

Reform of Fiscal Equalization and Functional Allocation in Switzerland

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Program

1. Swiss Federalism
2. Reform of Fiscal Equalization and Task Allocation between the Confederation and the Cantons
3. Reform of Fiscal Equalization and Functional Allocation in the Canton of Lucerne
4. Reform Process

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1. Swiss Federalism

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Federal form of government is guaranteed in the Constitution

Art. 1 The Swiss Confederation

The People and the Cantons of Zurich, Bern, Lucerne, ... Geneva, and Jura form the Swiss Confederation.

Art. 3 Cantons

The Cantons are sovereign except to the extent that their sovereignty is limited by the Federal Constitution. They exercise all rights that are not vested in the Confederation.

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Examples for functional allocation

- *Confederation:*
 - External affairs
 - Military defence
 - Regulation of financial markets, telecommunication, postal services
 - ...
- *Cantons:*
 - Social welfare
 - Hospital services
 - Primary and secondary education
 - ...
- Municipalities: according to Cantonal constitutions

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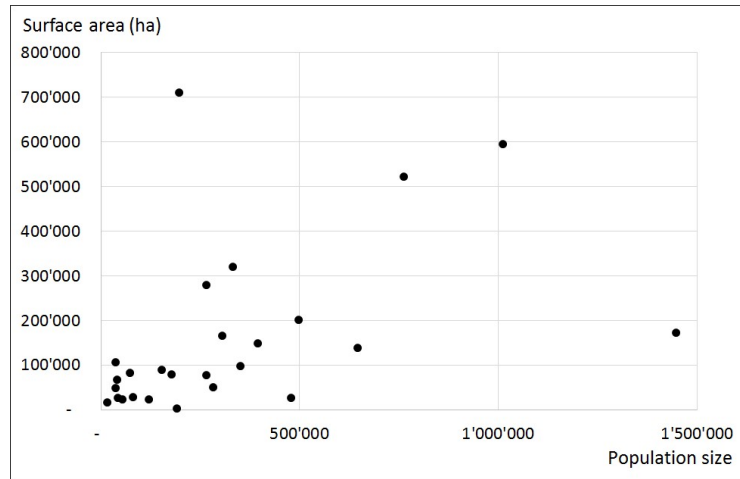
Federal structure of Switzerland

- Three levels of government:
 - Confederation
 - 26 Cantons (20 so called "full cantons", and 6 so called "half-cantons")
 - 2353 Municipalities (Jan. 1 2014)
- Well established and institutionalized inter-cantonal and inter-municipal cooperation
- Very intensive vertical cooperation between Confederation and Cantons, and between Cantons and Municipalities

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2.4 Large disparities between Cantons with respect to population size and surface area



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Main Features of Swiss Democracy

- Combination between parliamentary and direct democracy on the Federal and Cantonal level
- Constitution guarantees fundamental rights (equality before the law, right to life and personal freedom, right to privacy, etc.)
- Separation of legislative, executive and judicial power.
- Concordance systems on all levels of government:
The executives are usually composed of representatives of all major political parties
- Parliaments and membership is organized according to the "militia principle". Work is only part time and compensation does not correspond to a full time job.
- Direct democracy includes the right of launching popular initiatives and the right of referendum against laws adopted by parliament.

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2. Reform of Fiscal Equalization and Task Allocation between the Confederation and the Cantons of 2008 (NFA)

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2.1. Reform Process

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Growing Need for Reform in the 90s



Functional allocation:
Entanglement and
duplications

Creeping power shift to the
Central Government



In-effective and in-
transparent fiscal
equalization system



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Preliminary Analysis and Consultations

- 1991 Federal Finance Administration identifies the growing need for reforms
- 1994 Federal government installs a project organization (joint commission federal government / cantons)
- 1996 Consultation of a first report including the basic intentions
- 1999 Consultation of a second report with concretizations of the basis intentions

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Technical and Political Process

- 2003 Parliament adopts amendments to the constitution and a new law on fiscal equalization.
- 2004 Popular vote on constitutional changes
- 2006 Parliament adopts the adjustment of 33 existing laws.
- 2007 Decision in parliament about the funding of the new fiscal equalization system.
- 2008 The reform comes into effect.

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2.2. Basic Elements

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New in the Consitution: The Principle of Subsidiarity

Swiss Constitution Article 5a

The principle of subsidiarity must be observed in the allocation and performance of state tasks.

Swiss Constitution Article 43a, paragraph 1

The Confederation only assumes the tasks that exceed the power of the cantons or require uniform regulation by the Confederation

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New in the Constitution: The Principle of Fiscal Equivalence

Swiss Constitution, Article 43a paragraph 2:

The community, in which the benefits of a state service accrues, bears their costs.

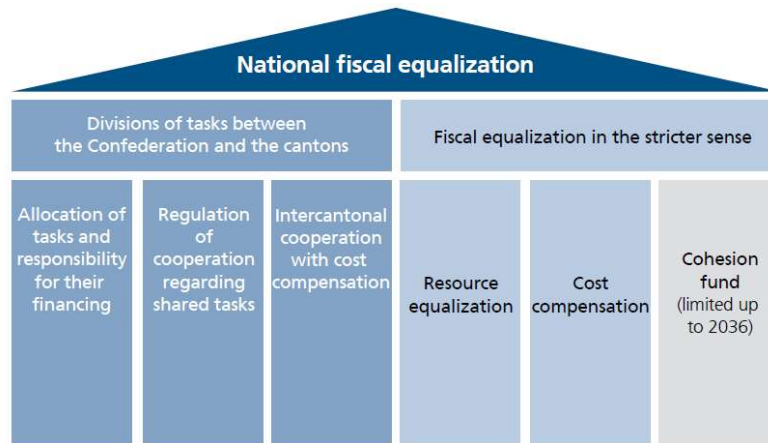
Swiss Constitution, Article 43a paragraph 3:

The community, which bears the cost of a state service, can decide over this service

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The Main Elements of the Reform



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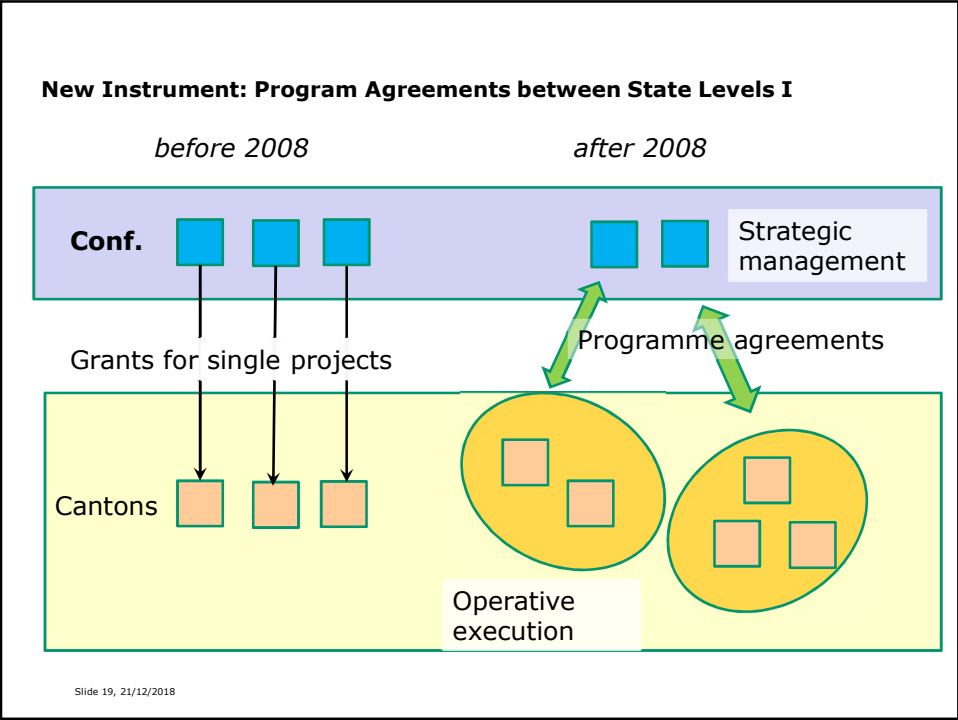
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Disentanglement of Tasks

- With the reform project, 17 of a total of 33 former shared tasks were disentangled.
- The Confederation is now solely responsible for seven task areas (e.g. motorways, AHV and disability pensions)
- The cantons are solely responsible for ten (e.g. construction and operating contributions to residential homes, workshops and day care centers within the scope of disability insurance).
- The Confederation and cantons continue to assume joint responsibility for 16 task areas.

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New Instrument: Program Agreements between State Levels II

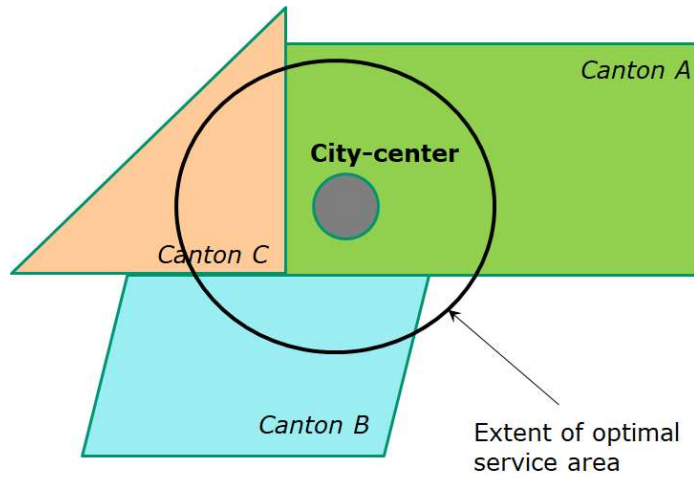
Swiss Constitution Art. 46: Implementation of federal law

- ¹ The cantons implement federal law in accordance with the constitution and the law.
- ² The Confederation and the cantons can agree that the cantons achieve certain objectives in the implementation of federal law and, for this purpose, implement programs that the Confederation financially supports.
- ³ The Confederation shall grant the cantons as much freedom as possible and take account of cantonal peculiarities.

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Horizontal Collaboration I



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Horizontal Collaboration II

Swiss Constitution: Article 48a

At the request of interested cantons, the Confederation may declare inter-cantonal agreements generally binding or oblige cantons to participate in inter-cantonal agreements in the following areas of responsibility:

- a. Execution of sentences and measures;
- b. Education with regard to the areas referred to in Article 62;
- c. Cantonal universities;
- d. Cultural institutions of supraregional importance;
- e. Waste management;
- f. Wastewater treatment;
- g. Urban transport;
- h. Top medical and specialty clinics;
- i. Institutions for the integration and care of invalids.

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Fiscal Equalization

Article 135

¹ The Confederation shall issue regulations on the appropriate resource equalization and cost compensation between the Confederation and the cantons as well as between the cantons.

² Resource equalization and cost compensation shall in particular:

- a. reduce the differences in financial capacity between the cantons;
- b. guarantee the cantons minimum financial resources;
- c. compensate the excessive cost of the cantons on the basis of their geographical, topographical or socio-demographic conditions;
- d. promote inter-cantonal cooperation with cost compensation;
- e. preserve the tax competitiveness of the cantons at national and international levels.

³ Financial resources for resource equalization are provided by the cantons with above average fiscal capacity and the federal government. The amount of the cantons with above average fiscal capacity amount to at least two-thirds and at most 80 per cent of the amount provided by the federal government.

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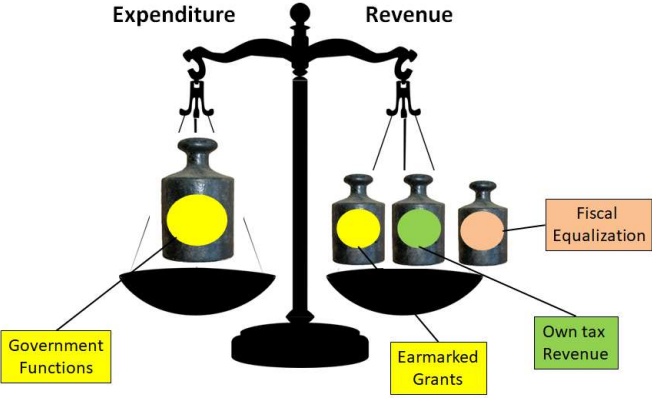
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2.3 The "Global Balance"

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Overall Objective: Balanced Allocation of Revenue for Financing Net-Expenditure on the National and Cantonal Level



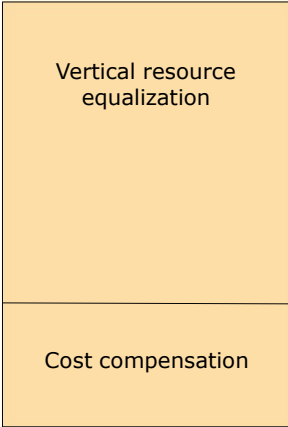
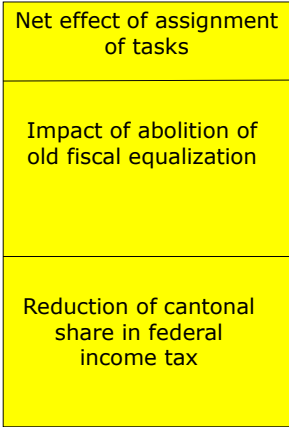
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Structure of the Global Balance

Decrease in net expenditure of the Confederation = Increase in net expenditure of the cantons

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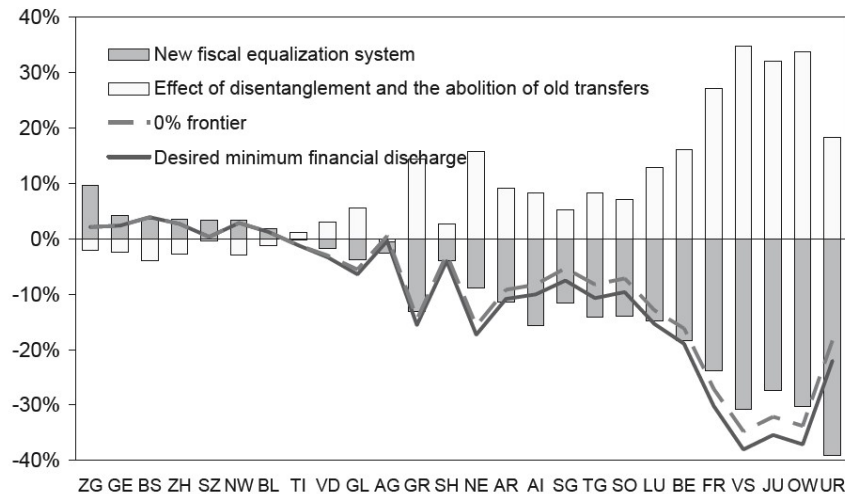


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Net Effects for Cantons

Net expenditure in percent of standardized tax revenue

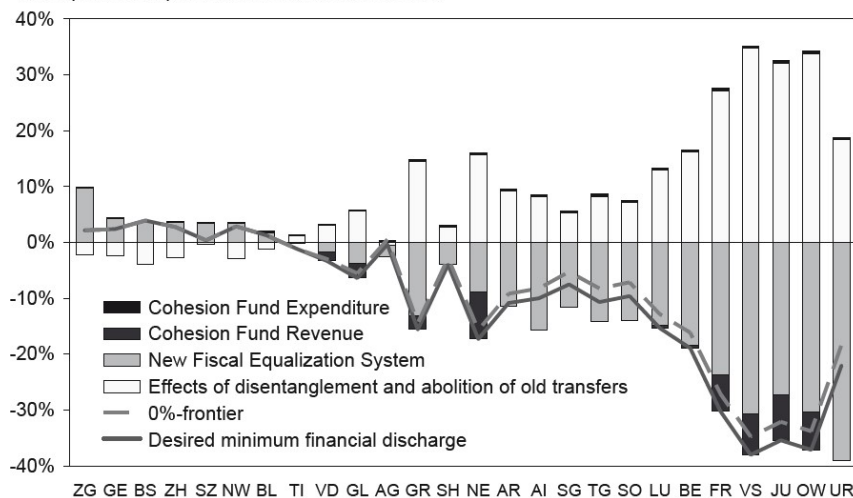


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Cohesion Fund: Temporary Guarantee of A Minimum Financial Discharge for Cantons with Below Average Fiscal Capacity

Net expenditure in percent of standardized tax revenue



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3. Reform of Fiscal Equalization and Functional Allocation in the Canton of Lucerne

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Major Reforms of Fiscal Equalization and Functional Allocation

- The canton of Lucerne has seen several reforms of functional allocation and fiscal equalization
- All the reforms were basically based on the principles of subsidiarity and fiscal equivalence, and they aimed at a disentanglement of tasks.
- However, a lot of compromises had to be made, deviating from the principles, mainly because the canton and the communes do not want to change tax rates of shared taxes (personal income tax, corporate income tax)



Source: Website canton of Lucerne

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Example: Fiscal Reform 2008

- Main Objective:
 - Taking into account the implications of the NFA on cantonal revenue and expenditure
 - Decentralized and disentangled functions had to be allocated to either the canton, the communes or as a shared function
 - Tax shares were adapted accordingly

- Problem:
 - In order to have a cost neutral implementation for the canton and the communes, cantonal functions are partly financed by mandatory per capita grants from communes
 - => Violation of the principle of fiscal equivalence

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Thank you!

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