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Regional Financing: Spanish Autonomous Communities versus German Länder

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Abstract

Spanish state decentralization is very similar to that in most important federal countries. In spite of advances in the regional financing system, the autonomy and financial sufficiency necessary to fund transferred competencies in Spanish autonomies have not been achieved.

From 1987 to the present, four different models of financing have been implemented. The last one was approved in 2001 and though it seemed to be successful, it is going to be remodelled shortly.

There are objective reasons to justify the system modification: evolution of public expenditure, immigration, and in general, society evolution. However, it is a political reason that has brought this change about. The latest proposal comes from the Cataluña government.

Some parts of the proposal are modelled on the German Länder financial system, especially the basket tax and the interregional solidarity system.

The aim of this research is to compare both the socioeconomic features in regions belonging to Germany and Spain as well as their financial systems in order to discover what the German system can contribute to an autonomous Spanish financing system. The reform proposed by the Cataluña government has also been studied with respect to its relationship to the German regional financing system.

I. Introduction

The financing system of German Länder is found to be of great interest for other regional governments, and, in particular, for Spanish regions, as is shown in the numerous studies to be found on the subject: Cantarero (2004), Utrilla and Herrero (2003), Giménez (2000), Martínez-Egaña (2000), Spahn (1997). In addition to these experts, other Spanish regional governments have also shown their interest in this financing system.

Since 1987, four different financing models have been applied in Spanish regions (autonomous communities-CCAA); the last of these was approved in the year 2001 and, although it seemed satisfactory at the time, a new reform is currently pending approval. Some objective reasons justifying this modification of the system are, for example, the evolution in public health spending, immigration and the general evolution of the population but, fundamentally, it has been a political reason that has laid this theme open to debate. The latest proposal for reform and regional financing has come from the Catalan government. Some of the points in the Catalan proposal take the financing system of the German Länder as a reference point, specifically the tax basket and the interregional solidarity system. The aim of our study is to compare the socio-economic characteristics of the regions in the two countries, as well as their financing systems. Although the latter has been dealt with by the experts already mentioned, we go on to compare the last proposal of the Catalan government and the agreement finally adopted between the central government and that of Cataluña. As far as the distribution of public expenditure is concerned, the decentralization of the Spanish state is very similar to that of most important federal countries. For example, the distribution of expenditure in Germany on a central, regional or intermediary and local level is the following: 63.5%, 20.5% y 16% respectively; the same distribution in Spain is 52% at the centralised level, 35% at regional level and 13% locally. However while noting the progress of the Spanish financing system, it has not given the Spanish CCAA the necessary autonomy and financial self-sufficiency to finance transferred competencies.

Our study is composed of the following parts:

The first compares Spanish regions (CCAA) to those of the German Länder, based on the most relevant socio-economic indicators. From this analysis conclusions are drawn about the degree of similarity between the regions of the two countries which directly or indirectly affect the rationale/justification of some of the aspects of the financing.

The second part describes Spanish CCAA financing systems and those of the German Länder, distinguishing between the financial resources that allow regions to have autonomy and those resources implicating the interregional level and the solidarity of each system.

The third part analyses the reforms proposed by the Catalan government, identifying their relationship with the German regional financing system.

The study concludes with an evaluation of the Catalan government proposals along with other conclusions about the possible application of the German system to Spanish regions.

II. Socio-economic comparison of German and Spanish regions

The comparison of the main socioeconomic data on the Länder and the CCAA lets us analyse which points Spanish and German regions have in common, and if, on the other hand, they are so different that it makes no sense to even compare their financial systems.

In table 1 there are data corresponding to the surface area and population of 16 Länder and 17 CCAA. The data on population is of great interest because public expenditure depends fundamentally on the number of inhabitants in each region. Moreover, the expenditure mentioned also depends, though to a lesser extent, on the surface area and, specifically, on the density of the population.

On the average, the Länder are more heavily populated than the CCAA. Furthermore the variation rate indicates that the differences between the Länder, in number of inhabitants (variation coefficient of 94.03), are greater than the differences of the population in the CCAA (variation coefficient of 84.84). Since the average territorial extension of the Länder is less than that of the CCAA, the population density is almost double that of the CCAA (1.7 times higher). These differences allow us to deduce, a priori, that there are greater expenses for the Länder and therefore greater financial needs as well, than for the Spanish CCAA, especially taking into account that the population is the principal variable affecting public expenditure, as previously indicated.

Table 1. Surface and population data of CCAA and Länder

LÄNDER	Surface (Km^2)	Population 2004 (thousands of people)	Inhabitants per Km^2	**CCAA**	Surface (Km^2)	Population 2004 (thousands of people)	Inhabitant per Km^2
Baden-Württemberg	35,751.64	10,717	300	Andalucía	87,591.00	7,687.52	87.77
Bayern	70,549.44	12,444	176	Aragón	47,698.00	1,249.58	26.20
Berlin	891.82	3,388	3,799	Asturias	10,604.00	1,073.76	101.26
Brandenburg	29,478.14	2,568	87	Baleares	4,992.00	955.04	191.32
Bremen	404.23	663	1.641	Canarias	7,447.00	1,915.54	257.22
Hamburg	755.24	1,735	2,297	Cantabria	5,253.00	554.78	105.61
Hessen	21,114.79	6,089	289	Castilla y León	93,814.00	2,493.92	26.58
Mecklenburg-Vorpommern	23,178.53	1,720	74	Castilla-La Mancha	79,409.00	1,848.88	23.28
Niedersachsen	47,619.63	8,001	168	Cataluña	32,091.00	6,813.32	212.31
Nordrhein-Westfalen	34,084.08	18,075	530	Valencia	23,254.00	4,543.30	195.38
Rheinland-Pfalz	19,853.48	4,061	205	Extremadura	41,634.00	1,075.29	25.83
Saarland	2,568.69	1,056	411	Galicia	29,574.00	2,750.98	93.02
Sachsen	18,414.70	4,296	233	Madrid	8,022.00	5,804.83	723.61
Sachsen-Anhalt	20,445.73	2,494	122	Murcia	11,313.00	1,294.69	114.44
Schleswig-Holstein	15,763.42	2,829	179	Navarra	9,801.00	584.73	59.66
Thüringen	16,172.08	2,355	146	País Vasco	7,089.00	2,115.28	298.39
				Rioja	5,028.00	293.55	58.38
Average (1)	22,315.35	5,155.69	285.44	Average (1)	31,538.38	2,690.94	162.52
Standard desviat.(2)	18,688.03	4,847.82	387.25	Standard desviat.(2)	30,453.38	2,282.52	169.81
Coeffic. Variac. (2/1)	83.75	94.03	135.66	Coeffic. Variac. (2/1)	96.56	84.82	104.49

Source: Federal Statistics Office and the Statistics Offices of the Länder and INE for CCAA and our own data

Table 2 holds the GDP percentage per capita of each region keeping in mind that the average of the European Union is 100. These data let us draw various conclusions. On one hand, the level of activity and development in the Länder is generally higher than that of the CCAA but, on the other, the differences between the Länder are greater than between the CCAA (the variation coefficient is ten points higher). However, these differences do not seem to lessen, at least in the period analysed from 2000-2002 but instead have actually increased, in both the Länder as well as the CCAA, although the coefficient of variation between the CCAA is lower in the year 2002 than in 2001. In the year 2002 the Länder whose GDP per capita was under 75% of the average in the EU, are: Brandenburg, Mecklenburg-Vorpommern, Sacasen, Sachsen-Anhalt and Thüringen, that is, the States of former East Germany, while the CCAA whose GDP per capita was under 75% of the EU average were Galicia, Extremadura and Andalucia.

Table 2. GDP per capita. Percentage on the average UE-25=100. Comparison Länder-CCAA

LÄNDER	2000	2001	2002	CCAA	2000	2001	2002
Baden-Württemberg	123.80	123.05	121.65	Galicia	72.7	72.6	74.7
Bayern	120.81	117.81	116.23	Asturias	78.3	78.9	80.7
Berlin	102.30	98.50	96.60	Cantabria	87.6	89.4	91.9
Brandenburg	75.30	73.70	73.20	Basque Country	113.8	114.5	117.1
Bremen	150.80	149.90	149.60	Navarra	115.4	116.1	119.6
Hamburg	190.40	188.80	187.80	La Rioja	105.3	105.3	106.7
Hessen	122.20	120.17	119.53	Aragón	97.3	97.8	101.7
Mecklenburg-Vorpommern	73.40	72.40	72.00	Madrid	122.8	124.4	126.7
Niedersachsen	100.53	97.60	95.85	Castilla y León	84.4	85.1	87.8
Nordrhein-Westfalen	110.40	108.20	106.32	Castilla-la Mancha	73.8	74.3	76
Rheinland-Pfalz	97.47	93.70	93.33	Extremadura	59.2	58.8	61.6
Saarland	103.00	103.40	103.30	Cataluña	110.1	110.1	112.3
Sachsen	74.73	73.53	73.53	Valenciana	87.7	88.4	90.7
Sachsen-Anhalt	71.53	70.70	71.20	Baleares	115.8	114.8	117.1
Schleswig-Holstein	102.90	100.90	99.00	Andalucía	68	68.6	71.1
Thüringen	73.80	72.80	72.70	Murcia	78.1	78.7	81.1
				Canarias	87.1	87	89

LÄNDER	2000	2001	2002	CCAA	2000	2001	2002
Average	105.84	104.07	103.24	Average	91.61	92.05	94.46
Standard deviation	31.93	31.88	31.64	Standard deviation	19.24	19.32	19.42
Coefficient variation	30.17	30.63	30.65	Coefficient. Variac.	21.00	20.99	20.56

Source: Eurostast and our own.

As far as the main budget data is concerned (Table 3), it is necessary to point out that these data do not permit a comparison between Länder and CCAA because the public services taken on by the CCAA are different than the expenditures the Länder are responsible for, and the financing systems themselves are also quite different. Moreover, in the case of the CCAA, two different systems of financing must be taken into account as well: the foral system applied in the Basque Country and Navarra, and the system of general or common financing applied in the rest of the regions.

In the general regime system, the State collects the principle tax revenues and later turns over part of these revenues to the CCAA. In the foral regime system, the process is reversed and it is the regions that collect the taxes and transfer a part over to the State, known as the quota that corresponds to the contribution of these communities to finance the expenditure that the State still renders in the Basque Country and Navarra. So the qualitative difference is very important, but not more so than the quantitative repercussions; while 90% of the revenues come from tax collection in the foral CCAA, in the regions of general regime this percentage only reaches an average of 70%. (See Table 2 of appendix.)

As far as the differences between public services assumed by the Länder and those by the CCAA, one must point out, for example, that the public health service in Germany corresponds to the Municipality, while in Spain the CCAA are in charge. Another important difference is related to the functions of social well-being, which are shared between the Länder and the Municipalities in Germany, while in Spain, many are still being covered by the central administration. These different competencies in certain areas, added to the differences in population in German regions as compared to Spanish ones, would explain the difference in expenditure between the Länder and the CCAA. Nonetheless, the data presented does not allow us to analyse the differences between the actual regions of the country.

The coefficient values of variation for income and public spending (under 100) indicate that the differences between the regions are not very great, except in the case of the CCAAs' debt, where there really are important variations; Cataluña, Valencia, Madrid and Andalucía are the regions with the highest debt. As far as smaller interregional differences in income go, interestingly enough, for both Länder as well as CCAA the income includes levelling transfers. That is why the data shows a variation coefficient under 100; this question is analysed in the following section. En cuanto a las menores diferencias interregionales en lo que a los ingresos se refiere, hay que indicar que, tanto en el caso de los Länder como en el de las CCAA, los ingresos, incluyen las transferencias de nivelación, de ahí, que los datos muestren un coeficiente de variación inferior a 100; esta cuestión es objeto de análisis en el siguiente apartado.

Table 3. Principle Budget Data. Comparison Länder- CCAA (millions of euros)

LÄNDER	Fiscal Revenue 2004 (1)	Expenditure 2004	Debt 2004	**CCAA**	Fiscal Revenue 2002	Expenditure 2002	Debt 2002
Baden-Württemberg	20,879	31,259	37,554	Andalucía	12,918.38	19,252.90	7,204.44
Bayern	24,751	34,249	21,24	Aragón	2,306.09	3,145.48	1,085.95
Berlin	11,321	20,526	53,876	Asturias	1,992.62	2,802.15	824.69
Brandenburg	7,152	9,504	16,397	Baleares	1,322.39	1,550.38	654.09
Bremen	2,102	4,228	11,27	Canarias	3,195.46	4,552.76	929.08
Hamburg	4,521	10,505	20,359	Cantabria	1,114.48	1,396.59	293.39
Hessen	11,857	17,926	28,617	Castilla y León	4,783.47	6,820.78	1,355.88
Mecklenburg-Vorpommern	4,952	6,96	10,283	Castilla-La Mancha	3,254.50	4,909.39	783.70
Niedersachsen	15,444	21,86	46,735	Cataluña	11,230.69	18,229.52	10,830.21
Nordrhein-Westfalen	34,974	48,101	102,494	Extremadura	2,172.56	3,181.93	782.49
Rheinland-Pfalz	8,126	11,65	23,242	Galicia	5,172.26	7,438.19	3,157.48
Saarland	2,442	3,236	7,371	Madrid	8,675.75	10,395.40	8,613.63
Sachsen	11,973	15,885	11,824	Murcia	1,897.04	2,502.76	684.36
Sachsen-Anhalt	7,167	10,097	18,006	Navarra	2,527.57	2,565.79	643.39
Schleswig-Holstein	5,555	7,933	19,594	País Vasco	5,786.01	6,035.79	1,351.83
ThÃ¼ringen	6,672	9,257	14,06	Rioja (La)	555.48	722.18	165.84
				Valencia	6,778.43	8,903.63	7,100.75
Average	10,582	15,481	26,054	Average	4,451.95	6,141.51	2,733.01
Standard Var.	8,941	12,306	23,899	Standard Var.	3,609.89	5,464.80	3,408.10
Coefficient Var.	84.50	79.49	91.73	Coeffic. Var.	81.09	88.98	124.70

(1) Incl. transfers and equalisation payments originating from the German Unity Fund, regionalisation funds (public short-distance passenger transport), supplementary federal grants and the Länder Government revenue-sharing scheme.

(2) Income corresponds to taxes and sufficiency funds, except for CCAA forals in which the data is of total income according to the budgets.

Source: Federal Statistical Office and the Statistics Offices of the Länder and IGAE for CCAA.

III. Regional Financing in Spain and Germany

The objective of this section is to briefly explain the financing of the regional governments in Spain and Germany, distinguishing between the resources that provide the regions with financial autonomy and the levelling instruments or solidarity of each system.

3.1. Autonomous financing

A) <u>Germany</u>

The system in Germany is based on the participation of different government levels in one single imposed system. There is a differentiation between revenues that are exclusive to each government level, and shared revenues. In the first case the payment of taxes is exclusively designated at the corresponding level of government, and in the following table 4 this distribution is described.

Table 4. Revenues pertaining exclusively to each German governmental level

Federation	Länder
- Fiscal monopolies and customs duties - Consumer taxes not attributable to the Länder (for example, sugar, salt, tobacco, coffee, alcohol, petrol) - Taxes on circulation of capital - Non-periodical taxes on Patrimony - Taxes on insurance policies	- Tax on Patrimony - Tax on Succession and Donations - Tax on Automobiles - Taxes on Property Transmission and Sale of Real Estate - Taxes on consumption not attributed to the Federation - Tax on Beer - Taxes on lotteries, betting and gambling establishments - Tax on fire protection

Source: our own.

With respect to normative capacity, the federal government has exclusive competence in the legislation of tariffs and fiscal monopolies (although the process of European integration has considerably reduced autonomy on these issues), and shares competence for remaining taxes whose collection corresponds partially or totally to the government. With respect to shared taxes, the Länder can only legislate if the federal government has not previously made use of its capacity to do so. In the Senate (*Bundesrat*) tributary norms are passed on shared taxes, which the Länder are not permitted to alter. In practice main taxes are centralised and federally regulated, the government setting the bases and imposing rates. Nonetheless, as A. Giménez Montero has indicated, while a priori it seems that the Länder have little tributary power, they become actually an indirect but significant power through representation in the Senate[1].

The administration of taxes is separate, each government level administering those taxes which it collects, although in the case of shared taxes, the management corresponds to the Länder as delegated by the federal government. There is a high degree of administrative coordination.

The taxes shared by the Federation and the Länder, as well as the percentages corresponding to each government level, are as follows (table 5); the main revenues are shared.

Table 5. Distribution of shared taxes in Germany

	Federation	Länder	Municipalities
Tax on personal income	42.5%	42.5%	15.0%
Tax on business societies	50.0%	50.0%	-
VAT	49.4%	48.4%	2.2%

Source: J. Lasarte and F. Adame, "La descentralización de ingresos tributarios en el derecho comparado", in V. Martínez-Pujalte (direct.), (2000), page 275.

The federal government and the Länder also share the Industrial Tax. The yield of direct taxes (income and business) corresponding to the Länder are seen as their own resources, and are set according to territorial tax collection, that is, adopting the form of territorial or *tax-sharing* participations where each Land receives a percentage of the collection of such taxes in its territory. With respect to the imposition of the VAT, the percentage corresponding to each government level has been modified on various occasions, like for example in 1992 when 65% corresponded to the federation while 35% fell to the Länder. In 1995 the percentages were 56% and 44% respectively and current percentages are shown in the table above. At the same time the VAT corresponding to the Länder is distributed among them in the following way: 75% is distributed in terms of the population and the remaining 25% following redistributive criteria, as will be seen further on.

Furthermore the Länder receive 20% of the revenues of the Tax on Economic Activities collected by the respective local governments.[2]

[1] A. Giménez Montero, (2000), page 9. The norm on taxes that depend totally or partially (shared taxes) on the Länder should count with the approval of the Senate, and this chamber has the right of veto on fiscal norms proposed by the federal government, which is, then, where the power of the Länder lies.
[2] The Tax on Economic Activities (TEA) corresponds to local governments, but since these obtain a 15% share of the Personal Income Tax, in exchange they transfer part of the TEA to the federal government and the Länder.

In order of importance, the taxes contributing the most resources to the Länder are: Personal Income Tax, the VAT tax, and the Tax on Company Revenues. The approximate percentage of these resources in the total tax income of the Länder is 84.7% and the rest corresponds to their own taxes, mainly the Tax on Motor Vehicles and the Tax on Patrimony.

B) Spain

In Spain the CCAA tax revenues come from the following sources: revenues generated by the CCAA themselves, revenues whose yield has been totally handed over by the central administration and those revenues which have been partially destined to the CCAA by the central government.

Table 6. Tax revenues of the CCAA

Tax revenues of the CCAA	- Tax on dumping refuse - Taxes on bingo - Tax on large commercial areas - Etc.
Revenues received from central government (100%)	- Patrimony - Succession and donations - Patrimonial transmission - Documented judicial acts - Gambling Taxes - Special tax on electricity - Tax on Vehicle Licenses - Tax on retail sales of hydrocarbons
Partially distributed taxes	- 33% Personal Income Tax - 35% VAT - 40% special taxes on: hydrocarbons, tobacco elaboration, beer, wine and fermented beverages, alcohol and alcohol derived drinks and related products

Source: of our own creation.

Observe the differences between the percentages of main revenues that are handed over to CCAA and the Länder: both the percentage of VAT as well as that of Personal Income. Tax rates are lower in the case of the Spanish CCAA. Moreover, these do not obtain any revenues from the Tax on Company Income, while the Länder receive 50% of this tribute. There are not only differences in the revenue percentages conceded, but also in the way in which the yield to be turned over is determined, as in the case of the VAT which is calculated according to a territorialized consumer index estimated by the Spanish National Statistics Institute while the Länder receive a distribution of 75% depending on the population and 25% according to distribution criteria, as already mentioned.

The CCAA are subject to regulation with respect to the revenues received, but this depends on the tax in question. The following table classifies the different types of taxes received, according to whether the pertinent regulations of the CCAA are extensive, limited or nonexistent.

Table 7. Extent of control over the revenues yielded

Extensive	- Patrimony - Succession and donation - Patrimonial transmission - Documented judicial acts - Gambling taxes
Limited	- Personal Income Tax - Tax on registration - Retail tax on the sale of hydrocarbons
Unregulated	- VAT - Special taxes on hydrocarbons,, tobacco elaboration, beer, wine and fermented beverages, alcohol and its derivative beverages and related products - Tax on electricity

Source: of our own creation.

Table 2 of the annex can analyse how important the different incoming revenues are for the CCAA at the closing of the budgets for the year 2002. Just as in the case of the Länder, the Personal Income Tax and the VAT are the revenues that most contribute to those of the CCAA; specifically in the year 2002, 55% of the incoming revenues corresponded to these two taxes. On average and according to data on the CCAA budget closing in 2002, the percentage of tax revenues in the total financing received by CCAA amounts to almost 70%,[3] and although this percentage represents considerable progress in autonomous financing in Spanish regions, it is still lower than that of the Länder.

3.2. Transfers, levelling system and solidarity

Intergovernmental transfers are necessary to compensate for the fiscal imbalances that have a double cause: a) the differences between the fiscal capacity of a subcentral level of government and its expense needs (vertical fiscal imbalances), and b) the differences between different subcentral government levels with respect to fiscal capacity or

[3] Nonetheless, there are important differences as far as the degree of auto-financing in the Spanish CCAA is concerned. For example, Baleares and Madrid finance 100% of their expenses with tax revenues, while in Extremadura and Canarias the degree of auto-financing does not reach 40%.

expense needs (horizontal fiscal imbalances)[4]. Other reasons are the need to coordinate economic politics, and the existence of external forces in acts of public service[5]; aside from these reasons, transfers are also the financial expression of the beginnings of solidarity. These transfers can be vertical, from the central government or federal for the regional governments, or horizontal, among regional governments themselves.

A) Germany

The German system is known for transfers of the two types indicated: those from the central government to the Länder and those among the Länder themselves. On the other hand it also distinguishes between unconditional transfers, whose objectives are stabling and distributive and conditional ones that are linked to concrete investments. Conditional or linked transfers are vertical, from the Federation to the Länder, and promote certain investments that contribute to stability and economic growth. There are three levelling mechanisms in Germany:

a) 75% of the distribution of VAT revenues pertaining to the Länder are with respect to population, and 25% have to do with guaranteeing the Länder who have less fiscal capacity a minimum fiscal income equivalent to 92% of every Land's average resources per capita

b) There is a zero sum fund whose objective is for all Länder to reach a minimum of 95% of total average resources. Contributions to this fund are made in the following way: taking 100 as an average of total resources, each Länder contributes to the fund whatever exceeds 100 according to the following criteria: the resources corresponding to the first two points over100 do not contribute, then 70% of the amount from 102 to 110 is contributed, and those resources more than ten points over these figures are all handed over[6]. With respect to the Länder who receive funds, if their financing capacity is less than 95% of the mean, they obtain income up to the said minimum limit, while those with an average capacity between 95% and 100% receive a compensation equivalent to 37% of this difference.

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[4] That is, vertical fiscal imbalance is a product of the financial capacity vs. the need for financial aid in one region, while horizontal imbalance is found comparing the capacity with the need for financial aid in different regions

[5] The fact that those benefiting from public spending at a subcentral government level are not only those residents of the area in question, justifies the central government's transfer of resources at said intermediate level for general use.

[6] This distribution of resources has a restriction and that is that the Länder that have to contribute to the poorest Länder can not finally have less than 95% of the average figure established.

The variables taken into account for the distribution of this zero sum fund are the capacity and fiscal need of each Land. The Länder contribute their excess of financial capacity to the fund according to their needs for financial aid, and the Länder that receive resources are those whose financial state is too low for what it needs. To calculate the rate of need, the number of inhabitants in each Land is taken into account considering the size and density of the population of the local communities in the Land.[7]. The indicator of fiscal capacity is the sum of the incomes that each Land gets from its own taxes and from those corresponding to local governments

In the year 2001 this fund handed out 8,173.76 million euros, the contributing Länder being Baden-Wurtemberg, Baviera, Hesse, Norte-Westfalia and Hamburgen while the rest of the Länder were the beneficiaries.

Asymmetric vertical subsidies from the federal government to the Länder can be, on occasion, of conditional or unconditional characteristics. In Germany, state projects adopted by the federal government and the Länder are usually co-financed. Subsidies are aimed to compensate for any remaining regional differences, in spite of the mechanisms already described, for example, in infrastructures. The finality of this type of vertical transfer is to achieve objectives with respect to stabilisation and regional development policies.

On the other hand, the system of transfers to East Germany which came into effect as part of the reunification process is also noteworthy. This issue is outside the limits of our study for which we recommend that the reader consult Spahn and others (1998); it is interesting to note that the integration of the Eastern States into the levelling mechanism previously described, especially the second, occurred gradually. The resources related to the so-called "Pact of Solidarity II", that insures transfers to federal Eastern states between the years 2005 and 2020, are 171,649.05 million euros.

B) Spain

In the CCAA financing system it must be pointed out that there are not such concrete levelling objectives as in the case of the Länder. The financing system establishes a "cut-off mechanism" in such a way that through the so-called "Self-Sufficiency Fund",

[7] It is accepted that the need for public spending increases with the size of a local community and the density of its population.

the CCAA receive an amount equivalent to the difference between their needs for expenditure and the resources obtained through the various revenues that they are financed with; in this way the system compensates for the differences between the fiscal capacity of each regional government and its spending needs.

Levelling is also implicit in the criteria used for distributing different funds that finance the services that are transferred to the CCAA. The system distinguishes between the financing of three blocks of public services: common services, Social Security health services, and social security services. The financing of each block of services is carried out with resources assigned to funds of a different nature, as can be seen in the following table 8.

Table 8. Financing system of the CCAA

BLOCKS	FUNDS	DISTRIBUTION CRITERIA
Financing common services	General Fund	94% Population 4.2% Surface 1.2% Dispersion 0,6% Insularity
	Funds for lower income CCAA	Distribution among CCAA whose GDP per capita are lower than the average GDP per capita
	Fund for the “density of population”	CCAA with a density under 27 inhabitants per km^2 and less than 50,000 km^2
Financing of health services of the SS	General Fund	75% protected population 24.5% population over 65% 0.5% Insularity
	Fund “Saving Program in Temporary Incapacity”	Distribution according to the protected population.
	Fund for “Displaced persons”	
Financing of social services of the SS		Population over 65 years of age-.

Source: of our own creation.

The Spanish levelling system is, moreover, more complex that that of Germany, because, in addition to what has already been explained, it establishes the maximum growth and the minimum growth obtained from each region, and this minimum differs according to the level of income per capita. The rate of variation in this income corresponding to an autonomous community cannot be over 75% of the average rate of variation in the whole CCAA group; on the other hand, the taxes of minimum variation in function of the level of income per capita are what are shown in table 9.

Table 9. Rate of growth of financing in common services

Level of income per capita	Guaranteed Minimum Growth
Income per capita is 70% less than average income	120% of the average rate of variation of the general CCAA group
Income per capita is between 70% and 75% of average income per capita	30% of the average rate of variation of the general CCAA group
Income per capita is between 75% and 82% of average income per capita	22% of the average variation rate of the general CCAA group

Source: CPFF Agreement on 27 July, 2001.

Observe that the system does not make the financing levels per capita equal for all the CCAA, since the initial distribution variables of the three funds include another type of variable besides the population. The minimum and maximum limits set with respect to the growth of the revenues does not insure reaching a concrete levelling objective either, like the one established in the German system, from which all Länder obtain at least 92% of the revenues per capita.

In addition to what has been presented, the Spanish system establishes some levelling allotments whose objective is to guarantee a minimum level in health and education services. When the protected population differs by more than three points from the average national total, the autonomic government will engage in a negotiating process with the central government to analyse the causes and determine the need for preparing an amount to compensate for this situation.[8].

Finally, just as in the German system, the federal government transfers resources to the States, in order to reduce differences in infrastructure and, in general, with characteristic goals of stabilisation and regional development policy, the same type of subsidies that also exist between the Spanish central government and the CCAA. The Fund of Interterritorial Compensation is the principle instrument in the regional development policy in Spain. It must also be pointed out that the CCAA beneficiaries are those who, in turn, belong to the 1st objective of European Union regional policy.

To sum up, the Spanish system does not establish a clear objective for levelling, although it introduces mechanisms to reduce the differences in financing that can exist among the CCAA due to the different financial resources in the system.

[8] In the case of education, the process is the same and the reference variable is the number of students in obligatory education in the autonomous community as compared to the national total.

IV. The proposal of the government of Cataluña and its relationship with the German system.

While we have been carrying out this study, the government of the autonomous community of Cataluña has reached an agreement with the central government about the reform of the autonomy statutes in this region as well as its financing. The aim of this part of the study is to analyse the financial proposals of the Catalan government and any possible relationship to the financing of the Länder, finalising with an exposition of the principal points agreed on by the Spanish government and the Catalan one about autonomic financing; what still is pending is how they are going to put these agreements into effect, especially those having to do with the levelling system.

The Catalan government's proposals referred as much to the amplification of basket taxes that Spanish regions currently count on, as to the system of levelling, or solidarity.

According to the government of Cataluña, the system of fiscal balance drawn up for Cataluña confirmed the need for a financing reform, since the contribution of Cataluña of those taxes paid by the residents of Cataluña to the state coffers is much greater than the benefits that they receive through state action; based on this supposition, they ask for the compensation contained in the statutes. Moreover, the Catalan government based its case on the Sentence of Nov 11, 1999 from the German Constitutional Tribunal, which backed the rights of the richest Länder (and therefore net resource contributors in the German levelling system) since it indicated that solidarity can not be limited, nor lead to excessive redistributing results. In other words, the benefiting states (net receptors of the funds) cannot end up receiving money that makes them exceed the average.

As far as income from taxes are concerned, according to the content of the reform proposal in the autonomic state of Cataluña, this regional government would obtain the income from all the state taxes paid in Cataluña, and would transfer 50% to the central government. Moreover, it would have the power to pass rulings on and also have fiscal responsibility for each and every one of the above-mentioned taxes, which would be under the control of the Tributary Agency of Cataluña with respect to management, collection, payment and the inspection of all state tax revenues.

With respect to the levelling system, the project for the reform of the Catalan Statutes sets certain general criteria to control the levelling and solidarity mechanisms between

Cataluña and the rest of the CCAA; these criteria, which are mentioned hereafter, are reasonable, especially as far as the first two are concerned: a) the contribution to a solidarity that has to guarantee levels of services corresponding to the amount of fiscal aid contributed ; b) the greater fiscal effort made in Cataluña (calculated from the taxes paid that were over the average in the Autonomic Community), has to translate into more income for the Generalitat; c) the application of the levelling mechanisms cannot end up altering the ranking of the per capita income among the autonomous communities. However, when levelling transfers have to be confirmed, the proposal of the Catalan government links these transfers to the differences that exist in the fiscal balance results.

The fiscal balance in a region is calculated as the difference between the public expenditure in a region and the total tax revenues paid by the residents in said region. The analysis of fiscal balance and the methodological variations that can be found in its elaboration, are outside the realm of this study, but to take an example – we can indicate that the fiscal balance that Cataluña has calculated shows that the most unfavourable fiscal balance ascended to -6,217 million euros (-7% of the Gross Domestic Product in Cataluña), while the most favourable was 294.4 million euros (0.03% of the GDP in Cataluña. From our point of view, this is not an argument that justifies a change in the levelling system; maintaining a zero fiscal balance would mean, for example, destroying the progressiveness of the fiscal system, and thus the policy of personal distribution, which is different than the policy of regional development. Moreover, this analysis must also take into account the amount of commercial balance between the region and the rest of the CCAA. For Cataluña this balance is positive, which results in greater income for the region and, therefore, indirectly for the amount of fiscal balance as well.

With respect to the sentence pronounced by the German Constitutional Tribunal, it is also an invalid argument because the German system of levelling is different from that in Spain. As a result of the mechanism described in the second epigraph of this study, some Länder are net contributors and others net recipients. And although it is also true that the Sentence previously cited resulted in a lower contribution from the richest Länder, it must be kept in mind that the contribution comes from the resources of the total financing obtained by each Land, and not from the revenues that the federal government receives from the citizens of the region, which would be the concept on which fiscal balances are built.

As has been mentioned above, the principle of solidarity can be implemented in two ways: a) through the existence of financial currents among the regions through a zero sum fund (horizontal solidarity), and b) through transfers of resources from the central or federal government to the regional governments (vertical solidarity). As the German system responds to the first type, while the Spanish one corresponds to the second, this explains why they really cannot be compared on the same basis.

The agreement reached by the central and the Catalan governments does not specify how the levelling transfers are to be carried out, and only center on the general principles, which practically coincide with those found in the Statute proposal. In the first place, the concept of solidarity is defined in exactly the same way as expressed in the Statute project: a level of services similar to the fiscal effort expended. In the second place, the levelling mechanism is to guarantee this objective (of levels similar to services) exclusively in the basic services of education, health and those social services essential for the welfare of the state. In the third place, the calculation of the needs professed by these services have to take into account, in addition to the population, a series of indicators (like differential costs, immigration and others) that, in the case of Cataluña, are of special importance. In the fourth place, the principle that guarantees that the greater fiscal effort made in Cataluña (calculated from the taxes paid over and above the average amount) has to translate into a higher income for the Generalitat, is also reflected in the agreement.

Finally, in fifth place, the final agreement maintains that the central government will guarantee that the application of levelling mechanisms should in no case alter the position of Cataluña in the CCAA ranking of income per capita.

FINAL CONSIDERATIONS

With respect to autonomous financing, the regional German financing system differs from the Spanish one, but not substantially. So, if we look at the main taxes we find that:

The Personal Income Tax in Germany is shared by the Länder and the federal government, the same as in Spain, although the current percentage received by the Länder (42.5%) is higher than that of the CCAA (33%). The share received by the CCAA could foreseeably go up to 50% after an agreement is reached between the central administration and the autonomous community of Cataluña. In the case of

Germany, this tribute is of federal ruling and the Länder have no power to alter it because it is the Federation's responsibility, although the Länder do have quite a bit of control over shared revenues and can veto fiscal legislation in the *Bundesrat*, (the Chamber of State Representatives, equivalent to the Spanish senate). The CCAA have a very limited control over Personal Income Tax (tax rate and deductions).

The Tax on Companies in Germany is shared; like the Personal Income Tax, it adopts the form of territorial participation, and the corresponding tax collection corresponding to the Länder is seen as one of their own resources. It is a federally ruled tax. Although the Catalan government proposed a distribution of 50% of this tax for each level of government (central and autonomous), this will actually not occur because in Spain the collection of these revenues is well enforced in only a few regions. Handing over its yield would give rise to great financial and autonomous differences between the Spanish regions.

The VAT in Germany is a shared tax, although the amount corresponding to each Land does not coincide with what is collected in the territory, but is rather a part received in function of the population while the rest follows distribution criteria. In Spain the percentage given over to this tax is currently less than that of the Länder although it will increase. As this is a tax recognised all over the European Union, the regions have no power to rule on them.

In general the degree of autonomy of the Länder is greater than that of CCAA , but if the agreement between the central government and that of Cataluña includes all the Spanish regions (all except the Basque country and Navarra which finance themselves through another method.), the financial autonomy of the CCAA could reach and even overtake that of the Länder. In Germany the Länder manage and collect all their shared revenues, while in Spain this is carried out by the State Tax Administration Agency (AEAT), but it is also foreseeable, according to the agreement between the State and Cataluña, that the CCAA could establish their own Tax Agencies that would manage and collect the shared taxes. The analysis of the advantages and drawbacks of this question would deserve a study of its own.

With respect to the levelling system, from our point of view the German system of transferring is more interesting, for two main reasons: a) there are not only transfers from the central government to the Länder but also within the Länder group from one to another; b) the levelling objectives are clearly defined (each Land must reach at least

95% of the total average Länder resources, and 92% of the average tax revenues per capita). There is no doubt that the effectiveness (and probably the efficiency too) of the transfer system is greater when levelling objectives are specified or quantified. This issue is independent of whether, on the other hand, it is considered that there is too much (or too little) levelling (solidarity); this last point could be resolved by fixing other objectives. With respect to its comparison to the proposal from the Catalan government, attention must be drawn to the fact that while this is based on the comparison of the fiscal balance results in order to set the limits of levelling, in the German system these results are not the starting point. Instead what is compared are the total revenues obtained by each Land, which is why, from our point of view, the 1999 Sentence of the German Constitutional Tribunal is not a valid argument to overhaul the Spanish levelling system and neither is the argument about the amount of fiscal balance, for the reasons indicated above.

The heart of the problem is that two types of CCAA exist in Spain along with two different autonomic financing systems: the foral communities in two of the regions and the CCAA in the general regime. The foral system affords the Basque Country and Navarra with greater financial independence because these regions themselves collect the taxes while the rest of the autonomous regions pay the taxes directly to the federal government which then distributes the same taxes back to them. This privilege of foral financing is of historic origin and is recognised by the Spanish Constitution. The general system of financing is beginning to approximate the foral system, but it still has a long way to go, which is why some CCAA aspire to achieve a similar system.

The application of the foral system of financing to the rest of the CCAA has also been a topic of study and researchers coincide in the conclusion that the foral system is not applicable to the rest of the CCAA for the following reasons:

- Some CCAA do not reach a high enough financial level to cover the cost of the services transferred (for example, Extremadura)
- The State has too few resources to finance the services not transferred to the CCAA, and yet it would have to continue assuming them. Moreover the CCAA that would benefit the most would be those with the greatest socioeconomic development.

- There are several reports by Spanish experts about a simulation of the results that could be obtained by the CCAA if a Länder-type financing system were applied, for example, Cantarero (2004) and Herrero and Utrilla (2002). All coincided in thinking that Cataluña would obtain better resources. However, the Catalan proposals are not trying to imitate the German system (characterised by its high degree of cooperation and coordination between the States and the Federation) but instead are aimed at a CCAA financing system at state-level in Spain (Basque Country and Navarra), based on a bilateral relationship. Moreover when the Catalan proposals are analysed in depth, they seem to be more like those of a Confederate State than a Federal one.

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APPENDIX

Table 1. Gross domestic product (GDP), market prices (millions of euros**)**

LÄNDER	2000	2001	2002	CCAA	2000	2001	2002
Baden-Württemberg	293,947.20	306,205.50	311,980.00	Galicia	32,932.90	34,849.00	37,175.50
Bayern	352,993.50	359,636.60	366,760.00	Asturias	13,765.20	14,611.90	15,423.00
Berlin	76,359.30	76,455.50	76,991.30	Cantabria	7,726.70	8,340.80	8,883.70
Brandenburg	43,474.50	44,055.80	44,617.30	Pais Vasco	39,213.00	41,723.90	44,182.60
Bremen	22,007.50	22,685.10	23,212.80	Navarra	10,355.90	11,060.50	11,844.20
Hamburg	71,844.50	74,473.10	76,267.30	La Rioja	4,653.10	4,953.20	5,226.30
Hessen	183,496.10	188,166.80	191,739.80	Aragón	18,970.70	20,110.50	21,613.90
Mecklenburg-Vorpommern	28,892.20	29,321.70	29,638.40	Madrid	105,523.30	114,319.90	121,664.60
Niedersachsen	176,498.40	178,477.00	180,294.70	Castilla y León	34,760.40	36,948.30	39,324.00
Nordrhein-Westfalen	448,820.30	458,125.30	463,364.60	Castilla-la Mancha	21,104.20	22,524.40	23,955.00
Rheinland-Pfalz	89,643.00	89,556.30	91,619.50	Extremadura	10,610.60	11,164.50	12,124.10
Saarland	24,304.20	25,304.20	25,873.20	Cataluña	113,356.20	120,666.70	128,079.10
Sacasen	72,801.70	73,845.00	75,203.40	Valencia	59,138.80	63,756.70	68,361.40
Sacasen-Anhalt	42,025.20	42,616.40	43,328.50	Illes Balears	15,254.70	16,389.60	17,662.10
Schleswig-Holstein	63,141.20	64,658.30	65,360.20	Andalucia	82,151.40	88,105.70	95,060.00
Thüringen	39,751.10	40,417.50	41,049.00	Murcia	14,656.40	15,811.30	17,043.90
				Canarias	24,543.10	26,618.80	28,829.60
Average	126,874.99	75,250.82	80,365.44	Average	35,806.86	38,350.34	40,967.82
Standard Desv.	130,429.17	133,628.52	135,642.35	Standard Desv.	34,105.68	36,630.22	39,027.65
Coefficient Varc.	102.80	177.58	168.78	Coefficient Var.	95.25	95.51	95.26

Source: Eurostat.

Table 2. CCAA Tax Revenue. Importance of the revenue and degree of financial autonomy (millions of euros 2002)

CCAA	Traditional Tax Revenues [1]	Personal income tax	VAT	Special Taxes	IEDMT + IVMDH [2]	RATES	Own taxes and Surcharge	TOTAL REVENUE	TOTAL FINANCING	DEGREE OF FINANCIAL AUTONOMY
Andalucía	1,534.2	1,750.1	2,221.2	1,190.6	306.3	156.3	27.2	7,185.9	12,918.38	55.63%
Aragón	381.2	493.0	433.1	258.2	61	22.8	1.9	1,651.2	2,306.09	71.60%
Asturias	222.2	390.3	392.6	180.1	42.4	27.5	34.6	1,289.7	1,992.62	64.72%
Baleares	362.1	361.1	661.8	232.9	50.7	13.8	42	1,724.4	1,322.39 [3]	130.40%
Canarias	384.0	522.1	0.0	44.4	0	26.9	225.5	1,202.9	3,195.46	37.64%
Cantabria	156.2	196.4	196.3	105.9	25.7	9.7	1.8	692.0	1,114.48	62.09%
Castilla León	563.8	750.3	795.5	504.2	120.6	62.9		2,797.3	4,783.48	58.48%
Castilla-La Mancha	310.4	398.5	474.6	392.7	88.8	33.1	10.7	1,708.8	3,254.50	52.51%
Cataluña	2,569.9	3,330.4	2,493.6	1,308.8	366.7	92.2	190	10,351.6	11,230.69	92.17%
Extremadura	121.3	193.8	280.5	166.0	35.7	20.2	30.6	848.1	2,172.56	39.04%
Galicia	482.9	746.4	848.8	450.5	109.5	50.7	29.2	2,718.0	5,172.26	52.55%
Madrid	2,673.2	3,556.3	2,227.7	915.2	429.3	117.2	79.6	9,998.5	8,675.75 [3]	115.25%
Murcia	268.6	298.9	357.8	243.5	64.3	12.2	4.2	1,249.5	1,897.04	65.87%
Rioja	94.8	105.0	93.8	53.0	13	3.5	5.3	368.4	555.48	66.32%
Valencia	1,440.1	1,405.6	1,442.1	828.2	228.1	48.2	22.2	5,414.5	6,778.431	79.88%
Average percentage of all taxes	22.20%	28.25%	26.80%	15.12%	3.76%	1.56%	2.32%	100%	Average degree of financial autonomy	69.61%

(1) I. Patrimony+I. Succession y Donations+I. Patrimony transmissions and AJD+Taxes on gambling

(2) Special tax for transport and taxes on retail sales of hydrocarbons. Source: IGAE

Source: IGAE and of our own creation.