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## LEGAL REGULATION OF TAXATION IN THE SWISS CONFEDERATION

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# LEGAL REGULATION OF TAXATION IN THE SWISS CONFEDERATION

Petro PATSURKIVSKYY<sup>1</sup>, Ruslana HAVRYLYUK<sup>2</sup>

## Abstract

*The article considers the Swiss model of fiscal municipalization from the ideological and methodological positions of the anthroposociocultural approach. Such components of this approach as historical and genetic methods together with the method of system-structural analysis were applied especially thoroughly and consistently. By means of them it was found that the Swiss model of fiscal decentralization is an attributive part of the construction of public power in Switzerland – municipalization from bottom to top. Special attention is drawn to defining the basic legal features of the Swiss model of fiscal municipalization.*

*It is argued that subsidiarity does not paradigmatically coincide with decentralization: the principle of subsidiarity postulates the sovereignty of the basic territorial collectives and considers the possible conditions for its limitation for general social needs and values. On the contrary, the principle of decentralization has the national level of governance as the starting point and considers the conditions of delegation of certain tasks and competences by the state to the lower levels of public power hierarchy in the principal frames of state sovereignty. Specificity of the principle of subsidiarity in Switzerland is that cantons play dual role from the standpoint of administrative federalism. On the one hand, they are the bearers of sovereignty of public power, including taxation. On the other hand, they are the sole bearers of administrative authority and are obliged to serve national interests, that is, the needs of the entire Swiss Confederation. Paradox is that this service function of the cantons gives them considerable benefits in the inevitable opposition to the Union state, when it comes to provision of services of the entire fiscal system and the entire system of public finance.*

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*Swiss fiscal municipalization, subsidiarity, sovereignty of the basic territorial collectives, Swiss instrumental state.*

**Setting the problem**

The adoption of European Charter of Local Self-Government in October, 15<sup>th</sup>, 1985, by definition of the Council of Europe, has become an important contribution to the construction of Europe based on the principles of democracy and the decentralization of power, expansion of citizens' participation in the conduct of public affairs, has marked a new stage in affirmation of European public order. The main goal of the Charter was to develop new common political, legal and financial instruments and to apply the acquired experience of enhancing local self-government in its sense as direct participation of people at large in the conduct of affairs to the fullest.

Article 9 "Financial resources of local authorities" of the Charter has become especially valuable for the development of local self-government from world-outlook and methodological standpoint. The first paragraphs of this article envisage: a) the right of local authorities to adequate financial resources of their own, of which they may dispose freely within the framework of their powers; b) a precaution that local authorities' financial resources shall be commensurate with the responsibilities provided for by the law of the state; c) a requirement that part at least of the financial resources of local authorities shall derive from local taxes and charges of which, within the limits of statute, they have the power to determine the rate [1]. From that time on, there has been developed as many models of fiscal sufficiency as there are countries in Europe. These models can be divided into two opposite types by criterion of their legal nature: the model of fiscal municipalization and the model of fiscal decentralization. These models are attributive parts of the same opposite types of construction of public power in European countries – municipalization from the bottom to the top and decentralization from the top to the bottom. The first of the aforementioned types is characteristic of the instrumental federal states, the second type – of the unitary substantial states.

The model of fiscal decentralization is the most widespread and obviously, it is therefore the subject of constant research [2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 16, 17, 18, 19, 20, 21, 22, 23]. This cannot be said

about the legal model of fiscal municipalization. The classic example of the complete and consistent putting this model into practice is the Swiss Confederation as an instrumental union state [24, 25, 26, 27].

**The aim of this article** is the analysis of the Swiss model of fiscal municipalization as the least researched. An additional important argument in favour of the topic choice was that the Swiss model of fiscal municipalization has made and is still making a considerable impact on the transformation of the EU from the union of the states into the union of regions, in European commonwealth of societies. It remains to be one of the most powerful multipliers of extending this transformation.

**The objectives of this article are** to determine the peculiarities of the state structure of the Swiss Confederation, which have determinately influenced the formation of the Swiss model of fiscal municipalization and uncovering the basic legal features of this model.

**The methodological background** of this article is determined by anthroposociocultural nature of tax law in general and the Swiss model of fiscal municipalization in particular. Anthroposociocultural approach is the most adequate for the research of the subject of this nature. Especially productively were applied such its components as historical and genetic methods together with the method of system-structural and institutional analysis. In achieving the aims of the article we have applied the research techniques of the legal regulation of public finance that were elaborated by Dmytro Kostya [28], Andrii Khudyk [29] and Viktoriia Raritska [30].

## **1. Special features of the state structure of the Swiss Confederation**

A long time ago most researches of Constitutional and Tax Law in Switzerland payed attention to the peculiarity of the latter and its law in general. Among the existing countries Switzerland is almost the oldest republic with absolutely most developed system of direct democracy. The history of modern Switzerland as the union of cantons and consolidations of self-governing communities traces to August 1, 1291 when three cantons – Shwyts, Ur, and Unterwalden ( later fell apart into Obwalden and Nidwalden) signed a Union letter, also known as Rutli's Oath [31: 19-20]. The key to understanding the constitutional-legal nature of Swiss model of

political sovereignty in general is article 3 “Cantons” of the Union constitution of the Swiss Confederation of April 18, 1999: “Cantons are sovereign, as their sovereignty is not restricted by Union constitution; they exercise all the rights which are not transferred to the Union” [32: 537]. That is, the union state in Switzerland is characterized by a truly instrumental feature. Taking into account a constitutional formula “Swiss people and cantons...give themselves the further Constitution” [32: 537], and also owing to a system analysis of the whole content of a valid Swiss Constitution, it is necessary to make a firm conclusion that cantons are not substantial formations either, they are only instrumental ones, and the sovereignty in cantons belongs to the communities living on a respective territory. It is the second methodological key to a real understanding of the constitutional-legal nature of Swiss model of fiscal municipalization.

For a deeper understanding and an adequate comprehension of the latter it is necessary to note that Switzerland, the territory of which is about 41 000 square kilometers and the population is more than 7mln, is the most structured federation in the world consisting of 26 cantons. Some of these subjects of federation, by such criterium as population, hardly satisfy the standards of viable municipal formation. Specifically, in 2001 the population of the canton Appenzel-Innerehoden (172sq.km) included only 15 000 people. On the other hand, in the canton Zurich which is 10 times larger in area (1728 sq.km), there lived about 1 229 000 people, or about 100 times more than in the canton Appenzel-Innerehoden. The specialists-analysts consider this fact to be a testimony of a direct asymmetry between the subjects of the Swiss Confederation by such important indexes as territory and population [33: 409]. The asymmetry is revealed in the sphere of public finance. Thus, the richest canton Zug exceeds by gross national income per capita the poorest canton Jura more than twice [34: 26]. Though, it by no means makes the Swiss perceive their state system negatively.

On the contrary, for the Swiss, as it is noted in the scientific literature, two idiosyncrasy are characteristic: scare and non-acceptance of potentially possible centralization, on the one hand, scare and non-acceptance of possible territorial enlargement, on the other hand, that is why they defend self- government paradigm developed historically so consistently and persistently. For example, the population of both cantons – urban Basel and rural Basel- rejected the project of politicians to unite them into one canton, they chose another model instead, of closer horizontal cooperation of the both cantons. The project of canton Wo and canton Geneva unification was in failure in the same way. The population of the

first canton rejected this idea by 77 per cent vote, the population of the other – by 80 per cent vote [35: 1]. It is quite obvious that, on the one hand the cantons of Switzerland value their confessional, national, linguistic and sociocultural originalities as the manifestations of their socio-cultural sovereignty. However, on the other hand, as the considerable historical experience convinces, the above mentioned is greatly promoted by mutually found out and tested by time Swiss constitutional-legal model of fiscal municipalization based on the principle of subsidiarity. In full correspondence with a given principle the basic powers, including those in the sphere of taxation, are attached to municipal communities and cantons, and only separate competences, specially stipulated in the Constitution of the Swiss Confederation, are delegated to the union state.

We have cited already the text of article 3 of the Constitution of the Swiss Confederation in which the principle of subsidiarity is not mentioned directly, but literal sense of this article indicates it directly: cantons are sovereign since their sovereignty is not restricted by the Union Constitution; they realize all the rights including those in the sphere of taxation which are not transferred to the Union. As a well-known specialist in the state system of Switzerland Eric Mottu writes, “the given article, both as a political principle and a legal one, attaches basic sovereignty to cantons, the confederation interferes only in the cases defined in the Constitution” [36: 2]. Moreover, in that extent and form in which the targets of the Union state are delegated by the Constitution of Switzerland to federal level, the Confederation has no right to assume more functions than necessary which practically means that the Swiss Constitution of 1999 acknowledges the principle of subsidiarity as the fundamental outset of federative relations. In general it corresponds to legal principle of determination of nature and limits of the authorities of public law subjects.

Many European scientists (among them already mentioned E. Mottu) consider article 3 of the Constitution of the Swiss Confederation of 1999 as a reaction of a constitution-maker on a real tendency to centralization outlined in this country in the system of public government in the second half of XX century and which started crippling the Swiss model of fiscal municipalization too. It is a question of purposeful support by the Union state of actual centralization by means of giving the subsidies to these or those cantons, provided with warnings and additional terms. The system like that practically turned federal finance support into purposive financing of certain targets and interests on the territory of a respective canton.

With some lateness the politicians of a canton level and a lot of independent experts sounded the alarm, since the financing of cantons needs on the part of Confederation undermined the spirit itself of “helvetic federation” which had attached basic sovereignty to the cantons and not to federal level of government. It also caused a disbalance among different levels of authorities and finance competence, contradicted the principle of a budget equivalency, in another words, the principle of congruency. This principle is known to require (1) the authorities (juridical, political and organizational) and (2) finance competence should not be broken up into different levels of authority relations but should be focused on one and the same level of government. Adherence to the principle of congruency (budget equivalency) allows us to determine precisely the subject of liability, first of all, in regard to beneficiary public services without leveling down this liability by its distribution according to different levels of public power which causes irresponsibility. Convincing example of the latter is a valid system of organization of public power in Ukraine [37].

## **2. Swiss model of fiscal municipalization**

The basic content of Swiss model of fiscal municipalization is given in chapter 3 “Financial System” of the Union Constitution of the Swiss Confederation. Specifically, paragraph 4 of article 128 “Direct Taxes” of the Swiss Confederation notes: “Tax is allocated and raised by cantons” [32: 561]. It is a fundamental principle. Only this single fact is enough to arrive to a conclusion that tax federalism, in other words, fiscal municipalization in Switzerland has a substantial character and distinguishes in one of the highest levels of decentralization in the world. Cantons have basic tax powers. On the contrary, tax competence of Federal state is restricted by taxes, specially determined in the Constitution as federal ones. Moreover, the list of federal taxes is subjected to periodic renewal and approval by canton referendums. Currently, federal taxes according to the Constitution of Switzerland contain: tax on surplus value, federal direct tax and tax on income from the entrepreneurial activity. Federal state may count into its profit from direct tax in amount: a) not more than 11.5 per cent from the income of individuals; b) not more than 9.8 per cent from net income of legal entities; c) not more than 0.825 per mille from the capital and the reserves of legal entities, and the Union while quoting tariffs, as it is noted in the Constitution of the Federation, takes into account direct taxes charge for the benefit of cantons and communities [32: 561].



In cantons the main source of tax supply is income tax from the income of individuals and legal entities. According to the Constitution of Switzerland, three-tenth of gross sum of taxes go to cantons, not less than one-sixth of it is used for equalization of provision with public financial resources among the cantons. It should be noted that the indicated amount of public financial resources assigned to use with the purpose of horizontal financial equalization among the cantons has only a low threshold which by no means can be reduced. Though, this quantity can be increased on mutually advantageous contractual basis among the cantons, what they have successfully being doing for a long time, bringing it to union state's notice.

The lion's share of tax supply – over fifty per cent – remains in communities, being their own resources. That is the quintessence of fiscal municipalization in Swiss. In the Swiss Constitution of 1999 the only article 50 of the chapter “Communities” is dedicated to communities – the starting level of self-government - paragraph 1 of which notes: “Community autonomy is guaranteed in conformity with canton law” [32: 544]. So, not a union state attaches autonomy to communities – they create it themselves together with the cantons, and national state only guaranties the community autonomy, “and in its actions takes into consideration their possible influence on communities”, “pays attention to a special conditions of cities and agglomerations, and also, to mountainous regions” [32: 544].

Switzerland has no unified system of local government, since owing to its self-government nature, practically every canton has its system of local self-government based on direct democracy (referendums, including those in tax problems and also people's legislative initiative, which means the right of a certain group of electors, having collected the signatures, to propose the project of the law to a canton or to a union state, which is subjected to a necessary consideration by a respective parliament), local parliamentarism and local executive bodies. The regulation of forms and procedures of direct democracy on a local level is established in canton legislation – constitution and laws. In general, the communities act in terms of the Union Constitution, legislation of cantons and own statutes. The statute of the community is adopted in every community and is valid after its approval by canton council.

Among municipal powers divided into legislative and administrative ones and which are essentially different in different cantons the mutual authority is local taxes, providing, as it was noted above, fiscal sovereignty of communities and their financial independence in principle. Again, in different cantons communities have not the same extents of financial

autonomy. Besides, the models of fiscal cooperation of cantons and communities differ with each other. However, the cantons usually approve financial decisions independently and they can charge the taxes in terms provided by the canton. All communities impose their citizens with their own income tax, the rate of which is discussed at the general meetings or the meetings of the community representatives.

Such an approach to a tax pie sharing stimulates all levels of public power to work efficiently and, the main, - induces the producers of gross national product and national income of the country which are the basis of aggregate tax returns of correspondent levels of public power, for highly productive work. This fairy-tale phenomenon for the most countries of the world is not a confrontation, but a unity of public power attempts on every of its levels and of the tax-payers in the sphere of taxation – but impossible even in a fairy tale for a current model of public power in Ukraine or Romania, is obtained due to realization not etatist doctrine of tax law in Switzerland but its anthropologic-sociologic one. In Switzerland the sphere of taxation practically stopped being of a corruption character, and tax paternalism, familiar to the citizens of most European countries, disappeared in Switzerland as a phenomenon of reality.

Article 129 “Tax Harmonization” of the Constitution of Switzerland obliges the Confederation to establish the principles of harmonization of direct taxes of all three levels of public power: Confederation itself, cantons and communities, taking into account harmonization aspiration of the cantons themselves. Harmonization extends to a duty of taxpaying, the subject and determination of the time for taxpaying, tax procedure law and tax criminal law. Out of harmonization are tariffs of taxation, rates of taxes and sums which are duty free. The Union also has the right to issue the regulations against unreasoned tax credits. Finally, article 134 “Exceptions of Canton and Community Taxation” of the Constitution of Switzerland notes: “The thing defined by the union legislation as the object of the tax on surplus value, special excise tax, stamp-duty and recalculated tax, or declared to be duty-free, cannot be levied with the same taxes by cantons and communities” [32: 562-3]. It is made with the purpose to prevent competitive taxation by different levels of public power. By the way, the Confederation has the right to establish special consumer taxes only in terms of exclusive enumeration in article 131 “Special Excise Taxes” of the Constitution of Switzerland (tobacco and tobacco products; alcohol production; beer; automobiles and their components; petroleum, other

mineral oils, natural gas and products of their refining, and also petrol) [32: 562].

Thus, as O.M. Chernenko notes, in general the principle of subsidiary, including the sphere of taxation, “means specific allocation of the spheres of liability, social tasks and functions. The main idea of the principle of subsidiary is in the fact, - continues she- that political power must interfere only when the society or another groups composing it, specifically local community, cannot provide various needs of its members. This principle provides the solutions of the tasks on the level they arise, and public services should be given by the bodies of the level closest to the consumers” [38: 9]. O.M. Chernenko singles out one another side of the principle of subsidiary – supplement, i.e., mutual assistance of federation and its subjects in the course of execution of powers belonging to a certain part of legal relations” [38: 9].

### **Conclusions**

Thus, according to the conclusion of above mentioned Eric Mottu, “subsidiarity does not coincide with the decentralization”. His arguments should be admitted as irrefragable: the principle of subsidiary postulates the sovereignty of basic territorial collectives and considers possible conditions of its restriction owing to social needs and values. On the contrary, the principle of decentralization, as Eric Mottu and many other authors state, takes national level of government as the point of departure and considers the terms of delegating by the state of some tasks and the competences to lower level of public-powerful hierarchy in principle terms of the state sovereignty. The specialty of the subsidiarity in Switzerland is revealed by the fact, that from the positions of administrative federalism, cantons play dual part. On the one hand they are the carriers of basic sovereignty of public power, including the sphere of taxation. On the other hand, they are the single carriers of administrative authorities and in a given quality their duty is to serve national interests, i.e., the needs of the Confederation. Paradoxically, but this service function of the cantons gives them essential advantages in inevitable confrontation with the Union state, when the talk is about the service of the whole fiscal system specifically, and the whole system of public finance, taken as a whole.

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