

# Intergovernmental financial relations as a paradigm of hyper-executive federalism: insights from the case of equalization mechanisms

*Francisco Javier Romero Caro, Alice Valdesalici\**

## 1. Introduction

The delineation between the legislative and executive branches constitutes a subject of considerable contention within the discourse on the operational dynamics of parliamentary systems. The theoretical construct of the separation of powers has progressively manifested in practical terms as a gradual attenuation of the distinct demarcation between the executive and the legislative. This phenomenon, prevalent in parliamentary models fashioned after the Westminster paradigm (the UK, Canada, Australia, etc.), has incrementally permeated continental European contexts. Although the empowerment of the executive over the legislative has occurred in some cases through constitutional reforms, as in the case of the amendments promoted by President De Gaulle in France aimed at fortifying the presidential role, culminating in the consolidation of the Fifth Republic, contemporary practice indicates an ongoing transformation within parliamentary systems. This metamorphosis has been accelerated by the exigencies posed by the pandemic, wherein the imperative of delivering a swift and efficacious response to the unprecedented challenges precipitated by the health emergency has propelled this incipient process of “presidentialization” in parliamentary systems. Consequently, the executive domain supersedes the legislative, relegating the latter to a subsidiary role, thereby mitigating its significance and reducing it to little more than a ratifier of governmental intent.

\* Francisco Javier Romero Caro is senior researcher at Eurac Research – Institute for Comparative Federalism, Eurac Research; Alice Valdesalici is research group leader at Eurac Research – Institute for Comparative Federalism, Eurac Research. The paper has been conceived in common by the two authors, nevertheless sections 1, 3 and 5 can be ascribed to Francisco Javier Romero Caro, whereas sections 2 and 4 to Alice Valdesalici; section 6 has been jointly drafted.

One notable manifestation of this phenomenon is the misuse of emergency legislation, originally conceived for exceptional circumstances and intended for temporary application, which has evolved into a routine legislative instrument. Consequently, the locus of legislative authority has progressively transitioned from the legislature to the executive, which not only directs the government's activities but also monopolizes the legislative agenda. Concurrently, mechanisms of oversight and control have been affected, yielding, in certain instances, novel dynamics wherein the government appears to exercise control over the opposition, as opposed to the traditional paradigm where the opposition scrutinizes and regulates the actions of the executive<sup>1</sup>.

This pervasive role of the executive in the legislative function finds an unprecedented amplification in the context of federal systems. Hence, the rise of "executive federalism", defined by Watts as "the processes of intergovernmental negotiation that are dominated by the executives of the different governments within the federal system"<sup>2</sup>. Financial relations and, among these, equalization mechanisms represent an emblematic forerunner of this phenomenon. The decision to isolate this specific segment of federalism studies serves a twofold purpose. First, it allows to investigate the role that remains to the elective assemblies in the elaboration of decisions in technical and complex areas like public finance. Second, it aims to analyze an area that is essential to the political autonomy of territorial authorities, thus allowing us to understand how these processes have developed and what their effects are on the institutional level.

To test this preliminary assumption, the study investigates decision-making procedures on equalization mechanisms from a comparative and constitutional law perspective, with the ultimate aim to verify the magnitude of the executive drift within the different paradigms in action. Equalization mechanisms are a crucial tool of federal systems as they aim at reducing inter-territorial fiscal inequalities via the redistribution of fiscal resources. In

<sup>1</sup> E. GRIGLIO, *Parliamentary oversight under the Covid-19 emergency: striving against executive dominance*, in *The Theory and Practice of Legislation*, 8(1-2), 2020, pp. 49-70; N. BOLLEYER, O. SALAT, *Parliaments in times of crisis: COVID-19, populism and executive dominance*, in *West European Politics*, 44(5-6), 2021, pp. 1103-1128.

<sup>2</sup> R.L. WATTS, *Executive Federalism: A comparative analysis*, Kingston, Institute of Intergovernmental Relations, 1989, p. 3.

practical terms, the degree to which this phenomenon materializes varies significantly, contingent upon the determinants encompassing the entirety of the process. The ultimate outcome is profoundly influenced by the prevailing legal framework, the institutional and procedural safeguards in effect, and the inherent legal constraints therein. Consequently, grants are frequently utilized to broaden political backing rather than to rectify horizontal imbalances. In other words, partisan political considerations influence (re)distributive policies, a dynamic ubiquitous in all federal systems<sup>3</sup>. The influence of political momentum invariably constitutes an integral facet of every equalization endeavor. Nevertheless, the extent of discretion and the constraints impinging upon the political process, as well as the interests motivating decisions, may diverge significantly from one case to another. As such, this study focuses on the institutions and procedures governing equalization mechanisms, as these are determinants of the functioning of a federal system. Put differently, the level of government in charge of defining the scheme of intergovernmental transfers, the existing guarantees, and the institutions that govern intergovernmental relations and settle intergovernmental conflicts are central features of a system and its functioning<sup>4</sup>. In fact, the procedural and institutional dimensions of equalization schemes end up determining the interests that are channeled through the process and its results. Besides being central in drawing a line between constitutional rules and political processes, these elements contribute to determining the overall federal equilibrium. Ultimately, the degree to which SNGs are involved in the decision-making process is telling about the impact on subnational accountability and autonomy. The overall acceptance of the redistributive scheme, and hence the extent to which solidarity is instrumental to the unity of the federal system, and does not end up in challenging the system itself.

<sup>3</sup> Among the many studies on the topic from a political economy perspective, see: A. WORTHINGTON, B. DOLLERY, *Fiscal illusion and the Australian local government grants process: How sticky is the flypaper effect?*, in *Public Choice*, 99(1-2), 1999, pp. 1-4; A. PORTO, P. SANGUINETTI, *Political Determinants of Intergovernmental Grants: Evidence From Argentina*, in *Economics and Policy*, 13(3), 2001, pp. 237-256; M. GOLDEN, L. PICCI, *Pork-Barrel Politics in Postwar Italy, 1953-94*, in *American Journal of Political Science*, 52(2), 2008, pp. 268-289.

<sup>4</sup> R. BAHL, *Intergovernmental Transfers in Developing and Transition Countries: Principles and Practices*, Washington D.C., World Bank, 2000, p. 429.

Accordingly, the different federal systems of interest have been identified with the aim to portray the existing variety of ‘architectural’ solutions, ie., including in the spectrum of analysis the different paradigms that can be detected in federal systems around the globe. Against this line, the following cases will be investigated: Australia as the prototype of tax-revenue sharing on a “technical base” (Commonwealth Grants Commission); Canada representing, in financial-related matters, the paradigm of federal-provincial diplomacy with little, if any, legal entrenchment; Germany as the prototype of tax-revenue sharing on a ‘legislative-assembly base’ (*Bundestag+Bundesrat*); and, finally, Spain with the quasi-constitutional institutionalization of the CPFF as a forum for intergovernmental financial relations.

## ***2. Australia: (not so) independent technical base sharing***

From a comparative perspective, the Australian system of fiscal equalization can be considered as the prototype of a tax-revenue sharing scheme on a “technical base”. The design and extent of equalization measures have traditionally been regarded as a technical matter entrusted to the Commonwealth Grants Commission (CGC), an autonomous statutory entity situated outside the realm of political influence.

In contrast to other federal systems, equalization is not constitutionally enshrined in Australia. Instead, the Australian Constitution features only a provision, section 96, which empowers the federal Parliament to “grant financial assistance to the States on such terms and conditions as the Parliament thinks fit”. Despite the lack of constitutional detail, equalization is an essential component of Australian federalism because of the coexistence of a significant horizontal imbalance combined with a substantial vertical fiscal gap. While States possess extensive authority in the provision of costly services encompassing education, healthcare, and law enforcement, the power to tax remains predominantly centralized. Simultaneously, among the six States and two self-governing Territories, significant variations persist in fiscal capacity and expenditure for delivering services. Subnational entities vary greatly in terms of community size, population growth, composition, remoteness, indigenous status, and economic vigor (mainly due to the abundance of natural resources in some states). This territorial diversity gives rise to notable horizontal

imbalances, which are addressed through a complex mechanism of revenue redistribution comprising both earmarked and unconditional transfers from the federal to the subnational level.

In 1998, the Special Premiers' Conference culminated in the establishment of the Intergovernmental Agreement on the Reform of Commonwealth–State Financial Relations that paved the way for the Goods and Services Tax (GST) Act of 1999. A decade later, the Intergovernmental Agreement on Federal Financial Relations was formulated under the auspices of the Council of Australian Governments (COAG). The Federal Financial Relations Act of 2009 is underpinned by this agreement, which serves as a comprehensive framework governing fiscal transfers between the Commonwealth and the various States, as well as fostering collaborative efforts concerning policy development and the delivery of services. Two categories of transfers were instituted. One, predominantly overseen by the CGC, is based on the apportionment of GST revenues in accordance with principles of horizontal equalization. This culminates unconditional payments disbursed to the States. Conversely, the second category encompasses a suite of specialized, often earmarked, transfers to cover spending in areas administered by the State. Within this framework, the CGC is entrusted with advising the Commonwealth on the redistribution of GST among States and Territories. This entails offering recommendations in alignment with the terms of reference established by the Commonwealth Treasurer<sup>5</sup>. In accordance with the CGC Act of 1973, the Commission is constituted by the chairperson and a minimum of two additional members, presently numbering three. These appointments are made by the Governor-General of the Commonwealth, based on recommendations from the Federal Executive Council, without a mandated stipulation for State representation. Nevertheless, it is customary for such appointments to follow consultation with the States. It is noteworthy that, in numerous instances, these experts have previously held positions within State administrations, underscoring the connection between the Commission and State-level expertise.

<sup>5</sup> On the evolution of the CGC role over time, see: R.A. WILLIAMS, *History of Federal–State Fiscal Relations in Australia: A Review of the Methodologies Used*, in *The Australian Economic Review*, 45(2), 2012, pp. 145–157.

The CGC defines the methodology for GST redistribution with the aim that States “receive funding from the Goods and Services Tax revenue such that, if each made the same effort to raise revenue from its own sources and operated at the same level of efficiency, each would have the capacity to provide services at the same standard”<sup>6</sup>. This process includes a quinquennial review of the methodology and calculations updates to ensure the distribution reflects changes in State circumstances. This methodology rests on an index of relative needs designed by a complex formula that assesses the differences between expenditure and revenue. Hence, States with a revenue-raising capacity below the average or higher than average spending requirements receive a greater allocation of GST payments.

Although, over the years, the Commission has garnered a reputation for its independence and impartiality in deciding the technicalities of the equalization program, this does not mean that this has been divorced from politics or, more precisely, from the power of the executive(s). Not only because equalization was enacted and designed via a series of intergovernmental agreements negotiated following the traditional vision of executive federalism, but also because the major changes to the program have not originated in recommendations by the CGC but on the will of the executives. This was the case of the Treasury Laws Amendment Act 2018 that mandated – among other things – a gradual transition from full to reasonable equalization. This makes it clear that the role of the CGC is complemented in practice by another institutional element based on “sophisticated institutional arrangements”, in which “the States are complicit and adept at working the system to their advantage”<sup>7</sup>.

In Australia, the financial rules of subnational financing are mostly the result of intergovernmental agreements reached among the executives of the two levels of government. This is partially favored by the scarce attention paid by the Australian Constitution to the institutions and procedures defining and governing financial relations. In fact, the financial

<sup>6</sup> CGC, *Report on GST Revenue Sharing Relativities: 2010 Review*, Canberra, 2010, p. 30.

<sup>7</sup> B. GALLIGAN, *Fiscal federalism: then and now*, in G. APPLBY, N. ARONEY, T. JOHN (eds.), *Future of Australian Federalism: Comparative and Interdisciplinary Perspectives*, Cambridge, Cambridge University Press, 2012, pp. 320-338, here: p. 321.

landscape has undergone significant transformations over time, a shift that was not brought about through constitutional amendment, but rather resulted from intergovernmental agreements. These agreements are considered an emblematic expression of the intergovernmental dimension of the Australian federation, as well as a determinant of the collaborative nature of Australian federalism<sup>8</sup>.

Financial relations between the Commonwealth and the States are dominated by the executive branches of both levels of government, with such institutional architecture being a “big contributing factor to hyper-executive federalism”<sup>9</sup>. At the apex of this structure lies the National Cabinet, through which the Commonwealth and the States enter into agreements and make all political decisions related to financial relations. The National Cabinet, made up of the Prime Minister, State Premiers and Territory Chief Ministers, replaced the Council of Australian Governments in 2020. Under the National Cabinet, the Council on Federal Financial Relations sits together the treasurers of the Commonwealth, the States, and the Territories. This body oversees federal-state financial relations and is responsible for broad economic and fiscal issues and legislative oversight of GST operations, with the support of the Heads of Treasuries which comprises the Secretary to the Treasury, and State and Territory counterparts from each jurisdiction<sup>10</sup>.

Executive federalism is also fostered by the adversarial nature of financial relations in Australia, especially during the periodical reviews carried on by the CGC. Divergent perspectives on the attributes and extent of equalization arise within the States’ consultations conducted by the CGC, primarily mirroring their respective economic prowess. Richer states, such as Western Australia, often raise doubts regarding the merits and efficacy of the system, leading to political strains among the States and between

<sup>8</sup> J.R. MADDEN, *Central Fiscal Dominance, Collaborative Federalism and Economic Reform*, in J.S. WALLACK, T.N. SRINIVASAN (eds.), *Federalism and Economic Reform: International Perspectives*, Cambridge, Cambridge University Press, 2006, pp. 85-142, here: p. 86.

<sup>9</sup> For a critical view on the Australian federal system on this perspective, see C. SAUNDERS, M. CROMMELIN, *Reforming Australian Federal Democracy*, in *University of Melbourne Legal Studies Research Paper*, 711, 2015.

<sup>10</sup> C. SAUNDERS, *A New Federalism? The Role and Future of the National Cabinet*, in *Governing during Crisis*, 2, 2020.

the States and the Commonwealth<sup>11</sup>. The 2020 CGC review highlighted the presence of varying viewpoints on the scope of equalization, albeit all States endorsed the objective of horizontal fiscal equalization. Notably, New South Wales dissented from this consensus, contending that GST revenue allocation should be based on a per capita distribution or an equal per capita basis.

The dominance of executive federalism also circumscribes the Commission's margin of discretion. Simultaneously, this process serves to temper the dominance of the Commonwealth in fiscal matters. The Commonwealth's power in financial matters must reconcile with the interests of the States, as conveyed by their executives through the institutions and practices of intergovernmental relations. This occurs not only by setting the general trajectories of the system via intergovernmental agreements, but also through the terms of reference delivered to the CGC. The latter is the instrument that links the political to the technical dimension of equalization, allowing that policy objectives and political decisions are reflected in the technical implementation and functioning of the system<sup>12</sup>. The Council on Federal Financial Relations (CFFR), comprising the treasures of the federal and state levels, meets in advance to discuss and *de facto* define such terms, albeit the final say is, in theory, up to the Australian government. At the same time, the recommendations processed by the Commission after consultations with the States are as a rule accepted by the Commonwealth, also due to the lack of unanimous support on the part of the States on alternative distribution schemes. In theory, they are considered by the CFFR, with the federal treasurer having the final say in determining how revenues are shared<sup>13</sup>. But as a norm, the CFFR does not make use of its power to dissent on the Commission recommendations and they are accepted by the Com-

<sup>11</sup> R. ECCLESTON, T. WOLLEY, *From Calgary to Canberra: Resource Taxation and Fiscal Federalism in Canada and Australia*, in *Publius*, 45(2), 2014, pp. 216-243, here: p. 235.

<sup>12</sup> J. SPASOVEJIC, M. NICHOLAS, *Fiscal Equalisation in Australia*, in: *Australian Journal of Public Administration*, 72(3), 2013, pp. 316-329, here: p. 318.

<sup>13</sup> R.A. WILLIAMS, *Federal-State Financial Relations in Australia: The Role of the Commonwealth Grants Commission*, in *The Australian Economic Review*, 38(1), 2005, pp. 108-118, here: p. 110.



monwealth<sup>14</sup>. As such, the space left for politics is smaller than in other federal systems, like Canada or Germany.

Although this system is functional to combine the different visions of the subnational funding system, it lacks accountability and transparency, as it is primarily based on closed door negotiations and political bargaining, with the legislative assemblies at all levels being mostly left aside<sup>15</sup>. Thus, the role of Parliaments, at both national and state level, is reduced to approving the legal transposition of these intergovernmental agreements, which occurs out of practice. Furthermore, little margin of discretion over their content is left to parliamentary assemblies, as these agreements result from experts' evaluations, adopted after consultation with the States but with the support of extensive internal research and expert external advice. This results in equalization being based on complex formulas that difficult their effective understanding, making parliamentary oversight very difficult to achieve<sup>16</sup>.

### 3. *Canada: hyper-executive federalism at its best*

The Canadian system of responsible government, modelled after the Westminster model, results in a centralization of power almost completely in the hands of the executive<sup>17</sup>. Thus, it must come as no surprise that Canada is portrayed as a model characterized by a clear "executive domination of Parliament"<sup>18</sup>. Thus, it is not difficult to understand that the trajectory of Canadian federalism in fiscal matters has resulted in a model dominated by hyper-executive federalism, in which most deci-

<sup>14</sup> N. WARREN, *Reform of the Commonwealth Grant Commission: It's all in the detail*, in *IUS-NW Law Journal*, 31(2), 2008, pp. 530-552, here: p. 548.

<sup>15</sup> C. SAUNDERS, *Towards a Theory for Section 96: Part 1*, in *Melbourne University Law Review*, 16(1), 1987, pp. 1-31; C. SAUNDERS, *Towards a Theory for Section 96: Part 2*, in *Melbourne University Law Review*, 16(4), 1988, pp. 699-724; N. WARREN, *Reform of the Commonwealth Grant Commission*, cit. p. 530.

<sup>16</sup> A. SHAH, *Horizontal Fiscal Equalization in Australia: Peering Inside the Black Box*, 2017, p. 30.

<sup>17</sup> D. BAKER, *Not Quite Supreme: The Courts and Coordinate Constitutional Interpretation*, Montreal & Kingston, McGill-Queen's University Press, 2010, p. 103.

<sup>18</sup> J. WEBBER, *The Constitution of Canada: Contextual Analysis*, Oxford, Hart Publishing 2015, p. 77.

sions are adopted behind closed doors with minimal participation from the legislative.

In fact, this model represents the paradigm of federal-provincial diplomacy through which the provinces try to influence the federal government's decision-making in managing the three main sources of federal transfers: the Canada Health Transfer for healthcare, the Canada Social Transfer for post-secondary education and social services, and, lastly, equalization to mitigate interregional disparities. While Canada is one of the federal states granting subnational governments relatively greater fiscal autonomy in comparative terms, federal transfers remain important. Equalization was not part of the original deal of Confederation. However, some traces of the importance of territorial solidarity can be found in articles 118 and 119 of the 1867 Constitution, with these providing for federal per capita subsidies to improve the provinces' financial situation. The equalization program was introduced only in 1957 under the Tax Rental Agreements. These agreements were negotiated by the federal government and the provinces, as provincial governments were required to enact legislation permitting the delegation of their tax powers to the federal level<sup>19</sup>. With the exception of Quebec, which refused to participate in all tax rental or tax collecting agreements concluded between the federal government and the provinces after World War II, all provinces agreed to this scheme<sup>21</sup>.

As a consequence, the equalization program quickly established itself as one of the core elements of Canadian federalism, providing financial stability to the provincial governments. Its primary aim was to give provinces unconditional payments equal to the amounts needed to bring the per capita proceeds of rental payments (or of the allowed tax abatement) to the level of the average per capita yield of the two provinces

<sup>19</sup> *Federal-Provincial Tax-Sharing Arrangements Act, 1956*, 4 & 5 Eliz. 2, ch. 29. With respect to provincial legislation aimed at its enacting, see the *Federal-Provincial Agreement Act, 1957*, ch. 142 in British Columbia or *The Tax Rental Agreement Act, 1957*, ch. 22, in Saskatchewan.

<sup>20</sup> M. JANIGAN, *The Art of Sharing: The Richer versus the Poorer Provinces since Confederation*, Montreal & Kingston, McGill-Queen's University Press, 2020, pp. 247-250.

<sup>21</sup> D. BÉLAND, A. LECOURS, *Accommodation and the politics of fiscal equalization in multinational states: The case of Canada*, in *Nations and Nationalism*, 20(2), 2014, pp. 337-354, here: pp. 343-344.

with the highest direct tax yield. Nevertheless, it will not be until 1982, as part of the patriation process, that the equalization mechanism – or more precisely, the principle of equalization – was enshrined into article 36.2 of the 1982 Constitution. The constitutional entrenchment of the program did not have a significant impact on its functioning. Due to the vagueness and reduced scope of section 36.2, equalization continues to be governed in practice by an act of Parliament. The primary legal framework governing equalization is, in fact, the Federal-Provincial Fiscal Arrangements Act of 1985. This legislation outlines the technical and operational details of the program, including aspects such as timing (Article 3.94) and the method for calculating payments (Article 3.2). Consequently, the equalization principle enshrined in section 36.2 of the Constitution does not impose significant limitations on the federal legislator. *De facto*, the executive enjoys considerable discretion to establish, modify, and terminate the terms of equalization transfers, provided they maintain a commitment to the principle of equalization in some form. This is because changes are enacted as part of the federal budget, as they represent federal spending programs<sup>22</sup>. As a result, the authority to make decisions on various aspects of the program, including the formula determining which provinces receive payments, rests solely with the federal government.

Also, provincial participation in the decision-making process over equalization is rather limited. Although provincial governments tend to be consulted, there is no legal obligation to do so, and the federal government may unilaterally alter or extend the compact without further discussion. Indeed, in 2018, the federal government opted to prolong the existing program until 2024. This decision was made notwithstanding the considerable grievances expressed by various provincial leaders who advocated for a comprehensive revision of the distribution of transfer payments. Provincial involvement was confined to a limited consultation during a Finance Ministers' meeting in December 2017. It is noteworthy that during this meeting, equalization was not even one of the primary sub-

<sup>22</sup> R. BOADWAY, *Fiscal Equalization: the Canadian experience*, in N. BOSCH, J.M. DURÁN (eds.), *Fiscal Federalism and Political Decentralization: Lessons from Spain, Germany and Canada*, Cheltenham, Edward Elgar, 2008, pp. 109-136, here: p. 132.

jects of discussion; rather, the discourse predominantly revolved around deliberations on cannabis taxation.

Consultation, if any, takes place within the context of the Federal-Provincial-Territorial Meeting of Finance Ministers, an intergovernmental body comprising the federal Minister of Finance along with their provincial and territorial counterparts that generally meets twice a year to discuss economic and fiscal issues. Embedded within this forum is a dedicated committee – the Fiscal Arrangements Committee – responsible for conducting consultations on fiscal transfers, encompassing the equalization program. This body provides the provinces with an opportunity to articulate their views regarding equalization and to demand changes to the compact. However, it is important to note that these deliberations are advisory in nature, rendering any agreement that may be reached as a mere recommendation to the federal government. Consequently, this intergovernmental body lacks decision-making authority.

The lack of provincial participation has led provincial governments to promote horizontal cooperation as a mechanism through which to make their demands known to the federal executive. The Council of the Federation (COF), an intergovernmental body established in 2003 comprising the provinces and territories, has taken on a proactive role in this regard. Confronted with Paul Martin's decision to implement a "new funding formula framework" in 2004, the COF commissioned an independent advisory panel to suggest changes to the Canadian system of financial relations<sup>23</sup>. This advisory panel operated concurrently with an expert panel known as the Expert Panel on Equalization and Territorial Formula Financing, appointed by the federal government with a mandate centered on the evaluation and assessment of the existing equalization program<sup>24</sup>. Both panels issued similar recommendations, with these being later adopted by the government of Stephen Harper. Likewise, Harper's government also welcomed some of the traditional demands of resource-rich provinces regarding the treatment of income

<sup>23</sup> Reconciling the Irreconcilable. Addressing Canada's Fiscal Imbalance, Council of the Federation, 2006.

<sup>24</sup> Achieving A National Purpose: Putting Equalization Back on Track, Expert Panel on Equalization and Territorial Formula Financing, 2006.

derived from natural resources in the formula. Through this decision, the federal government sought to address the concerns of resource-abundant provinces like Alberta and Saskatchewan, which had been vociferous critics of the system. Therefore, it is no coincidence to find that these provinces have played a pivotal role in Haper's victory after thirteen years of Liberal government. Simultaneously, the federal government aimed to preserve distinct arrangements for Newfoundland and Labrador as well as Nova Scotia, allowing these provinces to adhere to the previous framework for determining their payments, thus circumventing the new fiscal capacity cap<sup>25</sup>.

Since the mid-2000s, equalization has emerged as a significant source of intergovernmental conflict, encompassing both vertical and horizontal dimensions in Canada. The federal unilateralism that characterizes the governance of equalization in Canada, coupled with the zero-sum nature of the arrangement where any alteration in revenue distribution leads to winners and losers, has contributed to fuel disputes between receiving and not receiving provinces. This escalation in tensions is attributed to the heightened politicization of the program, as both federal and provincial politicians have vocally expressed different claims concerning its operation, with these increasing during periods of economic recession<sup>26</sup>. As a result, successive federal governments have used equalization as a means to court specific provincial electorates. This has involved either extending special arrangements akin to those negotiated with Newfoundland and Labrador and Nova Scotia, often referred to as side deals, or implementing adjustments to the formula to prevent abrupt reductions in equalization revenue in the event that Ontario, the most populous province in the federation, transitions to a recipient status<sup>27</sup>. The federal executive did not publicly announce this decision, and the lack of transparency was notable to the extent that opposition MPs and provincial governments

<sup>25</sup> J. FEEHAN, *Canada's Equalization Formula: Peering Inside the Black Box ... And Beyond*, in *The School of Public Policy Research Papers*, 7(4), 2014, pp. 1-30, here: p. 4.

<sup>26</sup> D. BÉLAND, A. LECOURS, *The Ideational Dimension of Federalism: The 'Australian Model' and the Politics of Equalisation in Canada*, in *Australian Journal of Political Science*, 46(2), 2011, pp. 199-212, here: pp. 207-208.

<sup>27</sup> J. FEEHAN, *Canada's Equalization Formula Program: Political Debates and Opportunities for Reform*, in *IRPP Insight*, 30, 2020, pp. 1-20, here: p. 9.

seemed to be unaware that, within the 584 pages of the Budget Implementation Act<sup>28</sup>, there was a provision to prolong the agreement until 2024. Subsequently, this information was brought to light by the press and later confirmed by the Minister of Finance.

To mitigate the controversy surrounding equalization and to avoid any potential escalation of intergovernmental tensions with the provinces, the federal government opted in 2018 to discreetly extend the program under its existing terms until 2024. The federal government refuted any intent to withhold the decision from the provinces and explained that federal officials had maintained close communication with their provincial counterparts in the preceding months, including a brief discussion during the Federal-Provincial-Territorial Meeting of Finance Ministers. Nevertheless, the Premiers of Saskatchewan and Alberta contended that while provinces were aware of the federal government's inclination to preserve the status quo, there had been no formal notification regarding the decision to prolong the existing formula. They further expressed their dissatisfaction with the federal government's reluctance to engage in discussions concerning their proposals for reforming the current allocation scheme among the provinces. Despite these critiques and repeated calls for reform, the federal government followed a similar course in 2023, extending the system until 2029 through a provision embedded in an omnibus law in Parliament aimed at implementing budgetary measures. The processes that led to the renewal of the equalization compact in 2018 and 2023 perfectly illustrate the internal traits of Canadian federalism with respect to financial relations: the dominance of federal unilateralism and limited intergovernmental cooperation, which is generally held behind closed doors and mostly informally. Because of this, Canada can be considered as the textbook example of (hyper) executive federalism<sup>29,30</sup>.

<sup>28</sup> See Division 3 of Part 6 of the *Budget Implementation Act*, 2018, No. 2 that amends the *Federal-Provincial Fiscal Arrangements Act*.

<sup>29</sup> The dominance of executive federalism has been challenged by Cameron and Simeon who argue that Canadian federalism was moving towards a more collaborative approach in intergovernmental relations although this collaboration has not yet reached equalization. See: D. CAMERON, R. SIMEON, *Intergovernmental Relations in Canada: The Emergence of Collaborative Federalism*, in *Publius*, 32(2), 2002, pp. 49-71.

<sup>30</sup> R.L. WATTS, *Executive Federalism*, cit. pp. 3-6.

As the experiences of 2018 and 2023 show, the role of parliaments at all levels of government was practically non-existent. The provincial legislatures did not intervene in the process, with all negotiations or lobbying being done by the provincial executives. At the federal level, the House of Commons and the Senate were mere rubber stampers of the decision of the federal government, without any meaningful decision-making power, especially if we take into account that both extensions were buried in long pieces of legislation initiated from the executive and that mostly dealt with other issues.

#### *4. Germany: an executive dominated second chamber*

In Germany, revenue sharing is an essential component of financial relations. Given the *Länder's* limited power to tax, they rely on federal transfers to cover their budgets. The German territorial financial system hinges on two constitutionally mandated instruments: a territorial-based tax revenue sharing framework (termed as primary distribution) and equalization mechanisms (referred to as secondary distribution). With regard to the latter, beginning in 2020, the system is founded upon two components: value-added tax (VAT) adjusted revenue sharing and federal supplementary transfers, encompassing both general and special-purpose allocations<sup>31</sup>. The legal framework governing these elements is stipulated in the Basic Law (Articles 106-107 BL), and later developed in two federal laws: the Revenue-Sharing Criteria Act (*Maßstäbengesetz - MaßstG*) and the Financial Equalisation Act (*Finanzausgleichsgesetz - FAG*) of 2001, last amended in 2018.

The primary distribution allocates revenue in accordance with the derivation principle (i.e., the local origin of the revenue), thus not serving an equalizing function. Conversely, the secondary distribution allocates VAT-revenue to rectify, without entirely eliminating, the disparity in financial capacity that persists among the *Länder* following the primary distribution of revenue. In other words, as the constitutional amendment of 2018 explicitly underscores, the instrumental role of VAT distribution

<sup>31</sup> The horizontal equalization among the *Länder* (so-called *Länderfinanzausgleich*) for which Germany is considered an emblematic case has been abolished with the 2018 constitutional reform, ceasing to exist as of 2020.

is to guarantee adequate compensation (*angemessenen Ausgleich*) for horizontal imbalances as prescribed following the mandate of Article 107.2 BL<sup>32</sup>.

Examining VAT revenue distribution in greater depth, it comprises two stages: the initial step seeks to delineate the respective portions allocated to the federal and subnational levels (vertical sharing), followed by a subsequent stage that allocates these revenues among the individual *Länder* (horizontal sharing). After the vertical allocation of VAT revenues, the resources attributed to the *Länder* undergo horizontal redistribution. Since 2020, this allocation continues to be primarily based on population, albeit adjusted with additions or deductions contingent on the financial capacity of the *Länder*. In essence, those *Länder* with a below-average financial capacity will receive a top-up, while those with an above-average capacity will see corresponding reductions in VAT-derived resources. These adjustments are calculated based on 63% of the deviation from the average financial capacity of the *Länder*. This serves to elevate the financial capacity of all *Länder* below the average closer to the national average, though it does not entirely eliminate existing disparities. Furthermore, the less prosperous *Länder*, whose fiscal capacity remains below average even after VAT redistribution, will receive additional vertical transfers in the form of general supplementary federal grants (Article 107.2 BL). Supplementary grants for well-determined special needs are also foreseen. Both forms of federal transfers are stipulated by constitutional provisions and subsequently delineated in detail in the aforementioned federal laws, subject to approval by the *Länder* via the *Bundesrat*.

The role of the “federal second chamber”<sup>33</sup>, the *Bundesrat*, is the distinguishing feature that characterizes the German system. As a result,

<sup>32</sup> On the new equalization mechanism and on the impact of the 2018 reform on the federal system as a whole, see: C. SEILER, *Flucht in die Intransparenz*, in *Jahrbuch des Föderalismus* 2017, 2017, pp. 52-67; J. WIELAND, *Notwendigkeit einer Föderalismusreform III – Wie kann die Finanzverfassung zukunftsfest gemacht werden?*, in T. SCHWEISFURTH, W. VOSS (eds.), *Haushalt- und Finanzwirtschaft der Länder in der Bundesrepublik Deutschland*, Berlin, Berliner Wissenschafts-Verlag, 2018, pp. 247-261.

<sup>33</sup> Although according to the constitutional jurisprudence, it cannot be considered as “a second chamber of single legislative body” – BverfG decision of 25<sup>th</sup> June 1974, BverfGE 37, 363, (380) – *Bundesrat*, prominent scholars (among the many: M. KOTZUR, *Federalism and Bicameralism - The German « Bundesrat » (Federal Council) as an Atypical Model*, in J. LUTHER, P. PAS-



Germany can be considered as the prototype of a tax-revenue sharing mechanism on a “legislative-assembly base”, with the *Länder* being indirectly involved in the management of the equalization program through the *Bundesrat*.

To better grasp the *Länder*’s role in shaping equalization, it is thus crucial to begin with an examination of the *Bundesrat*. This institution represents the executives of the *Länder*, playing a pivotal role in determining which interests will impact the adoption of equalization mechanisms<sup>34</sup>. The German approach entails conferring a co-legislative function to the *Länder* as the *Bundesrat* is expressly vested – among others in financial matters – with a legislative function equal to the one assigned to the *Bundestag*, the lower chamber of Parliament (Arts. 50 and 59.2 BL)<sup>35</sup>. Specifically, the *Bundesrat* is tasked with approving all constitutional and regular laws pertaining to financial matters, particularly those that have implications for the financial allocation of the *Länder*. Consequently, the consent of the *Bundesrat* guarantees the inclusion of territorial interests in the federal decision-making process, while simultaneously upholding the consistency of the public finance system across Germany.

This legislative framework ensures an equal role for both the *Länder* represented by the *Bundesrat* and the federal level represented by the *Bundestag*. This scheme safeguards the autonomy of subnational governments as the federal level alone cannot unilaterally alter the rules. However, it is important to note that the consent of the *Bundesrat* does

SAGLIA, R. TARCHI (eds.), *A World of Second Chambers. Handbook for Constitutional Studies on Bicameralism*, Milan, Giuffrè, 2006, pp. 257-290, here: p. 258) observe that from a functional standpoint (not from a formal one) the *Bundesrat* can be considered ‘a second chamber’ when it takes part in the legislative process.

<sup>34</sup> All legal acts in financial matters require the *Bundesrat* approval, if this is prescribed by a provision of the Basic Law. In sum, if the act affects the *Länder* finances, the consent of the *Bundesrat* is necessary. All in all, financial relations are an emblematic example of the phenomenon known as participatory federalism (*Beteiligungsföderalismus*). See: J. WOELK, *La forma segue la funzione: il Consiglio federale tedesco (Bundesrat)*, in E. ROSSI (ed.), *Studi pisani sul Parlamento*, Pisa, Pisa University Press, 2014, p. 161.

<sup>35</sup> Pursuant to art. 105.3 GG “Federal laws relating to taxes the revenue from which accrues wholly or in part to the *Länder* (omissis) shall require the consent of the *Bundesrat*”. The scope of the provision is rather broad, as it includes all major taxes of the system. It is estimated that 85% of overall tax-revenue comes from *Zustimmungsgesetze*, that is, laws that require the consent of both the *Bundestag* and the *Bundesrat*.

not directly uphold the autonomy of each individual *Land*. Instead, it facilitates a form of representation of territorial interests on a collective dimension. The subnational level, participating as a unified entity akin to a “second-level federal pact”<sup>36</sup>, results in the integration of individual units into the federal legal framework, albeit with some constraint on the autonomy of each entity due to the composition and functioning of the Bundesrat<sup>37</sup>.

The approval process of all equalization laws in Germany contains a certain paradox. Although the process formally requires the support of a majority of *Länder* (or a 2/3 majority in case a constitutional amendment is at stake), all federal laws on equalization have been approved by unanimity, only for later being challenged in front of the Federal Constitutional Court. This shows that although the content often reflects the compromise reached at the *Länder*-level, equalization is, per se, a divisive matter that pits the payers against the recipients<sup>38</sup>. Furthermore, it is worth noting that, in practice, these decisions are the outcome of an intergovernmental compromise, reached between the *Länder* and the *Bund*, with parliamentary approval often following suit.

The 2018 reform is a good example of the increasing weight of intergovernmental agreements in equalization related matters in Germany, departing from the pattern observed during the *Föderalismusreform* I and II. In fact, an initial phase was dominated by classic executive federalism, with discussion taking place behind closed doors among the Prime Ministers and Ministers of Finance of both the Federation and the *Länder*. Subsequently, negotiations shifted between phases where only the *Länder* were involved through the Conference of Prime Ministers (an informal body for horizontal self-coordination), and occasions where the federal level also participated in the discussions. After some deliberation, the *Länder* reached an agreement in December 2015. One year later, an intergovernmental agreement with the federal level was ultimately sealed

<sup>36</sup> F. PALERMO, J. WOELK, *Il Bundesrat tra continuità e ipotesi di riforma*, in *Le Regioni*, 6, 1999, pp. 1097-1122, here: p. 1103.

<sup>37</sup> J. WOELK, *La forma segue la funzione*, cit. p. 165.

<sup>38</sup> T. LENK, P. GLINKA, *Der neue bundesstaatliche Finanzausgleich – eine Reform und viel Reformaufschub*, in *Wirtschaftsdienst*, 7, 2017, pp. 506-512, here: p. 507-508.

in the form of a “package deal”<sup>39</sup> – a resolution criticized for its lack of transparency, colloquially described as the ‘Barter’<sup>40</sup>.

This process underscores the diminishing role of the legislator, who often finds themselves relegated to the task of ratifying decisions made elsewhere, resulting in the legislative assemblies being substantially deprived of their authority<sup>41</sup>. Thus, Germany seems to be witnessing a notable shift of decision-making authority away from parliamentary institutions and towards the executive of the various levels of government involved, reinforcing the role of executive federalism in financial matters and, in particular, in equalization related decisions.

### 5. *Spain: a center dominated model*

The 1978 Spanish Constitution paved the way for the political decentralization of the country. However, the initial phases of this process primarily focused on the delegation of policy responsibilities to the Autonomous Communities (ACs). A process that did not involve a concurrent transfer of financial authority. In fact, the fiscal autonomy of ACs operating under the common regime remained relatively limited, as key tax bases such as VAT, income tax, and corporate tax continued to be under the full control of the central State even after the enactment of the Organic Law on Financing of the Autonomous Communities (LOFCA)<sup>42</sup> in 1980<sup>43</sup>. The process of fiscal decentralization gained significant momentum with the

<sup>39</sup> A. BENZ, J. SONNIKEN, *Advancing Backwards: Why Institutional Reform of German Federalism Reinforced Joint Decision-Making*, in *Publius*, 48(1), 2017, pp. 134-159, here: p. 150.

<sup>40</sup> C. SEILER, *Flucht in die Intransparenz*, cit. p. 58.

<sup>41</sup> U. HADE, *Finanzausgleich: Die Verteilung der Aufgaben, Ausgaben und Einnahmen im Recht der Bundesrepublik Deutschland und der Europäischen Union*, Tübingen, Mohr Siebeck, 1996, p. 199.

<sup>42</sup> Ley Orgánica 8/1980, de 22 de septiembre, de Financiación de las Comunidades Autónomas.

<sup>43</sup> Together with the common regime ACs, two special regimes coexist in the Basque Country (*concierto*) and Navarre (*convenio*) as a result of various historical prerogatives recognized in the Constitution. In short, and in simplified form, these ACs have very broad powers regarding taxation and collect all taxes but custom duties and payroll taxes. They then make annual transfers to the central government, called quota in the Basque Country and contribution in Navarre, in order to fund the cost of states services (e.g. national defense, foreign service, infrastructures, social security etc.). This regime has been controversial, in particular regarding its application in the Basque Country, as the quota is agreed on a quinquennial basis through a

reform of the LOFCA in 1997. The ACs were granted the authority to determine tax rates and establish tax credits and allowances over ceded taxes for the first time. This marked a shift from an initial highly centralized tax sharing model, in which the ACs primarily relied on transfers and had no control over ceded taxes, to a system where the ACs possess some degree of discretion over ceded taxes. It is worth noting, however, that ceded taxes are created and regulated by the national legislator, who maintains the final authority in order to ensure a certain level of uniformity throughout the common regime territory<sup>44</sup>.

The progressive gain in fiscal autonomy that the Autonomous Communities have achieved through various LOFCA reforms has resulted in the augmentation of both their share of revenue and their level of control over ceded taxes. However, this has had the unintended consequence of widening regional disparities. Consequently, an equalization program called *Participación en los Ingresos del Estado* was created, consisting of an unconditional transfer targeting needs compensation. This transfer scheme was designed to furnish common regime Autonomous Communities with sufficient financial resources to meet their expenditure requirements. However, it was asymmetrical in nature due to two reasons: not all the ACs held the same level of competences at that time, nor did all of them benefit from ceded taxes. This model remained in place until 2001 when it underwent a reform and was renamed as *Fondo de Suficiencia*. This change was made after most Autonomous Communities had modified their Statutes of Autonomy to access the maximum level of competences accorded to them by the Spanish Constitution. The fund adhered to the same underlying principle of compensating for needs and was the product of a unanimous intergovernmental agreement reached by all common regime ACs, subsequently ratified by parliament as an amendment to the LOFCA<sup>45</sup>.

political negotiation that tends to underestimate the weight and cost of those services provided by the central state.

<sup>44</sup> J. ZORNOZA, *New Trends in Fiscal Decentralization: a Spanish View*, in S.A. LÜTGENAU (ed.), *Fiscal Federalism and Fiscal Decentralization in Europe: Comparative Case Studies on Spain, Austria, the United Kingdom and Italy*, Innsbruck, StudienVerlag, 2014, pp. 105-126, here: pp 109-114.

<sup>45</sup> Ley Orgánica 7/2001, de 27 de diciembre, de modificación de la Ley Orgánica 8/1980, de 22 de septiembre, de Financiación de las Comunidades Autónomas (LOFCA).

Against this framework, the Fiscal and Financial Policy Council (FFPC), established by Article 3 of the LOFCA, serves as the entity responsible for coordinating fiscal relations between the central State and the ACs. This intergovernmental body is comprised of the National Minister of Finance, the Finance Minister of each Autonomous Community (along with the Finance Councilors of the two Autonomous Cities of Ceuta and Melilla). Although the agreements reached within the CPFF are not legally binding, as they are presented as recommendations to the central government (as stated in Article 10 of the Council's charter), they hold significant political weight. To pass these recommendations, a two-thirds majority is required in an initial vote, while an absolute majority suffices in a subsequent vote, which must occur no later than ten days after the first vote. Regarding the voting system, it is noteworthy that the central government holds a privileged position in relation to the ACs. While each AC has one vote, the central government possesses the same number of votes as all the ACs combined. This predominance on the part of the central authority curtails the decision-making capacity of the ACs, as in a second vote, the central government can advance its position with just the support of one single AC. The publication of the initial results of the model approved in 2001 in 2005 revealed certain shortcomings<sup>46</sup>. Despite the clear need to reform the system, it was not until 2008 that the central government decided to set the reform process in motion. The first phase involved a series of bilateral meetings with the various Autonomous Communities to gather insights into their requests. This enabled the central government to develop a proposal, which was subsequently presented to all ACs within the FFPC. Following the formulation of the initial proposal, the central government engaged in further bilateral consultations with the ACs. Regrettably, this process was characterized by a lack of transparency, as the documents used as the basis for the calculations were not made public. Additionally, the interests of certain ACs, notably Catalonia, took precedence over those of others<sup>47</sup>.

<sup>46</sup> J. RUIZ-HUERTA, A. HERRERO ALCADE, *Fiscal Equalization in Spain*, in N. BOSCH, J.M. DURÁN (eds.), *Fiscal Federalism and Political Decentralization: Lessons from Spain, Germany and Canada*, Cheltenham, Edward Elgar, pp. 147-165, here: pp. 154-158.

<sup>47</sup> F.J. ROMERO CARO, *Horizontal cooperation and financial relations in Spain: An analysis on how the Autonomous Communities set the agenda for the reform of territorial financing*, in *Revista de Estudios Políticos*, 199, 2023, pp. 133-164, here: pp. 139-144.

In clear contrast to the unanimous agreement of 2001, this renewal process witnessed strong divisions along party lines, which not only pitted some ACs against others but also diffculted the necessary amendment of the LOFCA, which requires an absolute majority in Parliament to enact the new system. Ultimately, the national executive and its allies in Congress managed to secure the necessary majority by a slim margin of a single vote, leading to the formal enactment of the new system through Organic Law 3/2009<sup>48</sup>.

The 2009 reform constituted a substantive revision of the equalization model, which presently encompasses four distinct funds. Foremost among these is the *Fondo de Garantía de Servicios Públicos Fundamentales* (FGSPF). It is purposed to ensure that, in the event of each Autonomous Community exerting an equivalent tax effort, an equivalent per capita allocation of resources is provided to finance the indispensable services of the welfare state: education, health, and social services<sup>49</sup>. The fund encompasses both a horizontal component, wherein Autonomous Communities contribute 75% of their resources, and a vertical component entirely funded by the central government. The second fund, known as the *Fondo de Suficiencia Global* (FSG) or the *status-quo* clause, is the product of a consensus achieved by all involved parties during the negotiation phase. Its purpose is to guarantee that every AC receives at least the same resources than in the preceding system, irrespective of their financial requirements<sup>50</sup>. In addition, the system incorporates two convergence funds (which do not have an equalizing goal), akin to the FSG, which are entirely underwritten by the State: the *Fondo de Competitividad* and the *Fondo de Cooperación*.

The equalization compact, as established in 2009, was slated for renewal after a period of five years, in accordance with the provisions set forth by Law 22/2009. In 2017, during the *Conferencia de Presidentes*, Spain's main

<sup>48</sup> Ley Orgánica 3/2009, de 18 de diciembre, de modificación de la Ley Orgánica 8/1980, de 22 de septiembre, de Financiación de las Comunidades Autónomas.

<sup>49</sup> M. VILALTA, *Pasado, presente y future de la nivelación en el modelo de financiación de las Comunidades Autónomas*, in *Mediterráneo Económico*, 30, 2016, pp. 87-116, here: pp. 94-99.

<sup>50</sup> A. CASTELLS, *The Relation Catalonia/Spain: Some Financial and Economic Aspects*, in G. POLA (ed.), *Principles and Practices of Fiscal Autonomy: Experiences, Debates and Prospects*, Farnham, Ashgate, 2015, pp. 203-225, here: p. 212.

vertical intergovernmental forum, the national government and the Autonomous Communities reached a consensus to establish an expert panel entrusted with formulating a proposal. This panel comprised five experts designated by the central government, along with one appointed by each AC or Autonomous City. The ensuing proposal reflected the diversity of perspectives among the ACs. Notably, the proposition to eliminate the *status-quo* clause emerged as a particularly contentious issue, as some ACs expressed concerns over potential reductions in their allocations from the system. Strikingly, Catalonia opted not to play a leading role in this process and abstained from nominating any expert. Informally, the interests of Catalonia were represented by the nominee of the Balearic Islands. Moreover, Catalonia has refrained from participating in the intergovernmental Council (FFPC), contending that substantive deliberations are precluded, given that decisions are purportedly preordained by the central government. Regrettably, Catalonia's non-engagement, coupled with the central government's reluctance to initiate comprehensive reform during a period of heightened political instability – characterized by four general elections in less than four years, and compounded by the tensions stemming from the illegal declaration of independence by Catalonia in 2017 – culminated in the abortive progress of the reform endeavor. Despite the imperative nature of reform prompted by the pandemic and the ensuing economic downturn, political divergences have thus far impeded its initiation, notwithstanding the fact that the current system should have expired in 2014.

After years of delay, the reform of the system appeared to get underway in 2021 when the central government undertook to present the autonomous communities with a draft proposal on the main elements of the system. This proposal came in response to the mobilization of the regional executives, who had held several summits on the subject, grouping themselves into different groups based on their interests<sup>51</sup>. However, the process did not crystallize due to political instability and the proximity of regional elections, which made any agreement impossible.

<sup>51</sup> F.J. ROMERO CARO, *Horizontal cooperation and financial relations in Spain*, cit. pp. 144-153.

The experience of the last two reform processes (2008 and 2021) confirms the growing importance of executive federalism and bilateralism in Spain when addressing changes in the equalization system. Both processes have been characterized by parallel negotiations between the central executive and the Autonomous Communities, conducted outside the FFPC and formally confirmed in that forum only at a later stage without any real debate on their content. This lack of real debate is due to the FFPC being an institution dominated by the national executive. The role of the regional parliaments has been nil during these negotiation processes, limited, at most, to approving motions expressing their claims. In the case of the national parliament, its participation has become more important as a modification of the LOFCA is necessary for the entry into force of any reform. However, the role of parliament has been restricted to passing or rejecting the reform of the LOFCA as a whole, without the latter having been involved in the discussions that lead to the approval of the reform at the FFPC.

## 6. *Concluding remarks*

The article shows the dominance in all four cases of the hyper-executive paradigm of financial relations. The variety of institutional solutions in the legal framework fades away when the different systems are observed in action.

The undertaken analysis has, in fact, identified from 'the law in the books' perspective four different paradigms among federal systems. Two of them heavily rely on institutions, with tax-revenue sharing being carried out either by an arm-length agency on a 'technical base' - exemplified by the CGC in Australia - or by a 'legislative-assembly base' with Germany's *Bundestag+Bundesrat* as a reference model. In the other two cases, intergovernmental relations play -even at first glance- a decisive role, although with different degrees of institutionalization, varying from the quasi-constitutional Spanish CPFF as a forum for intergovernmental financial relations to the almost non-existent legal entrenchment of the Canadian model of federal-provincial diplomacy.

Having a closer look at the dynamic dimension of equalization, ie., into the folds of how the rules work in practice, emerges however a clear trend which leads the different paradigms to converge towards a common point of reference. In all systems, the involvement of subnational



governments undergoes a twist, which shows the clear dominance of the intergovernmental dimension, with an emphasis on the executives of the levels of government involved.

From a comparative constitutional perspective, the question arises whether such an outcome has anything to do with the existing diversity in terms of rules entrenched in the financial constitutions, understood in the broad sense. If the latter are investigated, in fact, it emerges that constitutions of European federal systems tend to have a greater degree of detail than those of common law, or those that are (or have been) part of the Commonwealth. In Germany, the provisions concerning the decision-making dimension of equalization have a significant degree of detail, and the involvement of the *Bundesrat* finds express and clear guarantees as to the rights and limits of the *Länder*. In comparison, the Spanish financial constitution contains very few provisions referring to fiscal federalism. However, it provides (quasi-)constitutional anchorage to the FFPC in the LOFCA, where the Council composition, role, and tasks are thoroughly regulated. Contrariwise, the Canadian constitution mandate the principle of equalization without any further specification as to the scope and the institutional dimension thereof. Australia is even more extreme as a case in point, considering that the very principle of horizontal equalization is only carved out by expansive interpretation of Article 96, initially meant to guarantee general financial assistance to the states. Furthermore, there is no constitutional entrenchment of any institution (except for the Loan Council) vested with the task of governing financial dynamics. Only if the fiscal constitution in the broad sense is taken as the parameter, the CGC is in theory the institution in charge of determining scope and limits of equalization and its adaptation over time. Despite the detected diversities characterizing the different financial constitutions, when put in motion all systems show the emergence of intergovernmental fora, dwelled by the executives of the different levels of government that end up dominating decision-making processes and determining scope and limits of equalization. To be more precise, all cases under scrutiny are strongly conditioned by practice, which shows that even when the role of the executives at all levels is not prescribed by law, it becomes *de facto* advisable or even necessary from a political point of view. This is with no doubt the case of Australia, with the

executives of the States being consulted during the entire process from the appointment of the CGC members to its recommendations, and of Canada as the federal government usually advances its plans on equalization to the provincial government before implementing them through the federal budget. But this shift also entails Germany and Spain. In Germany, the involvement of the *Länder* executives is twofold: preliminarily, due to the increasing weight of intergovernmental agreements in equalization related matters, and subsequently through the *Bundesrat* in the parliamentary process of approving the law. Whereas in Spain, the Autonomous Communities and the national government meet at the FFPC, which despite its flaws, has become the forum that channels territorial participation in financial related matters, with the executives of the latter negotiating with the national government any possible changes and de facto making the final decision.

This doesn't contradict the constitutional nature of equalization. First, the very nature of the constitutionally entrenched rules for this specific segment of financial relations is typically limited to the proclamation of the principle thereof, or at best to the prescription of 'loosely knit' rules through the use of vague concepts. Second, practice itself in this field is typically included under the umbrella concept of financial constitution. The latter expression could be considered an evolution of the notion of fiscal constitution that first appeared in 1977 in The University of Chicago Law Review thanks to a contribution by Professor Kenneth W. Dam (law and economics)<sup>52</sup>, and later used by two famous American economics scholars—James Buchanan and Richard Wagner—to refer to those written or unwritten rules that guide fiscal decisions in the United States<sup>53</sup>. As such, it takes credit for including not only rules “formally incorporated in some legally binding and explicitly constitutional document”, but also unwritten rules like “customary, traditional, and widely accepted precepts”, thus giving relevance to political facts and economic rules that impact on the interpretation and implementation of the rules, as well as on the way in which a system functions and evolves.

<sup>52</sup> K.W. DAM, *The American Fiscal Constitution*, in *University of Chicago Law Review*, 44 (1977), pp. 271–320.

<sup>53</sup> J.M. BUCHANAN, R.E. WAGNER, *Democracy in Deficit: Political Legacy of Lord Keynes* (New York: Academic Press, 1977).

Such a converging trend brings to the fore another important element exhibited by all four cases and strongly conditioned by the hyper-executive nature of financial relations, as well as by the role of practice as a determinant of the functioning of equalization mechanisms in all systems under scrutiny, with no exception. This is about the relevance of partisan politics and their influence over (re-)distributive politics in federal systems, with the political momentum being sometimes decisive to reach agreements, as the cases of Germany and Spain clearly illustrate. This is favoured by the vague nature of the constitutional provisions governing this matter. This choice of constitutional design enables the political dimension of equalization to condition the performance of the program in practice; in fact, a balance between the best outcome in redistributive terms and what is politically feasible needs to be worked out and adjusted over time. As a result, the 'renewal' processes of the different equalization programs often bring high peaks of intergovernmental tension in which the different actors vie for concessions of a larger slice of the pie. Although the controversy generated by these political processes does not (necessarily) question the need for inter-territorial solidarity programs, it offers clear-cut evidence of divergences among SNGs about the level and scope of equalization. Interestingly, this can be seen in all federations: not only in diverse federations like Canada and Spain but also in homogeneous federations like Australia or Germany – where all federal laws providing for equalization have been approved by unanimity of the parties involved, but later have been challenged in front of the Federal Constitutional Court.

Beyond the impact exerted by the formal nature of financial constitutions, such a 'political' drift is favoured by the very function of equalization mechanisms. By pitting the richer/donor subunits against their poorer/receiving counterparts, it opens a window of opportunity for subnational governments to mould the system to their own advantage and for the centre to use these mechanisms for expanding their political support rather than for reducing horizontal imbalances. Further, in centre dominated models, solidarity has also become an instrument to maintain the unity of the federal system or, at least, to try to accommodate certain nationalist demands regarding territorial financing within the constitutional boundaries. The Spanish experience, with Catalonia's intention to limit its contribution to horizontal solidarity being a central issue during the

negotiations leading up to the 2009 model, or the political impossibility of reforming certain aspects of the Canadian program that would harm Quebec's interests are two excellent examples of this practice.

In the light of this dynamic, it seems to be possible to conclude that the disempowerment of parliamentary bodies in the context of financial relations is not an anomaly of singled-out cases, but a common trait of all federal systems, especially when observed in their functioning. There is, as a rule, an expansion of the role of the executive with reference to the intergovernmental dimension. The democratic principle lies (if any) within the domestic jurisdiction, that is, when the exercise of the political autonomy of the individual entity on its territory is at stake, but when transcending the boundaries of the single unit, intergovernmental relations record a central role of the executives.

Such a drift is overall favored by the progressive overcoming of all forms of dual federalism, in favor of a cooperative dimension, which by nature is dominated by intergovernmental relations, with the executives of the different levels of government assuming out of necessity a key role<sup>54</sup>. This brings about a decision-making structure in which there is the need to find composition to the function of federalism as a multiplier of democracy, on the one hand, and the manifestations of the federal principle in its operation, on the other. While the traditional conception holds that democracy requires effective citizen participation in representative forums, on the other hand, for federal systems to function, the creation of a network of relationships and interactions of a political as well as technical-administrative nature is vital. To the extent that all federal systems have responded to these needs by creating formal and informal instruments and intergovernmental consultation processes, which involve senior officials or political figures of their respective administrations: the so-called 'institutions of executive federalism'<sup>55</sup>.

Rather, the pervasive nature of the phenomenon under consideration makes it necessary to reflect differently, that is, not so much on the pos-

<sup>54</sup> CLEMENT AKWASI BOTCHWAY, *The need for executive federalism in federal-provincial relations: The Canadian example*, in *Journal of Public Administration and Policy Research* 5 (2017), pp. 68-75.

<sup>55</sup> For a review of the literature on the subject, see: F. PALERMO, K. KÖSSLER, *Comparative Federalism: Constitutional Arrangements and Case Law*, Hart, 2019, p. 253 ss.

sibility of eliminating such solutions, but rather on whether and how it is possible to recover on the front of democratic control, making the functioning of these institutions more transparent, without detriment to the functionality of federal systems, that is, succeeding in reaching decisions that in traditional parliamentary fora would be out of reach, or would require extenuating negotiations.

Le relazioni finanziarie intergovernative come paradigma del federalismo iper-esecutivo: spunti dal caso dei meccanismi di perequazione  
*Francisco Javier Romero Caro, Alice Valdesalici*

Abstract: Il ruolo pervasivo dell'esecutivo nella funzione legislativa trova un'amplificazione senza precedenti nel contesto dei sistemi federali, da cui il concetto di "federalismo esecutivo", con le relazioni finanziarie e, tra queste, i meccanismi di perequazione che rappresentano un precursore emblematico di questo fenomeno. La scelta di isolare questo specifico segmento di studi sul federalismo ha un duplice scopo. In primo luogo, permette di indagare il ruolo che rimane alle assemblee elettive nell'elaborazione di decisioni in ambiti tecnici e complessi come la finanza pubblica. In secondo luogo, mira ad analizzare un ambito essenziale per l'autonomia politica degli enti territoriali, consentendo così di capire come si sono sviluppati questi processi e i loro effetti a livello istituzionale. Per verificare questo assunto, lo studio indaga le procedure decisionali sui meccanismi di perequazione da una prospettiva comparata e di diritto costituzionale, con l'obiettivo ultimo di verificare l'entità della deriva esecutiva nei diversi paradigmi in atto. Di conseguenza, i diversi sistemi federali di interesse sono stati individuati per rappresentare la varietà di soluzioni "architettoniche" esistenti, includendo cioè nello spettro di analisi i diversi paradigmi che possono essere individuati nei sistemi federali di tutto il mondo. Su questa linea, verranno analizzati i seguenti casi: L'Australia come prototipo di condivisione delle entrate fiscali su una "base tecnica" (Commonwealth Grants Commission); il Canada che rappresenta, nelle questioni finanziarie, il paradigma della diplomazia federale-provinciale con scarso, se non nullo, radicamento giuridico; la Germania come prototipo di condivisione delle entrate fiscali su una "base legislativa-assembleare" (Bundestag+Bundesrat); e, infine,

la Spagna con l'istituzionalizzazione quasi-costituzionale della CPFF come forum per le relazioni finanziarie intergovernative.

**Abstract:** The pervasive role of the executive in the legislative function finds an unprecedented amplification in the context of federal systems, hence the concept of “executive federalism”, with financial relations and, among these, equalization mechanisms representing an emblematic forerunner of this phenomenon. The decision to isolate this specific segment of federalism studies serves a twofold purpose. First, it allows us to investigate the role that remains to the elective assemblies in elaborating decisions in technical and complex areas like public finance. Second, it aims to analyze an area that is essential to the political autonomy of territorial authorities, thus allowing us to understand how these processes have developed and their effects on the institutional level.

To test this preliminary assumption, the study investigates decision-making procedures on equalization mechanisms from a comparative and constitutional law perspective, with the ultimate aim to verify the magnitude of the executive drift in the different paradigms in action. Accordingly, the different federal systems of interest have been identified to portray the existing variety of ‘architectural’ solutions, i.e., including in the spectrum of analysis the different paradigms that can be detected in federal systems around the globe. Against this line, the following cases will be investigated: Australia as the prototype of tax-revenue sharing on a ‘technical base’ (Commonwealth Grants Commission); Canada representing, in financial-related matters, the paradigm of federal-provincial diplomacy with little, if any, legal entrenchment; Germany as the prototype of tax-revenue sharing on a ‘legislative-assembly base’ (*Bundestag+Bundesrat*); and, finally, Spain with the quasi-constitutional institutionalization of the CPFF as a forum for intergovernmental financial relations.

**Parole chiave:** federalismo fiscale; perequazione; federalismo esecutivo; relazioni intergovernative; centralismo

**Keywords:** Fiscal Federalism; Equalization; Executive Federalism; Intergovernmental Relations; Centralism