can spend may depend on how “developed” the societies are. Obviously, all the countries in our sample are “developed”; nevertheless, if we use GDP per capita as a measure of “development” we do find differences.8 According to “Wagner’s law” stated in 1883, only at a certain level of development can the diversion of scarce resources for welfare purposes be permitted.

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7 The more general measure of left votes rather than left seats in parliament or left seats in cabinets, is used in this study. The reason why this measure was chosen is that it captures are wider, more diffuse demand for policy production and is less partisan than the other two measures. Ultimately, neither one of these partisan measures proved to be significant in the empirical analysis.

8 I am quite aware of the difficulties in using GDP per capita as a measure of “development”. However, space does not permit me a thorough critique of this measure. It has become the established operationalization for capturing the concept of Wagner’s law.
Thus, it is expected that the higher GDP per capita, the higher transfer payments and the higher government consumption will be. As far as taxation is concerned, a similar positive relationship is expected. In addition, for the year of 1973 and 1979 oil dummy variables were introduced to gauge the effect of the quadrupling of the oil prices and the ensuing supply shock. Finally, the “crisis of aging” puts enormous demographic pressures on social welfare provision. To capture this dynamic, the percentage share of population that is above 65 years of age is also included as a control variable.

This study will employ the Beck and Katz (1995) method of using panel corrected standard errors in order to mitigate the statistical problems generated by panel data for ordinary least squares regression (OLS). The greatest advantage of this type of research design is that it increases the sample size, allowing for a higher number of variables to be introduced without drastically reducing the degrees of freedom. However, this type of panel analysis presents particular statistical problems since the difficulties of both cross-sectional analysis (heteroskedasticity) and time series (autocorrelation) are compounded in pooled analyses. In addition, errors may be correlated across cross-sections at the same point in time.

Nathaniel Beck and Jonathan Katz (1995) have shown that if the error structure in ordinary least squares is properly corrected for, traditional OLS methods produce unbiased and efficient results unless contemporaneous correlation (when large errors for unit i at time t are associated with large errors for unit j at time t) is unusually high, which rarely occurs in practice. This is a time dominant design (t=23, N=15) calling for control of serial correlation. Beck and Katz suggest using a lagged dependent variable to control for autocorrelation.
However, more recent research shows that lagged dependent variables tend to usurp much of the variation of the dependent variable and tend to “dominate the regression and destroy the effect of other variables…” (Achen, 2000, 14) particularly in the presence of heavy trending in the exogenous variables which is the case in our dataset. Achen (2000, 7) describes the effect of including a lagged dependent variable into a regression as acting “… as a proxy, picking up some of the effect of unmeasured variables. However, the autoregressive term does not conduct itself like a decent, well-behaved proxy. Instead, it is a kleptomaniac, picking up the effect, not only of excluded variables, but also of the included variables if they are sufficiently trended. As a result, the impact of the included substantive variables is reduced, sometimes to insignificance”.

Thus, we have decided to use the Prais-Winsten (1954) transformation to control for autocorrelation rather than using a lagged dependent variable. The Prais-Winsten method uses a differencing method to remove autocorrelation and is very similar to the Cochrane-Orcutt method with the additional advantage that the Prais-Winsten method retains the first observation. Therefore, our research design uses panel corrected standard errors to deal with heteroskedasticity, but will use the Prais-Winsten transformation to control for autocorrelation rather than using a lagged dependent variable.

Recently, some scholars such as Garrett and Mitchell (2000) have suggested that in pooled/time series designs, country as well as year fixed effect models should be introduced by using country and year dummies in order to capture country specific and time specific distinctions that cannot be measured by a specific variable. We have refrained from the use of such a fixed effects model for two reasons: first a practical and secondly a substantive reason. The practical reason is that using such a model with
country as well as year dummies, a tremendous amount of multicollinearity is introduced into the equation to such an extent that the full model cannot be estimated and variables have to be dropped to avoid perfect collinearity among predictors. Our substantive concerns refer to the use of dummy variables without a theoretically derived conceptual purpose. This does not further our theoretical understanding of the complex effects that country and year dummies may exert, but may, in fact, be a “cover up of our ignorance”. (Kmenta, 633).

Findings

The following three tables are divided into an aggregated and a disaggregated model. Aggregated means that composite measures were used for collective and competitive veto points (each consisting of five elements) and globalization, another composite measure consisting of three elements: in- and outflow of direct foreign investments as a percent of GDP, trade (imports and exports as a percentage of GDP), and a rank ordering on capital de-regulation. The disaggregated model, as the name implies, provides estimates for the constituent elements of globalization as well as for one institutional element each for collective and competitive veto points.

Table one demonstrates that, as hypothesized, collective veto points tend to buoy current disbursements, while competitive veto points tend to restrict them. The positive coefficient of globalization indicates that globalization, rather than reducing current disbursements, actually tends to increase them. Unemployment, not surprisingly, shows a positive coefficient as well, together with “age” variable indicating that rapidly aging
populations are strongly driving welfare provision. These two control variables are positive and significant in all of the six models. Surprisingly, the variable percentage left vote fails to reach significance in any of the six models introduced while the “oildummy” variable is negative and significant in five out of the six models.

Table one about here

Disaggregating the institutional variables and the globalization measure yields very similar results with regard to the institutional variables. Corporatism and federalism have a significant positive and negative effect on current disbursements, respectively. Interestingly, while trade and capital deregulation have a positive effect on current disbursements, foreign direct investment has no significant effect.

The general argument made throughout this paper, is that globalization is mediating the effects of institutions. Such a theoretical argument is modeled by using interactive (multiplicative) terms. In the equations in tables one (current disbursements) and three (social transfer payments), such interaction effects have been explored, but no significant results were found. However, table two, which examines civilian government consumption (CGC), the aggregated model indicates significant interaction effects between the institutional variables and globalization. Globalization and competitive veto points both affect CGC negatively with an interaction coefficient that is also negative. This means that the level of competitive veto points significantly mediates the effect of globalization on CGC. Given the degree of globalization, the effect of competitive veto points on CGC is negative, beyond what its level would be if the effect of globalization were zero; in other words, globalization adds to the negative effect competitive veto points already have on CGC. Remarkably, this is precisely the same finding as Swank
(2001, 150), even though different measures and time periods were used in the two studies.

Table 2 about here

The disaggregated results in Table two show that collective veto points are highly positively related to CGC, while competitive veto points fail to reach significance. Among our three measures of “globalization”, capital deregulation does not affect CGC while both trade and foreign direct investment negatively influence government consumption (again, a similar finding is reported by Swank 2001).

Table 3 about here

Inspection of the parameters in table 3 which examines social transfer payments, we encounter a similar story: collective veto points and globalization have positive effects, while in the disaggregated model, corporatism has positive and federalism has negative effects. Among the disaggregated globalization measures, trade and capital deregulation have both positive significant effects on social transfer payments, with foreign direct investments being non-significant. Similarly, the two core theoretical variables, collective and competitive veto points, behaved as hypothesized with collective veto points expanding the various redistributive measures and collective veto points restricting them, providing strong evidence that not all veto points are created equal; some have “enabling” effects while others have “restrictive” effects.

Discussion
We started out with two puzzles: first, if it is indeed true that more veto points (which are understood to be political parties in most of the veto point literature) means more difficulty in changing the status quo, how is it possible that the governments that have produced the most extensive welfare states are exactly the ones which are generally characterized by multi-party or oversized coalitions? It is known that in the late 1950s and early 1960s there were very little differences in government expenditures between the advanced universal welfare states of Scandinavia and the residual, liberal Anglo-Saxon welfare states, and the catholic-reformist welfare states in the middle of the spectrum. A path-dependency argument does not assist either in understanding why a “fanning-out” process took place in the early 1960s that led to the intriguing variation among welfare states today. According to some observers of the veto-points literature, multi-party systems should have a higher difficulty to change the political status quo than single-party, bare majority systems. Empirically, however, the most “developed” welfare states are exactly those that generally have a higher average number of governmental parties that share power than “residual” welfare states, which generally have a lower number of governmental parties in power.

This study provides an answer to this puzzle by taking a closer look at the concept of “veto points” and separating them into “collective” and “competitive” veto points. Not all veto points have the same effects. What is termed “collective veto points” tend to have “enabling” effects, in other words: because power is shared, political actors interact with each other on a face-to-face basis, and responsibility for political success or failure is shared, such a configuration of institutions leads to a form of cooperation that easily falls victim to collective action problems whereby a particular political action (i.e. insisting
that other parties should start cutting their part of the budget first, or that expenditures for one parties’ constituency are perceived to be crucial for the reputation of a party leading to a logrolling dynamic, etc.) is individually rational, but collectively irrational.

This study found strong evidence that this expansionary tendency of collective veto points is actually occurring. Competitive veto points, on the other hand, function in a manner consistent with the claims made by observers of the veto points literature. This type of veto points, relies on separate agencies, endowed with mutual vetoes leading to restrictive effects as collective action problems can more easily be resolved. This form of separation of powers, represented most clearly in the government of the United States of America, may lead to serious problems of accountability as the habitual finger pointing between members of the two houses of the American Congress and/or the President attests to or even to the shutdown of government as it occurred during the winter of 1995/96. Some members of some branches of governments may even prey on the dynamic of separation of powers insofar as they calculatedly introduce dubious legislation knowing full well that the other branch will not accept it, only in order to shift the blame to the vetoing institution.

Whether legitimate or not, separate agencies with mutual veto powers have been designed deliberately by the Founding Fathers to restrict government, making the American Constitution an example of “gridlock by design”. Our findings are consistent with such arguments. In all six models, competitive veto points (or the variable “federalism”) have a negative and significant effect on civilian government consumption, internal transfers, business taxes, personal income taxes and total taxes.
The second puzzle referred to the purported effects of globalization on the state’s capacity to redistribute incomes and extract revenues. The preceding analysis suggests that there is very little evidence that globalization systematically undermines the government’s capacity to fund the welfare state. Neither current disbursements, nor social transfer payments are negatively affected by globalization, in fact, the opposite is true. However, there is evidence that government consumption is negatively influenced, particularly by the in- and outflow foreign direct investments, and trade. Public sectors may be increasingly forced to deregulate in the face of pressures from domestic or foreign private companies, which can provide services more cheaply and more effectively.

This analysis has shown that political institutions continue to have dramatic importance in shaping policy trajectories in industrialized democracies despite, and because of, globalization. Different institutions refract the pressures of globalization differently. In order to better understand the dynamics of the welfare state, not only the pressures of globalization need to be examined but also a more refined understanding of veto points is necessary to comprehend that not all veto points have the same effect and that not all veto points are created equal.
Appendix: Data Sources.

Dependent variables: (all as a percentage share of GDP).


Measures on globalization:


Capital Deregulation: This is a rank ordering of capital openness ranging from 0 (completely closed) to 14 (completely open). Source: Dennis Quinn (1997). “The Correlates of International Financial Liberation”. American Political Science Review. 91:531-551.
Institutional measures:

**Collective and competitive veto points**: These are Arend Lijphart’s (1999) five measures for the “executive-parties” (effective number of parties, proportionality of electoral system, corporatism, executive-legislative balance of power, and executive power sharing in coalitions) and “federal-unitary” (federalism, bicameralism, rigid constitutions, judicial review and independent central banks) dimension of democracy respectively. All five were standardized for the 15 countries in this study, added up, and standardized again to create the composite score of collective and competitive veto points.

Control variables:


**Unemployment**: Source: OECD *Economic Outlook*. Various editions.

**GDP per capita**: OECD *Economic Outlook*. Various editions.

Table one: Current government disbursements as percentage of GDP for 15 OECD countries from 1973 to 1995.

<table>
<thead>
<tr>
<th></th>
<th>Aggregated model</th>
<th>Disaggregated model</th>
</tr>
</thead>
<tbody>
<tr>
<td>Collective Veto points</td>
<td>2.0 (.63)***</td>
<td>1.6 (.7)***</td>
</tr>
<tr>
<td>Corporatism</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Corporatism</td>
<td>1.6 (.7)***</td>
<td></td>
</tr>
<tr>
<td>Competitive Veto points</td>
<td>-.56 (.37)*</td>
<td>-.37 (.27)*</td>
</tr>
<tr>
<td>Federalism</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Globalization</td>
<td>.42 (.29)*</td>
<td></td>
</tr>
<tr>
<td>Foreign Direct Investment</td>
<td>-.05 (.05)</td>
<td></td>
</tr>
<tr>
<td>Imports and Exports as % of GDP</td>
<td>.06 (.017)***</td>
<td></td>
</tr>
<tr>
<td>Capital Deregulation</td>
<td>.35 (.20)*</td>
<td></td>
</tr>
<tr>
<td>Control variables:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Percent of population over 65 years of age</td>
<td>2.1 (.21)***</td>
<td>1.7 (.20)***</td>
</tr>
<tr>
<td>Unemployment</td>
<td>1.1 (.10)***</td>
<td>1.04 (.09)***</td>
</tr>
<tr>
<td>GDP per capita</td>
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<td>6.0e-6 (6.1e-6)</td>
</tr>
<tr>
<td>% left vote in gen. Elections</td>
<td>-.004 (.02)</td>
<td>.002 (.003)</td>
</tr>
<tr>
<td>Oildummy</td>
<td>-.77 (.33)**</td>
<td>-.66 (.30)**</td>
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<tr>
<td>Constant</td>
<td>9.1 (3.0)***</td>
<td>6.3 (3.4)*</td>
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<tr>
<td>Adjusted R²</td>
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<td>.71</td>
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<tr>
<td>Degrees of Freedom:</td>
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<td>321</td>
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Panel corrected standard errors in parentheses (z-scores). One tailed tests.*=P[z]<.1, **=P[z]<.05, ***=P[z]<.01. (one-tailed tests). See appendix for data sources.
Table two: Civilian government consumption as percentage of GDP for 15 OECD countries from 1973 to 1995.

<table>
<thead>
<tr>
<th></th>
<th>Aggregated model</th>
<th>Disaggregated model</th>
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</thead>
<tbody>
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<td>Collective Veto points</td>
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<td>1.1 (.3)***</td>
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<tr>
<td>Corporatism</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Competitive Veto points</td>
<td>-.35 (.17)**</td>
<td>.08 (.13)</td>
</tr>
<tr>
<td>Federalism</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interaction terms:</td>
<td></td>
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<td>Coll. veto points*globalization</td>
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<td></td>
</tr>
<tr>
<td>Comp. veto points*globalization</td>
<td>-.23 (14)*</td>
<td></td>
</tr>
<tr>
<td>Globalization</td>
<td>-.19 (.13)*</td>
<td></td>
</tr>
<tr>
<td>Foreign Direct Investment</td>
<td></td>
<td>-.062 (.028)**</td>
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<tr>
<td>Imports and Exports as % of GDP</td>
<td></td>
<td>-.012 (.007)*</td>
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<tr>
<td>Capital Deregulation</td>
<td></td>
<td>.03 (.08)</td>
</tr>
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<td>Control variables:</td>
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<td></td>
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<tr>
<td>Percent of population over 65 years of age</td>
<td>.59 (.11)***</td>
<td>.48 (.13)***</td>
</tr>
<tr>
<td>Unemployment</td>
<td>.25 (.05)***</td>
<td>.23 (.05)***</td>
</tr>
<tr>
<td>GDP per capita</td>
<td>1.0e-5 (2.4e-5)</td>
<td>5.6e-6 (2.8e-6)</td>
</tr>
<tr>
<td>% left vote in gen. elections</td>
<td>.01 (.17)</td>
<td>.011 (.017)</td>
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<tr>
<td>Oildummy</td>
<td>-.35 (.14)***</td>
<td>-.38 (.14)***</td>
</tr>
<tr>
<td>Constant</td>
<td>5.8 (1.5)***</td>
<td>8.1 (2.1)***</td>
</tr>
<tr>
<td>Adjusted R²</td>
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<td>.62</td>
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<td>Degrees of Freedom:</td>
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Panel corrected standard errors in parentheses (z-scores). One tailed tests. *=P[z]<.1, **=P[z]<.05, ***=P[z]<.01. (one tailed tests). See appendix for data sources.
Table three: Social transfer payments as percentage of GDP for 15 OECD countries from 1973 to 1995.

<table>
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<th>Aggregated model</th>
<th>Disaggregated model</th>
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<tr>
<td>Collective veto points</td>
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<td>1.2 (.38)***</td>
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<tr>
<td>Corporatism</td>
<td></td>
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<tr>
<td>Competitive veto points</td>
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<td>Federalism</td>
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<td>Globalization</td>
<td>.33 (.17)**</td>
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<td>Foreign Direct Investment</td>
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<td>-.02 (.03)</td>
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<tr>
<td>Imports and Exports as % of GDP</td>
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<td>.037 (.009)***</td>
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<td>Capital Deregulation</td>
<td>.21 (.11)**</td>
<td></td>
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Control variables:

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<th>Variable</th>
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<th>Disaggregated model</th>
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<td>Percent of population over 65 years of age</td>
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<td>.56 (.14)***</td>
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<tr>
<td>Unemployment</td>
<td>.61 (.05)***</td>
<td>.62 (.05)***</td>
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<td>-9.9e-07 (2.7e-6)</td>
<td>3.4e-5 (2.8e-5)</td>
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<tr>
<td>% left vote in gen. elections</td>
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<td>Oil dummy</td>
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<td>.58</td>
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Panel corrected standard errors in parentheses (z-scores). One tailed tests.*=P[z]<.1, **=P[z]<.05, ***=P[z]<.01. See appendix for data sources.
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