

Economic theory

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**WAGNER'S LAW:
AN INTRODUCTION TO AND A TRANSLATION
OF THE LAST VERSION
OF ADOLPH WAGNER'S TEXT OF 1911***

There exists a large number of articles and books dealing with the so-called Wagner's Law; many of them have been published in Public Finance/Finances Publiques. Adolph Wagner (1835–1917), one of the leading German economists of the second half of the 19th century, developed his «Law on the expansion of public, in particular State activities» during a long period of more than fifty years. The latest version published by him is the one of 1911 where the «Law» is to be found in the fourth section of a larger article devoted to the economic functions of the State and the public sector. Given that this text seems not to be available in an English translation, but that his proposition in an often very simplified form still stimulates discussion, it seems to be useful to publish an English translation of it. A few introductory remarks are added in order to

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This last version of the so-called Wagner's Law on the expansion of public, in particular State activities is to be found in section 4 of Adolph Wagner's «Staat in nationalökonomischer Hinsicht», in J. Conrad et al (eds.), Handwörterbuch der Staatswissenschaften, 3rd completely revised edition, vol. 7, Jena 1911, pp 727–739 resp. 734–36. An English translation of section 4 is printed below under II. Economic Functions of the State.

allow the reader to locate Wagner's Law in the historical context and to suggest an extended and more differentiated approach to testing Wagner's Law.

I. Introduction

«Observation, as can be proved historically and statistically, shows that there exists in the State a clear tendency for an expansion of public, respectively State activities together with the progress of the economy and of culture in the domains of the two organic State purposes. This expansion appears as something so regular and can so clearly be traced back to its inner causes and prevailing conditions that it seems to be permitted to speak of a «Law» of an increasing expansion of public (including communal), especially State activities in the sense in which this term is being and justifiably can be employed in the field of socio-economic phenomena».

This is a translation of the first paragraph of Adolph Wagner's text of 1911 (section 4) in which he dealt for the last time with his «Law». He has been preoccupied with this issue during almost fifty years according to the dates of his relevant publications, and presumably for more than five decades, if the time before and after his publications is taken into account. According to Norbert Andel¹, Wagner first developed the basic idea of his Law in 1863 in a study dealing with the State budget and the public debt of Austria². The final version of the Wagner's Law is to be found in Wagner's contribution to the *Handwörterbuch der Staatswissenschaften* entitled «Der Staat in nationalökonomischer Hinsicht» (translated here by «Economic Functions of the State»). This text can be considered to represent something like Wagner's legacy, summarising what he had thought, discussed and published regarding the role of the public sector and of the State in particular from a long-term perspective.

In their famous *Classics* volume, Richard A. Musgrave and Alan T. Peacock³ published three Extracts from Adolph Wagner's publications concerning «The Nature of the Fiscal Economy»⁴, «The Basic Principles of Taxation»⁵ and «Justice in Tax Distribution»⁶. Wagner himself mentioned briefly his Law in these texts, but since they deal with taxation, he did not discuss it in detail. At the be-

¹ Norbert Andel, *Finanzwissenschaft*, 4th ed., Tübingen, 1998, p 189.

² Cf. Adolph Wagner, *Die Ordnung des österreichischen Staatshaushaltes mit besonderer Rücksicht auf den Ausgabe-Etat und die Staatsschuld*, Wien 1863.

³ Richard A. Musgrave and Alan T. Peacock (eds.), *Classics in the Theory of Public Finance*, International Economic Association, London/New York 1958.

⁴ Extract from Adolph Wagner, *Finanzwissenschaft*, part I, 3rd rev. ed., Leipzig 1883, pp. 4–16, 69–76.

⁵ Extract from Adolph Wagner, *Finanzwissenschaft*, part II, 2nd rev. ed., Leipzig 1890, pp. 207–208. 299–305

⁶ Extract from Adolph Wagner, *Finanzwissenschaft*,. part II, 2nd rev. ed., Leipzig 1890, pp 381–387.

gining of the first extract dealing with the nature of the fiscal economy, Wagner states: «This is not the place to discuss whether, when and how the compulsory acquisition of goods by the State is justified», because he had done this elsewhere, i.e. in his *Grundlegung der politischen Ökonomie* (Foundations of Political Economy) of 1893. The editors of the Classics in a footnote also explain this. They add that Wagner's discussion «is in historical terms (italics Dieter Biehl) and consists of an elaboration of the «law of the increasing expansion of public activities», mentioned here at the end of section I».

Given the title of their book, «Classics in the Theory of Public Finance» (italics Dieter Biehl), this could be interpreted as meaning that Musgrave and Peacock did not see a sufficiently strong theoretical content in Wagner's Law and, therefore, abstained from including an extract dealing with this Law. Indeed, the presentation in Wagner's *Grundlegung* is more «historical» and far less «theoretical» than his text of 1911. Some readers might well argue that the text of 1911, too, does not represent «theory» in the traditional sense. Wagner's view is a much more comprehensive one, a *Gesamtschau*, a holistic vision presumably influenced by the Hegelian philosophy of history, but at the same time adequately differentiated. It combines elements of what we nowadays would call theories of public goods, of multi-level government and decentralisation, of regulation, of industrialisation and urbanisation, of social cost and ecological values and of a sociological theory of group behaviour.

At any rate, Wagner's Law has attracted considerably more interest than his statements on taxation. A large number of books and articles demonstrate that many scholars felt inspired by the stimulating propositions of Wagner's Law. However, in most of this literature, including public finance textbooks, the wealth of Wagner's ideas has been reduced to a Law of public expenditure growth. One of the reasons seems to be that such a simplified version, where expenditure growth is a function of rising per capita income, can easily be tested econometrically. Another reason could be that because there exists no English translation of Wagner's Law, non-German speaking authors had difficulties in getting direct access to Wagner's complex and differentiated ideas.

There is no doubt that the public expenditure analyses of Wagner's Law – some of which were published in *Public Finance/Finances Publiques* – have contributed to better understanding the causes of long-run public finance growth in many countries. And Wagner himself argued that all the developments and driving forces he discusses will result in increasing absolute and relative expenditure and taxation levels – but he also wrote: «The State will act with legislative and administrative measures and with financial means» (cf. the translation of Wagner's text below under II).

This statement and similar ones in Wagner's texts seem to have been overlooked for a long time. They imply – and this is not only a Wagnerian, but also a general proposition – that the public sector in general, and the State in particular, possess two large sets of instruments: legal and administrative ones on the one hand, and financial ones on the other. This suggests that in order to

really obtain a full picture of the expanding public sector, appropriate indicators for the first set of government instruments, too, should be constructed and included in the analysis.

A second suggestion for future research concerning Wagner's Law could be to investigate as to whether there exists a sort of substitution effect between the two sets of instruments: for example, a government can reduce taxes and expenditures, but at the same time expand the use of legal prescriptions and regulation as policy instruments. Since many countries from time to time cut both taxes and expenditures, their expenditure shares may have remained constant or may even have fallen. As a consequence, the traditional testing for Wagner's Law would result in rejecting the hypothesis of an expanding public sector. However, if the same countries continued to produce thousands of new legal and administrative rules during each election period and moreover at all levels of government, thereby shifting the burden of public activities to the private sector, the reduced shares of expenditure would give a wrong picture as to the overall influence of the public sector. It seems, therefore, necessary to define and introduce additional variables in the testing of Wagner's Law that would represent the up-to-now neglected first set of public sector instruments.

The worst scenario would obviously be one where expenditure in respect of public administration is drastically cut while the process of producing new laws and administrative rules continues requiring an increased bureaucracy as the new rules will have to be controlled and sanctioned in case of violations. The consequence could be a serious disfunctioning of the public sector where the rule of law will no longer be fully guaranteed. The suggested extension for research in Wagner's Law is, therefore, in no way of purely academic interest, but could help to enrich the public debate, to better understand the relationships between the public and the private sectors, to improve the quality of government advice and to prevent undesirable developments.

A third suggestion is related to Wagner's distinction between what he called «the two organic State purposes», i.e., «law and power» (Rechts- und Machtzweck) and «culture and welfare» (Kultur- und Wohlfahrtszweck). Wagner argues that in the latter domain of public activities, «there does not exist the same need for uniformity, concentration and centralisation of the provision of services by public authorities, in this sphere partly the opposite is true» (cf. the following translation of Wagner's text below under II, p 108). This statement (and similar other ones) indicates first that his Law should not be misinterpreted as if each individual public activity and every public expenditure category will always follow the same development path. Furthermore, an additional suggestion for testing Wagner's Law could be derived from this statement. According to Wagner, the two domains could differ in respect to their relative degrees of uniformity, concentration, and centralisation/decentralisation. This proposition also offers new possibilities for a more differentiated testing of his Law in replacing or supplementing the traditional income per capita variable by indicators of «uniformity, concentration, and centralisation» – in modern terms indicators of different degrees of publicness.

Last but not least, there is a final (minor) reason for publishing a translation of Wagner's last text on his Law. As Managing Editor of Public Finance/Finances Publiques, I still receive papers dealing with Wagner's Law. Instead of writing individual letters and explaining again and again Wagner's ideas to the authors and referees concerned, I think that communication is facilitated if an English translation is available that could be consulted by potential authors when preparing their manuscripts. Admittedly, I have to accept the criticism that Wagner's text should have been published earlier.

Some additional information on Wagner's personality and the context of his time may be helpful for the reader to better understand his Law and the reactions to it. These are only a few personal remarks that in no way can claim to give a full picture.

Who then was Adolph Wagner?⁷

Adolph Wagner (born Erlangen 1835 – died Berlin 1917) has been one of the great German economists and an influential political figure during the second half of the 19th century. Due to his wide economic interests, in particular in the sphere of social policy and public finance on the one hand, and his political activities on the other in order to contribute personally to the implementation of what he considered to be adequate policies, his life and his career are impressing colourful and multifaceted. He – and many other economists of his time – were convinced that in the emerging German economy of the second half of the 19th century, but also in many other countries, the State should play a major role in avoiding both a one-sided «Manchester capitalism» (as it was called at the time), but also at the same time a socialist or even communist society.

Wagner's insistence both in his economic writings and in his political activities on the role of the public sector in a (from his point of view) well balanced division of labour between the private and public sectors made him a representative figure of what we nowadays would call a «mixed economy» paradigm with a strong and increasing public sector. One could also characterise him by saying that he was both a welfare economist and a welfare politician. This combination seems to have been, and still is, the cause of much criticism raised against Wagner's ideas and personality. Some of these criticisms are⁸:

- As Wagner presented both a theoretical concept and empirical support for it, he is often criticised for having derived unacceptable generalisations from unreliable data.
- The factors Wagner is referring to may explain an absolute, but not necessarily a relative increase in the share of public expenditure.

⁷ The following brief text does not intend to present a biography of Adolph Wagner. Its sole purpose is to provide some information on Adolph Wagner in order to allow the reader to better understand the personal, historical, and scientific background of his writings.

⁸ Cf. Norbert Andel (1998), p 191.

- Wishful thinking may have seduced Wagner to mix up social policy postulates and scientific analyses. One has to take into account that Wagner was a so-called «Kathedersozialist» who for ideological reasons pleaded for a stronger role of the State.

The term «Kathedersozialismus»⁹ had been invented in 1871 as a nickname by H.B. Oppenheim, also a Professor of Economics, but a strongly convinced «free trader». He originally used this term in an article defending free trade against the positions of leading members of the so-called historical school of economists in Germany, in particular Roscher, Schmoller and Schönberg¹⁰. Since Wagner participated in the debate and presented the position of the reformers, in particular those engaged in social policy, the label was also stuck to him despite the fact that Wagner clearly rejected socialism and communism both as ideologies and as bases for practical policies. Nevertheless, from the point of view of the free traders, social policy as advocated by Wagner and others, and what we today would identify as a characteristic of the Welfare State, was equivalent to State Socialism

Wagner was also one of the initiators of the «Verein für Socialpolitik» (Association for Social Policy), founded in October 1872; the forerunner of the present German Economic Association (that still keeps the original title as a second name). The label «Kathedersozialisten» was also attached to members of the «Verein», although many prominent personalities that belonged to it were conservative and only one third of members at the time had been professors¹¹.

II. Economic Functions of the State¹²

Economic Functions and the State: Development Trend of Public, in particular State Activities in the Modern State of Law and Culture

by Adolph Wagner

⁹ «Kathedersozialismus» is the German name for the pulpit from which professors used to give their lectures.

¹⁰ See Lexis (1911), «Kathedersozialismus», in: Ludwig Elster (ed.), Wörterbuch der Volkswirtschaft, 3rd completely revised ed., Jena, pp. 37–38.

¹¹ Cf. Lexis (1911), p 37.

¹² English translation by Dieter Biehl of section 4 of the last published version of the so-called «Wagner's Law» as Wagner himself formulated it in 1911 (cf. Adolph Wagner, «Der Staat in nationalökonomischer Hinsicht» (translated here as «Economic Functions of the State»), in J. Conrad et al. (eds.), Handwörterbuch der Staatswissenschaften, vol. 7, Jena 1911, pp 734–36. I should like to thank Stephen F. Frowen of the University College London and St. Edmund's College Cambridge for his advice and comments on the translation. All errors are mine.

Observation, as can be proved historically and statistically, shows that there exists in the State a clear tendency for an expansion of public, respectively State activities together with the progress of the economy and of culture in the domains of the two organic State purposes.¹³ This expansion appears as something so regular and can so clearly be traced back to its inner causes and prevailing conditions that it seems to be permitted to speak of a «Law» of an increasing expansion of public (including communal), especially State activities in the sense in which this term is being and justifiably can be employed in the field of social and economic phenomena.

In a macroeconomic understanding, this law means an absolute and even relative expansion of public, in particular State and community forms of organisation besides and sometimes in place of private forms of organisation within a national economy. The causes are to be found in the emergence of new, increasing and refined public needs, especially community needs concerning all aspects of people's life. The conditions consist to a large extent of changes in production and transport technologies that make possible and at the same time desirable a greater involvement of the State, which would be in addition or maybe even instead of other public, local or other functions. The consequence is that the needs of individuals and of private agents is better served through the State and other public corporations as intermediaries. In exchange, private agents pay taxes and fees or the State and these corporations take over private sources of revenue and partly cover the cost of public services with surpluses so obtained. Preconditions and again consequences are in particular economic and financial ones common public norms of remuneration replace private ones, fees, public charges and taxes substitute the free market exchange price. Both the revenue and expenditure side of government budgets and the budgets of other public authorities expand and take on new forms «Taxes increase» without predetermined limits, but taxpayers, the population at large, obtain a satisfactory return in full through increased and improved public services. However, not every person will always be consulted about his individual share in public services received, about the utility of his share and about his individual contribution in accordance with the private economy principle of correspondence, that determines the relationship between the value of specific public services received and the financial contribution made. This appears to apply only to cases where a fee is charged and in other similar cases, such as court charges, administrative costs, school fees, transport fares, etc. Predominantly, public services are provided to the population as a whole and to individuals as part of it. According to the public economy principle of general remuneration, specific norms that are considered to be appropriate are applied. The purpose of this procedure is to obtain individual contributions for covering costs which in general are based on coercion, in other words, individuals are taxed according to their ability to pay. The

¹³ These two «organische Staatszwecke» (organic State purposes) are the «Rechts- und Machtzweck» (Law and power purpose) and the «Kultur- und Wohlfahrtszweck» (culture and welfare purpose). See below for Wagner's explanation of these two terms.

development and expansion of public services as well as the increase of public, in particular State, finances reflect the expansion of public activities.

This development emerges from both domains of State activities, but is more pronounced in the domain of «law and power» («Rechts- und Machtzweck»). This is true in view of the trend of historical developments, and, as mentioned above, the emerging needs arising from the equitable and proportional distribution of public institutions and functions within the territory involved. All this will have the effect that it is the State as such that takes over exclusively the main tasks of legal protection within its borders and in relation to foreign countries (military organisation, the system of courts, police, legislation and foreign policy generally). In the past some of these functions were at least partly in the hands of other public corporations and public bodies, such as local governments and landlords. In the domain of culture and welfare («Kultur- und Wohlfahrtszweck»), there does not exist the same need for uniformity, concentration and centralisation of the provision of services by public authorities; in this sphere partly the opposite is true. Here, other public bodies are providing services jointly with or instead of the State, a tendency that is increasing. A new administrative arrangement, such as the organisation of larger bodies of self-administration in-between the local community and the State («associations», counties, districts, and the so-called «new bodies of self-administration at a higher level») serve that purpose.

With cultural progress, again both as a precondition and consequence, there is the advantage of guaranteed undisturbed legal security within the country and within the national economy, as well as in relation to the outside world, to countries and peoples. This also benefits the solution of problems arising from an increasing population density, a more pronounced concentration of the local population (urbanisation and industrial location), the steadily developing division of labour, as well as the increasing complexity of transport, economic, and legal interrelationships. All these are signs of a decisive evolution that leads to an extensive and intensive increase of public and particularly State activities in the domain of law and power. By coincidence, these are the same forces that cause the preventive principle¹⁴ and its corresponding institutions to emerge as dominant factors, as shall be explained later. The needs of a developed national economy are the driving forces in these two directions, that in turn and in a re-

¹⁴ Wagner distinguished between a «Repressivprinzip» (principle of repressivity) and a «Präventivprinzip» (principle of prevention). The first concerns ex post reparation or compensation of already existing violation of legal positions, the second is oriented towards ex ante prevention of such possible violations. According to Norbert Andel, Wagner changed his evaluation as to the effect of the principle of prevention. In his *Grundlegung* of 1893, prevention is linked with increasing expenditure whereas in the present text of 1911 (but in the sections not translated here), this expenditure effect is no longer mentioned (cf. Norbert Andel (1998), p 190). In section 5 of 'Der Staat in nationalökonomischer Hinsicht', Wagner also argues that one could even speak of a «Law» of increasing predominance of the principle of prevention that increasingly will crowd out the principle of repression (p 737).

ciprocal interrelationship become the preconditions for new economic progress and through this, will also lead to a generally higher level of civilisation. The great similarity in the development of public institutions and services in the domain of law and power shows clearly that there is a general need but also conditions for development.

In the domain of culture and welfare, the expansion of the State, of local institutions, of associations and their services is again effect and consequence and at the same time it is the cause and the precondition for economic and cultural progress. However, here the development in temporal and in local spatial respect is less regular and is exposed temporarily and permanently to different influences. This is especially true as far as the distribution of institutions and services among the State (the «Reich»), associations, organisations, local governments or bodies created only for one specific purpose is concerned. Nevertheless, this expansionary tendency too has the character of a development law. Material goods production and its legal and economic foundations, land, buildings, investment capital, especially in the transport sector, all represent to a considerable extent the development of production technology, the needs of large enterprises, the evils of speculative private capital and its forms of organisation (shares, stock exchanges), general climatic conditions, sanitation, ethical and political interests of the community and the people and their residential areas. All these factors contribute to the fact that public institutions, other facilities, services of the State and of associations as well as of local governments take the place of private institutions, of individuals and of private enterprises. This is linked with maintaining or expanding «public» property (even by private law) as to land, buildings, transport facilities, investment capital (State forests, mines, banks, enterprises, transport services, postal and telegraph services, railways, insurance companies, communal facilities of transport, of markets, of gas and electricity, of sanitation, etc.). All this demonstrates extensively and intensively an ever-richer development of public institutions and services in the different special fields of the production of material goods and of transport services again without determinable borders. But according to previous experience, always only in special fields, due to special reasons and depending on decisions to be considered case by case, not following a general formula or an absolute principle, which has been a major error of socialism. Ordinary main fields of economic life, such as agriculture, trade and commerce, are and presumably will rightfully remain, at least at their core, outside the reach of take-overs by public and local authorities.

In other fields of civilisation, we find similar but in general more extensive and intensive developments towards a take-over of institutions and services by the State, local governments and associations. This applies especially to education, training, schooling, sanitation, the support of the poor, welfare, etc. One of the reasons is that these tasks represent, according to the prevailing ideas of the civilised world, vital issues of great concern to the community. They concern societal duties towards its socially and economically underprivileged members. The issues of considerable general interest to all people include greater security

and a greater quantity and quality of services to cover the needs concerned, necessarily involving high cost, a best possible access on the part of all layers and classes of people, the consequences of scientific progress in different fields, the exploitation of its results for the benefit and sustainability of welfare, the protection against dangers and the abolishment of evils. The State will act with legislative and administrative measures and with financial means. This will be done in addition to, but also instead of smaller local organisations, as greater equality of institutions and services has to be provided in the interest of success. An additional reason is that the State is the best guarantor to provide what is necessary and perhaps also because the State can supply the funds needed at the lowest cost and/or redistribute the burden among the citizens in the best and fairest way (taxes, fees). There are other things, which also influence the process of expanding public and State activities in the general interest in order to guarantee adequate welfare conditions. Among these are the scientific progress in the interest of health and conquering diseases of mankind as well as of animals, of plants, progress in respect of light, air, water, food, housing, disease-causing agents, preventive measures.

The preventive principle points to the particular importance of the factor «capital». Capital is invested in permanent institutions and bodies providing similar facilities. Partly linked with this is the investment in qualified labour, including well-trained civil servants and soldiers.

There is no field of State activity where this development shows up more magnificently and with more effect, also in economic and financial terms, than in the establishment of standing armies, in particular with the generalised obligatory military service, the big fortresses, the navy and all other facilities linked with these. Characteristic and important evidence is provided by the vital existence of the security police and its big institutions (gendarmerie, protective forces), the whole organisation of justice with its permanent courts, always ready to act, the prison system, the diplomatic and consular services, and in the domain of culture and welfare many preventive facilities and measures in the fields of sanitation, medical services, help and support for the poor and welfare services. The great uniformity in the development of these public institutions and services in the domain of law and power clearly shows that there exist general needs and the conditions for development.

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