

Comparative Fiscal Federalism

Country Report Germany

Work Status: September 2021

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2nd Intermediate Workshop

September 30, 2021

General Structure

1. The goals of the system according to legal order and tradition
2. **Origin and Development of Federalism in the German Federal state**
3. Distribution of tasks and expenditure in the German federal state (passive fiscal equalisation)
4. Distribution of revenues in the German federal state (active fiscal equalisation)
5. **The role of the municipalities in the German federal state**
6. **Current advantages, problems and reform considerations in the German federal state**

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Chapter Structure

2. Origin and Development of Federalism in the German Federal state

- ▶ A. Debates within the framework of the Herrenchiemsee Constitutional Convention
- ▶ B. Grundgesetz 1949
- ▶ C. "Small Financial Reform" 1955
- ▶ D. "Great Financial Reform" 1969
- ▶ E. German reunification
- ▶ F. Federalism Reform I 2006
- ▶ G. Federalism Reform II 2009
- ▶ H. Federalism Reform 2017

2. Origin and Development of Federalism in the German Federal State

- ▶ **A. Herrenchiemsee Constitutional Convention (10-23 August 1948)**
 - ▶ Presentation of discussions and recommendations by Convention regarding distribution of legislative power, tax legislation and allocation of revenues
- ▶ **B. Grundgesetz (Basic Law) 1949**
 - ▶ Presentation of discussions in the Parliamentary Council, conflict with the Allied Forces regarding distribution of power and responsibilities between the federal levels, agreement on proposal and proclamation of the Basic Law, relevant Articles regarding fiscal federal order
- ▶ **C. „Small Financial Reform“ 1955**
 - ▶ Description of objectives and changes, reformulation of Articles 107 (tax revenue distribution, Länder fiscal equalization, supplementary allocations) and 106 (revenue authority and financial allocations)

2. Origin and Development of Federalism in the German Federal State

- ▶ **D. „Great Financial Reform“ 1969**
 - ▶ Recommendations of Troeger commission regarding implementation of „cooperative federalism“
 - ▶ Details of Municipal finance reform
- ▶ **E. German reunification**
 - ▶ Description of developments and changes in the fiscal federal relations due to unification
- ▶ **F. Federalism Reform I (2006)**
 - ▶ Description of objectives and core changes (distribution of tasks, transparency regarding interdependencies etc.)
- ▶ **G. Federalism Reform II (2009)**
 - ▶ Description of objectives and core changes (introduction of debt brake (Art. 109 GG and Art. 115 GG) and Stability Council (Art 109a GG))

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5. The role of municipalities in the German federal state

- ▶ A. The ambivalent position of municipalities in the federal structure
- ▶ B. The role of municipalities in the fulfilment of public tasks
- ▶ C. Economic disparities
- ▶ D. Municipalities within the fiscal equalization systems

5. The role of municipalities in the German federal state

- ▶ **A. The ambivalent position of municipalities in the federal structure**
 - ▶ description of municipalities as components of the federal states vs. local self-administration law and right to financial independence
- ▶ **B. The role of municipalities in the fulfilment of public tasks**
 - ▶ Introduction of economic functions of the municipal level, significance for the fulfilment of public tasks
- ▶ **C. Economic disparities**
 - ▶ Presentation of disparities at municipal level (between the municipalities of individual Länder, within the Länder, between independent towns and district areas)
- ▶ **D. Municipalities within the fiscal equalization systems**
 - ▶ Description of the role local authorities in the context of the equalization of financial strength between the Länder, local fiscal equalization systems

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6. Current advantages, problems and reform considerations in the German federal state

► Advantages

- strong solidarity and high level of equalization payments secures fiscal and economic strength across the territory and prevents cyclical downturns
- especially after unification, the Eastern Länder were strengthened by high transfer payments and a relatively smooth integration in the fiscal equalization scheme
- tradition of tight coordination and cooperation fosters solidarity, while securing a certain amount of autonomy; e.g. system of joint taxes is based on mutual cooperation (federal government cannot withdraw money unilaterally!, in stark contrast to e.g. the UK), but guarantees all units predictable revenues

6. Current advantages, problems and reform considerations in the German federal state

▶ **Problems**

- ▶ tendencies of erosion of solidarity (mainly led by Bavaria); existing fiscal equalization scheme has repeatedly been challenged before the federal constitutional court
- ▶ intransparency and complexity of the system - unintelligible for ordinary citizens, fosters diffusion of accountability
- ▶ fiscal and economic sustainability after the pandemic is questionable

6. Current advantages, problems and reform considerations in the German federal state

▶ Reform considerations

- ▶ level of equalization and norm of solidarity - towards more fiscal stratification and autonomy/ granting more tax levying or tax varying powers to the Länder?
- ▶ dealing with the inherited debts (Altschuldenproblematik) at Länder and local level - attempts at communalization
- ▶ consolidation path and debt brake in the aftermath of the pandemic
- ▶ structural deficits of the local level in the light of rising expenses for tasks assigned to local governments