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**A Reflection on the Pareto-Griziotti and Pareto-Sensini letters
on Ricardian Equivalence and Fiscal Theory***

by

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Abstract: This paper reflects on the influence of Vilfredo Pareto's letters to two of his ex-students, Benvenuto Griziotti and Guido Sensini, on Ricardian equivalence and fiscal theory. The letters are of historical interest because of their emphasis on the need for fiscal studies to consider "social equilibrium" and because they were written when Italian fiscal sociology was in its formative stages. It is suggested that the two sets of letters had quite different consequences; with Griziotti rejecting Pareto's contention that social equilibrium should play a central role in fiscal studies and Sensini attempting to develop an approach to public finance where the relationship between fiscal phenomena and social equilibrium is presented as the central issue in the theory of public finance. Griziotti's approach, which accommodates a fiscal sociology that focuses on specific political and legislation issues rather than general social equilibrium, proved more influential than Sensini's approach, but the Pareto-Sensini line of investigation is of greater current relevance.

Key Words: Fiscal Sociology, Public Finance, Vilfredo Pareto, Benvenuto Griziotti, Guido Sensini

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An Italian Foundation for New Fiscal Sociology: A Reflection on the Pareto-Griziotti and Pareto-Sensini letters on Ricardian Equivalence and Fiscal Theory

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1) Introduction

The establishment of fiscal sociology as a field of study is usually associated with the work of Rudolph Goldscheid and Joseph Schumpeter, undertaken towards the end of World War I, on whether states that fund their expenditures from taxation will inevitably become indebted and decline into fiscal crisis. It is less well known that a fiscal sociology also emerged in Italy at around the same time, and that the impact of tax and debt, in the form of discussion over the validity of the ‘Ricardian equivalence’ between public debt and supplementary taxation, was discussed privately and publicly in the context of economic equilibrium and social equilibrium.

Italian fiscal sociology developed under the indirect influence of Vilfredo Pareto, with work in the field mainly progressed by his ex-students such as Gino Borgatta and Guido Sensini. To provide insight into Pareto’s indirect influence on the development of Italian fiscal sociology, this study considers Pareto’s 1917 letters to his ex-student Benvenuto Griziotti, addressing shortcomings in the science of public finance generally and Griziotti’s analysis of Ricardian equivalences specifically, and his letters of 1905, 1917 and 1920 to Guido Sensini, on the importance of non-logic in fiscal decisions and encouraging Sensini to develop his fiscal studies. The main contribution of this study is that it considers the historical significance and current relevance of Paretian social equilibrium in Griziotti’s interpretation of the Italian tradition in fiscal studies and in Sensini’s approach to fiscal theory.

Section 2 reviews Pareto’s letters to Griziotti and Sensini, focusing on his concern that fiscal studies, including investigations into Ricardian equivalence, do not pay adequate consideration to social equilibrium. Pareto’s criticism of Griziotti is contrasted with his support for, and encouragement of, Sensini. Section 3 looks at the historical significance of the Pareto inspired fiscal sociology in Italy in light of Griziotti’s assessment of the issue and Sensini’s specific approach to fiscal studies. It is suggested that Sensini’s limited success was, in part, a consequence of his failure to clearly demonstrate the analytical gains from a focus of social equilibrium, which was partly due to an inadequate recognition of the varying degrees of theoretical determinism in the study of economic equilibrium (which is highly determined) and social equilibrium (which is less highly determined). Section 4 considers the

current relevance of Pareto's letters, and their influence on Griziotti and Sensini. It is suggested that the Pareto-Sensini line of investigation has a significant potential to influence developments in modern fiscal sociology. The conclusion is included in Section 5.

2) Pareto's letters to Griziotti and Sensini on Ricardian Equivalence and Fiscal Studies

When laying out the fundamentals of value theory in part 1 of "Considerzioni sui Principii Fondamentali dell'Economia Politica Pura", Pareto also stressed the limitations of such theory. Even at this early stage, his concern with the reliance of public finance on the hedonistic principle was foreshadowed:

"Limits of hedonistic theories: To us the defect [of treating everyone as perfect hedonists]... seems most serious when one wants to turn the principles of the new science to studies of phenomena that are not exclusively economic. As an example, the science of finances, in many cases, and governments, in nearly all cases, fall into gross errors. When these are combined with postulates of the kind that concern the character of State ethics, ..., they become like fairytales, less amusing but no more real than the travels of Astolfo on the moon." (Pareto [1892] 1882, pp88-89).

Subsequent to this, many of Pareto's most original contributions to economic and social theory were associated with his attempts to confine economic theory within its scientific limits. Among other things, this was achieved through: the development of a choice theory (Pareto 1900), which relies on the fact of choice rather than the existence of ophelimity or of measurement of marginal utility; his work in the first decade of the 20th Century clarifying the distinct meanings of logical and non-logical conduct; and the decision to complement the pure theory of economic equilibrium with a general theory of social equilibrium in the *Trattato di Sociologia Generale* (Pareto [1916] 1935). In contrast, studies in public finance tended to broaden the scope of economic analysis by studying public finances from a hedonistic and/or partial economic perspective. In the years after 1892, the considerable distance between the Paretian approach to the study of economic and political behaviour and the approach taken in the science of public finance continued to widen.

Therefore, it is something of a curious fact that while Pareto's important contributions to the fields of economics and sociology coincided with the period when the Italian tradition in the "scienza delle finanze" was in its "greatest bloom" (da Empoli 1991, p.143), Pareto never came to embrace public finance as a scientific discipline. When comments were made, mainly in the *Sociologia*, they were largely hostile to the proposition that public finance is significant in a scientific sense. Equally curious is the fact that, despite Pareto's indifference (at best) to public finance, the enormous respect among many Italian scholars for Pareto's

intellectual achievements ensured that his approach to methodology and systems of analysis were studied within Italian public finance circles, with his indirect influence on fiscal studies being significant. In this regard, Mauro Fasiani (1950) placed Pareto's contributions to public finance in three broad categories: fragmentary contributions to public finance themes, such as issues relating to Pareto's Law concerning income distribution, analysis of progressive taxation and analysis of public debt; methodological problems, such as the methodology of the social sciences in general and its applicability to public finance; and fragmentary contributions to a general theory of public finance, such as his critique of the notion of public goods and his analysis of collective welfare.

However, within the general field of Italian fiscal studies, Pareto's most unique influence concerns the development of an Italian fiscal sociology. As already noted, Pareto's ex-students played a prominent role in this process, not only as developers and disseminators of a Pareto inspired field, but also as thoughtful critics who reflected seriously on Pareto's approach and then rejected or significantly modified much of it. In this regard, ex-students who contributed to developments in the sociological approach to public finance include Gino Borgatta¹ (1913, 1920) and Guido Sensini (1920, 1929), whereas the relevance of Pareto's sociology for the study of public finance was assessed by Benvenuto Griziotti (who not only studied with Pareto but also Maffeo Pantaleoni, De Viti de Marco and Luigi Einaudi)² in a polite but much more critical manner.

Pareto and Griziotti

Pareto's letters to Griziotti were written somewhat reluctantly, and only because of Griziotti's persistent requests for comments, and clarification of comments, on his work into Ricardian equivalence. While there is some uncertainty as to which Griziotti article Pareto commented on (Busino in Pareto 1975a, p.983), the letters' subject, their dates and Pareto's acknowledgement that the article is in the *Giornale degli Economisti* suggest that the paper in question is "La diversa pressione tributaria del prestito e dell'imposta" (Griziotti [1917] 1992).

Griziotti contested the then received view in Italy that Antonio De Viti de Marco ([1992] 1893) had not only proven Ricardo's proposition that public debt and supplementary taxation impose the same costs on current and future taxpayers who own capital, but extended the proposition to include wage and salary earners who do not own capital. A feature of

¹ Borgatta's contribution to Paretian fiscal sociology is not considered in this study because Pareto did not appear to correspond with him on the issue and because it would introduce distracting complexities associated with the evolution of Borgatta's fiscal studies, including the role of social equilibrium within such studies.

² These affiliations have been extracted from Ghessi (1997, 2002)

De Viti de Marco's analysis was his assumption of intergenerational continuity whereby the obligation to pay tax is an inherited liability in the same sense that family wealth can be an inherited asset. On this basis, future generations are reduced to the conceptual equivalent of the current generation, with parents not only bequeathing property and other assets to their children, but also debt related liabilities such as tax obligations.

Griziotti objected to the presumption of continuity on the grounds that it is at odds with obvious economic circumstances and, therefore, facilitates derivation of a theoretical outcome that does not approximate fact. These 'obvious economic circumstances' include demographic factors (the new generation only descends from a subset of the current generation) and the varying degrees of inter-jurisdictional mobility for different types of capital. Griziotti also recognised that changes in tax obligations are interdependent with changes in the distribution of income, and that in the case of wage earners without capital, a supplementary tax is more likely to reduce consumption by current generations than lead to an increase in private debt to pay the supplementary tax. Consequently, fiscal pressures on current and future generations must differ between an extraordinary tax and public debt for wage earning taxpayers. Furthermore, while fiscal equivalence can be axiomatically demonstrated for taxpayers who own personal property, commercial property or real estate, Griziotti argued that the restrictive assumptions ignore the political dimension to fiscal decisions, so equivalence would be rare.³

Griziotti's critique of De Viti de Marco reflects many of Pareto's methodological themes. In particular, he is critical of "mere inventions" that are divorced from reality, which echoes the Paretian relationship between fact and theory in the social sciences. However, if Griziotti was anticipating agreement from Pareto, he was soon to be disappointed. Pareto's first letter, written on 31 August 1917, notes that:

"Your work looks praiseworthy to me when the principles of the "science of finance" are accepted; and you cannot do otherwise if you do not wish to be against all your learned peers. But, note that I am a heretic among those believers; and some of the reasons for this can be found in my *Sociologia*" (Pareto 1975a p.983).

This comment does not reveal any recognition of Griziotti's deliberate differentiation of his views from the received view of Italian public finance. One may even suspect that Pareto drafted his first letter in haste without fully reflecting on the methodological basis underlying

³ For example, additional taxes to service debt may not equate to debt servicing costs, non-property owners are likely to be included in the tax base and, because of discontinuity and conflicting interests between groups in society, only a subset of the owners of real estate or commercial and personal property (or their children) will be liable for taxes.

Griziotti's work, particularly as, like Pareto, Griziotti differentiated fiscal decisions and consequences from that of market choice:

“... for some time now I have found myself increasingly at odds with the intellectual line of De Viti de Marco and the majority of academics, who interpret the question of public finance using economic criteria. In my opinion, public finance activity is essentially political in nature.

The allocation of the burden of public expenditures ... is nearly always a result of complex battles between the different classes of taxpayer. It does not, therefore, provide a solution to the problem of value, nor is it necessarily influenced by economic laws.” (Griziotti [1917] (1992) p.81).

However, in the course of the correspondence it becomes evident that while Pareto is, like Griziotti, concerned with mere inventions, his concern is not limited to the presumption of continuity, but to the entire notion of Ricardian equivalence and to much of public finance itself.

“I have never found a taxpayer who undertook Ricardo's calculations, or those of others similar. From this I conclude that its existence is like the Arab Phoenix. Facts show me that the metaphysical entity referred to as the State imposes all that it can on taxpayers and then spends it.” (Pareto 1975a p.983).

While both Pareto and Griziotti regard fiscal behaviour as something distinct from voluntary individual choice, Griziotti accepts Ricardian equivalence as an appropriate point of departure from the prevailing approach to fiscal studies, while Pareto preferred to ignore it as altogether irrelevant. Instead, his interest in fiscal matters concerned their impact on equilibrium, which Pareto considered as inadequately treated in public finance. Pareto's next letter (2 September 1917) stresses that it is not possible to compare the effects of loans with the corresponding effects of tax without first knowing how they respectively modify economic and social equilibrium in the present and in the future, and complains that:

“... the “science” of finance knows little of economic equilibrium and nothing of social equilibrium; therefore in place of an understanding of real effects it substitutes a presumption of imaginary effects.

... how would the use of economic goods have been altered if there were neither the loan nor the tax? I cannot concede that the economic state and the social state are not variously modified by various changes in the use of economic goods; but if we do not know the modifications in these states, how can we possibly compare them.” (Pareto [1917b] (1975) p.984).

social welfare and the ongoing struggle between political elites to maintain or acquire political power by indirect and cunning means (foxes) or by direct and confrontational means (lions). Fiscal redistribution that alters control of capital may be the result of interaction between economic and political actors, such as patron-client associations between speculators and foxes emphasizing individuals' rights and allocation of capital to risky activities, or between rentiers and lions emphasizing the State's rights and allocation of capital to low risk activities. The behavioural balance considers the incidence of conformist and non-conformist sentiment given the social norms prevailing across the collective. While this is affected by economic and political elites, the satisfaction that individuals experience from their behaviour is largely determined by their personality and sentiments. Consequently, individuals' innate propensity to behave in a conformist or non-conformist manner sets the basic parameters within which political and economic elites can effectively act to influence the conduct of the masses (with behaviour outside those parameters tending to destabilize the social equilibrium).

In this context, Pareto's second letter to Griziotti briefly suggests that the interdependencies that comprise social equilibrium simply cannot be ignored when political bodies introduce fiscal programs. However, the problem for Pareto was, although he appreciated that the partial nature of public finance theory could lead to misleading outcomes, he had no detailed general alternative to offer. The actual form of social equilibrium, both before and after the introduction of a new fiscal program, was simply beyond the scope of 'general' sociology because his theoretical exposition focused on broad regularities associated with the stability and instability of social equilibrium that can be observed across many forms of society. He could only advise Griziotti that "... at least I have the merit, like Socrates had, of knowing my own ignorance" (Pareto [1917b] (1975) p.984).

Nevertheless, in his third and final letter (5 October 1917), Pareto provided some indication of his starting point for studies of the relationship between public debt and taxes:

Debt is a way of making the population accept that which would not be acceptable through taxes, and this effect is so large that consideration of every other "pressure" is secondary and can be neglected." (Pareto [1917c] (1975) p.988-9).

While among Italian scholars this observation is not unique to Pareto,⁴ what is unique is the suggestion that it needs to be analysed from a 'sociological' perspective. In the same letter Pareto also indicated that the analytical categories utilised by Griziotti (land owners, capitalists workers etc) are a lot less important than the sociological classifications of human

⁴ Fasiani (1950, p271 and p278) argues that Pareto was wrong to look down at the scientific contributions of important figures in public finance because, among other things, Puviani had come to the same conclusion in his 1903 theory of fiscal illusion.

action in his *Sociologia* (which have regard to the distribution of human sentiments across elites and the broader community). Within this context, public debt is simply a means of appropriating or despoiling the wealth of some to benefit others. However, as Pareto stressed, there can be no *a-priori* expectation that such despoiling has a positive or negative impact on social welfare; it will depend on sentiments among the despoiled and benefited groups and the use that the benefited groups make of such resources.

Pareto and Sensini

In contrast to his relationship with Griziotti, Pareto actively encouraged Guido Sensini to undertake fiscal studies. As early as 1905, more than a decade before the publication of his *Sociologia* or his correspondence with Griziotti, Pareto advised Sensini to treat public finances in the context of non-logical action:

“You would do well to occupy yourself with the science of finances. In that field everything is yet to be done... The problem must be considered from two sides. One is that of pure science ...; the other is that of the synthesis, that is, the study of concrete phenomena to discover if there are any uniformities that can assist pure science. Do not be in a hurry. If you want, publish some monographs every now and then, but for the pure science, wait until your studies are well matured. The principle problem in all this is the need to construct the edifice completely a-new. *Scientific theory* will have little or no assistance from treatises on the “science” of the public finance that have been published to date. From the perspective of *scientific theory*, their best value is close to zero.

Take care to note that considering the taxpayer as an ophelimity maximising operator will only give part, very often a small part, of the phenomenon. The taxpayer is not aware of many of the effects of taxes, or fiscal measures more generally, so his actions are not of the logical type considered in economics, for which theory is less difficult; rather, they are of a non-logical type, for which theory is much more difficult.” (Pareto [1917d] 1975 p.958).

Pareto’s logical conduct concerns behaviour directed to achieve a given end, with: (i) the subjective purpose of the end conforming perfectly to the objective meaning of the end; and (ii) the means employed to achieve that end involving minimum effort/cost. Non-logical conduct is not illogical conduct; but the expected subjective benefits from obtaining an end may not be realised because such benefits are not necessarily independent of the means employed to realise the end. In modern terminology, preferences related to logical conduct are exogenous and path-independent, whereas preference related to non-logical conduct are endogenous and

path-dependent (see McLure 2001). In recognition of the endogenous and path-dependent nature of political processes, Pareto insisted that non-logical conduct should be considered within fiscal theory.

On 5 April 1917, five months before Pareto's letters to Griziotti, and in response to a letter in which Sensini advised that he is considering a book on public finance, Pareto reiterates essentially the same message:

“It appears to me that you would do well to publish ... a book on the science of public finances ... Until now the *science* of public finances is just a name; it has simply become the art of dressing up that which they wish to roast on a spit as food to be served to the dominators of the country. Those who judge the book that you want to write are adept in this art, and they will follow its principles in the judgement of your work” (Pareto [1917e] 1975 p.958).

A few months later, on the 3 September 1917, Pareto again confirmed his harsh judgment of progress within the discipline of public finance, although this time he emphasized the importance of social equilibrium to the study of fiscal matters:

“Our friend Griziotti insisted on knowing my opinion of his study on the pressure of debt or taxes; and in view of this I was forced to tell him that, it appears to me, ... such studies lack all foundation since one cannot build this without an understanding of the effects of a measure (in this case: tax or debt) on the economic equilibrium and on the social equilibrium.” (Pareto [1917f] 1975 p.985).

These letters appear to have encouraged Guido Sensini's interest in the specific question of Ricardian equivalence, and further encouraged his interest in the general scope of fiscal theory. Of particular importance is Sensini's “La teoria di Ricardo sui diversi effetti del prestito e dell'imposta” (Sensini 1920), which is critical of the Ricardian equivalence theorem on the grounds that it is only a ‘financial-mathematic’ equivalence. In addition to formalising the equivalence conditions⁵ and pointing out that these conditions are largely at odds with observed human behaviour, Sensini attempted to spell out the theoretically correct specification of the economic impact of debt and extraordinary taxes in a manner that derives directly from Pareto's concerns with fiscal theory.

Firstly, he suggested that the equations for static general economic equilibrium should be modified to include financial variables (taxes paid and public services received) so that static equations for general economic-financial equilibrium can be generated. The effect on

⁵ That is: the existence of a potent sentiment to provide inheritance for successive generations of descendants; the requirement that the value of goods inherited remain invariant across the centuries; the specification of the ordering associated with hereditary sequences; and the requirement that the rate of interest on savings to remain constant over time.

individual taxpayers (or given groups of taxpayers or all taxpayers) of funding extraordinary spending by ‘debt’ or by ‘extraordinary tax’ could then be calculated through comparative static analysis between the original equilibrium and a new equilibrium subsequent to a fiscal variation. The fundamental difficulty with Sensini’s recommended approach to economic-financial equilibrium concerns the valuation of economic goods when voluntary choice is directly and indirectly constrained by political/fiscal factors. While not explicitly raising this issue as a matter of concern, he nevertheless noted three constraints that prevent calculation of the economic consequences of fiscal decision. These are, an ignorance of: the actual equations of economic-financial equilibrium at a given point; the paths followed when moving from one point of equilibrium to another following a fiscal change; and the actual form of the functions that act within the equilibrium systems. Furthermore, Sensini highlighted that his discussion of economic-financial equilibrium, with all the associated unknowns, only provides a particular perspective on a more general issue. The most general treatment of the matter must consider the effects of an extraordinary tax and debt on social equilibrium. However, “given the current level of knowledge, it is impossible to find a general solution to that problem”. (Sensini 1920a p71).

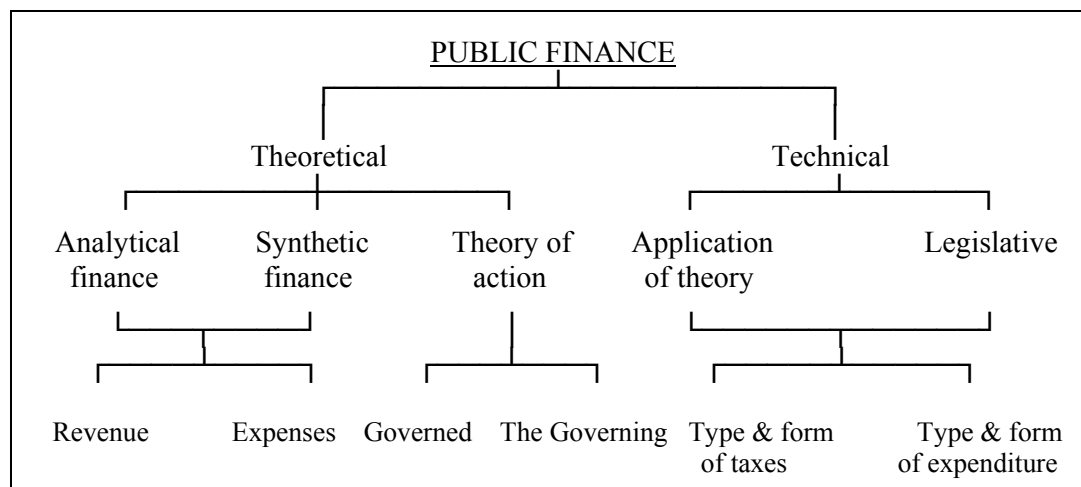
Consequently, the historical relevance of Sensini’s “La teoria di Ricardo ...” is mainly that it is a formal attempt to outline and clarify Pareto’s view on the relationship between fiscal phenomenon and economic equilibrium. It is also important for reiterating Pareto’s view on the importance of social equilibrium for a truly general understanding of fiscal phenomena, albeit without adding new insights into the relationship between fiscal activity and social equilibrium.

Sensini’s next major fiscal study, “Classificazione generale dei problemi principali della finanza” (Sensini 1920a), was a preliminary attempt at developing a methodological schema for examining the principle problems in public finance.

Given Sensini’s nomenclature lined in the table below, the theoretical aspect of public finance is purely Paretian. *Analytical finance* concerns the interdependence between economic and financial quantities (focusing on economic-financial equilibrium), *synthetic finance* is the name that Sensini assigns to ‘fiscal sociology’, re-named to emphasis the synthesis of a financial fact with economic, political, financial and psychological factors, and the *theory of action* covers Pareto’s theory of logical and non-logical conduct, with particular reference to the political process and the relationship between the governing elite and the governed. Sensini’s inclusion of technical public finance in his general classification also provides a bridge between the general theoretic expression of finance inspired by Pareto and the narrower approaches to the science of public finance and fiscal law being progressed by

more orthodox scholars in Italy. In regard to the practical application of fiscal theory, to determine the method and form by which governments raise funds and expend these funds on providing services, Sensini comments favourably on the work of Tangora, Einaudi and Floria – although he also emphasised the importance of non-logical actions, which had yet to be properly accounted for in fiscal theory.

Figure 2: Sensini’s Preliminary Classification of Public Finance



Source: Derived from “Quadro 1”: Sensini (1920a, p271)

Sensini’s “Classificazione generale dei problemi principali della finanza” was, therefore, an attempt to systematically identify the main issues in fiscal studies and the methodological basis for examining such issues. Interestingly, Pareto approved of, and even encouraged, this approach. In a letter to Sensini written shortly after the article was published, Pareto indicated that he read the article and noted that “you would do well to progress your studies along that path” (Pareto 1975g, p.1044).

While Sensini gave further consideration to the classification of fiscal studies (Sensini 1920b), his mature approach to fiscal studies did not emerge until the end of the decade in “Cenni di Finanza” (Sensini 1929). This reflected a long gestation period and several imperfect starts, with the article including a note that, among other things, the study replaces earlier works (including Sensini 1920a, and 1920b). This definitive framework for fiscal studies advances the Paretian approach by defining the two general problems for the theory of public finance as: determining income and expenses; and establishing the effects of income and expenses on social equilibrium.

In regard to the first point, Sensini continues to advocate use of Pareto’s theory of action when analysing the determination of governments’ income and expenses. That is, the mix of logic and non-logic is important in understanding the composition of public sector finances. In regard to the second point, five categories of fiscal effects on social equilibrium

are identified: (i) economic effects, whereby the incidence of particular initiatives on individuals and its effects on equilibrium are examined; (ii) economic prosperity effects, whereby the impact of fiscal phenomena on the prosperity of the collective is examined; (iii) financial effects, whereby the types and forms of fiscal instruments which characterise a State's budget are examined to establish their impact on the equilibrium balance of public accounts; (iv) political effects, whereby the impact of circulation of governing elites on public finances is examined; and (v) other effects, including the effect of psychological influences on behaviour and fiscal phenomena.

Therefore, Sensini (1929) attempts to enhance understanding of the effects of fiscal phenomena through five successive approximations, each of which is concerned with a particular or primary effect. While sociology is fundamental to the approach, particularly with respect to the study of economic prosperity effects, political effects and psychological effects, non-sociological public finance has also been included in the treatment of social equilibrium, particularly for the study of economic effects of fiscal phenomena (which Sensini considered the subject of 'pure finance') and also implicitly in the study of financial effects of fiscal policy (which, in effect, is an applied public finance of the relationship between revenue raising from, and expenditure among, the various classes in society and the implications for regularities in this relationship for public sector deficits or surpluses).

Sensini's development of fiscal studies can therefore be characterised as an attempt to maintain Pareto's notion of social equilibrium (which includes the notion of economic equilibrium) as the primary phenomenon in fiscal studies. However, unlike Pareto, he set about achieving this by embracing core theoretical elements developed within orthodox public finance theory, such as the incidence of fiscal activity.

3) Historical Significance

The historical significance of Pareto's influence on Benvenuto Griziotti and Guido Sensini vary considerably between the two authors. Griziotti, reflecting a critical appreciation of Pareto's methodology and sociology, went on to become one of the leading figures in Italian fiscal studies during the first half of the 20th Century. In stark contrast, Sensini has been criticised for undertaking fiscal studies which followed Pareto in blind faith⁶ (Fasiani 1950 p. 306) and did not enjoy the same level of influence in the field of fiscal studies that Griziotti achieved.

⁶ As Sensini attempted to integrate elements of the science of public finance, which Pareto had largely rejected, within the framework of social equilibrium, the claim that Sensini followed Pareto in blind faith is something of an exaggeration.

Griziotti on Pareto's Legacy: Fiscal Sociology as 'Fiscal Politics'

In his splendid “Alla Scuola di Vilfredo Pareto e Maffeo Pantaleoni” (Griziotti 1950), Griziotti reflected on the developments in Italian fiscal studies subsequent to his correspondence with Pareto. He conceded the legitimacy of Pareto’s desire for a renewal in public finance to take account of political and social consequences, as well as economic consequences. However, he also insisted that such a renewal had actually commenced prior to 1917 when Pareto wrote his letters, and that by the mid 20th Century the renewal was not only largely completed, but actually exceeded the positions indicated by Pareto on the subject. In this regard, Griziotti cites three streams of Italian fiscal studies – (i) the science of finance, (ii) the political economy of finance (such as anti-cyclical fiscal policy, public investment policy and policy on fiscal balances) and (iii) fiscal sociology (governing the interrelations between the state and social phenomena, partly studied through the history of social legislation).

However, while Griziotti considered fiscal sociology in Italy as falling within the scope of Pareto’s methodology, it did not adopt the scope of Pareto’s analysis or place broadly defined social equilibrium at the centre of analysis. That is, he suggested that Italian fiscal sociology developed from a critical appreciation of Pareto. In this regard:

“The scientific method learned at the school of Vilfredo Pareto has kept me from blindly following the Master in the study of fiscal sociology.” (Griziotti 1950 p.342)

While Pareto’s methodological focus on the relationship between fact and theory is clearly replicated in Griziotti’s approach to fiscal studies, he tailored his own approach around four central elements: the active subject (the state and its entities); the passive subject (individuals and legal entities); the objects (the means of fiscal operation)⁷; and fiscal programs (spending and revenue raising). In regard to the specific issues that Pareto raised in his sociological critique of Ricardian equivalence, Griziotti contends that the points Pareto raised were long period concerns. In support of this, he pointed to Pareto’s methodological proposition that uniformities endure for centuries (Griziotti 1950, p346). As many matters in public finance don’t concern uniformities that continue for centuries, the influence of sociological influences on fiscal studies, including interests, passions, sentiments and other things of interest to Pareto are considered with direct reference to fiscal programs and not with direct reference to Pareto’s broad notion of social equilibrium.

In effect, Griziotti’s use of “passive subject” and primary focus on “fiscal programs” implicitly assumes that the incidence of conformist and non-conformist conduct is stable

⁷ In addition to the economic and social functions of political choice, Griziotti insisted that the political aspects of the law, as manifest by the creation and operation of fiscal legislation, should be considered in fiscal studies.

across the collective and that governing elites do not act as forces for increased individual rights (to accommodate non-conformist conduct) or state rights (to enforce conformist conduct). Otherwise, social equilibrium is likely to become unstable and the issues raised by Pareto in his critique of Ricardian equivalence, which Griziotti set aside as long-term concerns, will again become significant. Consequently, Griziotti retained Pareto's methodological relationship between fact and theory, but abandoned the broad sociological focus on social equilibrium in favour of a narrower focus on fiscal programs and political opportunism and legislation. What Griziotti refers to as 'fiscal sociology' would be more precisely labelled if it were termed 'fiscal politics'.

Of course the similarities between Pareto's preferred approach and Griziotti's approach to fiscal studies should not be overlooked. Both acknowledged the political basis of fiscal decisions, the interaction between political and economic elites and the associated links between fiscal activity and changes in distribution and the influence of group interests. Griziotti did consider two of the main elements of Paretian social equilibrium: the economic equilibrium (although he focused on labour and owners of various types of capital rather than rentiers and speculators); and the political conduct (although he did not assign priority to the balance between individual and states rights). However, as Griziotti's approach is silent on the remaining major element of Paretian social equilibrium – the behavioural balance - there is a significant difference in scope between the two.

Celestino Arena also reflected on Italian fiscal sociology late in his career, and like Griziotti he rejected a fiscal sociology that focuses on social equilibrium. He rejected the view that problems in public finance should be studied using methods and objectives substantially different from those employed by economists because the focus on non-logical actions and social equilibrium yields vague and indeterminate results. Nevertheless, he saw a non-theoretical fiscal sociology as providing an historical perspective that provides useful insight that into the dynamic aspects of economic/financial equilibrium.

“The fact that the fiscal phenomenon is an aspect of the social and political forces of society and its equilibrium does not imply but that problems in public finance are exclusively, or essentially, sociological and that studies based on sociological methods and objectives far removed from those of the economist should be used. The primary motives of financial choice (such as non-logical actions... inspired from movements and contrasts between groups, their interests, feelings and illusions, abuses give to be able, actions of force, etc.) concerns the vague and indeterminate study of fiscal sociological, not fiscal economics.

The financial activity of public institutions has political and social as well as economic components which connect to the so called sociological equilibrium. Part of this equilibrium has economic value...[, and we must establish] the extent to which it is possible to isolate this more or less essential aspect from the political and social postulates that affect fiscal activity.

In this context, the historical elements of a fiscal sociology can be usefully placed as a research instrument for the most completed studies of dynamics, as this does not submerge logical research methods, necessary for economic science to be gradually modified, with the vague method of a 'sociology of finance' that has been vainly followed for too long." (Arena 1963, pp29-30)

Consequently, Arena accepts an even narrower scope for useful fiscal sociology than Griziotti, probably reflecting the diminution of interest in Italian fiscal sociology in the second half of the 20th Century.

An Assessment of Sensini's Ambitious Fiscal Theory

While Italian fiscal sociology generally developed along the lines suggested by Griziotti, with the associated tendency to move away from Pareto's broad focus on social equilibrium towards a narrower focus on political and legal influences, the historical significance of Sensini approach is two fold. First, counter to the prevailing developments in fiscal theory, Sensini continued to place prime importance on the Paretian focus on social equilibrium within the study of public finance. Second, he pursued his focus on social equilibrium without outright rejection of the 'pure' theory of public finance.

However, Sensini's contributions were not seminal moments, as they did not inspire other scholars to undertake fiscal studies which focus on the relationship between fiscal phenomena and social equilibrium. While this limited influence would be due to many factors, the most important factor concern the shortcomings of Sensini's work. In this regard, while the relationship between Pareto's economic and sociology is synthetic, the synthesis is not arbitrary. Sensini's main error, an error in synthesis, was that he did not take due regard to the empirical and theoretical consequences of the varying degree of determinism in Pareto's approach to equilibrium theory.

McLure (2001) reveals that the degree of determinism in Paretian theory varies depending on whether preferences are path-independent, as in the case of logical conduct where preferences are exogenous and conserved over time, or path-dependent, as in the case of non-logical conduct where preferences are endogenous and not conserved over time. In

summary, Pareto's pure economics is a formal study of equilibrium on the presumption that preferences are path-independent, with the degree of determination so high that an equilibrium point is in commodity space. However, the *Sociologia* is not constrained by assuming that conduct is logical, so utility is path-dependent and Pareto recognised that presenting social equilibrium as a point in commodity space would simply be a false determinism. To prevent theoretical false determinism, social equilibrium is only considered in a very general case: only the stability or instability of social movement and variations in the degree of centralisation in the main balances that comprise social equilibrium are examined. The actual form of such movements is not the study of general sociology, as such movements are path-dependent, but the subject of special sociology (i.e. applied studies of particular societies).

This explains why Pareto confessed to Griziotti that he could not see how to test the relative economic and social effects of tax and debt, as a focus on specific aspects of fiscal programs that incorporates sociology would require a greater degree of scientific determinism than Pareto's approach to social equilibrium could provide. However, this limitation should not prevent sociological studies of finance, but it does define the scope for undertaking such studies on a scientific basis. In particular, it means that fiscal phenomena being studied should, like the question of social equilibrium itself, be specified in a very general manner. Otherwise, a sociological investigation into specific fiscal programs will confront the same range of problems associated with path dependence and endogeneity which Pareto faced in his sociology and which he resolved by focussing on the substantive features of social equilibrium, and not the form that social equilibrium takes.

A Paretian fiscal sociology has the greatest prospect of success if it studies the substantive aspects of both fiscal phenomena and social equilibrium and their interrelationship. Since the substantive features of Pareto's sociology relate to the degree of social decentralisation and level of stability/instability of the social equilibrium, a general fiscal sociology can most profitably consider the relationship between: (i) the degree of fiscal decentralisation and the degree of decentralisation in economic, political and behavioural balances; and (ii) the level and stability/instability of fiscal activity and stability of social equilibrium.

While Sensini should be credited with developing a Paretian approach to fiscal sociology, his success was limited because he was unable to demonstrate to scholars that a focus on the relationship between fiscal programs and social equilibrium can add significant new scientific insights into fiscal phenomena. His synthesis was undertaken without systematically considering the implications of the low degree of determinism in social equilibrium when considering fiscal issues and, as a consequence, he was unable to highlight the potential scientific gains from a fiscal sociology that focused on social equilibrium. Essentially his ambitions for fiscal theory were too high given the level of development in economic, sociological and fiscal theory.

4) Current Relevance

As outlined in McLure (2003), there has been something of a revival in fiscal sociology in the last decade. In contrast to above assessment of Griziotti's and Sensini's relative historical significance, the Pareto-Sensini's approach to fiscal studies has the most relevance to this re-emerging fiscal sociology (McLure 2003). In this regard, not only have recent studies on fiscal sociology emphasised elements of Pareto's work that Sensini attempted to develop, these contributions have the potential for further development once the deficiencies noted in Section 3 have been addressed.

In a recent essay on "The Value of the History of Economic Thought", Ian Kerr (2001) notes a number of reasons why students and practitioners should read the history of economic thought. These reasons can be grouped into three broader categories: historical interest (intrinsic value, preservation of alternative paradigms, transcending fads and fashions and neglected holism⁸), educational merit (enrich understanding of the economics discipline) and current relevance (avoid errors of the past, unfulfilled evolutionary potential of previous works, expanding the range of hypotheses).

The potential for past methodologies and theories to scientifically influence current theories is likely to be very low in well-developed disciplines, especially when they have been developed with limited reference to other disciplines that consider related phenomena. At such a stage of development, aberrations in logic associated with the actual historical paths of scientific progress would have been redressed. In contrast, the potential for past methodologies and theories to influence new theories is somewhat greater when an a-historical rational presentation of the theory reveals: logical deficiencies; poor integration between theoretical concepts; and/or an inconsistent relationship between the methodological framework and the theory.

It is the contention of this study that many of the historical issues examined in Section 2 and 3 are of current relevance because modern fiscal sociology is not a well-developed sub-discipline. Using Kerr's schema, Italian intellectual history in this field enables us to: avoid errors of the past, fulfil the unfulfilled evolutionary potential of previous works, and expand the range of hypotheses.

⁸ Holism is used here to reflect "the full potential of system-wide theorising". However, students of Pareto will appreciate that system-wide analysis can also be achieved through synthetic successive approximations even when methodological individualism is given some prominence.

Avoiding Errors of the Past

The major ‘error’ to avoid is Pareto’s almost complete rejection of the science of public finance. Neither Sensini nor Griziotti agreed with Pareto on this matter, at least not when the economic and economic-financial aspects of fiscal studies are considered. A Paretian approach will shed more light on the relationship between fiscal phenomena and social equilibrium when it is complemented by the findings of public finance theory.

The extent of Pareto’s rejection of public finance – or the extent of Pareto’s ‘error’ – is disputed. Domenic da Empoli (1991) interprets Pareto’s comments as suggesting that he was essentially concerned with the use of public finance to develop arguments in support of particular normative goals. While there is no doubt that Pareto was seriously concerned about the use of public finance to rationalise normative goals, his letters to Griziotti and particularly Sensini strongly suggest that his concerns extended to the ‘scientific’ or positive foundations of public finance.

To correct this ‘error’, the fundamental features of Pareto’s relationship between ‘pure economics’ and ‘general sociology’ (as outlined in McLure 2001) can be extended to define the relationship between ‘public finance’ and ‘fiscal sociology’. That is, as a first approximation, the theory of public finance may consider the impact of fiscal phenomena on economic equilibrium on the assumption that preferences are path-independent and conserved over time, with fiscal sociology clarifying the consequent impact of path-dependent fiscal programs and the implications of this for economic and social equilibrium.⁹

This solution complements the propositions of Musgrave (1992), that fiscal sociology not only should address macro issues it should also recognise micro issues and the insights into micro issues provided by public finance theory, and Backhaus (2002), that fiscal sociology is a policy synthesis of disciplines like economics, including public finance, sociology, law etc. The sociological focus on path-dependence of preferences is also consistent with the constitutional approach to fiscal sociology advanced by Wagner (2002a, 2002b). Interestingly, Pareto and Wager have two different approaches to controlling the complexities associated with endogenous and path-dependent preferences. Pareto’s solution was to focus on general or substantive regularities that apply to all forms of society, so the actual path-dependent forms of particular political conduct were set aside as the subject of applied (or special) studies. In contrast, Wager adopts the approach to constitutional political economy where complexities associated with endogeneity can be adequately controlled by

⁹ To the extent that such analysis is related to a specific fiscal program, the analysis will necessarily reflect a partial equilibrium analysis. Given that this readily lends itself to Marshallian (and subsequently Pigovian) analytics, and bearing in mind Pareto’s hostility to Marshall and the representation of theoretical economics on a partial equilibrium basis, one can safely assume that Pareto would neither acknowledge his ‘error’ or accept the proposed solution to the error.

focusing on the rules defining the parameters of fiscal decisions, as such rules limit the possible range of forms that political conduct can take to desirable forms. That is, Pareto attempted to gain a ‘helicopter’ perspective on conduct by abstracting from problems of endogeneity, whereas Wagner is suggesting these problems can be controlled by a closer look at rules (governing decisions in fiscal and social institutions), subject to the *a priori* normative assumption that liberal governance is a goal.

Fulfilling the unfulfilled Evolutionary Potential of Previous Works

The issue of whether there is unfulfilled evolutionary potential from the Pareto-Griziotti and Pareto-Sensini letters and consequent works centres on the current relevance of social equilibrium to fiscal studies. If Griziotti and Arena were correct, there would be little or no potential benefit from reintroducing a fiscal sociology that focuses on social equilibrium. However, a benefit from focusing on social equilibrium can emerge if the theoretical shortcomings of Sensini’s approach to fiscal theory are addressed.

In Section 3, it is suggested that Sensini’s inability to demonstrate the benefits of fiscal studies that focus on social equilibrium was partly due to his focus on the form or detail of fiscal phenomena (rather than the basic substantive aspects of fiscal and social phenomena). A less ambitious fiscal sociology may well be more successful, particularly if it focuses on the degree of fiscal decentralisation and the level of fiscal activity, and considers how these substantive fiscal factors relate to the degree of decentralisation in economic, political and behavioural balances and to the stability of social equilibrium. This would be complemented by studies of the economic impact of particular fiscal instruments and/or specific fiscal programs using the conventional theory of public finance, provided that such studies are only used during periods of stable social equilibrium.

Furthermore, the enormous increase in fiscal documentation over the 20th Century means that it is possible to accurately address what Sensini calls the first general question in fiscal theory: establishing the mix of logical and non-logical fiscal decisions. Budget papers now link fiscal programs to performance criteria that are referenced to expected outcomes (Pareto’s subjective intent), outputs (Pareto’s objective end) and inputs. In particular, the same mix of inductive techniques that Pareto used in his examination of social doctrines to identify the constant and variable influences on human action¹⁰ can be used to identify constant and variable influences on the logic and non-logic of fiscal decisions.

¹⁰ Resulting in the theories of residues and derivations respectively.

Expanding the Range of Hypotheses

A potential hypothesis that emerges from a new approach inspired by Pareto and Sensini is that fiscal fundamentals are directly correlated with social fundamentals. A specific hypothesis requiring examination is that fiscal decentralisation is correlated with economic decentralisation, political decentralisation and behavioural balances biased in favour of non-conformist conduct. Complementary exploratory hypotheses could also be developed concerning the relationship between: instability of the social equilibrium and instability in fiscal phenomena; the stability/instability of social equilibrium and changes in the level of fiscal activity; and variations in the level, stability and decentralisation of fiscal phenomena relative to variations in each of the individual balances that comprise social equilibrium (i.e. the economic, political and behavioural balances).

5) Conclusion

The Pareto-Griziotti letters, the Pareto-Sensini letters, the reflection by Griziotti on Pareto's influence on fiscal sociology and Sensini's attempts to develop Paretian fiscal studies provide considerable insight into Pareto's influence on the development of fiscal sociology in Italy. The approach to fiscal studies endorsed by Griziotti, with public finance complemented by a fiscal sociology that considers the political and legislative aspects of fiscal phenomena, enjoyed wider acceptance than the largely Paretian approach developed by Sensini where fiscal theory considers the mix of logic and non-logic on fiscal decisions and their relationship with social equilibrium. As the taxonomy that Sensini employed did not adequately account for the varying degrees of determinism in economic and sociological approaches to fiscal phenomena, he was unable to contribute significant new findings on fiscal phenomena.

Nevertheless, the Pareto-Sensini approach is of considerable current relevance because the development of a fiscal sociology that considers the relationship between substantive fiscal issues and the elements of social equilibrium has unfulfilled evolutionary potential. In particular, there is considerable potential to develop a new fiscal sociology which establishes social laws on the relationship between fiscal decentralisation and social equilibrium, such as economic decentralisation, political decentralisation and behavioural balances biased in favour of non-conformist conduct.

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