

The autonomous funding of Catalonia

Executive summary



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THE AUTONOMOUS FUNDING OF CATALONIA

REPORT

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Consell de Treball,
Econòmic i Social
de Catalunya



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1. Executive summary

Since the adoption of the Spanish Constitution in 1978 the funding of the powers transferred to the autonomous communities (AC) has been configured through the successive agreements concerning the autonomous funding model which result in the establishment of six financing periods to the present: until 1986; 1987-1991; 1992-1996; 1997-2001; 2002-2008 and from 2009 onwards.

The last funding agreement, which has as one of its main references the adoption of the Law 6/2006, of 19 July, reforming the Statute of Autonomy of Catalonia, is approved in 2009 through the reform of the organic Law 8/1980 of 22 September, on the funding of the autonomous communities through the organic Law 3/2009 and the subsequent approval of Law 22/2009 of 18 December, which regulates the funding system of the common-scheme autonomous communities and of the cities with statute of autonomy and also amends certain taxes.

Since the launch of the autonomous funding system, Catalonia has made a positive net contribution to the Spanish territorial cohesion. The results of Catalonia's fiscal balance with the central Government in a relatively long period of calculation make it clear.

This contribution in the years 2002-2009 –neutralizing the public deficits/surpluses effect of the central Administration- stood on average at 8.6% of Catalan GDP, using the monetary flow methodology, and at 6.1% following the burden benefit methodology. This contribution, according to both methodologies, has been reduced by around 1.6 percentage points during these same eight years.

It is also noteworthy that Catalonia's contribution to this territorial balance, from the perspective of its institutional composition, is channeled mainly through the Catalanian fiscal flows with the State. Measured in per capita terms and with regard to the average fiscal balance per capita of all AC, the relationship with the State means, in the years 2002-2009, almost 80% of the relative per capita fiscal balance with the whole of the Central Administration, while the relationship with the Social Security Administration would represent 18.5% of this relative balance. Regarding the relations of Catalonia, on the one hand with the autonomous institutions of the State and its public bodies, and on the other with public companies (mainly AENA and Ports of the State), Catalonia maintains a fiscal balance per capita which is positive in both cases, although in the first case it receives net resources per capita below the average of the positive fiscal balance of the set of autonomous communities, and in the second case it does above this average with a combined effect that practically compensates.

In this last period Catalonia makes an average annual net contribution to the Central Administration of 1,504 euros more per inhabitant than that made by the whole of AC, as a result of a per capita income contribution higher than the average contribution of the AC and of the perception of a per capita expenditure which is below the average of the AC.

On the revenue side, in this period Catalonia contributes annually 1,182 euros per inhabitant more than the average of the AC to the revenues of the Central Administration. Direct taxes (especially the income tax and, to a lesser extent, the corporation tax) paid to the State and the Social Security contributions paid to the Social Security Administration are the main components of income explaining the greater relative contribution per capita of Catalonia, with a contribution of 484 euros more per inhabitant and 504 euros more per inhabitant, respectively, than the average contribution of the AC. Thus the effect of a progressive taxation on a country with a higher relative per capita income is included. Of the remaining revenue, it is also remarkable the contribution made by the added value tax to the relative balance, with 152 euros more per capita than the AC average.

Concerning expenditure, in this same period Catalonia receives annually 322 euros less per capita than the set of the AC. The expenditures of the State and, to a lesser extent, those of its autonomous institutions and public bodies explain the negative differential of the expense per capita of the Central Administration in Catalonia, whereas both the Social Security Administration and the public companies are spending in Catalonia an amount per capita which is higher than the one received by the set of AC.

Catalonia contributes to the territorial balance largely through the autonomous funding system. Thus, among the expenditures of the State, the transfers associated with the autonomous funding model are the main component in which the expenditure per capita of the State is placed differentially below the one of the set of AC.

Therefore, it is found that the differential in the contribution of net resources per capita made by Catalonia is mainly a result of the per capita income differential that the Central Administration obtains from Catalonia in relation to those which it gets from the set of AC. Revenues in the years 2002-2009 have contributed on average 78.6% of the sign of the relative fiscal balance per inhabitant of Catalonia. However, the expenditure received by Catalonia from the Central Administration contributes on average in the same period the remaining 21.6% of this relative balance. Thus Catalonia has been a net contributor to the territorial balance not only by the fact that, according to its greater relative income it has contributed more income per capita than the set of AC, but also because it has received a expenditure per capita from the Central Administration which is below average. This result alters the conclusions of some previous analysis that placed the net contribution of Catalonia strictly in the field of revenues, whereas the expenditure received per capita was placed above average.

Without questioning the virtues of a net contribution of a territory such as Catalonia that has a per capita income above the average, different analysis have shown the effect on domestic demand and job creation in Catalonia that the persistence of excessive fiscal deficits with the Central Administration may have. On the other hand, to provide greater autonomy and fiscal responsibility for the AC can make more efficient and effective their response to the crisis and allow that the boost to growth that may arise at this level of government is made keeping the step between income and expenses.

From the perspective of the redistributive equity that works through the action of the Central Administration, the funding of the different levels of government related to the territorial organization of the State shows a fiscal imbalance as the result of a mismatch between the vertical distribution of powers and the vertical distribution of tax revenues among these levels of government, especially between the State and the AC, which implies a clear financial insufficiency of the sub-central governments of the AC – the autonomous Administration and local corporations - and therefore an insufficient vertical equity.

During the period 1995-2010, the Central Administration has had available on average a percentage of the income of all the Spanish public sector exceeding 17.1 percentage points in the share of the public expenditure which is under its responsibility. In a first period, 1995-2001, the gap was 18.3 percentage points, while in the following period, 2002-2010, it is reduced to 16.2 percentage points.

At the same time, the CA have had available a percentage of revenue which is 14.6 percentage points lower than the percentage of expenditure that they managed in accordance with the powers transferred. Between 1995 and 2001 this difference was on average 16.4 percentage points, whereas there is a relative improvement in vertical equity in the years 2002-2010, when this difference is reduced to 13.2 percentage points.

In an international comparative perspective, countries like Germany, Austria, Switzerland or Canada, with territorial federal-type structures which are comparable to those of Spain show for the same period, 1995-2010, a greater balance in financing the different levels of government. In Germany the difference, in consolidated terms, between the percentage of obtained income and the percentage of expenditure managed by each level of government does not exceed in any case, in average terms, 5 percentage points; in Austria and Switzerland it does not exceed 9 percentage points, and in Canada it does not exceed 10 percentage points.

In the case of France, Italy and the UK, with an administrative structure organized in two levels of government, central and local administration, France and Italy, especially in the first case, keep a smaller imbalance between the weight of revenue and the consolidated expenditure under the responsibility of each level of administration in comparison with the situation in Spain, whereas in the case of the UK this imbalance is higher.

The economic crisis and the tax reduction policies put into operation the years 2007-2009 have significantly eroded the resources of the funding model despite the new contributions that the State has made to the new funding model. At the same time, the expenses of the AC, linked to powers with a high social character, such as education, health and social care services, which have a higher weight at this level of government than at the central level have continued to grow.

With the latest data from the final settlements of the funding model for 2009, the weight of the regional funding resources on non-financial expenditure of the Generalitat has been reduced from 77.8% in 2007 to 54.9% in 2009, in a very similar process to that followed by the set of the common-regime autonomous communities.

The 2009 funding model brings to Catalonia resources worth 17,855.9 million euros, 0.2% less than in 2008, although with a relatively better outcome than that of the set of common-regime AC, in which the global resources of the model have fallen 8.5%. Although the total collection in Catalonia (State and autonomous part) of the partially ceded taxes has decreased 20.7%, the largest transfer of the income tax, VAT and special taxes has allowed that the revenues from the partially ceded taxes increase by 30.5%, while revenue from other taxes, the wholly ceded ones, reduce 26.4%. Thus, altogether, the tax revenues of the model increased 11.8%, an increase that was offset by the reduction in State transfers and non-tax resources, which in relative terms fall 53.6%.

The new resources provided by the State to the 2009 funding model rebalance partly the relative position of Catalonia in the autonomous funding, to be the main recipient of these new resources, with 1,986.1 million euros the year 2009. It is necessary to add to these resources that part of 2,400 million euros provided by the State to the model in 2010, which will correspond to Catalonia in the settlement of the system done in 2012.

The new model has managed that resources per capita of all AC converge towards the average, and the level of dispersion in the final results of the model reduce. So Catalonia and Madrid end, just after the levelling, with resources per capita above the average and the Balearic Islands are located in the middle. As for Cantabria and La Rioja, which still start from fiscal capacities above average, after levelling they improve their relative position, while Valencia and Murcia are still battered by the AC system.

The consequence of these overlevellings is a breach of the principle of ordinality in the results of the new model. Catalonia, to equal fiscal effort as the rest of AC, is the third community in fiscal capacity, with a regulatory tax revenue per adjusted inhabitant 20.7% higher than the average. Once applied all the levelling and compensation mechanisms established and deduced the funding of the specific powers, Catalonia obtains resources per adjusted inhabitant in homogeneous terms and with an equal tax burden which are 3.6% higher than the average, although it is placed in the eighth position in relative terms. The fact of adding the use of the autonomous regulatory capacity

has placed Catalonia in the fourth position in resources per adjusted inhabitant in homogeneous terms.

In this context, the funding model itself, regardless of its mechanism of evolution, establishes its five-year review, which was carried out in late 2013.

The growth and the potential of responding to the current economic crisis by the AC also depend on the distribution and the level of the investment effort that the State's public sector makes in the various territories.

The State's public sector has made a growing investment effort in the years 2001-2008, which reaches a peak in 2008 with 31,809 million euros of real budgeted investment. From 2009 the budgeted investment is reduced in the context of the economic crisis, to almost half in the 2012 budget, with 15,532 million euros, a level of real planned investment which is lower than the one budgeted in 2001.

In this relatively long period of eleven years, 2001-2012, Catalonia is the second AC in the real investment forecasts in absolute terms, with 14.6% of the regionalized investment, behind Andalusia, with 16% of the investment, and almost the same as the Community of Madrid, with 14% of the investment.

The investment effort of the State in Catalonia, from the beginning, in 2001, of large infrastructure projects, grew consistently until 2009 and subsequently reduced as a result of crisis, following broadly the trend of the total investment of the State, both from the perspective of the budgeted and regionalized data of real investment of the public sector and the executed and regionalized data of the real investment of the Foment group, primarily responsible for real investments in infrastructure made by the public sector.

The regionalized State investment in Catalonia, that made a significant jump from 2001, maintains a relatively stable weight in the total regionalized investment of the State's public sector in the years 2001-2012, being the average 14.6%. The years 2001-2006 that weight is 15% and 14.3% in the years 2007-2012; this slight decrease is due primarily to the effect on the average that the Draft of the State's General Budget has for 2012, which places the weight of investment in Catalonia in the 11.1% in relationship to the regionalized total.

The executed data of the regionalized investment of the Foment group until 2010, where Catalonia has a relatively higher participation than in the overall investment of the State's public sector, also show the relatively stable profile of the territorial distribution of the investment that Catalonia receives. The weight of the executed real investment of the Foment group in Catalonia is 17.1% on average in the years 2001 to 2010; 16.8% in the years 2001-2006; and 17.5% in the years 2007-2010.

Nevertheless, it is important to emphasize that this investment effort of the Foment group has remained below what was initially budgeted. Between 2001 and 2009 the degree of implementation of the investment of the Foment group in Catalonia is 78.9% on average, while in the whole State is 87.5%.

In general terms, the real budgeted investment of the State's public sector in the years 2001-2012 has foreseen, for those AC with a lower GDP per capita, a distribution of real investment over its population and economic weight, whereas in the autonomous communities with a GDP per capita which is higher than the average the budget foresees a distribution of the real investment below their population and economic weights.

Among the ten autonomous communities with a GDP per capita below the average we should emphasize the cases of Galicia, Asturias, Castile and León and Castile-La Mancha, which maintain a weight of budgeted investment well above their population and economic weight, whereas Valencia and the Canary Islands receive a distribution of investment clearly below this weight.

Among the seven autonomous communities with a GDP per capita above the average we should emphasize the cases of Aragon, especially, and La Rioja, because of the fact that they maintain the weight of investment during the period above their population and economic weights. In the communities of Catalonia, the Balearic Islands, Navarre and the Basque Country the distribution of budgeted investment stays below their population and economic weights, whereas in Madrid, although the distribution of investment has remained below the weight of its GDP, it is just above its population weight.

From 2006 different autonomous communities such as Catalonia, Andalusia, Aragon, Castile and León and the Balearic Islands have adopted new autonomy statutes which include provisions establishing, temporary or indefinitely, the volume of investment that the State should allocate to these territories. This volume is set on the basis of an indicator of population, GDP or surface, according to what benefits most each territory.

The real regionalized investment in the years 2007-2012 maintains the overall pattern of the period 2001-2006, although the following elements can be highlighted:

Eight of the ten AC with a GDP per capita below the average (Extremadura, Andalusia, Castile-La Mancha, Murcia, Galicia, Valencia, Asturias and Castile and León) improve the weight of their investment distribution both in relationship to the population and GDP whereas the Canary Islands and Cantabria worsen the weight of the budgeted investment both with regard to its weight in GDP and to its population. However, Valencia and the Canary Islands still maintain a distribution of the budgeted investment below their population and economic weight.

As for the seven AC with a GDP per capita above average, five of them, Madrid, Catalonia, the Balearic Islands, La Rioja and Aragon lose weight in the distribution of budgeted investment and reduce this weight both in relation to its population weight and to the economic one, whereas the Basque Country and Navarre increase the weight of the budgeted investment in relation to its population and economic weight. However, Aragon and La Rioja continue to maintain a distribution of investment above its population and economic weight.

As for Catalonia, with a distribution of 14.3% of the real investment, it worsens the distance both in relation to its population and to its economic weight.

The case of Madrid is also noteworthy, since, during the years 2007-2012, its investment weight has been clearly placed below its economic and population weight.

The territorial distribution of the real liquidated investment of the Foment group in the years 2001-2010 follows roughly the same distributive patterns than the set of the real budgeted investment of the State's public sector.

In this period, the autonomous communities with a GDP per capita below average receive a distribution of the real executed investment above their economic and population weight and, as it happens with the real budgeted investments, the communities of Galicia, Asturias, Castile and León and Castile-La Mancha are the ones where this difference is significantly higher. The communities of Valencia and the Canary Islands receive a weight of the real liquidated investment that is below their population weights, as it happens with the budgeted data; the case of Murcia should be added to that of these two AC, whereas Andalusia, also in this case, maintains a liquidated investment which is below its population weight and above its economic weight.

As for the autonomous communities with a GDP per capita above average, the Basque Country, Navarre, the Balearic Islands and La Rioja have a weight of the real liquidated investment below their population and economic weight along the last ten years. Only Aragon, as it happens also with the real budgeted investment of the State's public sector, receives a distribution of investment above its population and economic weight. It is noteworthy that Catalonia, unlike what happens with the data of real budgeted investment of the State's public sector, receives a weight of the real liquidated investment above its weight population, although it remains below its economic weight. The same happens in Madrid, although with a weight of the real liquidated investment just above its population weight and clearly below its economic weight.

The 2006 Statute of Autonomy of Catalonia (EAC) provides in its third additional provision that the State investment in infrastructure in Catalonia shall be compared with the weight of the Catalan GDP in relationship to the Spanish GDP over a period of seven years, 2007-2013.

This agreement reflects the will to offset a persistent deficit in matters of infrastructure investments of the State in Catalonia, which had placed the investment in the territory of Catalonia below its weight population.

In average terms of the years 2007-2010, the executed investment in compliance with the third additional provision of the EAC has been 15.8% of the territorially executed investment of the State, and therefore it is placed just below the average population weight of Catalonia in these four years, 15.9%, and clearly below the average weight of the Catalan GDP, 18.7%.

The liquidated investment of the State in Catalonia, once incorporated the adjustments foreseen in the compliance methodology of the Agreement on the implementation of the third additional provision, accumulates in the years 2007-2009 an outstanding balance on investment in Catalonia of 759 million euros in 2008, 211 million euros in 2009 and 719 million in 2010.

The year 2010 shows the worst level of compliance of the third additional provision of the EAC as a result of the low level of implementation of the infrastructure investment in the whole State, 73%, derived from the cuts associated to the austerity measures following the approval of the budget, and of a more intense effect of these cuts in the investment executed by the State in Catalonia, where the degree of implementation of the investment is 65.1%.

This low level of execution fails to honour the commitment acquired in the methodology of implementation of the third additional provision of the EAC, which states that the degree of implementation of the State investment in Catalonia shall not be less than the State average execution and not less than the average of the two previous years.

The Parliament of Catalonia has set up a New Financing Model Study Commission based on the Economic Agreement, which concludes that:

The application to Catalonia of a funding system based on the economic agreement model is compatible with the Constitution, the Statute and the law of the European Union.

Given the absolute primacy which the Constitutional Court attaches to the Organic Law on the financing of the autonomous communities (LOFCA) in consolidated jurisprudence, although questionable, to establish the general framework of the funding system, the implementation of a model based on the economic agreement should be articulated through a reform of this rule.

According to the conclusions of the Parliamentary Commission, the establishment of a model based on the economic agreement involves modifying the Organic Law on the financing of the autonomous communities (LOFCA) to introduce an exception to the common funding scheme and to regulate the essential features of the new model, which will be necessary to develop later through

a law passed by the General Courts with prior agreement in the State-Generalitat Joint Commission on Economic and Fiscal Affairs.

The essential features to be collected in the new funding scheme are, in the line indicated by the Parliamentary Commission:

- A bilateral relationship between the Government of the Generalitat and the State. However, given the absolute lack of legal guarantees in front of hypothetical unilateral State decisions deriving from the fact that the introduction of the new scheme should be done through an amendment to the LOFCA, it would be necessary to foresee mechanisms to strengthen to the maximum the character of bilateral pact.

- The establishment of an own comprehensive tax system that determines:

- The full regulatory power over all taxes generated in Catalonia within the framework of the EU tax harmonization.

- The effective assumption by the Government of the Generalitat of the powers on exaction, collection, management, settlement, inspection and review of all taxes generated in Catalonia and managed by the Tax Agency of Catalonia.

- The establishment of the quota that must be submitted to the State as aliquot part of the cost of the powers or the common services exercised by the State and which are of its own and by way of interterritorial solidarity, considering that, once that the contribution is made, Catalonia cannot lose fiscal capacity, and the amount for this concept should be allocated to the most basic policies of the welfare state.