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The Spanish Tax Reform: Overview and Lessons

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Fiscal Reform in Spain

Accomplishments and Challenges

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STUDIES IN FISCAL FEDERALISM AND STATE-LOCAL FINANCE

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14. The Spanish Tax Reform: Overview and Lessons

Jorge Martinez-Vazquez*¹

INTRODUCTION

Very few countries in modern history have shown as radical a transformation of society from its political system to its economic institutions and performance as has Spain over the last 30 years. As described in many of the chapters in this volume, the Spanish tax system began an extensive period of reform from 1977 onward, beginning two years after the death of General Francisco Franco. This reform process, which now has been ongoing for the last three decades, has put Spain's public finances on a sound footing and it represents one of the most identifiable key factors behind the "Spanish economic miracle."

This chapter has three main objectives. First, we provide a summary overview of the evolution and performance of Spain's tax system over the last three decades.² Although many of the chapters in this volume have looked at different aspects of the reforms and performance of the system, it is desirable to summarise that performance focusing on several aggregate indicators, which may not have been fully integrated in the previous chapters of this volume. Second, the ultimate test of the performance of the fiscal system of any country is to examine how its citizens feel about it. We do that by looking at how "tax morale" among Spanish citizens changed over this period. Even though the average citizen ended up paying considerably more in taxes, it is quite extraordinary that compliance with these higher tax burdens was in large part voluntary, as reflected by the significant increases in tax morale over the years. This has been a long way to come for a country where as early as 1970s tax evasion was not only rampant but also a socially condoned activity. Over the journey of reform, the average Spaniard's willingness to pay taxes voluntarily increased quite dramatically and citizens became more approving of their government's

fiscal policies. Third, it is fitting to close this volume by extracting some lessons from Spain's experience with tax reform for other countries. In recent times, countries like Argentina and Mexico have unsuccessfully, because of a variety of circumstances and reasons, tried to reform their tax systems. Although every country has its own features and peculiarities which require highly customised tax reform efforts, we believe that Spain's experience can offer some valuable lessons for what to do and what not to do in carrying out successful tax reform in these and other countries.

THE PERFORMANCE OF SPAIN'S TAX SYSTEM

Several dimensions of the performance of Spain's tax system need to be highlighted. Perhaps the most impressive of these dimensions is the consistent increase in tax to GDP ratio over the last three decades (see Figure 14.1). It is important to clarify that there is no unique or most desirable level of tax effort for a country; how much a country decides to tax itself is eminently a political collective decision that reflects society's preferences toward public goods versus private goods, degree of social solidarity, and so on. There is no right or wrong in this decision. However, it is both important and desirable that a country collect in taxes the right amount of income that it wants to spend through public sector budgets. From the beginning of the transition years to democracy after Franco's death there was a wide consensus in the country, as reflected in the Moncloa Pacts, that the country lacked basic public services, welfare programs for population groups in need, and public infrastructure. In short, there was the political will to spend a significantly higher share of national income through the public sector. To maintain economic stability, this desire to expand the public budgets could only be met with sizeable increases in tax effort.

As can be seen in Figure 14.1, Spain did undergo a considerable increase in tax effort. In 1975 total tax revenues as a percent of GDP stood at less than 20 percent. By comparison, at that time, the OECD average country was collecting in tax revenues 31 percent of GDP. By 2002, Spain had converged to the OECD average with total tax revenues representing over 35 percent of GDP. This overall increase in tax revenues had a mirror image in the "buoyancy" of the tax system vis-à-vis GDP. From 1975 to 2002, the buoyancy coefficient of tax revenues (without social security contributions) was 1.6 and that for social security contributions, 1.1. Naturally, there were significant differences in the buoyancy of different taxes. While the buoyancy for the personal income tax over the same period was 2.4, the one for the corporate income tax was only 0.6. In the case of

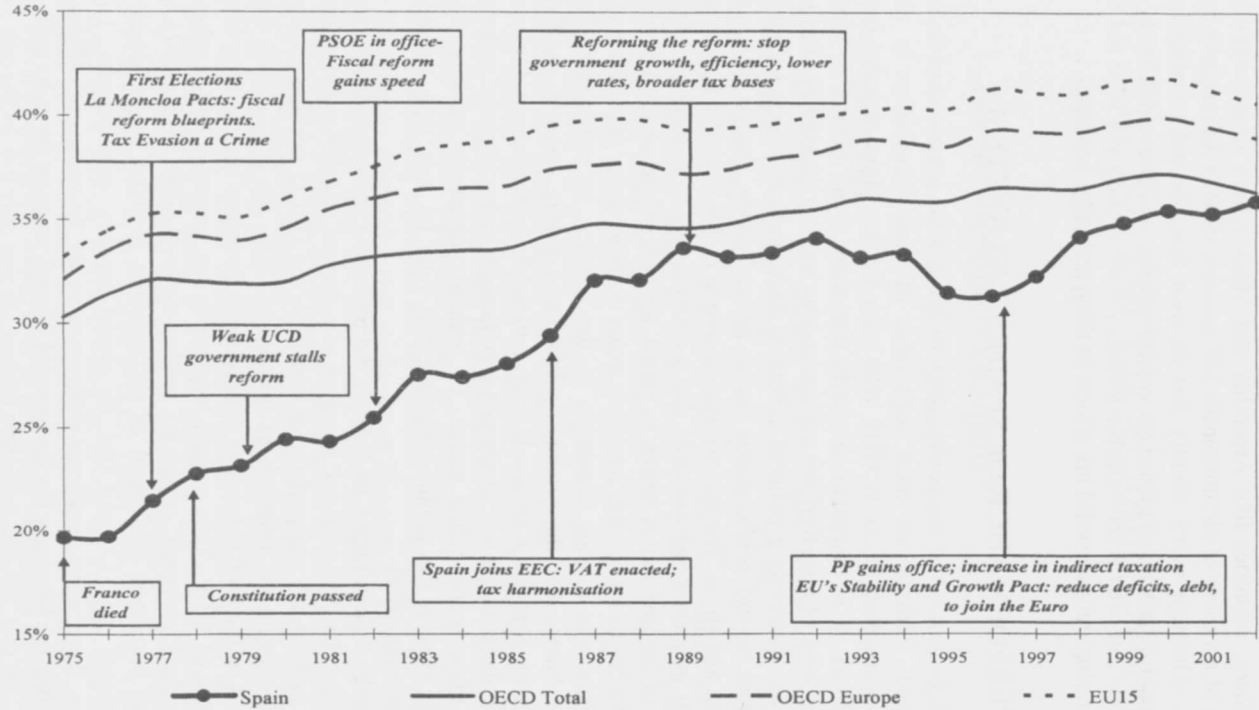


Figure 14.1 Spain's fiscal reform road: selected events (total tax revenue as % of GDP)

indirect taxes, the general consumption tax (VAT) had a buoyancy of 2.3 while that of excise taxes was only 0.3. Taxes on property performed poorly with a buoyancy coefficient of 0.25.

However, as can be seen in Figure 14.1, the rise in tax revenues as percent of GDP was far from steady. At the time of Franco's death in 1975, the Spanish economy was suffering from the aftershocks of the worldwide recession associated with the oil crisis of 1973-74. The critically important Moncloa Pacts provided the blueprints for fundamental tax reform but the politically weak Unión de Centro Democrático (UCD) government elected in 1977 stalled the reforms and only managed to pass some "urgent tax reform measures," while the modernization of the tax administration got frozen. Tax reform finally got in gear with the Socialist Party's (PSOE) ample win in the elections of 1982 and the reformist momentum in policy and administration got a significant push in preparation for Spain joining the European Economic Union in 1986. This required, among other things, the introduction of a modern VAT harmonised with the EEC. The sub-period from 1990 to 1996 saw a decline in tax effort, with an intervening economic recession in 1992-93 and fiscal policy focused on controlling growth in government expenditures and on reducing tax rates and broadening tax bases. Spain had moved swiftly towards reaching the tax paradigm existing in the rest of Western Europe at the beginning of the transition to democracy in the mid-1970s. However, when it reached it by the mid-1980s, the model prevailing in Europe was already under reform, thus moving away from where Spain was going. The fiscal reform blueprint was also in need of reform. After the center-right Partido Popular (PP) won the elections of 1996, the ratio of tax revenues to GDP recovered and resumed growth with the main aim of satisfying the European Union's Stability and Growth Pact and joining the Euro in the areas of budget deficits and overall debt burdens.

In the area of overall fiscal discipline (as measured by government budget deficits and the accumulation of debt) Spain's record over the last three decades shows a more uneven profile but in the long run a rather successful one. The need to close large gaps in capital infrastructure³ and social programs meant that expenditures often ran ahead of revenue collections. These expenditure demands together with fiscal stabilization policies implemented in recession periods following international macroeconomic shocks pushed the budget deficit into the neighbourhood of 7 percent in the mid 1980s and again in the mid 1990s (see Figure 14.2). However, by 2002 Spain was operating with a balanced budget, as when the country had started the journey of democratization and reform in the mid-1970s. With the approval of the Fiscal Stability Law, which took effect

in the 2003 budget, each government level must keep accounts in balance or with a surplus.

The accumulation of government debt during the approximately last three decades offers a mirror image of the evolution of government budget deficits (Figure 14.3). From very low levels of government debt as percent of GDP at the beginning of the journey, government liabilities accumulated at a fast pace especially in the mid-1980s and mid-1990s following the recession periods associated with international macroeconomic shocks. In the mid-1990s, general government gross liabilities as percent of GDP had reached in Spain for the first time the average level of OECD countries. Nevertheless, in preparation for joining the Euro zone, debt levels decreased sharply and Spain was able to meet the Maastricht criterion of an overall debt level of not more than 60 percent of GDP.

Another important dimension of the performance of Spain's tax system has been the evolution in the composition of revenues. In the 1970s Spain's tax system was characterised by a high dependency on social security contributions and indirect taxes. In 1975, as shown in Figure 14.4, social security contributions represented 43 percent of general government revenues, domestic taxes on goods and services, 17 percent, and related "other taxes," 9 percent. On the other hand, direct taxes on income and profits represented only 17 percent of general government revenues. The tax structure was characterised by narrow bases and in some cases, such as social security contributions, by very high rates that yielded less revenue than in other OECD countries.⁴ The high dependence on indirect taxation in combination with many special privileges and high levels of tax evasion translated into a regressive tax system, and one that also performed poorly in terms of horizontal equity.⁵

The 1980s and 1990s saw a period of adjustment in tax structure with increases in the relative importance of direct tax collections accompanied also by increases in collections from domestic taxes on goods and services, proper, especially after the introduction of VAT in 1986 (Figure 14.5). By 2002, as shown in Figure 14.6, taxes on income and profits represented 27 percent of general government revenues while domestic taxes on goods and services represented 25 percent. On the other hand, social security contributions had shrunk to 34 percent of general tax revenues. Overall, the significant increase in tax effort over the period was largely accompanied by a fairer distribution of tax burdens and the elimination of large tax distortions that had affected the efficient operation of the economic system. Improvements in tax administration, which allowed the reduction of tax fraud and evasion, together with the elimination of a variety of preferential treatments, increased the progressivity of the tax system and reduced horizontal inequities.⁶



Figure 14.2 Spain's budget deficit (general government net lending)

Source: OECD.

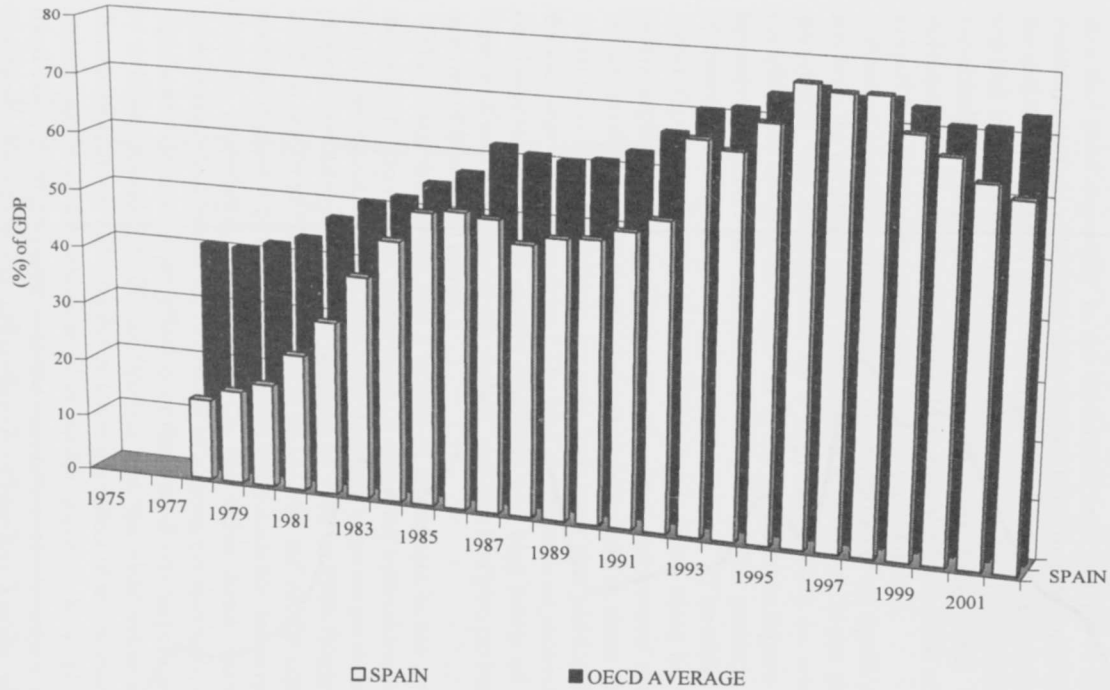


Figure 14.3 General government gross liabilities (as % of GDP)

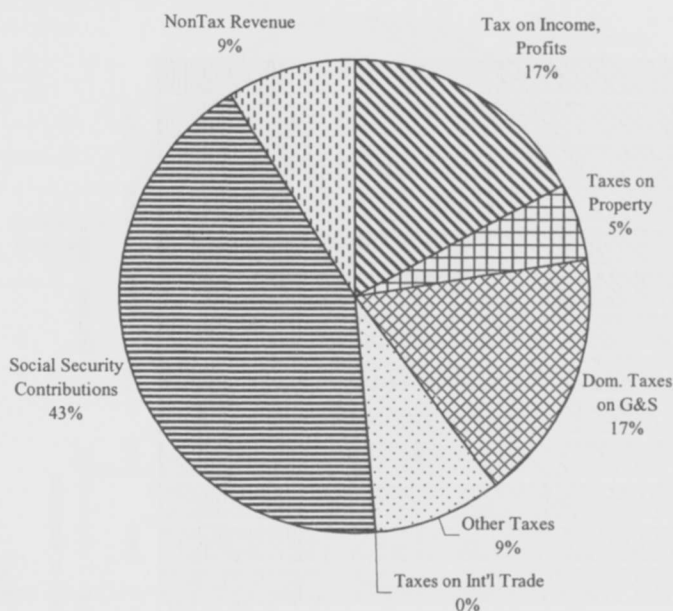


Figure 14.4 General government revenues by source (1975)

However, not everything has been ideal. Despite the rapid process of reform, Spain's tax system has continued to play catch-up with that of its European neighbours. For example, despite better administration and enforcement, tax evasion continues to be relatively high, the tax system is still lagging in international competitiveness, especially in the area of capital income taxation, and tax-induced distortions in labor markets and savings are still present. For better or worse, the tax to GDP ratio lies still below the EU average and the relative importance of income tax revenues still lies below most OECD countries.

Outside the fiscal area, Spain has faced other important economic problems. The government was better able to address the problem imposed by the deteriorating financial position of many public enterprises (ultimately through closings and privatization), than the problems of rising unemployment (particularly among the youth), and the increasing burden imposed by generous pensions and unemployment compensations, especially in light of worsening demographic trends.⁷ Labor market rigidities have continued to aggravate the unemployment problem.

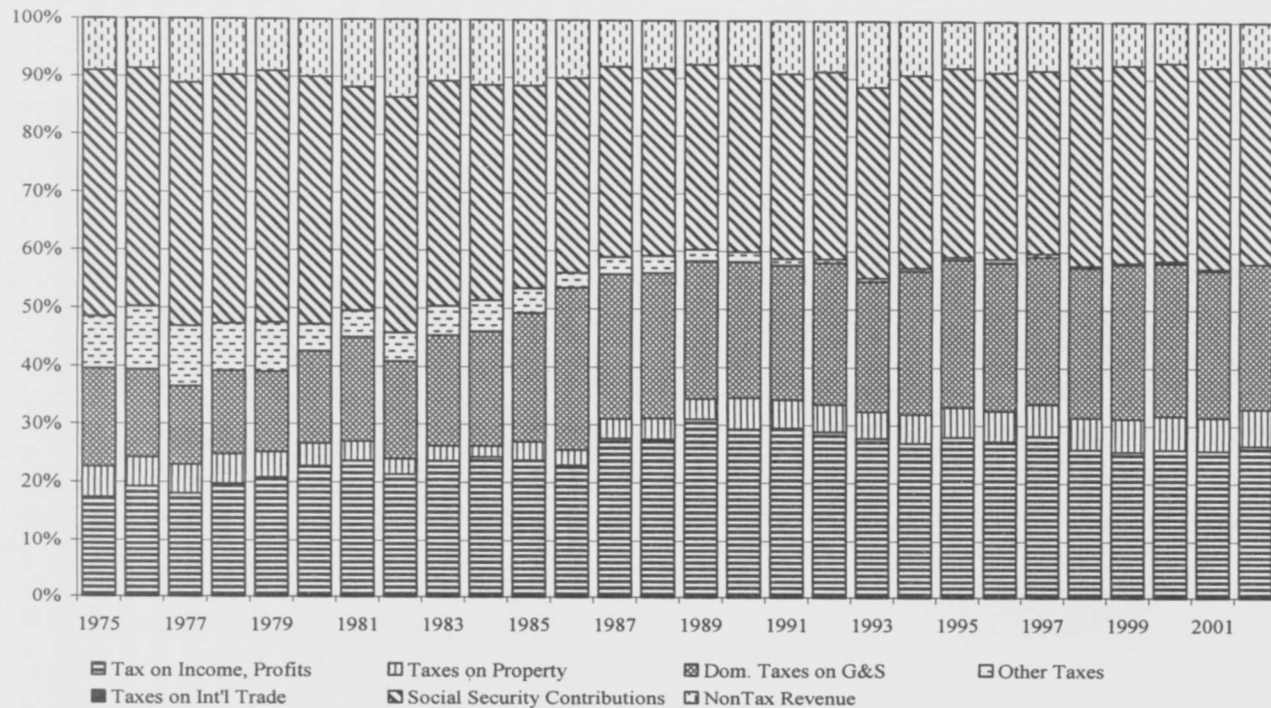


Figure 14.5 Consolidated general government revenue sources (by type)

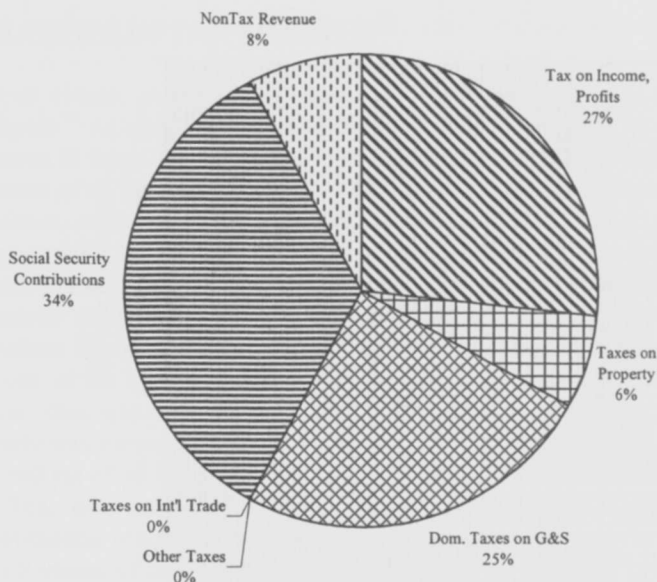


Figure 14.6 General government revenues by source (2002)

One last item in the performance of Spain's tax system is the intergovernmental composition of tax revenues. This is without any doubt the worst performing aspect of Spain's tax system. Despite the fact that Spain has undergone a radical decentralization process, going from one of the most centralised countries in the world in the 1970s to one of the most decentralised today, most of this decentralization has been on the expenditure side of the budget. While the combined share of regional and local governments in total public expenditures is close to 50 percent today, their share in total revenues is just over 30 percent. As shown in Figure 14.7, revenue decentralization, providing regional and local governments with own or autonomous tax sources, has been slow in coming.⁸ In 2003, as reported by López Laborda and Monasterio (this volume), 65 percent of all revenues of the regional governments were still coming from tax sharing and other central government transfers. Other than the possibility of using some sort of piggyback personal income tax, with discretion over the rate schedule and credits, all other taxes devolved to sub-national governments are of minor revenue importance.⁹ Unfortunately, the heavy dependence on and availability of revenue sharing and transfers has created some sort of soft-budget constraint for regional governments leaving them with little or no incentive to make greater use of their own taxes.

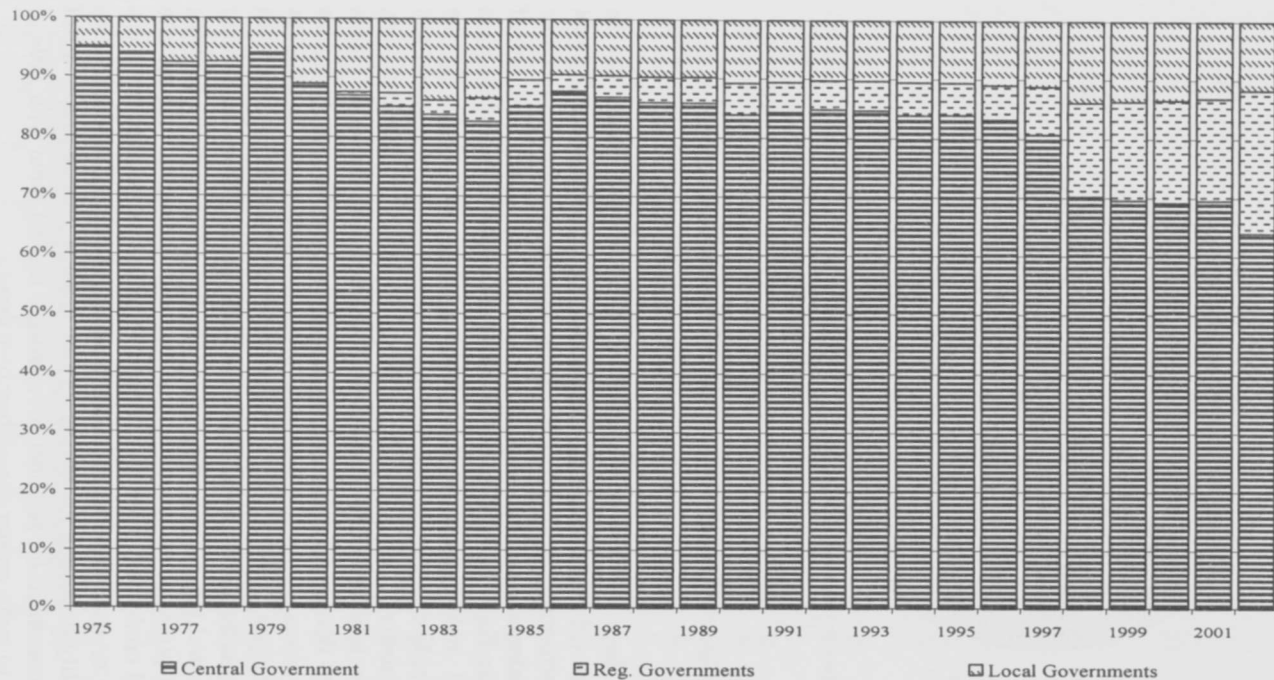


Figure 14.7 Revenue collection by levels of government

Notes: Data from 1998 to 2002 uses gross of transfer figures.

CHANGES IN TAX MORALE¹⁰

By all counts, at the end of Franco's regime, tax evasion in Spain was rampant.¹¹ As reported by Comín (this volume) at the end of the 1970s tax evasion in Spain was estimated at 40 percent of tax receipts and above 90 percent of all Spanish taxpayers recognised the existence of fiscal fraud. In addition, at the same time the fiscal system provided ample tax evasion opportunities for the wealthy, there was no political will to prosecute fiscal fraud. In particular, tax evasion was not a criminal offense and evaders only received small administrative sanctions. As in the case of some other Southern European countries, evading taxes had long been acknowledged as one of the most popular "sports" among Spanish citizens. Not paying taxes often was considered a badge of honor and a reason to boast. This clearly was a serious handicap to modernising the tax system and increasing overall tax effort in the country.

Thus, one important question in Spain's transition is whether the fundamental changes the country underwent regarding the role and effectiveness of the public sector since the death of Franco in 1975 affected people's attitudes toward government, and more in particular, their willingness to comply with their tax obligations. Citizens' attitudes toward paying taxes, their "tax morale" or the intrinsic motivation to pay taxes, far from being exogenously determined by cultural traits and mores, appears to have been responsive in other countries to citizens' overall perception of government.¹² The question of the evolution of tax morale in Spain during the last 30 years has been recently examined in Martínez-Vazquez and Torgler (2005) using survey data from the World Values Survey (WVS) and the European Values Survey (EVS). These databases allow the observation of the evolution of tax morale in Spain at four benchmark years: 1981, 1990, 1995, and 1999/2000.¹³

We would expect that the major changes that have occurred in Spain's political and economic system over the past 20-30 years would have impacted (increase or decrease) tax morale. However, isolating the reasons for possible changes in tax morale is not an easy task because of the presence of multiple confounding factors. Using individual response data from the WVS and the EVS helps to control for some of those factors.¹⁴

The overall picture of the evolution of tax morale in Spain is shown in Figure 14.8 which provides the distribution of aggregate tax morale scores for the years 1981, 1990, 1995, and 1999/2000; the mean values for these four time periods are calculated as the simple average across all individuals in the data sets. Note that the natural cut-off point is at the value 1 because many respondents assert that cheating on tax is "never justified." Therefore, the tax morale variable takes the value 1 if the respondent says that cheating

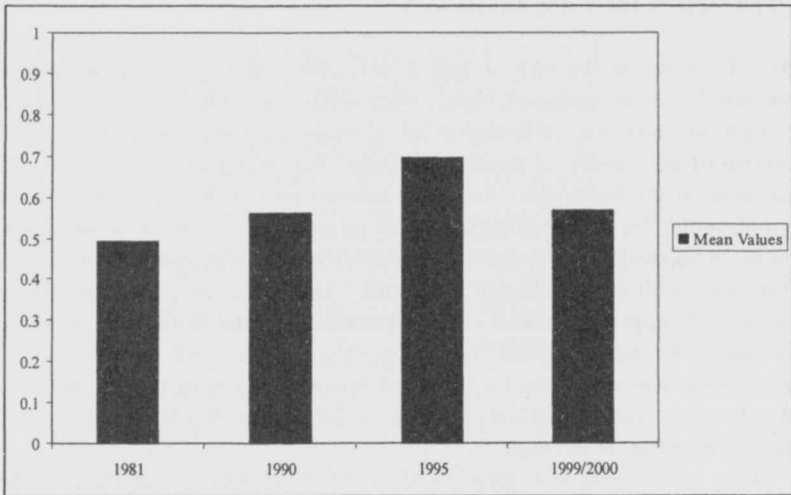


Figure 14.8 Aggregate tax morale in Spain over time (1981-2000)

on tax is “never justified” and 0 otherwise. The interesting result is the strong increase in tax morale in Spain between 1981 and 1990 and a further increase between 1990 and 1995. On the other hand, there is a significant decrease observable between 1995 and 1999-2000.

These changes in the overall level of tax morale would seem to fit well, perhaps up to the observation of 1999/2000, with what has been happening to and around Spanish citizens in the transition years to a democratic regime and thereafter. In 1981 citizens’ tax morale was relatively low. By that date, the fiscal system had advanced little from its dismal performance during the late years of Franco’s dictatorship. There was still widespread perception of tax evasion, failing economic performance, an inadequate social welfare system, and so on; this overall performance would not have encouraged much intrinsic motivation to pay taxes. The sharp increase in tax morale from 1981 through 1995 is quite consistent with the role of social norms in tax compliance; during those 14 years, the socio-economic conditions for Spanish citizens improved across the board, as the level and quality of public services also improved steadily. The strengthening of institutional structures, in particular the reform of the tax system and tax administration with increased overall fairness, likely produced an affirmation of the public belief in government, at the same time income opportunities improved for a large share of the population. Quite likely, taxpayers reacted favorably to the economic and tax policy changes and

public expenditure initiatives that were intended to bring Spain closer to the economic performance of most of its European partners. In summary, the restoration of democracy, the strengthening of social and economic institutions, the process of fiscal decentralization and the creation of a welfare state could have brought a higher level of trust in the state and more positive individual attitudes toward paying taxes through 1995.

The backtracking in the level of tax morale between 1995 and 1999/2000 is harder to explain. Politically, the big change in this period was the change in government when the PSOE lost the elections to the PP in 1996. It is unlikely that this democratic political change is behind the drop in tax morale. More likely, other factors were at play. These may have included the corruption scandals in the last years of the Socialist government, the high unemployment rate during this period, the partial dismantling of the never fully achieved welfare state, or perhaps a growing perception of unfairness associated with the tax reforms aiming at cutting rates and broadening tax bases, which had been introduced around that time.

At any rate, we think it is very relevant for the overall success of Spain's tax reform effort over the last 30 years that tax morale significantly improved over this period even though not in a linear form. We are inclined to believe that the tax and other institutional reforms that got started with the Moncloa Pacts and continued through the accession to the European Economic Community quite likely helped boost Spanish citizens' tax morale. The small but significant decline in tax morale during the second half of the 1990s remains somewhat of a puzzle although some likely causes include institutional changes such as corruption in the public sector, a perception of lower levels of tax fairness, or even high levels of unemployment in the economy. There can be little doubt that the Spanish tax reforms and tax administration modernization efforts resulting in nearly double the tax effort for general revenues, from 22 percent of GDP in 1976 to 39.9 percent of GDP in 2002, has a lot to do with improved tax morale of Spanish citizens. Clearly, tax morale is not something fixed in the culture of the country and keeping tax morale high is a valuable asset for the entire country.

SOME LESSONS

It is, of course, risky to attempt to draw general conclusions and lessons on tax reform, or for that matter on anything else, from the experience of a single country, in this case Spain. However, the Spanish experience with tax reform over the last 30 years, although not without some mistakes and

backward steps, also exemplifies what has worked almost universally in other countries that succeeded at fundamental tax reform.¹⁵

The Role of Careful Study and Preparation

The start of the tax reforms in the late 1970s and early 1980s were preceded by an intense and often frustrating period of careful study and preparation with little or no policy action.¹⁶ However, that work bore fruit; when the time came for reform to be both feasible and also politically desirable, a quite complete and well-documented blueprint for reform was ready. Because of the careful study and preparation, there was much less room for the mistakes and missteps frequently associated with hurried tax reform efforts in many other countries in the past. The preparation for the reforms could have had more depth in empirical estimates of the potential effects of the reforms on revenues, the distribution of tax burdens, and so on. However, the quality of the political debate was enhanced by the availability of the serious work completed up to that point. Because of that, there was less room for some decision makers to assume populist or demagogic positions regarding the reform.

Timing of the Reform

The implementation of fundamental tax reform is more difficult in good economic times. When revenue collections are being propelled upwards by an expanding economy, it is all too difficult to convince the political class to immerse themselves in the difficult and sometimes arcane issues surrounding tax policy reform. Furthermore, tax reform can put at risk political positions by moving the discourse into a territory that at the very least is highly controversial and politically divisive. It is a well known fact among students of tax policy reform that the opportunity for fundamental tax reform becomes more available when the economy is performing poorly and when budget deficits are high on the national agenda. Even more so, the opportunity for fundamental tax reform is enhanced in the presence of political and/or economic shocks. That shock was present in the case of Spain after the end of Franco's dictatorship by the need to catch up for lost time for a period spanning over three decades.

One interesting aspect of Spain's tax reform is that, despite having been implemented by governments with different ideological leanings, overall it has been lineal and persistent. Even though there were temptations to deal with short-term crises, these short-term interventions for the most part never undid or went against the fundamental tenets of the tax reform process set out early in the process. Thus, it is important to differentiate

short-term and long-term objectives and to isolate the long-term objectives from temporary pressures and temptations.

Importance of a Comprehensive Approach to Tax Reform and the Facilitating Role of Comprehensive *Fiscal* Reform

Much has been written about the virtues and shortcomings of a big-bang versus a sequenced incremental approach to tax reform and it is fair to say that there is little consensus in the literature and among policymakers regarding the most desirable approach. However, there is much less disagreement about the necessity of an explicit blueprint and strategy linking together all aspects of the reform and making the different parts fit together. The lesson from Spain's tax reform is that a sequenced approach to implementation worked well, but perhaps it might have been more desirable to have taken advantage of the window of opportunity provided by the political consensus in the Moncloa Pacts and have implemented much of the reform in a big-bang at that point. But more important for overall success than the speed of implementation of the reforms was the existence of an explicit blueprint and strategy that generally was followed, at least until quite recently, by the different governments in the process of reform. Without a comprehensive blueprint that looked to reform every aspect of the tax system thus making all stakeholders both winners and losers, it would have been so much harder to reach consensus and provide continuity to the different phases of the reform. Thus a comprehensive approach to tax reform was an important ingredient for overall success.

Another important ingredient was that tax policy changes were clearly linked, at least at the beginning of the reforms, with changes in expenditure policy; that is, with fiscal policy reform in the broad sense. There is little question that a broader scope to the reform to include other fiscal reforms on the expenditure side of the budget significantly facilitated acceptance of the tax reform measures. The development of social programs, with a special impact on the welfare of the lowest income groups helped to diffuse some attention for trying more aggressively to attempt to redistribute income through the tax system. Acceptance of higher taxes in any country is generally not forthcoming unless there is a clear sense about how the increased revenues will be used and at the same time, there is general approval for the use of those revenues. This is a lesson that has been frequently ignored in recent attempts at tax reform, for example in Mexico by President Vicente Fox's administration's failed attempt at tax reform at the beginning of his mandate.

Tax Reform Measures Need to Mesh with Other Economic Policy Measures

Tax systems do not operate in a vacuum. Depending on how they are designed, taxes may hinder or enhance the workings of the economy, but clearly there are many other policies (e.g., monetary policy, regulatory policies and so on) that can impact the overall performance of the economic system and ultimately the effectiveness of the tax system. Tax reform efforts are more likely to succeed if they are meshed with other economic policy measures. There is nothing worse for tax policy reform than to be followed by weak and declining tax revenues; the tax reform may have been a technical success for the quality of the measures adopted but would nevertheless appear to be a political failure.

Spain's tax reform program was accompanied by a fairly intensive reform in other areas of public policy, in many cases pushed by the integration agenda with the European Union. However, in some other policy areas, such as labor market liberalization, pension and social security, reforms were slow in coming. Nevertheless, the economy managed to grow at a very healthy pace, although with some vicissitudes, in some cases driven by international economic events.

Reaching a Balance between Efficiency, Equity, and other Objectives in the Reform Package

Tax reform must be a balanced exercise among multiple goals and objectives. There are three possible fundamental objectives behind any tax reform: revenue adequacy, increased efficiency, and a fairer distribution of tax burdens. In the case of Spain's tax reform, the relatively low level of tax effort in the country and the marked needs in social services and public infrastructure meant that a marked increase in tax collections was very desirable. This goal we have seen took precedence but in balanced way with reducing tax distortions in the economy and improving vertical and horizontal equity in the distribution of tax burdens. Although in the initial phases of the tax reform there were signs of pursuing aggressive redistributive policies with high progressive rates, very soon the reform process was channeled toward more modest goals in terms of nominal progressivity with more attention paid to broadening the tax bases. Effective progressivity was increased by reducing the tax burdens on the lower income groups of the population.

Need to Get Tax Policy Right before or at the Same Time as Tax Enforcement and Administration Reform are Tackled

There continues to be a lively debate in the tax reform literature on what should come first, tax administration reform or tax policy reform. It can be argued that improvements in tax administration effectiveness should always be welcome regardless of the presence or not of tax policy reform. On the other hand, stricter enforcement of a tax policy system that is considered unfair and inefficient or exposed to high levels of corruption may be so much harder or even counterproductive. The lesson is to try to get tax policy right, before embarking on a major overhaul of the tax administration system with the goal of significantly increasing tax compliance.

The reform and modernization of the tax administration system were of fundamental importance for the overall success of Spain's tax reform. Although perhaps not entirely intentional, the reform of the tax administration came into being after much of the new tax policy architecture had been designed and to some extent had been put into place. Stricter enforcement of the tax system that was broken and not respected by the people would have been ineffective and counterproductive. Actually, far from causing a taxpayer rebellion, the tough tax enforcement measures, including the criminalization of certain tax offenses introduced in 1977, actually increased tax compliance in an overall atmosphere of increased tax morale. This rather radical change in the effectiveness of tax administration and the turnaround in taxpayer sentiments would not have happened without the reform of the tax system. We must also note that the reform was not only a tax reform but also, as discussed above, a fiscal reform. The changes in expenditure policies and programs actually also played a very significant role in the acceptance of the new tax administration paradigm. It is an important lesson in itself that the very significant tightening in tax enforcement can be accompanied by increases in citizens' tax morale.

Spain's experience comes to highlight the importance of the "small print" in fiscal reform. The improvement of tax administration rarely appears as a significant item in the political agenda; governments tend to pay too little attention to it because it is unlikely to be popular with voters and the results are likely to be seen in the longer run when the incumbent government may be already out of office. However, parallel improvements in tax administration can make the difference between "just on paper" tax reform and real tax reform.

Tax Reform is Not a Once-and-For-All Activity

It is practically impossible to get everything right in a tax reform no matter how integral and fundamental the reform. It is also true that even if we were able to accomplish everything, we should expect the tax system to get partially obsolete as the structure of the economy changes, as evidenced by increasing globalization and the increasing importance of services and e-commerce surpassing more traditional activities in the manufacturing sector. For these reasons, we should expect tax reform to go on over time. However, the need to adapt the tax code to the new economic environment and to correct aspects of the tax laws that are problematic should be balanced with the importance of stability and continuity in tax institutions to avoid confusion and higher costs of taxpayer compliance and administration. Investment and other decisions by economic agents may be put on hold when there is excessive uncertainty about tax institutions.

The Spanish experience with tax reform demonstrates rather well the lesson that tax reform is a continuous process. Having, at least to start with, general blueprints for the direction of the reforms significantly helped keep the process on track. Catching up and adapting Spain's tax system to those of its European partners also helped to provide the reform effort with an internal logic that might otherwise not have been the case.¹⁷ Finally, even though there were a number of tax reform initiatives over the last three decades, these were not so frequent as to impart too much uncertainty and instability in the system.

Original Decisions Cast Long Shadows and are Difficult to Undo

Reaching a consensus on the substance of the reforms is always difficult; compromise and negotiation are usually intrinsic parts of the process. However, one must warn against delaying key points for negotiations. Once new laws are implemented it becomes much harder to re-negotiate or address unsolved issues; "new rights" are acquired and positions are typically hardened. The Spanish tax reform process contains lessons on the dangers of these "original sins." These are most clearly present in the institutional architecture for fiscal decentralization. Three examples will suffice. First, adducing "historic acquired rights," two regions (the Basque Country and Navarre) argued for and got at a time of new beginnings and national consensus special treatment regarding their financial arrangement with the central government.¹⁸ The asymmetric treatment provided these two regions with advantageous financing conditions and represented and continues to represent an unfair and highly inequitable deal for all other regions in the country (those under the general or common regime). Second, revenue assignments initially provided little tax autonomy to the

autonomous communities and relied instead on revenue sharing and other forms of transfers for financing the decentralised governments. Over time, as more expenditure responsibilities have been decentralised, the necessary financing has increasingly come more from revenue sharing and transfers, while the modest increases in revenue autonomy provided to the Autonomous Communities has gone for the most part unused, leading to low political responsibility and accountability of regional governments. Third, there has been very little focus since the start on the decentralization at the local level, as opposed to the regional level. This reflects the fact that the Spanish decentralization agenda was, and continues to be, largely driven by political considerations and much less by the efficiency issues typically associated with decentralization policy.

NOTES

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1. I am grateful to Gabriel Leonardo for his research assistance.
 2. See the essays in Fuentes (1990) and Lasheras and Menendez (1998) for earlier assessments.
 3. In the earlier years, much of capital expenditures were fundamentally transfers to public enterprises.
 4. See, for example, OECD (1978).
 5. In addition, ceilings on wages liable for social security contributions worsened vertical equity.
 6. See Onrubia (this volume).
 7. See Zubiri (this volume).
 8. Note that Figure 14.7 does not properly reflect the level of revenue decentralization after 1998; it was not possible to net out intergovernmental transfers.
 9. See Table 11.5 in López Laborda and Monasterio (this volume) for a description of those taxes.
 10. This section draws on Martínez-Vázquez and Torgler (2005).
 11. See Comín and also Onrubia in this volume.
 12. See Torgler (2006), Alm and Martínez-Vázquez (2003) and Bird, Martínez-Vázquez and Torgler (2006).
 13. The issue of tax morale so far has not been widely researched in Spain. However, in a recent paper, Prieto Rodríguez et al. (2005) look at the status of tax morale in Spain's Comunidades Autónomas using cross-section data for 1998 from the International Social Survey Programme (ISSP). A main finding of this paper is that tax morale is lower among the supporters of the nationalist regional parties in Catalonia and the Basque Country.
 14. These surveys are based on representative national samples of at least 1000 individuals and are conducted via face-to-face interviews at the respondents' homes.
 15. See, for example, Harberger (1989), Martínez-Vázquez and McNab (2000), Bird (2004), Bahl (2006).
 16. See Fuentes (1973, 1976).
 17. See the discussion in González-Páramo and Hernández de Cos (this volume).

18. See the paper by Lopez Laborda and Monasterio in this volume for a full description of the "foral" or special regime.

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