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Article

# The Coexistence of Fiscal Sovereignties: The Post-Pandemic European Union in Comparative Perspective

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## Abstract

Thanks to the recovery fund Next Generation EU, the EU considerably increased the size of its fiscal capacity by increasing its borrowing power. Yet, the post-pandemic EU has left the key issue of how to distribute fiscal sovereignty across the EU and the member states unsolved. Departing from influential concepts in the political science literature, this article argues that we still lack a thorough analytical framework to operationalise the coexistence of two fiscal sovereignties—the fiscal sovereignty of the centre (here, the EU) and the fiscal sovereignty of the units (here, the member states). By resorting to comparative federalism, the article first operationalises fiscal sovereignty as the power to collect, administer, and spend resources. A level of government (the centre or the units) is fiscally sovereign if it can decide on its revenues, the administration of its resources, and its expenditures alone or together with the other level of government (what I call “fiscal self- or co-determination”). The coexistence of fiscal sovereignties becomes impossible if one level systematically and unilaterally encroaches upon the other (“fiscal out-determination”), as is still the case with the post-pandemic EU. On the contrary, in a union of states by aggregation like the EU—namely, Switzerland—the centre (Confederation) has its own fiscal powers, while the units (cantons) retain most of their fiscal sovereignty: The coexistence of fiscal sovereignties is thus possible. The article concludes by outlining which “fiscal features” of the Swiss system could not work in the EU and which could instead potentially work.

## Keywords

comparative fiscal federalism; European Union; fiscal capacity; fiscal regulation; fiscal sovereignty; Switzerland

## Issue

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## 1. Introduction

This article deals with the distribution of fiscal sovereignty between the EU and its member states (MSs) after the adoption of the recovery fund Next Generation EU (NGEU) during the Covid-19 pandemic. Under NGEU, the European Commission can borrow an unprecedentedly high amount of money and distribute funds to the MSs under conditionality. This borrowing capacity was made possible by not only raising the own resources’ ceiling of the EU budget from approximately 1.2 to 1.4% of the EU’s MSs’ combined gross national income (GNI) but also by adding a temporary increase of 0.6% of EU GNI to the Council’s own resources decision to cover the EU’s liabilities when borrowing on international cap-

ital markets (Council Decision of 14 December 2020, 2020). In addition, the EU planned new own resources for the EU budget. Some part of the literature considers these steps a paradigmatic change through which the EU moves closer to becoming a proper fiscal union. Other authors are more cautious and stress that NGEU is a temporary programme that lasts until 2026 and does not structurally change the EU budget, which remains, for more than 60%, dependent on transfers from the MSs.

The political science literature—to which this article primarily seeks to contribute—has adopted a number of useful concepts, such as fiscal capacity, fiscal regulation, and fiscalisation, to assess the changes that EU fiscal integration underwent over time, including after NGEU.

Thus, while before the pandemic the EU was considered to have strong fiscal regulation and weak fiscal capacity, the literature has stressed that the post-pandemic EU fiscal capacity has become larger in size and more diversified in composition. Yet, it is still uncertain which type of fiscal integration the EU will pursue after the end of 2023 (when the Stability and Growth Pact [SGP] re-enters into force) and after 2026 (when NGEU expires). Importantly, the EU has left the crucial issue unsolved about how to distribute fiscal sovereignty across the EU and the MSs, and how to organise the coexistence of two fiscal *sovereignties*—the fiscal sovereignty of the EU and the fiscal sovereignty of the MSs.

This article argues that the existing analytical concepts are ill-equipped to deal with this crucial issue for two main reasons. First, they focus on specific constitutive elements of EU fiscal integration, such as borrowing, spending, or regulatory power. Second, they often refer to the fiscal power of either the EU or the MSs, without approaching them as part of a system in which fiscal sovereignty is distributed between the two levels of government. Hence, so far, we lack an analytical framework that brings together the different constitutive elements in order to come up with the operationalisation of the coexistence of fiscal sovereignties. This is surprising and problematic because the EU is currently in a “fiscal limbo”: It has significantly changed compared to the time prior to the pandemic but it has not yet set the next direction. How many new fiscal powers will the EU get (fiscal sovereignty of the centre [FSC]) and how will this impact the MSs (fiscal sovereignty of the units [FSU])?

Against this background, the article first develops a new analytical framework that allows us to systematically and thoroughly assess which fiscal powers each level of government (EU and MSs) has and how the two fiscal sovereignties coexist. By building an innovative “fiscal sovereignty toolkit,” the article extends and complements the existing analytical concepts which provide only a partial and incomplete picture of the distribution of fiscal sovereignty. Then, the article applies the new analytical framework to answer the following research questions: How does the EU organise the coexistence of two fiscal sovereignties after the Covid-19 pandemic? Are we still in a context of no fiscal sovereignty of the EU and constrained fiscal sovereignty of the MSs?

Afterwards, I investigate the coexistence of fiscal sovereignties in unions of states through federal comparison by asking: How does a union of states by aggregation like Switzerland make the FSC (the Confederation) coexist with the FSU (the cantons)? Unlike another case of union of states by aggregation which is the United States, Switzerland has been compared less often to the EU. Yet, as a strongly decentralised union of states, Switzerland resembles the EU and can thus offer useful insights.

The article is organised as follows. Section 2 reviews the existing literature and shows the gap that the article aims to fill. Section 3 presents the analytical framework

developed to operationalise the coexistence of two fiscal sovereignties. Then, Section 4 applies the framework to the post-pandemic EU after the adoption of NGEU. Based on this analytical framework, Section 5 analyses the coexistence of fiscal sovereignties in Switzerland. Section 6 compares the EU to Switzerland. The article concludes by outlining which “fiscal features” of the Swiss system could not work in the EU and which could instead potentially work.

## 2. Research Gaps and Contribution to the Existing Literature

The aim of this article is to contribute to the political science literature on EU fiscal integration through the lens of comparative federalism. A rich political science literature exists on EU fiscal integration. This literature is centred on the influential distinction between fiscal regulation and fiscal capacity (Genschel & Jachtenfuchs, 2013). Fiscal regulation means the ability of the EU level to adopt binding legal rules that regulate the discretion that MSs retain in their spending policy. Prominent examples are the well-known 3% ratio of deficit to gross domestic product (GDP) or the obligation to submit the draft of the national budgetary law to the European Commission for approval. Fiscal regulation implies that MSs retain their fiscal powers, which are, however, constrained by the EU fiscal rules (Zgaga et al., 2023). The EU, instead, has only a weak fiscal capacity, defined as the ability to collect and spend resources—either directly at the EU level or through transfers to the MSs. Since the creation of the Economic and Monetary Union, MSs have pursued fiscal integration through regulation as a way to retain their fiscal sovereignty (Buti & Fabbrini, 2023). As a result, the EU’s fiscal capacity has remained weak: Until today, the EU budget is very small (around 1.4% of EU GNI) compared to the budget of consolidated federations such as the United States or Germany (Bauer et al., 2017).

“Fiscal regulation” and “fiscal capacity” have been explicitly or implicitly applied to explain the development of EU integration through crises. The EU has approached the euro crisis by strengthening fiscal regulation, while only slightly strengthening its fiscal capacity through weak financial support mechanisms (Howarth & Quaglia, 2021). There is general agreement that the EU’s response to the Covid-19 pandemic marked an unprecedented increase in the EU’s fiscal capacity (F. Fabbrini, 2022). Learning from the shortcomings in dealing with the euro crisis, the EU mobilised large resources to help MSs recover (Ladi & Tsarouhas, 2020). However, scholars have pointed out that, although significant, the NGEU does not represent a “paradigmatic change” to EU fiscal integration comparable to what the Hamiltonian moment was for the United States. Through the general escape clause, the EU has suspended some provisions of the SGP until the end of 2023, but other parts of fiscal regulation are still in place as part of the conditionality related to the use of the NGEU (Schelkle, 2021).

The article identifies three main gaps in this literature. Firstly, the key terms “fiscal regulation” and “fiscal capacity” are only broadly defined but their constitutive elements have not been properly spelt out and operationalised. For example, which type of fiscal regulation can we concretely distinguish (numerical rules, expenditures rules, rules on providing information about the national budgetary law, debt issuance, etc.)? Similarly, what does “fiscal capacity” entail in terms of the amount and composition of resources that the EU can collect and on which items it can spend money? Secondly, the two terms focus, on the one hand, on the power to collect and spend resources, and, on the other hand, on the power to regulate, but they neglect the important component of administering the resources and implementing the rules. Thirdly, fiscal regulation and fiscal capacity do not account for the institutional dimension. To analyse and explain EU fiscal integration, we need to outline which institutions play which role in each constitutive element of both fiscal regulation and fiscal capacity. If an intergovernmental institution like the Council is the crucial decision-making actor on most of these constitutive elements, then EU fiscal integration will be subject to the influence of competing national interests. Fourthly, and crucially, fiscal regulation and fiscal capacity do not provide information about the EU’s fiscal sovereignty. Stronger fiscal regulation will further limit MSs’ fiscal sovereignty, but this does not tell us much about EU fiscal sovereignty. Similarly, the EU can increase the size of its fiscal capacity but if the additional resources that it can collect and spend mainly come from national transfers, then the dependence on the MSs persists (Woźniakowski et al., 2023). To overcome the limitations of the term fiscal capacity, Woźniakowski (2022, p. 10) coined the concept of fiscalisation, defined as “a process through which a certain level of government (supranational/federal/central) expands its power to raise its own sources of revenue, and in so doing it decreases the level of vertical fiscal imbalance,” namely the dependency on national transfers. This is a useful concept that underlines that, in order to be independent of the MSs, a central level of government like the EU needs to collect resources that legally and undisputedly belong to it (and not to the MSs). Yet, the concept points to the FSC but does not include information on the FSU.

In light of the above, this article argues that we need an analytical toolkit—which the literature lacks—to perform an in-depth and comprehensive analysis of the EU’s fiscal powers *in relation to the fiscal powers of the MSs*. To do so, the article resorts to comparative federalism.

### 3. Operationalising the Coexistence of Fiscal Sovereignties

#### 3.1. Analytical Framework

Following Riker (1975), a federation is a political system made of two main levels of government—the federal

centre or federation and the constituent units or units—each of which has some policy competences for which it bears exclusive responsibility. Prominent examples of federations are the United States, Canada, Germany, and Switzerland. The key feature of federations is that sovereignty is vertically divided and shared across the two levels of government (S. Fabbrini, 2019). The federal division of sovereignty also applies to fiscal sovereignty. In its simplest form, in a federation, fiscal sovereignty can be defined as the ability of a level of government to raise and spend a significant amount of its own resources, without depending on another level of government for its financing (Zgaga, 2023).

Federations are systems of dual sovereignty (Rodden, 2006), where two fiscal sovereignties coexist: the FSC and the FSU. This means that both the centre and the units have the ability to obtain revenues and perform expenditures to finance the exercise of their competences (Kelemen, 2004). For the units, fiscal sovereignty is the quintessence of their sovereignty and serves for national spending. For the centre, it serves three main purposes: creating stabilisation policies, supplying public goods, or providing transfers to the units (Buti & Fabbrini, 2023). Elements of the two fiscal sovereignties are connected and partially overlap. For example, the revenues from the income tax may be shared across the centre and the units.

But what are the constitutive elements through which to operationalise two fiscal sovereignties? Based on the political science literature on comparative fiscal federalism (see, for instance, Hallerberg, 2006; Hueglin & Fenna, 2015; Rodden, 2006; Shah, 2007), this article proposes an essential operationalisation that includes three fundamental fiscal powers from which all the other related fiscal powers derive: collecting resources, managing (administering) resources, and spending resources. Each of these powers applies to both the centre and the units. Each of them has a number of *constitutive elements*.

I start with FSC. With regard to revenues, the *amount* refers to how many resources a level of government can collect. The amount is connected to the competences the centre has, which can vary based on the political system. Hence, in order to compare the amount of resources that the centre has regardless of its competences, the article considers the revenues of the centre as a share of the GDP. This can be regarded as one measure of the degree to which the centre controls the economy’s resources. The *composition* of revenues indicates the type of resources that the centre can raise. The main revenues usually come from taxes (personal income tax, wealth tax, social security contributions, value-added tax [VAT], excises, corporate income tax, etc.). An important factor concerns the *ownership*, i.e., to whom the resources belong. This can be represented by the share of resources that the centre owns over the resources that the units transfer to it. If the centre receives many transfers, it depends on the units for its financing. Transfers

are not resources owned by the centre because they originally belong to the units. Resources consisting of transfers are first generated by—and then made at disposal through—the units. Taxes are instead an example of revenue ownership because there is agreement—within the federation—that specific revenues formally (for instance, based on the constitution) belong to the centre and not to the units. Besides revenues, an important element pertains to the extent to which the centre is able to *administer* its revenues without relying on the units. In terms of expenditure, we distinguish how many resources the centre directly spends and on which items. Other than *ordinary expenditures*, the centre can transfer resources to the units, for instance as part of a so-called *equalisation mechanism* aimed at reducing disparities across the units. Expenditure can also take place in *extraordinary cases* and/or through the issuance of *debt*. In terms of FSU, the same indicators apply to revenues (amount, composition, and ownership) and the management of resources as for FSC. With regard to expenditures, besides ordinary expenditures, units may transfer resources to the centre and/or to other units. Moreover, they may issue debt.

Once I have provided an essential operationalisation of FSC and FSU, the key question is under which conditions each of the two exists. I argue that fiscal sovereignty (be it FSC or FSU) exists if a level of government can decide on each of the above constitutive elements of its fiscal sovereignty—alone or together with the other level of government (fiscal self- or co-determination)—and is not subject to unilateral decisions (meaning decisions that it cannot substantially change) by the other level of government (fiscal out-determination). Hence, this article provides a requirement for fiscal sovereignty based on institutional governance. Federations have institutions representing the interests of the centre or the federation as a whole (its citizens) and institutions representing the units. For example, in Switzerland, the National Council represents the Swiss citizens, while the Council of States represents the units (the cantons). Fiscal self- or co-determination implies that each level of government has full decision-making—or shares decision-making—on all elements of its fiscal sovereignty through the institutions that represent it. For instance, in Germany, the federal legislative (Bundestag) and the federal executive (Bundesregierung), as institutions representing the German federal centre (Bund), decide on the FSC, with the legislative institution representing the Länder (Bundesrat) being involved in the decisions but being unable to unilaterally determine the FSC.

But when, then, can two fiscal sovereignties (FSC and FSU) coexist? When they display fiscal self- or co-determination, and not out-determination. In other words, each level of government needs to have a say on each constitutive element of its fiscal sovereignty. If out-determination applies to one or both levels of government, the coexistence of fiscal sovereignties becomes impossible because one level systematically and unilaterally

encroaches upon the other. This is in line with federalism's core assumption of two levels of government that coexist without any of the two dominating, meaning restricting the competences, of the other.

### 3.2. Case Studies, Data, and Methodology

The analytical framework of the coexistence of fiscal sovereignties has been designed for federations. Federations differ in the way in which they allocate fiscal sovereignty to the centre and to the units. Some federations, such as Germany and Austria, are overall centralised and, thus, grant strong fiscal sovereignty to the centre. In other federations, the units retain strong fiscal sovereignty while the centre is fiscally weak. This is the case of federations that were historically born through the aggregation of states that had previously been independent for a long time. In these systems, also called unions of states by aggregation, since “the states or cantons were the source of the process of federalization, they tried to retain as much power as possible from their previous independent status” (S. Fabbrini, 2017, p. 583). In these systems, the centre has only a few, enumerated competences. Examples of unions of states are the United States and Switzerland.

What about the EU? Formally, it is not a federation. Yet, it is a union of states by aggregation (S. Fabbrini, 2019) because it has two distinct levels of government (EU and MSs), each with its own exclusive competences, but at the same time, it remains decentralised, if one considers the “competences not conferred upon [it] in the treaties remain with the member states” (Consolidated Version of the Treaty on European Union, 2016, Art. 4). Hence, it is possible to apply the new analytical framework in order to assess the post-pandemic coexistence of fiscal sovereignties in the EU.

By adopting the most similar comparative research design (Berg-Schlosser & De Meur, 2009), the article compares the coexistence of fiscal sovereignties in two unions of states by aggregation: the EU and Switzerland. By doing so, it goes beyond the well-established literature comparing the EU and the United States (for an overview, see Tortola, 2014). Switzerland is one of the most decentralised unions of states by aggregation worldwide. As such, it can potentially deliver particularly useful insights to the EU as a similarly very decentralised system. The EU and Switzerland have been the object of comparison in the past (for an overview, see Hueglin & Fenna, 2015). Yet, this article brings in what, to the best of my knowledge, is a so-far unexplored comparison between the EU and Switzerland because it concerns the coexistence of fiscal sovereignties.

The article does a systematic content analysis of EU treaties and legislation as well as policy documents that are relevant to the EU's fiscal sovereignty. With regard to Switzerland, I consider the constitutional provisions on fiscal powers. In both cases, I complement these sources with data on revenues and expenditures. Systematic

content analysis is a methodology used to carry out descriptive inference (King et al., 1994) from the data, i.e., to scientifically extract information from them which provides us with a deeper knowledge, in this case with regard to the EU's fiscal sovereignty. Systematic content analysis takes place through coding, i.e., by assigning conceptual labels (categories) to text passages (segments) that foster an understanding of the data. This article adopts the constitutive elements of fiscal sovereignty presented in Section 3.1 as deductive categories, i.e., categories developed from the research question and from existing literature (Mayring, 2014). I use them to assess the EU's fiscal sovereignty and to perform comparisons with Switzerland. The research is not historical: I consider fiscal sovereignty in the three cases at the time of writing.

#### 4. Fiscal Sovereignties in the Post-Pandemic EU

I start with the fiscal sovereignty of the EU. Through the recovery fund NGEU, MSs in the Council unanimously authorised the Commission to borrow more money (€806.9 billion, in current prices) than ever before in the history of the EU's crisis management. Hence, the EU's fiscal capacity grew in size, moving from the Multiannual Financial Framework (MFF) worth €1,287 billion prior to the pandemic to €2,018 billion, made up of the MFF 2021–2027, equal to €1,211 and NGEU equal to €806.9 billion. If the annual EU budget is equal to roughly 1.4% of the EU's GNI, NGEU is “the equivalent of 6% of 2020 EU GDP” (Freier et al., 2022). Hence, although NGEU represents a significant addition to the MFF 2021–2027, its resources are temporary.

Before NGEU, the ceiling of own resources that the EU could annually allocate to cover appropriations for payments and commitments could not exceed, respectively, 1.23% and 1.29% of the sum of the MSs' GNI. To make NGEU possible, the EU's own resources ceilings were raised to 1.40% for payments and 1.46% for commitments, and a temporary increase of 0.6% of EU GNI was introduced until the year 2058 to cover the EU's liabilities when borrowing on international capital markets to address the consequences of the Covid-19 pandemic (Council Decision of 14 December 2020, 2020).

In January 2021, a new own resource based on non-recycled plastic waste was introduced. Moreover, the Commission proposed three other own resources as revenues for the EU budget: They are based on the EU Emissions Trading System, on the Carbon Border Adjustment Mechanism, and on the reallocated profits of very large multinational companies (European Commission, 2021). Even if these resources were introduced, however, the EU budget would remain small compared to the budget of consolidated federations. In 2021, revenues of the EU budget were equal to approximately €240 billion (in current prices; European Commission, 2023); the EU's GDP in 2021 was equal to €14,500 billion (Eurostat, 2023b). Hence, the revenues of the EU budget in 2021 were equal to 1.65% of the EU's GDP.

In comparison, the 2021 ratio of government revenues as a percentage of GDP was 32.2 in Austria, 13.1 in Germany, 11.6 in Switzerland, and, on average, 22.1 in the European MSs (Eurostat, 2023a). With regard to a revenue source, in 2021, out of the EU's €240 billion total revenues, €140—equal to 58%—consisted of national contributions. The other revenues (42%) were customs duties, a rate of the VAT collected by MSs and a contribution based on the non-recycled plastic packaging waste. As a result, the post-pandemic EU budget remains dependent on transfers from the MSs. During the negotiations of the MFF 2021–2027, MSs tried to limit their contributions to the budget and keep its overall size small.

Most (about 80%) EU resources are jointly managed by the Commission and national/regional authorities; the rest (roughly 20%) are directly managed by the Commission (European Commission, 2023). Hence, owing to its small public administration, the EU depends on its MSs for the management of its fiscal capacity. Under NGEU, the Commission was empowered because it assesses the National Recovery and Resilience Plans through which MSs explain how they spend resources from the Recovery and Resilience Facility (RRF), the largest part of NGEU, but the final decision on the disbursement of funds remains within the Council.

The maximum amount of allowed EU expenditures under the MFF is slightly lower than the revenue ceiling in order to avoid MSs having to contribute more than the own resources ceiling. In the face of unforeseen events, resources of flexibility and special instruments can be spent also beyond the expenditure ceiling of the MFF, but they cannot exceed the own resources ceiling. The EU spends resources in different policy areas organised under the current headings: the single market, cohesion, environment, migration and border management, security and defence, neighbourhood and the world, and European public administration. Due to its small public administration, the EU transfers most resources to the MSs rather than directly spending them at the European level. The “transfer capacity” also makes up the RRF, worth €723.8 billion out of the overall €806.9 billion of NGEU. The no-bailout clause prevents transfers from the EU to the MSs or between MSs in order to finance national debts or in the form of a large-scale equalisation mechanism (see Consolidated Version of the Treaty on European Union, 2016). Cohesion funds aim to reduce disparities between European regions but are not targeted at the MSs as a whole.

The Commission can borrow resources, as it did, for instance, recently to support Ukraine under the Macro-Financial Assistance+ programme (€18 billion); or in the past through the Support to Mitigate Unemployment Risks in an Emergency (€100 billion). However, to borrow large-scale resources like NGEU, or to extend NGEU by a similar amount after 2026, the unanimous agreement of the MSs and the subsequent ratification by national parliaments is needed. This is because NGEU is part of the so-called own resources decision. The own resources

decision is the Council's decision on the amount and composition of resources that the EU budget can collect and spend. Although the own resources decision foresees an initial proposal from the Commission and the opinion of the European Parliament, the Council retains the last decision-making power.

NGEU does not alter the fiscal sovereignty of the MSs as operationalised in this article. The MSs retain full discretion on the amount and type of revenues they can collect. Their expenditures are quantitatively limited by the deficit and debt to GDP rules of the SGP, currently suspended until the end of 2023. Yet, MSs retain full discretion towards what they can spend resources on, with the obligation set by the treaties to report large plans for investments and debt issuance to the Commission. Moreover, in order to receive RRF funds, MSs need to comply with the so-called Country-Specific Recommendations that the Commission issues to them under the SGP (F. Fabbrini, 2022). Under the RRF, those MSs most severely hit by the Covid-19 pandemic, such as Italy, Spain, France, and Germany, received unprecedented resources not only in the form of loans but also grants (money not to be repaid).

## 5. Fiscal Sovereignties in Switzerland

Switzerland has two main levels of government: the centre (Confederation) and the units (cantons). The country has a strongly decentralised organisation of power because the cantons are sovereign insofar as their sovereignty is not constrained by the constitution (Mueller & Fenna, 2022). Switzerland is a federal union that emerged as the aggregation of the previously independent cantons. As a result, the Confederation has only the tasks expressly assigned to it in the Swiss Constitution (see Swiss Confederation, 2022, Art. 42), specifically those "that the cantons are unable to perform or which require uniform regulation by the Confederation" (Swiss Confederation, 2022, Art. 43). Unlike in the EU treaties, in the Swiss Constitution, there is no list of exclusive or shared competences. The distinction exists, but it is spread over the constitution.

I first deal with the fiscal sovereignty of the Confederation. The Swiss Constitution does not have a provision explicitly guaranteeing the Confederation the necessary means to exercise its competences. Since 1941, the cantons have agreed on temporarily providing the Confederation with the power to collect a federal income tax and a VAT with maximum rates enshrined in the constitution. Although such tax capacity has never become permanent, it has been constantly renewed over time—lastly from 2020 to 2035—through popular referenda preceded by a political debate in the country. Thus, formally, the federal income tax, today called direct federal tax (DFT), and the VAT are limited in time. De facto, however, DFT and VAT have become permanent confederal taxes. While the DFT is shared between the Confederation and the cantons, VAT is an exclusively

confederal tax. DFT is levied on the income of natural persons and on the net profit of legal entities. Together, in 2022, both DFT (32.7%) and VAT (34.9%) represented 67.6% of confederal revenues. The other revenues were the withholding tax (5.1%), the mineral oil tax (5.8%), the stamp duty (3.2%), the tobacco duty (2.7%), other tax receipts (9.4%), nontax receipts (5.4%), and extraordinary receipts (2.1%; Federal Finance Administration, 2022). Hence, the constitution assigns a number of specific revenues to the Confederation. These resources encompass the most important (in terms of revenues) taxes, specifically income, corporate, and VAT. The units do not transfer resources to the Confederation. The constitution foresees upper tax rates that the Confederation can levy: up to a maximum of 11.5% on the income of private individuals, up to a maximum of 8.5% on the net profit of legal entities, and a standard rate of a maximum of 6.5% "on the supply of goods, on services, including goods and services for personal use, and on imports" (Swiss Confederation, 2022, Art. 130). Moreover, Art. 128 of the Swiss Constitution enumerates items on which the Confederation has the right to levy taxes. VAT is charged for the acquisition of domestic goods, services, and imports but not exports. The Confederation can legislate on "customs duties and other duties on the cross-border movement of goods" (Swiss Confederation, 2022, Art. 133). Since Switzerland is a case of perfect or symmetric bicameralism, when the Confederation legislates, the agreement of both the National Council (directly elected and representing citizens) and the Council of States (directly elected and representing the cantons) is needed (Swiss Confederation, 2022, Art. 156).

The expenditures of the Confederation in 2022 included social welfare (32.7%), finances and taxes (14%), transportation (13.2%), education and research (9.7%), security (7.9%), agriculture and food (4.5%), international relations (4.7%), and remaining task areas (institutional and financial conditions, culture and leisure, health, protection of the environment and spatial planning, economic relations, 13.2%; Federal Finance Administration, 2022). Art. 126 of the Swiss Constitution foresees a debt brake: The Confederation can borrow and spend to the extent that expected receipts, after taking account of the economic situation, cover expenditures. In extraordinary circumstances, such as natural disasters and recessions, the Confederation can exceed the expenditure ceilings, but this expenditure must be compensated for in the following years. The Swiss budget is jointly adopted by the National Council and the Council of States. The Federal Tax Administration, subordinated to the Federal Department of Finance, is in charge of collecting and managing the revenues of the Confederation. Like the EU budget, the Swiss budget is also a transfer budget, meaning that:

Hardly one-third of the total expenditures of the [Con]federation is used for the tasks of the [Con]federation. More than two-thirds consist of

transfers to sub-national government (cantons and municipalities), the social security funds (old age and war victim pensions, disability insurance) and other semi-autonomous public institutions. (Kraan & Ruffner, 2005, p. 48)

The Confederation may financially support regions that are facing an economic threat (Swiss Confederation, 2022, Art. 103). An equalisation system with the aim of better horizontal (intercantonal) and vertical distribution of resources (Swiss Confederation, 2022, Art. 135.1) is in place. The constitution details the objectives of the equalisation system: It should reduce economic disparities between the cantons, guarantee them a minimum level of financial resources, support those cantons that have particularly strong burdens due to their geographical or demographical situation, encourage intercantonal cooperation, and maintain their tax competitiveness (Swiss Confederation, 2022, Art. 135.2). Both the Confederation and the cantons shall contribute to the equalisation mechanism with the necessary funds (Swiss Confederation, 2022, Art. 135.3), but the Confederation should contribute more.

What about the fiscal sovereignty of the cantons? The Confederation harmonises direct taxes imposed by the three levels of government (Swiss Confederation, 2022, Art. 129). However, the cantons are free to decide their amount and types of revenues—specifically, to set their tax rates. They do not depend on transfers from the Confederation. Given that “the cantons...exercise all rights that are not vested in the Confederation” (Swiss Confederation, 2022, Art. 3), the cantons retain control over potentially all resources not constitutionally assigned to the Confederation. The cantons also retain large discretion on how much they spend and for what. Their capacity to issue debt is not limited by the Confederation. Since Art. 100 of the Swiss Constitution mentions that “the cantons shall consider the economic situation in their revenue and expenditure policies” (Swiss Confederation, 2022, Art. 100), most cantons have adopted debt brake rules. However, unlike MSs in the EU, cantons in Switzerland are not subject to a debt brake rule originating from the Confederation.

## 6. Comparing the Coexistence of Fiscal Sovereignties: The EU and Switzerland

This article argued that the well-established political science concepts of fiscal regulation and fiscal capacity are ill-equipped to analyse EU fiscal integration after the Covid-19 pandemic and the adoption of NGEU for three main reasons. First, they are only broadly defined and their constitutive elements have not been properly operationalised. Second, they neglect the administrative dimension: What do these concepts tell us about how EU resources are managed? Third, fiscal regulation and fiscal capacity do not shed light on the distribution of fiscal sovereignties in the EU.

To overcome the limitations of these concepts, the article operationalised fiscal sovereignty as the power to collect, administer, and spend resources. For each of these powers, it proposed a number of constitutive elements derived from the political science literature on comparative fiscal federalism. Fiscal sovereignty (be it FSC or FSU) exists if a level of government can decide on each constitutive element of its fiscal sovereignty alone or together with the other level of government (fiscal self- or co-determination) and is not subject to unilateral decisions (meaning decisions that it cannot substantially change) by the other level of government (fiscal out-determination).

Based on the involvement of institutions representing the interests of each level of government, FSC and FSU can coexist if each of them displays self- or co-determination, but not out-determination. Each level of government needs to have a say on its own fiscal sovereignty. If its fiscal sovereignty is entirely determined by the other level of government, then the two fiscal sovereignties cannot coexist.

Has the post-pandemic EU evolved towards a condition of coexistence of two fiscal sovereignties? Under NGEU, the post-pandemic EU strongly increased its fiscal capacity. Yet, this is a temporary step. Moreover, the EU budget remains extremely small in relation to GDP also after the introduction of the plastic-based own resource in 2021 and the prospect of new own resources. No proper taxes able to generate significant revenues have been introduced—National contributions still represent more than 60% of budgetary revenues. In addition, the EU transfers most resources to the MSs and directly spends only a small part on proper European public goods. Crucially, also after NGEU, MSs, through the Council, retain the ultimate decision-making power over changing the revenues of the EU: Unanimity among national governments and parliamentary ratification by all MSs is required. Hence, to increase the size of the EU budget or to engage in further large-scale borrowing modelled on NGEU, the institution representing national interests—the Council—is the crucial veto player. The Commission and the European Parliament as institutions representing European interests are involved—the former as proponent of new own resources and the latter in the adoption of the annual budget—but they do not have a say on how many and which resources the EU has at its disposal. At the same time, the fiscal sovereignty of the MSs has not been undermined by NGEU. On the contrary, MSs temporarily retain more discretion in spending thanks to the suspension of the SGP. Moreover, some of them can rely on an unprecedented amount of transfers as part of the RRF. In sum, the post-pandemic EU is characterised by a scenario of substantial FSU and still no proper FSC. Based on our analytical framework, the FSC displays out-determination: The MSs are the key decision-makers on the revenues and expenditures of the EU; notwithstanding the empowerment of the Commission in the management of the RRF, the EU still needs the MSs



when administering most of its resources. Since FSC is subject to out-determination, FSC and FSU still do not properly coexist in the post-pandemic EU. This leaves a fundamental issue with the future of European integration unresolved.

In Switzerland, the constitution assigns specific revenues to the Confederation. The Confederation is also entitled to a portion of revenues from VAT, income, and corporate taxes. Unlike in the EU, in Switzerland, there is no upper revenue ceiling. The Confederation does not depend on the cantons for its financing but resources are allocated to it on a temporary basis (currently, from 2020 to 2035). However, the Confederation can only raise a maximum tax rate specified in the constitution. This still leaves the Confederation with enough resources to spend on a number of public goods, such as transport, education and research, but also a significant amount on social welfare (32.7% in 2022). Yet, like in the case of the EU, most resources are transferred to the units. However, fiscal administration at the central level is more developed than in the EU: The Confederation has its own Federal Tax Administration that collects and manages the revenues of the Confederation.

To change the revenues of the Confederation, a constitutional amendment is required. In order for the referendum to pass, both the cantons and the People (meaning the Swiss citizens) would need to agree. Hence, the crucial difference to the EU is that the units (the cantons) cannot determine the resources of the centre (the Confederation) alone, as it happens with the MSs in the EU. The institutions representing both interests (centre and units) have a say in the financing of the centre (co-determination). The same holds true for the adoption of the budget where both the National Council and the Council of States need to agree.

Hence, this analysis showed that Switzerland is characterised by a scenario of substantial FSU *and* substantial FSC. Based on our analytical framework, the FSU displays self-determination. This is in line with a union of states by aggregation being decentralised systems where most competences lie within the units. Yet, the Confederation has a limited but constitutionally well-defined fiscal sovereignty that allows for self-financing and rules out financial dependence on the cantons. Since FSC is subject to co-determination and FSU to self-determination, FSC and FSU can coexist in Switzerland. The EU can learn something from this.

## 7. Conclusions: Lessons from Switzerland for the EU

The comparative approach of this article does not imply that the EU should become more like Switzerland. This is not only politically unfeasible but also analytically misleading. Each political system has its own peculiarities which cannot simply be “exported.” Hence, there are “fiscal features” of the Swiss system that could not work in the EU, while others potentially could. I will discuss them briefly.

I start with four points on what could not work. First, Switzerland’s unique feature is direct democracy. The people are an important source of representation of the interests of the whole Confederation, next to the National Council. The people also vote—together with the cantons—on the system of revenues of the Confederation. Such a large-scale use of referenda across the EU to vote on the EU’s revenues would be rather politically impossible, or at least it would require time and first be “tested” on less politicised issues. Second, income tax is probably the most sensitive type of tax because it is symbolically associated with national sovereignty and it also generates large revenues. If the EU gets a taxing power, it should start with less sensitive taxes, such as VAT. Third, in Switzerland, the Confederation spends the most on social welfare (32.7% of confederal expenditures in 2022, equal to approximately 30% of the country’s GDP). In the EU, social policy is the responsibility of the MSs which consider it a competence closely related to national citizenship. Fourth, the lack of strict rules on budgetary discipline at the central level to prevent the units from profligate spending would face strong distrust among those European MSs which attach crucial importance to budgetary discipline, especially Germany and the so-called “Frugal Four” countries. In other words, a debt brake at the level of the units as in Switzerland would arguably not be enough in the case of the EU.

What features of the Swiss system could work in the EU? First, if the EU has to increase its source of revenues and get access to taxes, this should be enshrined in the founding treaties—as it occurs in Switzerland with the constitution. Through a “constitutional codification,” some (new) revenues would be legally guaranteed to the EU and, thus, removed from the realm of political negotiations, but this would require a thorough amendment of the treaties. To be sure, the EU treaties also currently provide for legal guarantees on the EU’s financing. However, not only does the EU lack the power to tax but MSs also periodically (at the beginning of the MFF) engage in long and tough negotiations on their contributions to the budget. Afterwards, they are committed to contributing, but before, they seek to minimise their contributions. Second, instead of having (comparatively very low) revenue ceilings, the EU should follow the Swiss example and not limit the maximum amount of overall revenues of the centre, but rather grant the EU access to taxes by clearly fixing upper tax rates. So, for example, the EU could levy up to a fixed maximum rate on the net profit of legal entities, a standard rate on the supply of goods and services and—perhaps in the longer term—a fixed maximum rate on the income of individuals, while MSs would be free to set much higher rates. So, for instance, citizens would pay most of their income tax to their MSs and a small part to the EU. This makes sure that citizens and legal entities mostly remain subject to taxation at the level of the units, but they also still contribute to the financing of the centre, without the units losing

revenues. Third, MSs could grant the EU new revenues on a temporary basis, establishing a term like 15 years in Switzerland (the DFT has been renewed from 2020 to 2035). Hence, the EU could plan its expenditures based on the new resources but, before any renewal, a political debate could take place on how well resources have been used and which resources are needed in the future. Fourth, the EU should grant the institutions representing the interests of the centre the same role as the institutions representing the units when it comes to deciding the amount and type of revenues. This means that the European Parliament and the Commission should co-decide the EU's revenues together with the Council. This would mark the end of the fiscal dependence of the EU on the MSs and would contribute—together with other changes to the status quo—to the coexistence of fiscal sovereignties in the EU.

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### Conflict of Interests

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