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# The Territoriality of Fiscal Solidarity: Comparing Swiss Equalisation with European Union Structural Funding

by

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## Abstract

This article theorises the territorial solidarity and fiscal federalism and compares Switzerland with the European Union. While inter-territorial solidarity is a prerequisite for legitimate fiscal equalisation, such equalisation in turn also contributes to the legitimacy of and solidarity within federal political systems. By cutting across territorial and ethno-national communities, fiscal transfers often contribute to both a “civic” sense of belonging and a “cosmopolitan” identity. After placing types and degrees of (inter-)territorial solidarity at the heart of our conceptual perspective, we discuss the effects of such solidarity through an analysis of two different forms of “federal” equalisation. Comparing the recently reformed Swiss fiscal equalisation system with the EU structural funds allows us to infer if, and how, the fiscal dimension of federalism matters for feelings of solidarity, reciprocity, unity and, ultimately, for the legitimacy of the very (nation-state or Union) structures that are to contribute to the ever-growing prosperity and happiness of their people(s). In Switzerland, a civic understanding of nationhood and cross-cutting cleavages were necessary conditions for extensive, effective and legitimate fiscal equalisation. We infer that, for the EU, this means that strengthening the equalisation component of the structural funds would contribute to an ever closer Union in a political sense: because fiscal equalisation and inter-territorial solidarity are interdependent, reinforcing the one also means cementing the other. Future studies of the EU and federal-type arrangements are advised to pay more explicit attention to the solidarity-element of territoriality – or the territoriality of (fiscal) solidarity.

## Key-words

Territorial solidarity, fiscal federalism, European Union, Switzerland



## Introduction

This article theorises solidarity in multi-level systems and compares the recently reformed fiscal equalisation scheme of Switzerland with the EU's structural funds. Our point of departure is that inter-territorial solidarity (between cantons, *Länder*, states, provinces, autonomous communities or EU Member States) is a prerequisite for fiscal equalisation, as much as inter-personal and inter-group solidarity are for many national-level redistributive policies. Equalisation in turn contributes to the overall legitimacy of a polity because – ideally – transfers contribute to a “civic” sense of belonging and a “cosmopolitan” shared identity by cutting across entrenched ethno-national communities, creating *une solidarité de fait*, as Robert Schumann (1950) once described. Fiscal federalism and connected financial equalisation schemes can also contribute to a stronger feeling of a “shared destiny” among the territorial units and the people within a federal system. This feeling of solidarity and reciprocity is a key element of federal democracy and federal political culture (Burgess 2012). To what extent this ideal applies to the EU, particularly by scaling down to the regional level (Hooghe and Marks 2001), is the focus of this article.

Our method to answer this question empirically is to offer a short analysis of Swiss fiscal equalisation, which maximises both the legitimacy and solidarity dimension and whose political system, through strong cantonal identities and due to its confederal nature especially in the fiscal domain, approximates the EU system better than any other currently existing political system (Church and Dardanelli 2005).<sup>1</sup> The stability of the Swiss system, the creative character of its fiscal equalisation (in force only since 2008), and its resemblance to the EU as regards bottom-up, executive federalism allow us to draw conclusions on when, how and why fiscal equalisation is able to maximise solidarity. We then apply these conclusions to the EU in the form of hypotheses, analysing in particular a) the constellation of “fiscal losers” and “winners” at Member State level; b) the impact of this constellation on EU-wide feelings of inter-territorial solidarity; and c) potential avenues to increase inter-territorial solidarity – plus, through this, to achieve a stronger feeling of common belonging and shared identity at Union-level – by reforming the EU's fiscal equalisation.



The first section conceptualises territorial solidarity in connection to fiscal equalisation. The second describes Swiss fiscal equalisation while the third section is dedicated to analysing both equalisation and solidarity within the EU. The fourth section compares the two systems before we conclude.

## 1. Inter-territorial solidarity and fiscal equalisation

The literature on solidarity and fiscal equalisation is both vast and scarce. It is vast, because scholars from political economy, federalism, EU integration and even nationalism studies have at times discussed the importance of the fiscal dimension for polity-building (e.g. Burgess 2006a; Kymlicka 2001; Lijphart 1977). The importance of fiscal arrangements as part of the “self-rule” and “shared-rule” dimension in federal states has already been pointed out by Kenneth Wheare (1964). Other authors, such as Oates (1999) and Dafflon (2012), have also pointed towards the connection between federalism, fiscal relations and solidarity. However, scarcity arises in the sense that rarely has a causal connection between inter-territorial solidarity (as different from inter-personal solidarity) and fiscal equalisation been made, let alone been “tested” empirically. The recent outpour on “multi-level governance” (e.g. Bache & Flinders 2004, Benz 2009, Piattoni 2010) has only partially filled this lacuna.

The problem is that while we may observe a “re-territorialisation” (Burgess 2006b) of politics, the various mechanisms that link territory to politics at the nation-state level – e.g. collective identity (Risse 2010), imagination (Anderson 1983), control (Sack 1986), instinct (Ardrey 1975 [1966]), or societal diversity (Livingston 1956) – cannot be transformed “upwards” (to the EU) or “downwards” (to the regional level) without not also modifying their scope. A case in point is solidarity. For solidarity to make analytical sense in multilevel polities such as the EU, inspiration must thus be drawn from federal political systems, where both the constituent units and the overarching polity have a direct effect on the citizenry (Forsyth 1981). Moreover, the relations between states, regions and the European level become even more complex than in federal states, because in addition to the interaction between the European, state and regional level, in the EU also bargaining *among* states (and competition between regions) can be observed (Keating 1988, Bartolini 2005).



There also exists a *direct* link between regions and the European level symbolised by the Committee of the Regions.

Nevertheless, even in federal studies solidarity as a key element of fiscal equalisation is rarely made explicit, so that one has to turn to political geography and studies of state formation to make sense of a) what binds people together not so much within, but rather across different territories; and this b) to an extent that they are willing to sacrifice some of their own wealth in favour of that of others.

The Oxford English Dictionary defines solidarity as “unity or agreement of feeling or action, especially among individuals with a common interest; mutual support within a group.” Less visible but equally crucial, solidarity underpins most redistributive policies at nation-state level, not just since the advent of the welfare state (Companje et al. 2009). Such policies in turn contribute to ever-growing feelings of solidarity (de Beer and Koster 2009, 50). For the EU, this translates into output-oriented legitimacy (Scharpf 1999, 5), which in turn depends on a “rescaling” of policies, politics and polity (Delaney 1997, Somerville 2004) to the European and/or the regional (and even local; cf. the European Charter of Local Self-Government of 1985).

Deductively, then, we can imagine solidarity between individuals and solidarity between collectives; additionally, there is solidarity between territorial and solidarity between non-territorial collectives. Significantly for us, the Lisbon Treaty lists both under Article 2: “solidarity between generations and [...] solidarity between Member States.” Table 1 shows all three possible combinations of solidarity – by definition, individuals are non-territorial, hence the one empty cell.

<b>Level/Basis</b>	<i>Non-territorial</i>	<i>Territorial</i>
<i>Individual</i>	Inter-personal solidarity	-
<i>Collective</i>	Inter-group solidarity	Inter-territorial solidarity

Table 1: Forms of solidarity

Classic accounts of liberal democracy have tended to focus on the first column and placed individual rights above territorial claims to justice (Greer 2006), which is precisely why federalism can be perceived as having a slightly undemocratic touch (Basta Fleiner 2000: 94). In the French ideal of republican equality and in the Anglo-American conception



of liberty, the state is either regarded as a means to foster unity and cohesion (through Jacobin centralisation) or to be kept small to allow markets to thrive (privatisation). And yet only a federal ideology “in the weak sense” (King 1982) is able to reconcile all three forms of solidarity in a legitimate way.

First, by reconciling deep-seated collective *and* territorial imaginations with the need to collaborate in a mutually binding way on a greater scale. Federations, by breaking larger entities down into several smaller polities, allow for inter-personal solidarity in, ideally, the same homogeneous entities that Rousseau envisaged as *conditio sine qua non* for democracy to work.<sup>II</sup>

Second, within the overarching whole, these entities are the bearers of territorial group rights, whether in essentially bi-national (e.g. Canada or Belgium), multinational (e.g. Bosnia), and multi-lingual federations (Switzerland), or in the traditional mono-national federations (Germany, Australia, USA). This creates the basis for inter-territorial solidarity – or its waning, if to strengthen ties within a community means questioning those between them.

Finally, any remaining collective but non-territorial interests (be they socio-economic, ideational, religious, or non-territorial minority groups) can organise at the “national”, “regional” and/or the “local” level to argue their place in deciding on inter-group solidarity. Consequently, it can be argued that the application of the federal principle to diverse societies contributes to inter-group solidarity by allowing a re-adjustment of political categories on different political and territorial levels as well as between them, and therefore contributes to a greater sense of justice in both a normative and a practical sense (Wayne 2001, Requejo 2005).

Focusing on inter-territorial solidarity in particular, its importance for federal political systems<sup>III</sup> is expressed in the need for fiscal equalisation to address both horizontal and vertical imbalances (Watts 1996: 41). Equalisation in narrower terms refers to transfers that stem from

a recognition that disparities in wealth among regions within a federation are likely to have a corrosive effect on cohesion within a federation. Indeed, it is for this reason that in most European federations equalisation transfers have been labelled “solidarity” transfers. (Watts 1996: 45)



Because disparities might threaten unity, equalisation is an expression of solidarity. But the relationship between inter-territorial solidarity, fiscal equalisation and overall legitimacy can only be circular, as we show in Figure 1.

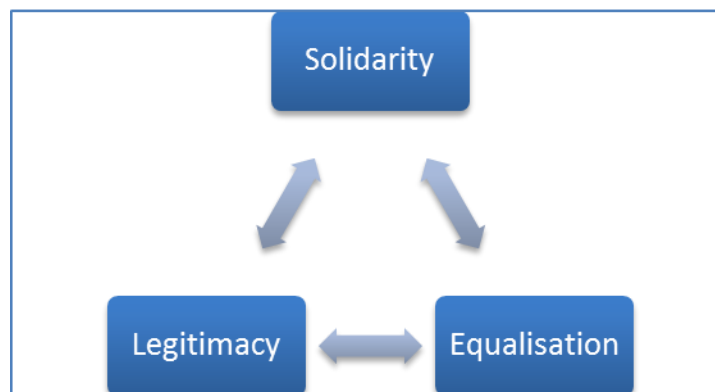


Figure 1: The circularity of inter-territorial solidarity

There are thus three interactions at work. First, between solidarity and equalisation: a minimum level of solidarity is a condition for fiscal equalisation. Both the extent and the very existence of fiscal equalisation constitute the ultimate test of inter-territorial solidarity. However, some examples demonstrate a fundamental dilemma in this circular relationship: whether it is Catalonia’s call for fiscal autonomy à la Basque Country and Navarre, or even for independence because it does not want to fund the other Spanish regions’ expenditures by having to cut its own budget; Bart De Wever’s disagreement over Flanders having to “pay for the unemployed in Wallonia”; or Bavaria’s appeal to the Constitutional Court over the current inter-*Länder* fiscal equalisation.<sup>IV</sup> Thus, solidarity and equalisation are permanently contested and re-negotiated in federal systems, because commitments to financial equalisation among federal units can be seen as a limitation to the autonomy of the (richer) units in a federal system.

Second, financial equalisation has become more and more frequent in federal and non-federal countries – but also more contested – since it also relates to wider economic questions of fair competition and fiscal discipline (Rodden 2006). Thus, to be perceived as legitimate, equalisation must give expression to territorial differences on both sides of the equation, i.e. at the paying as well as at the receiving end. Equalisation only contributes to the legitimacy of a polity if not only the net recipients, but also the net contributors regard



it as necessary. The EU accomplishes this sort of “output legitimacy” with the trick of “rescaling” its projects to the regional level, but then consistently aggregating the benefits to the national level – in this way, because every Member State has regions that receive money, there simply are no losers.

Third, legitimacy strengthened in such a way contributes to solidarity and makes the circle come to a close. This is because the legitimacy of each policy contributes to the aggregate legitimacy of political decisions in general. Equalisation is thus not only a consequence, but also a cause of solidarity through the provision of specific benefits. Hence, one would expect those who profit the most from a given equalisation system to be amongst the most ardent favours. Therefore, in a democratic setting where decisions are taken by majorities (i.e. anything ranging from simple plurality to unanimity), equalisation can only work if there are more winners than losers, defined in the very territorial terms used by the equalisation system itself. As the Swiss description below demonstrates, the new fiscal equalisation scheme was overwhelmingly approved because all but very few (and small) cantons are now better off. The open expression of such a form of inter-cantonal solidarity (in a nation-wide referendum) has in turn significantly strengthened the overall legitimacy of the Swiss political system.

Some argue that the EU will never be able to reproduce societal togetherness with the same intensity as has been achieved at the national level. Hence, no (*inter-personal*) “duty to accept solidaristic sacrifices derived from the premises of essential sameness” will ever arise (Scharpf 1999: 12). At the same time, however, the crises in Greece, Portugal, Ireland and Cyprus and the adoption of the European Stability Mechanism (ESM) have lifted EU-wide (*inter-territorial*) solidarity – at least for the Eurozone-members – to an unprecedented level that could well pave the way for a banking union and, indeed, to the “ever closer union” outlined by Barroso (2012):

The stronger countries must leave no doubts about their willingness to stick together and about their sense of solidarity. [...] Fairness is an essential condition for making the necessary economic reforms socially and politically acceptable and, above all, because fairness is a question of social justice. [...] the economic and monetary union raises the question of a political union and the European democracy that must underpin it. [...] Let us not be afraid of the word: we will need to move towards a federation of nation states.





Our argument is that in the absence of a strong sense of togetherness (or inter-personal solidarity), which at the nation-state level has been a condition for (the legitimacy of) redistributive policies, the economic challenge posed by the current crisis could well work as a trigger to increase the equalisation component within the cohesion policy to an extent that it becomes a powerful creator of inter-territorial solidarity, which in turn legitimises (further) equalisation and political union.

Centring this debate on solidarity gives expression to the fact that in multi-level polities two challenges arise: a) how to achieve solidarity between territorial communities that goes beyond mutual recognition, i.e. one that involves a willingness to make specific sacrifices that explicitly benefit others; and b) how to reconcile such inter-territorial solidarity with other (territorial or non-territorial, personal or collective) forms of solidarity. Is this a zero-sum game, or are the two mutually enhancing? For lack of space, this article deals exclusively with the first challenge. Ultimately, however, while it is true that “a solidaristic substrate is required for the formation of a collective identity” (Eriksen 2011: 83), what is equally true is that multiple layers can give rise to multiple forms of solidarity. We now turn to the Swiss case for an illustration of how the relation between inter-territorial solidarity, legitimacy and fiscal equalisation can be empirically assessed and what lessons can be learned from this.

## 2. Fiscal Equalisation in Switzerland

The purpose of this section is to show how fiscal equalisation and territorial solidarity relate to each other in one particular case. Studying Switzerland is useful because it is, for some, “the most federal” country in the world (Elazar 1993: 12), meaning that its three-layered structure of governance can serve as an inductive model. The second reason is that Switzerland has recently reformed its fiscal equalisation scheme: the current system was approved by a referendum in 2004 and has entered into force in early 2008. The 2004 popular vote also allows us to observe how the different cantons (that is, their electorates) have received the reform. The old system combined a convoluted list of subsidies with cantonal shares in federal revenues and scaled cantonal contributions to federal social expenditure (Dafflon 2005: 132–4). The new system is structured into three “pots”, each with a different logic and payments detached from the other two. The following



subsections discuss the legal framework, provide data for the years 2008 until 2013, and draw three conclusions which we then apply to the EU.

#### *Legal framework*

The Swiss fiscal equalisation scheme is regulated by the Federal Act of 3 October 2003 on Fiscal Equalisation and Cost Compensation (*Bundesgesetz über den Finanz- und Lastenausgleich*, FiLaG) and the accompanying Ordinance of 7 November 2007 (*Verordnung über den Finanz- und Lastenausgleich*, FiLaV). The goals of the equalisation scheme are to “strengthen the financial autonomy of the cantons” and “decrease differences in terms of fiscal capacity and tax burden” between the 26 sub-national units (Art. 2a-b FiLaG). Money is redistributed both horizontally, from the “richer” cantons, and vertically, from the Confederation, to the “poorer” cantons in both cases. There are two ways in which the dichotomy of “rich”/”poor” is defined: cantonal economic resources and extra “costs” arising from a canton’s topographical and/or social structure. Finally, there is a temporary compensation (for the 28 years from 2008 until 2036) for the losers in the transition away from the previous system.

First, the “resource” or “tax potential” of each canton represents the sum of taxable income of private individuals, their property, and the taxable profit of corporations divided by the resident population (Art. 3.2 FiLaG; see Dafflon 2005: 156, for the precise formula). The nationwide average forms the benchmark against which each canton is then measured. Cantons below this average count as “resource poor”, cantons above as “resource rich” (Art. 3.5 FiLaG). Figure 2 shows the Swiss cantons and their position in the resource index for 2012. The money received from this and the other two pots can be disposed of freely by the cantonal authorities – unlike in the previous system, where around 75 per cent of the money distributed vertically was earmarked for specific projects (through matching grants in the form of subsidies; Dafflon 2005: 140).

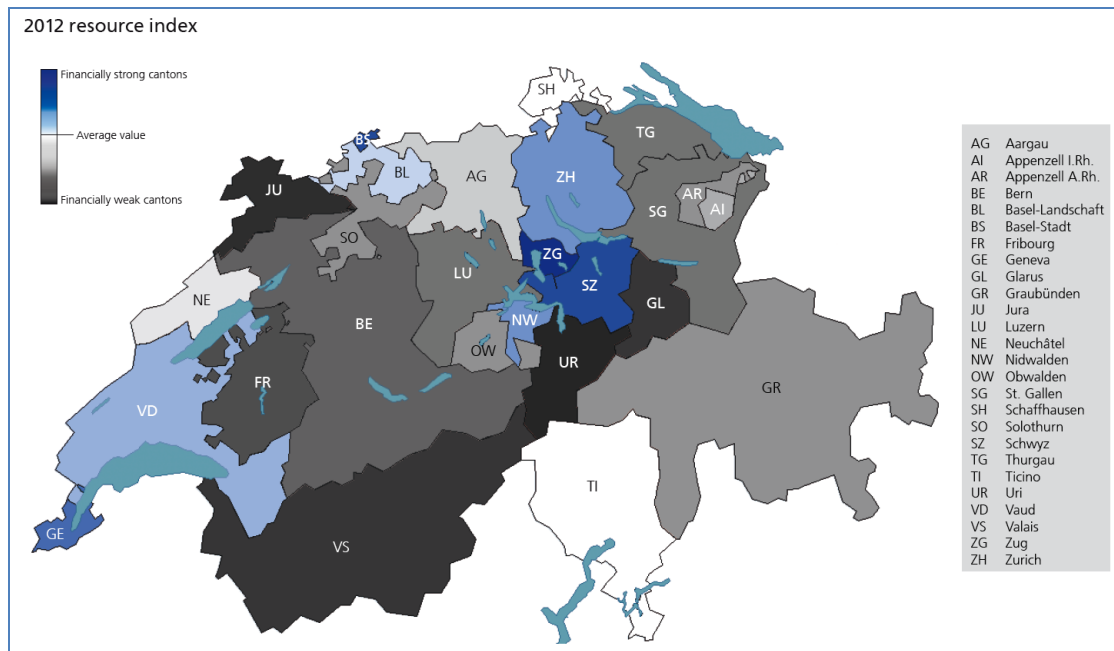


Figure 2: The “rich” and “poor” Swiss cantons (EFV 2012: 11)

Figure 2 clearly outlines that despite the fact that Switzerland is generally seen as a very rich country, with a strong tradition of banking and solid fiscal policies, there is nevertheless a strong pattern of economic diversity among the cantons. In this, the differences between the cantons in term of fiscal possibilities not only cut across classic cleavages, such as the linguistic<sup>V</sup> and the religious<sup>VI</sup> cleavage, but also across a newer, urban-rural divide (Linder et al. 2008), given that both the urban cantons Zurich (ZH), Geneva (GE), Basel-City (BS) and Vaud (VD), as well as the more “peripheral” cantons Zug (ZG), Schwyz (SZ), Nidwalden (NW) and Basel-Countryside (BL) count as rich in this sense.

The second fiscal equalisation stream centres on extra costs. Significantly, this stream was added at a later stage in the reform process and was meant to buy the support of net contributors by giving them something in return (Cappelletti et al. 2012: 12–3). It pays money to cantons suffering from either or both of two types of burdens: those arising from peripheral location, inaccessibility of the cantonal territory, and/or low density structures (Art. 7 FiLaG), on the one hand, and extra costs arising from an above-average proportion of elderly, poor, and/or unemployed persons (Art. 8 FiLaG), on the other. A total of eight geo-topographical and socio-demographic variables are taken into account for



the operationalisation of “costs” of this kind: average altitude, terrain steepness, settlement structure, and inverse population density for the first compensation mechanism; poverty, age, share of foreign nationals, and a “core city indicator” for the second (EFV 2012, 14). Some of these criteria lack economic justification (Dafflon 2005: 170-2) and respond more to the needs of creating a sufficiently large majority of cantons in favour of the overall system – a “package deal”, as Cappelletti et al. (2012: 9–10) call it.

This is even more valid for the third stream, limited in time to 2036 and designed to compensate cantons that excessively lost in the transition away from the old equalisation scheme (Schaltegger and Frey 2003: 252). In allusion to EU terminology, the official English translation of this third stream is “cohesion fund” (EFV 2012, 15), but the literal translation of the German *Härteausgleich* would be “duress equalisation” (Art. 19 FiLaG). Figure 3 depicts the financial flows for 2012 including all three fiscal streams.

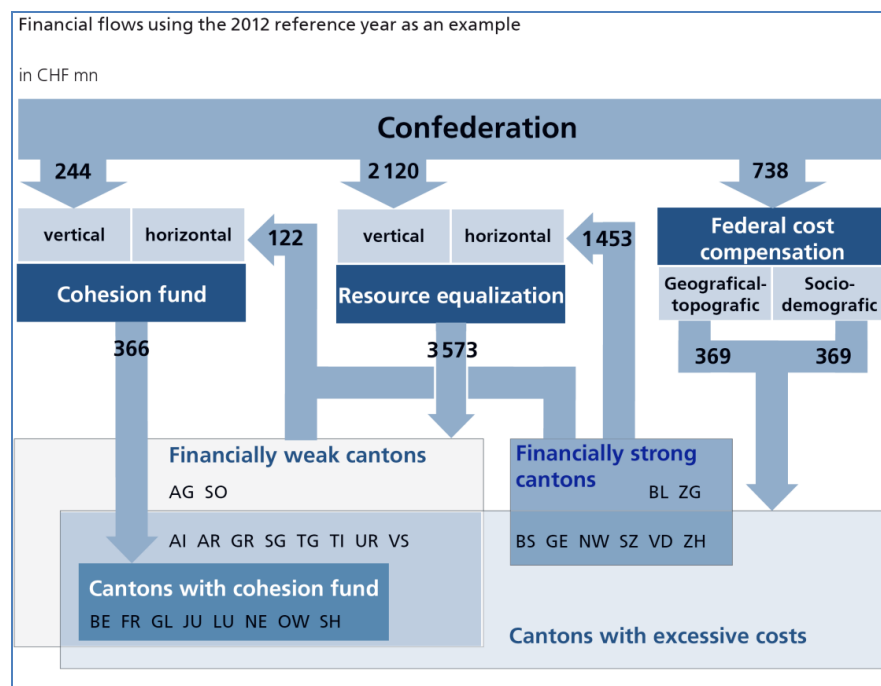


Figure 3: Swiss fiscal equalisation, 2012 (EFV 2012: 17)

As can be seen, five groups of cantons emerge. Eight cantons (bottom left) draw a net profit from the cohesion fund, are financially weak and subject to excessive costs. Hence, they are *triple winners*. Of the eight financially strong cantons (on the right), on the other hand, only two do not fall prey to excessive costs and are therefore payers on all three



accounts (*triple losers*). The other six financially strong cantons at least profit from cost equalisation, although situated above the Swiss average in terms of financial resources (*cost winners*). Two other cantons (Aargau (AG) and Solothurn (SO)) are financially weak, but do not have excessive costs, nor are they transition losers (*resource winners*). A final group of eight cantons is financially weak and has excessive costs, but does not receive payments through the – transitional – cohesion fund; cantons in this group we can be called *cost and equalisation winners*.

#### *Winners and losers*

All but the two cost compensation mechanisms (second stream) are funded by *both* federal and cantonal contributions. The ratio of this division is one third for the cantons and two thirds for the Confederation, for the Cohesion Fund (Art. 19.2 FiLaG): all cantons pay into the fund according the number of inhabitants, but only eight also receive something in return. For resource equalisation, the cantonal share is “between at least two thirds and a maximum of 80 per cent of federal payments” (Art. 4.2 FiLaG). In 2012, the amount paid by all cantons together was equivalent to 40.7 per cent of the contribution effectuated by the Federal Government; in 2008, it had been a high 70 per cent (EFV 2012).

A more interesting statistic is that of net per capita payments. Figure 4 shows the average annual net per capita payments for each canton between 2008 and 2012 in CHF; a negative payment denotes a disbursement to a canton, a positive payment means the canton had to contribute. Seen as the aggregate over the last five years, there were thus eight “net losers” and 18 “net winners”. The eight losers are the same that were expected to be net contributors at the time the federal referendum took place (Cappelletti et al. 2012: 11), so this division has remained stable over time. Moreover, the latest official policy evaluation shows that the rich cantons have grown by an average of 22.3 per cent, between 2007 and 2011, while the poor cantons have grown by “only” 17 per cent (EFV 2011, 8). The potential of Zug, Vaud and Schwyz has even increased by a record 35.7, 34.1 and 33 per cent, respectively (*ibid.*).

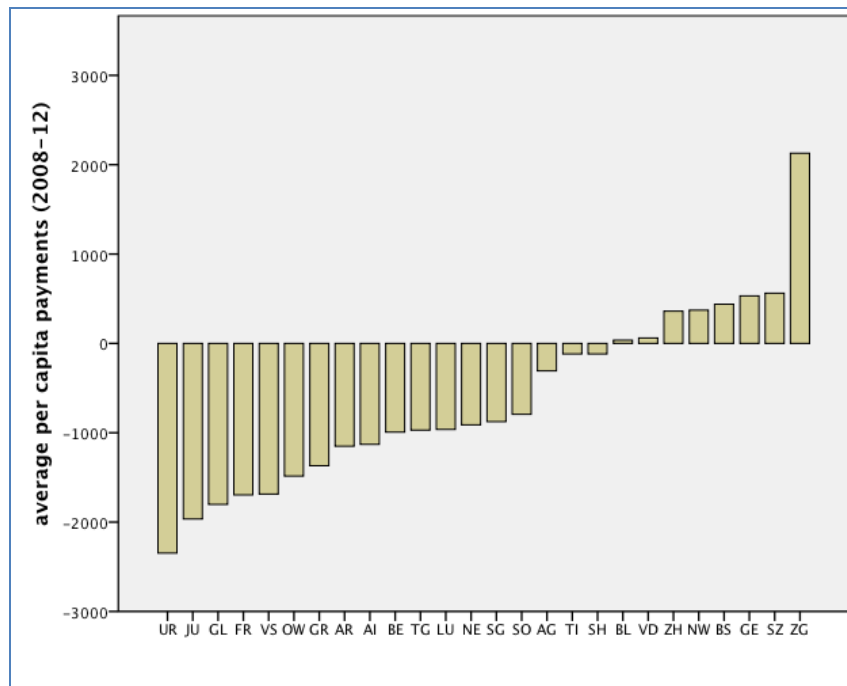


Figure 4: Net contributors and recipients in Switzerland, 2008-12

### 2.1. Inter-territorial solidarity in Switzerland

Because the Federal Act of which the new fiscal equalisation was part entailed wide-ranging modifications of the Federal Constitution, a popular vote had to take place that needed to muster a majority of both individual and cantonal votes (BR 2004). On 28 November 2004, a large majority of both cantons (23 out of 26) and citizens (64 per cent) agreed to the new division of tasks between Confederation and cantons and, through this, also to the new equalisation scheme (*Neugestaltung des Finanzausgleichs und der Aufgabenteilung zwischen Bund und Kantonen*, NFA). Only in three cantons did a majority of citizens reject the NFA; turnout was a low 36.9 per cent (BK 2004).

Analysing the 2004 referendum more closely allows us to draw several conclusions as to the underlying feeling of solidarity. Clearly, the more a canton was to profit from the new equalisation scheme, the more its citizens were in favour of it. Figure 5 shows the strong correlation between the share of no-votes in 2004 and the average per capita payments over the entire period for which we have data (Pearson's  $r = .754$ ,  $p < .01$ ). The only three cantons that rejected the NFA (Zug, Schwyz and Nidwalden) were all to consistently pay more into the equalisation schemes than they would receive (ranking first,



second and fifth in Figure 4), while the highest approval rates were registered in the cantons benefitting the most (e.g. Uri, Jura, Fribourg, Obwalden).

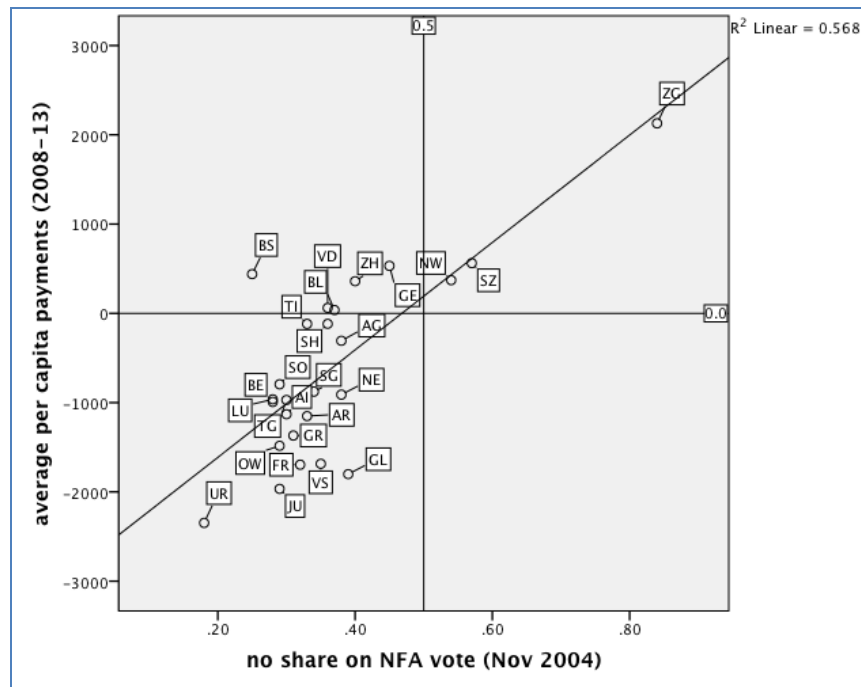


Figure 5: Benefits of Swiss fiscal equalisation by its approval rate

Three conclusions can be deduced from this. First, the perception of profit seems to have had an influence on attitudes towards nationwide solidarity. If the NFA was regarded as the most important element of nation-wide solidarity, then support for it was strongest at the receiving and weakest at the paying end of the fiscal equalisation scale.

Second, the reform managed to create few losers in the sense of consistently having to pay and never receiving anything in return. The three different pots have allowed 18 of 26 cantons to end up with a positive balance after six years. Moreover, only three of the six net payers rejected the NFA, and they are all very small and Catholic cantons, whose combined weight of no-votes (54'644) was less than, for example, the number of yes-votes in St. Gall alone (64'749). Bringing many cantons, and especially the larger ones, on board was therefore key to the success of the reform.

Third, achieving this degree of consensus is expensive. For 2012, the Swiss Confederation paid 3'102 million CHF (ca. 3.2 billion USD), whereas all the cantons together paid 1'575 million CH (ca. 1.6 billion USD). Achieving a strong sense of territorial



solidarity therefore requires a strong centre *and* strong component units, in terms of being able to share the overall financing of the system: the vertical component significantly lessens the individual contribution each canton has to make. However, where cantonal contributions rise disproportionately and in times of general fiscal crisis, fiscal equalisation is questioned as being derailed and exaggerated.<sup>VII</sup> We now apply these three conclusions to the EU polity.

### 3. The EU System

EU Regional Policy is one of the oldest policy areas of the European Union and has been a constant issue of discussion among Member States (Miric 2010, Mellors & Copperthwaite 2005 [1990], Balchin et al. 1999). While it was recognised that the creation of a Single Market, amongst a variety of Member States with different economic strengths and weaknesses, needed to be counter-balanced by some form of financial support for under-developed regions, the exact amount of money and its implementation via EU Regional Policy have been at the centre of a number of heated debates within the EU (Tondl 2004). However, the fact that Regional Policy has become the single most important policy in the EU budget demonstrates the importance of this policy. Moreover, at least one instrument explicitly makes the same point as we advance it here: the EU “Solidarity Fund”, through which “the Community should show its solidarity” by providing grants to help after natural disasters (cf. Council Regulation 2012/2020, preamble). But what kind of fiscal equalisation does the EU have to give expression to inter-territorial solidarity?

#### *EU “fiscal equalisation”*

Börzel and Hosli (2003: 188) write that “in contrast to federal systems, the EU is not endowed with an overall redistributive responsibility at the central level, despite the existence of the Structural and Cohesion Funds. The EU’s current setup clearly differs from most existing federal systems in its lack of a general income redistribution scheme.” One reason for the absence of explicit redistributive activity is certainly a lack of a substantial EU budget. The EU’s sources of income can be divided into three groups: customs duties on goods coming from outside, a share in the VAT levied on all goods sold within the EU, and Member State contributions as a percentage on their GNP (which is by





far the biggest share of the EU's overall budget). Nevertheless, precisely because most of the EU's expenditures fall into a quasi-redistributive basket based on territory, it is appropriate to regard the structural funds<sup>VIII</sup> as the functional equivalent to fiscal equalisation – all the more so since, again for Börzel and Hosli (2003: 191), “the EU largely resembles a system of cooperative federalism”, where the upper level regulates and lower levels execute.

But unlike the current practice in Switzerland, there is no explicit horizontal transfer of funds.<sup>IX</sup> EU structural funding works indirectly and vertically. It is paid by the EU, whose main source of funding is through Member State contributions. But since these are based on a country's GNP, richer Member States pay more into the pot for structural funds, while poorer countries tend to have poorer regions and therefore profit more from the funds. In practice, this means that Member States contribute to the EU budget, and the EU Commission (together with governments and regional representatives of the Member States) decides which regions should be awarded funding from the EU's budget pot on regional funding. While “cohesion” has political, social, and economic connotations, specifically the first one as expressing “solidarity for the weaker regions” (Evans 2004, 21) interests us in this discussion.

At the national-level, because all EU Member States are recipients of money from the structural funds (e.g. Cadman et al. 2010), there are no losers, only those who win more and those who win less. Matters are different if we turn to what remains after a Member State's contributions are subtracted from the benefits received through the structural funds. Figure 6 lists the countries by per capita net recipients, i.e. how much money each resident theoretically received after deducting payments to the EU budget in 2010 (negative amounts mean net payments).<sup>X</sup> Similar to the Swiss case, there are more territorial net recipients (16) than net payers (11), but the latter constitute a much larger group, both in terms of members and population size.

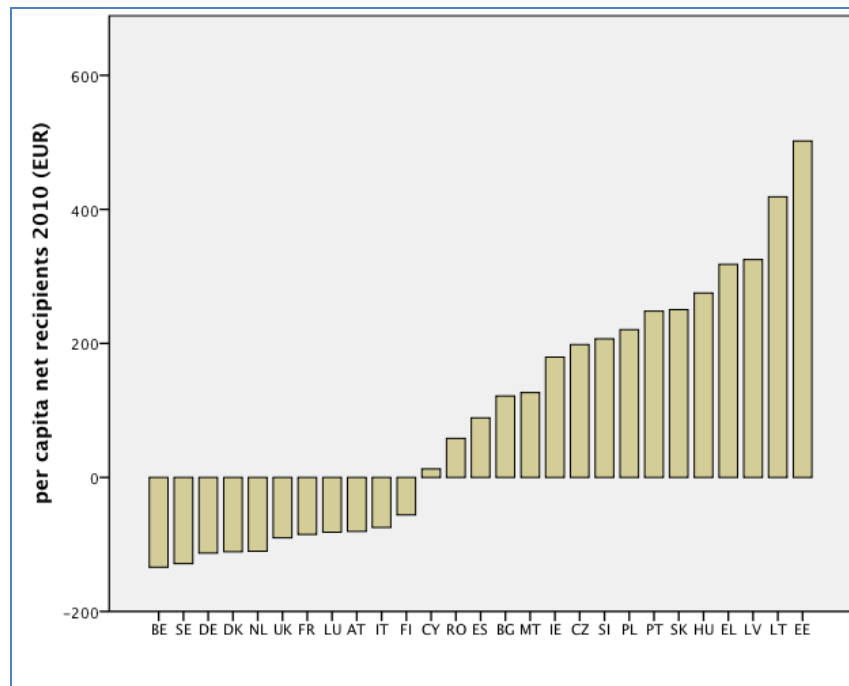


Figure 6: EU per capita net recipients in 2010

*Citizen perception*

EU citizens never had a chance to vote on the all-encompassing system of the structural funds in a binding way, unlike the Swiss electorate in 2004. The only way to gauge the legitimacy of the structural funds is therefore through surveys (Osterloh 2011: 2). In this section we compare EU-enthusiasts and -sceptics with net recipients and contributors using Eurobarometer and other European survey data. The main question to be answered is how Europeans perceive the current system of what we call the EU fiscal equalisation system, i.e. the structural funds. What are changes over time and across countries? Are Germans really the most sceptical because they are paying the most, as we would expect from our Swiss observation, and South- and East-Europeans the most supportive of the funds – and, by implication, also of the EU as such?

At the national level, Figure 7 plots the mean attitude to EU unification against the share of residents for whom EU membership is a good thing.<sup>x1</sup> While except for Latvia, the UK and Hungary all countries are situated above one of the two arithmetic means, for the overwhelming majority of EU citizens membership is principally a good thing. Obviously the two measures are positively correlated (Pearson’s  $r = .444$ ,  $p < .01$ ).

However, while the correlation between net recipients (in 2010) and mean attitudes to



EU unification is positive and significant (Pearson's  $r = .420$ ,  $p < .01$ ), the correlation between per capita net recipients and mean attitudes to EU unification is only very small and insignificant ( $r = .106$ ,  $p = .599$ ). Moreover, the correlation between per capita net recipients and the proportion for whom EU membership is good is *negative* ( $r = -.315$ ,  $p = .109$ ). Indeed, the strongest and most significant correlation is that between the proportion of those for whom EU membership is a good thing and per capita contributions – but this correlation is positive, contrary to our expectations (Figure 8). Richer states are therefore more supportive of the EU than poorer ones, which clearly contradicts our expectations.

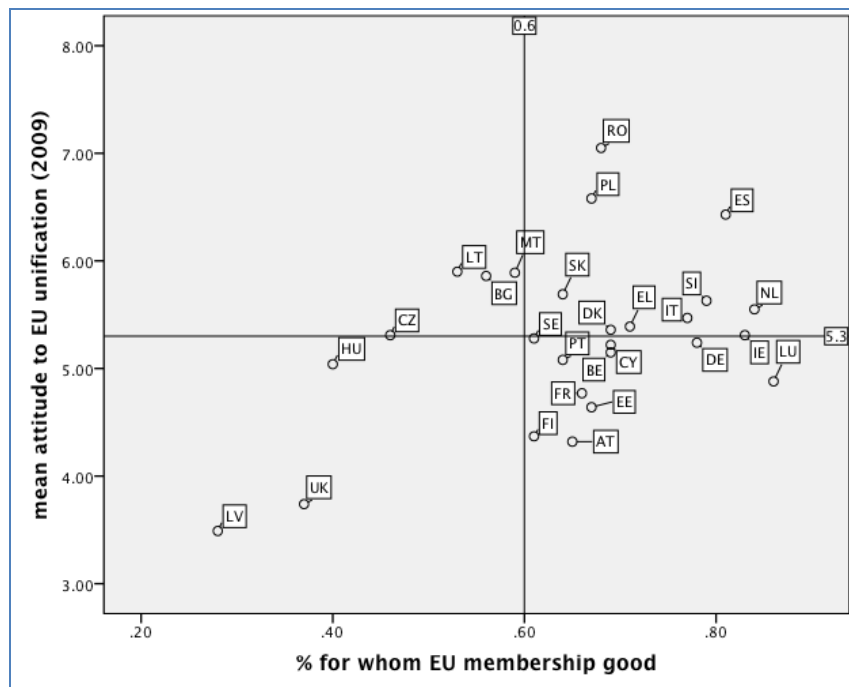


Figure 7: Citizens' perception of EU unification and membership

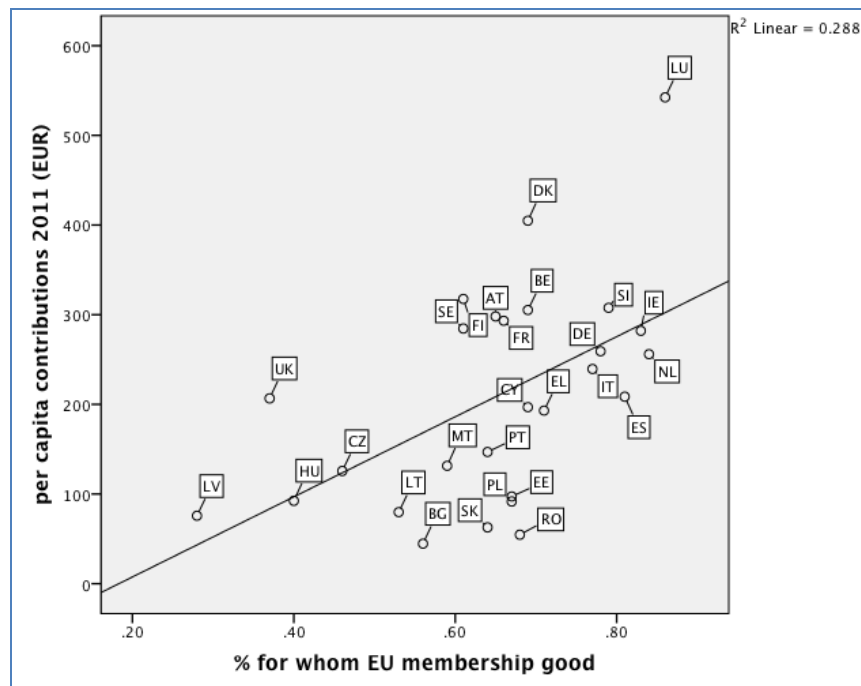


Figure 8: Contributions by perception

There are two possible conclusions: either the EU's peoples are happy to contribute in proportion to their wealth to the EU budget, or they are unable to make this connection and this correlation is spurious. The one Eurobarometer of 2008 (Flash no. 234) that asked respondents to evaluate regional policy comes to equally contradicting conclusions. Overall, 85 per cent of citizens agreed that EU Regional Policy should primarily target the poorest regions; approval was lowest but still very high in Austria (77 per cent), Denmark (79 per cent) and the Czech Republic (80 per cent) (ibid. 13–4). Nevertheless, 58 per cent also thought that the EU should help *all* its regions; only in Portugal and Spain (two “traditional” net recipients) was a majority of the view that the EU should focus on the poorest regions exclusively (ibid. 14). Finally, at the regional level, Osterloh (2011: 20–1) finds that the more *both* region *and* country benefit from structural funds, the more its citizens support EU membership, controlling for education, ideology, income, and duration of a citizen's country's EU membership, amongst others. In particular, “an increase of per capita transfers [to one's region] by 100 Euro increases the probability of being supportive of the EU to the extent of 11%” (Osterloh 2011: 19–20), and “being a direct recipient of structural funds increases the probability of supporting the EU by 13.2%” (Osterloh 2011: 27). Crucially, though, “spill-over within the countries” (Osterloh



2011: 29) makes the nation-level citizenry in general more supportive of the EU.

#### 4. Comparative Reflections

Comparing the data on Switzerland and the EU, several observations can be made. The findings on Switzerland are much clearer in pointing to the existence of inter-cantonal solidarity and its direct link with fiscal equalisation. The vast majority of Swiss people and cantons supported the new financial equalisation system in 2004. The three cantons that voted against the new system did so not because they were generally against any form of equalisation and redistribution, but because they were net-contributors that had to contribute the most to the equalisation mechanisms and received no (Zug) or only little (Schwyz and Nidwalden) support. However, the fact that other cantons whose contributions would also be higher than their gains voted in favour of the NFA demonstrates the existence of strong bonds of solidarity and the recognition among Swiss citizens that some form of fiscal equalisation should exist to ensure equal opportunities across the country.

Moreover, while the three cantons that voted against the NFA are German speaking and predominantly Catholic, the fact that other cantons – German, French and Italian speaking as well as both Protestant and Catholic ones – voted in favour of the new fiscal equalisation scheme demonstrates that the recognition of solidarity amongst cantons cuts across established cleavages. Probably a major reason why so many people voted in favour of the NFA was the fact that it was carefully “packaged” to ensure most cantons would profit from it (hence the three pots) and that especially the bigger cantons would be in favour of it, creating thus not just a cantonal but also a popular majority (Schaltegger and Frey 2003, 253).

Our discussion and data on the EU are less clear. This has to do with the fact that the EU, unlike Switzerland, never had a referendum on Regional Policy or fiscal equalisation. Therefore, conclusions remain limited. Nevertheless, we can clearly see that most citizens believe their country’s membership in the EU to be a good thing. There is also both general support for the EU’s Regional Policy and a specific positive perception of the EU in recipient regions, although data on this are relatively sparse. Clearly, support for the EU is related to direct benefits from membership in the EU, be they Regional Funds, more



political prestige or an improvement of a country's security. Furthermore, the strong support for Regional Funds allows us to conclude that there is a general awareness among European citizens about the need for fiscal equalisation, which furthermore seems to “spill-over” from the regional to the national realm. While there might not (yet) be a EU “togetherness”, a certain degree of implicit solidarity amongst the EU's constituent units can nevertheless be observed when interpreting the data.

Are there general lessons to be learnt from this comparison and what implications does our analysis have for inter-territorial solidarity within the EU? The first lesson is that there is a direct link between solidarity and fiscal equalisation and that the two reinforce each other. We have shown this in our analysis of Switzerland, but even the more limited analysis of the EU has demonstrated that citizens support the EU if they benefit from it, and that they are able to understand the need for fiscal equalisation in a complex multi-level system such as the European Union.

The second lesson is that the success of both fiscal equalisation mechanisms lies in the fact that many profit, while there is only a small number of “losers” – in the case of the EU, at the state-level there are literally none! This means that one of the reasons why people support the EU's structural funds across the Union and voted in favour of the NFA in Switzerland is because their canton/state would profit from it in one way or another.

A third lesson is the obvious need for constant re-negotiation and flexibility. Both within the EU and its Member States, but also among the Swiss cantons and between the Swiss cantons and the Confederation, there is a permanent dialogue about the arrangements for fiscal equalisation. Be it through regular budget debates or as part of specific reform packages, fiscal and economic conditions change and adjustments are therefore frequently required. However, this dialogue also ensures the best use of funds and is important, because it gives fiscal equalisation and therefore the whole polity more legitimacy. Debates – or “deliberation”, for Besson (2007) – are what ultimately make the virtuous circle of solidarity, equalisation and legitimacy turn.

This brings us back to our theoretical discussion at the beginning. While we have stipulated that solidarity is a prerequisite for fiscal equalisation and fiscal equalisation in turn strengthens solidarity, it is important to emphasise that the existence and re-adjustment of fiscal equalisation gives polities such as Switzerland and the EU further legitimacy. If people feel that their needs are addressed and that policy decisions have a



positive long-term impact, then they are more likely to support policies and accept tough decisions by elites. It comes as no surprise therefore that access to Regional Funds is one of the main reasons why other countries want to join the EU. Thus, fiscal equalisation contributes not only to economic development, but also to creating a “factual solidarity” amongst different territorial communities.

Going back to theories on comparative federalism and federation, what can be learnt from our comparison is therefore not that fiscal equalisation is the answer to all problems of legitimacy and democratic deficits. However, fiscal equalisation, if designed properly, strengthens solidarity and this in turn increases the legitimacy of the overall political system. In that sense, the current fiscal crisis within the EU might well function as a trigger to strengthening inter-territorial solidarity through more explicit redistributive policies. What differentiates the conditions for these from a classic understanding of nation-state building is that instead of being inter-personal, solidarity now “only” needs to be inter-territorial, given that EU Member States are themselves sufficiently legitimated to ensure that the other two types of solidarity – inter-personal and inter-group – are operating within them in a complementary fashion.

## 5. Conclusion

This article has tried to shed some light on the complex and dynamic relations between territorial solidarity, fiscal equalisation and legitimacy in multilevel settings. We have compared two political systems: While Switzerland benefits from a high degree of solidarity and legitimacy, which together were able to make a reform of its fiscal equalisation become overwhelmingly approved (Braun 2009), in the EU equalisation is formally vertical (from the EU to the regions) but factually horizontal (inter-state payments), making it both difficult and contentious to compare each individual member’s costs and benefits.

Of the many conclusions that we have already drawn, only the most important deserves to be repeated here: to be able to contribute to the legitimacy of a federal political system, fiscal equalisation needs to address inter-territorial differences and allow for an agreement on how best to transform abstract solidarity into specific benefits. For this process to work in the EU, three conditions need to be fulfilled. The EU would first have to completely overhaul its intricate system of inter-territorial funding. This should include new criteria for



regions being awarded funding and a more direct link between those who contribute and those who receive to strengthen horizontal solidarity amongst regions and countries.

Second, to alleviate tensions arising from this new situation, the EU would need to increase its own budget. An efficient and legitimate system of fiscal equalisation that produces “win-win situations” is expensive, as has been demonstrated in the case of Switzerland. Finally, the EU should allow its constituent units to bindingly express their consent. While the data used for the EU reveal strong support for EU Regional Funding, linking one of the biggest success stories of EU integration to people’s perception of the overall polity would not only increase the legitimacy of the Union, but would also allow people to recognise the positive effects of their country’s membership in the EU. The paradox is, of course, that all three steps require a prior commitment to “make sacrifices”, i.e. an initial degree of inter-territorial solidarity. Nevertheless, the current fiscal crisis might provide exactly such an opportunity and thus create a “critical juncture” in which structural constraints are temporarily relaxed to allow for the kind of agency that Barroso himself emphasised.

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<sup>I</sup> Of course we are also aware of the differences between Switzerland and the EU, in particular the fact that the EU is neither a state, nor a mono-national polity (Dardanelli 2008). However, for the purposes of this paper and its particular focus on fiscal equalization, we believe that both similarities and differences in structures, aims and implementation of fiscal equalization allow for a useful comparison.

<sup>II</sup> On the Swiss cantons as “cantonal democracies” cf. Vatter (2002).

<sup>III</sup> In the broad sense as defined by Watts (1996: 6–7).

<sup>IV</sup> See, amongst many others, the *Neue Zürcher Zeitung* of 9 October 2012, p. 5; 15 October 2012, p. 3; and 18 July 2012, p. 5, as well as 6 February 2013, p. 3, respectively

<sup>V</sup> Switzerland has four official languages: German, French, Italian and Romansch. The majority of Swiss speak German, followed by French. Italian is spoken only in Ticino and some areas of Graubünden; the latter is also the only canton in which Romansch is spoken.

<sup>VI</sup> The religious cleavage divides cantons with a protestant majority and cantons with a catholic majority, and leaves only a few bi-confessional cantons.

<sup>VII</sup> E.g. by Zurich, Zug or Schwyz: cf. *Neue Zürcher Zeitung* of 20 October 2012, p. 11; but also by recipients like Berne: cf. *Tages-Anzeiger* of 14 October 2012.

<sup>VIII</sup> We shall use “structural funds” and “regional policy” interchangeably, referring to the sum total of money disbursed via the European Regional Development Fund (ERDF), the European Social Fund (ESF), the Cohesion Fund and for projects in European territorial cooperation as well as regional competitiveness and employment (cf. Evans 2004, 2).

<sup>IX</sup> This was the case until the bailouts for Greece, Ireland, Portugal and Spain. Since then the EU Member





States have set up the ESM, which casts a form of horizontal financial equalization to some extent. However, the bailouts for some Eurozone countries are not given as grants but as loans.

<sup>x</sup> Source: Folketing EU Information Centre, at [http://www.euo.dk/euo\\_en/spsv/all/79](http://www.euo.dk/euo_en/spsv/all/79) (last updated 15 February 2012, last accessed 12 October 2012). Contributions include only individual countries' contributions in the form of own resources; administration costs not included in EU expenditures. Method: a) proportion of individual country's contribution of total contribution of VAT and GNP; taken to calculate b) the amount Member State should receive from the EU if there were to be a balance between payments and receipts between the Member State and the EU; c) amount country actually receives from EU minus b) and minus individual country's contribution to financing the British rebate; d) divided by population (EUROSTAT).

<sup>xi</sup> Source: EES 2009; variables: q80 (respondent's attitude to European unification): from 0 = "unification has already gone too far" to 10 = "unification should be pushed further"; and q79 (EU membership good or bad): 1 = "good thing", 2 = "bad thing", 3 = "neither".

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