

**International Forum on Federalism in Mexico: Local and Global Challenges
Veracruz, Mexico, 15. - 17. November 2001**

**Report on the workshop about
“Federalism and public finance”
Thursday, November 15, 2001, 12:00-13:30**

Introductory words by the rapporteur

Very basically speaking, two main sources of income are to be distinguished for the federal level as well as for the sub national entities. The first source consists of taxes collected by the entity that actually uses them to finance the services it delivers to its citizens. The second source consists of the result of the redistribution of finances within the frame of the fiscal equalization. Contrary to other Federations, in none of the presented cases the own revenue of the sub national entities provides them with a sufficient level of income that would allow them to finance its basic public services to a larger extent. For this reason, the vertical fiscal equalization from the federal level to the sub national entities is indispensable in order to enable the latter to deliver public services, and the reallocation of resources is the main topic of discussion. In particular, the key questions are, who gets which percentage of the cake, and how does the redistribution have to be characterized in order to be just and not to restrain the autonomy of the sub national entities.

Resume of the presentations and discussions

According to Juan Marcos Gutiérrez Gonzáles, the very low level of decentralization within the United States of Mexico has led to the situation, that most of the resources, especially the taxable objects, were exploited by the Federation, and the proper income of the states has diminished to a very low level. The new decentralization tendencies led, among others, to a revision of the Law about Fiscal Coordination with the effect, that about 60% of the federal revenue is now redistributed to the states and municipalities. However, there is to be precised, that about one half of those allocations are bound to conditions. These allocations, to which he refers as “aportaciones”, are not freely usable by the states, but have to be utilized for the services that are defined by national legislation. Thus the center gives the states more resources on the one hand, while their autonomy is restrained on the other hand. Therefore, this “aportaciones” have an inherent centralizing character and do not fit into the modern concept of “real federalism”. J. M. Gutiérrez G. describes the „aportaciones“ as necessarily transitional, although they are not conceived as such within the legislation. To move away from them, he proposes two approaches. Allocations that are not bound to conditions should slowly replace the aportaciones. And secondly, the states should enhance their own allocation strategies in order to get more independent from the center. The latter approach causes some discussion, as it seems that new local taxes would be required. Such taxes are already under discussion, for instance a tax on local consumption or on petrol. However, J. M. Gutiérrez G. is of the view, that the existing tax bases are sufficient, if the collection of those taxes would be done in a more efficient way.

In South Africa, the reallocation of resources is being directly related to the topic of human and social rights. According to Murphy Morobe this is mainly due to the very particular history. Federalism emerged in South Africa only after the old apartheid regime was replaced. Before that, decentralization was used by the Apartheid regime as an instrument to further marginalize the black rural communities. This explains why a strong skepticism against federalism exists, and the latter is not expressively mentioned within the 1996 constitution. What the constitution does mention is the decentralized character of the country with its three distinctive, interdependent and interrelated “spheres” of government. Although the provinces and the municipalities do have their own resources (mainly from taxes for the delivery of goods as electricity etc.), the main discussion topic is the reallocation of

finances from the national sphere to the two other spheres of government. It is mainly the independent Finance and Fiscal Commission which must be consulted by the parliament for each project about reallocation and must determine whether such proposals respect the principles established by the constitution. While the main criteria is the principle of equity, this must be considerate from the perspective of the “Bill of Rights”, that guarantees towards South Africans citizens basic social rights such as education, health and welfare. In this sense, solidarity between the rich and the mainly rural poor provinces is the main issue when speaking about public finances.

In Nigeria the system of the allocation of public finances is deeply conditioned by the historical evolution of the country. Alex Ekwueme makes the point that the regions have gone through a multitude of stages as regards their financial independence. After achieving the independence in 1960, the country consisted of three strongly autonomous provinces, which raised their own taxes. Today, the country has been split into small states which are not able anymore to execute their fiscal powers independently. This has resulted in the reality that the largest part of the taxes are collected centrally, and the main revenue of the states consists in the financial transfers from the central government. The main criteria for the determination of the amounts allocated to the individual states are mainly driven by the idea of solidarity towards the less developed regions. Nevertheless in order to improve efficient tax collection, competition between the states is tried to be achieved by the rule that 10% of the total redistribution amount is allocated to those states where most of the taxes were collected. This raises the controversial question whether states with bigger natural resources (for instance when talking about offshore mineral oil resources) should profit more from these central allocations than states with less resources. However, the reallocation as well as other urgent federal issues are being discussed and likely to change within the coming years. For instance, the Revenue Mobilization, Allocation and Fiscal Commission has recently proposed a new Revenue Allocation Formula which will be considerate by the National Assembly.

Comment on the discussions by the rapporteur

As mentioned above, fiscal equalization is not the only source of income for sub national entities. Sub national entities usually have their own sources which function independently from allocations made by the central government. In such cases, one could argue that horizontal as well as vertical fiscal equalization are tools to correct inequalities between different regions of a federation and between the central government and the sub-national entities, rather than being the main source of income for the sub-national entities. All the three presentations gave a good discussion about the proportion of the reallocation of resources. However, the discussion on the question, if own resources and own internal tax bases should be exploited and how this could be done efficiently was not as extended as it could have been.