

**FISCAL CONSTITUTION AND REGIONAL DISPARITIES IN ECONOMIC  
DEVELOPMENT: AN EXPLORATION OF THE CASES OF COLOMBIA,  
CANADA AND SPAIN**

by

**Jorge Armando Rodríguez**

B.A. in Economics, Universidad Nacional de Colombia, 1986

M.Phil. in Economics, University of Cambridge, 1996

Submitted to the Graduate Faculty of  
the Graduate School of Public and International Affairs in partial fulfillment  
of the requirements for the degree of  
Ph.D. in Public Policy

University of Pittsburgh

2009

UNIVERSITY OF PITTSBURGH  
GRADUATE SCHOOL OF PUBLIC AND INTERNATIONAL AFFAIRS

This dissertation was presented

by

Jorge Armando Rodríguez

It was defended on

January 26, 2009

and approved by

Louise Comfort, Ph.D., Professor, GSPIA

David Y. Miller, Ph.D., Associate Professor, GSPIA

Lisa S. Nelson, Ph.D., Assistant Professor, GSPIA

George Reid Andrews, Ph.D., Distinguished Professor, Department of History

Dissertation Advisor: Louise Comfort, Ph.D., Professor, GSPIA

Copyright © by Jorge Armando Rodríguez

2009

## **ABSTRACT**

### **FISCAL CONSTITUTION AND REGIONAL DISPARITIES IN ECONOMIC DEVELOPMENT: AN EXPLORATION OF THE CASES OF COLOMBIA, CANADA AND SPAIN**

Jorge Armando Rodríguez, Ph.D.

University of Pittsburgh, 2009

Inquiring into the fiscal constitution and the regional economic geography of Colombia, this dissertation carries out an exploration of the linkages running from the fundamental fiscal rules of the country's multilevel system of government to the disparities in economic development among its regions, or, more precisely, among the jurisdictions of the intermediate level of government. With a comparative focus and with an eye to identifying factors that accentuate or moderate regional economic disparities in Colombia, it also offers an analysis of selected aspects of the fiscal constitutions of Canada and Spain, where, akin to the Colombian case, a less uneven regional economic development is a constitutionally declared governmental goal. Three dimensions of regional economic development are considered, namely, education, health, and income.

Similarities and differences in the assignment of functions of government and the design of taxes, intergovernmental transfers and the rules of public indebtedness between cases belonging to the same legal tradition (Colombia and Spain for the civil law tradition) and to different legal traditions (e.g., Colombia vis-à-vis Canada, where the latter to a good extent fits in the common law tradition) are singled out and illustrated, and so are relevant quantitative patterns of the multilevel government finances and the outcomes in the three dimensions of development under study, using longitudinal and cross-section data for within and between country analysis. A sample of policy makers affiliated with the Colombian national and subnational levels of government, interviewed for the study, provide insights into the workings

of intergovernmental relations, especially regarding the pros and cons of political and fiscal decentralization, as designed and implemented in Colombia, for regional and local development. The dissertation discusses and exemplifies some ways of assessing the adaptability and robustness of the Colombian fiscal constitution and of harnessing the fiscal state, through the legal system, to deal with regional economic disparities, drawing from the international comparative exercise and from a variety of theoretical approaches, including the economic analysis of law and the theories of public finance and public policy design.

## TABLE OF CONTENTS

|            |   |           |
|------------|---|-----------|
| <b>1.0</b> | <b>INTRODUCTION.....</b>  | <b>1</b>  |
| <b>2.0</b> | <b>CONSTITUTIONALISM AND ECONOMIC DEVELOPMENT IN THE THEORETICAL LITERATURE .....</b>                   | <b>10</b> |
| <b>2.1</b> | <b>CONSTITUTIONAL DESIGN AND THE CONCEPT OF FISCAL CONSTITUTION.....</b>                                | <b>10</b> |
| <b>2.2</b> | <b>ECONOMIC DEVELOPMENT AND ITS GEOGRAPHY.....</b>  | <b>15</b> |
| <b>2.3</b> | <b>LINKS BETWEEN THE FISCAL CONSTITUTION AND THE SPATIAL DISTRIBUTION OF ECONOMIC DEVELOPMENT .....</b> | <b>21</b> |
|            | <b>2.3.1 Taxation and Other Revenue Sources.....</b>  | <b>25</b> |
|            | <b>2.3.2 Intergovernmental Transfers.....</b>   | <b>25</b> |
|            | <b>2.3.3 Public Borrowing .....</b>   | <b>27</b> |
| <b>2.4</b> | <b>COLOMBIAN CONTRIBUTIONS AT A GLANCE .....</b>  | <b>28</b> |
| <b>3.0</b> | <b>UNDERLYING MODEL .....</b>   | <b>30</b> |
| <b>4.0</b> | <b>CONSTITUTIONAL ARCHITECTURE OF MULTILEVEL GOVERNMENT</b>   | <b>36</b> |
|            | <b>4.1 LEVELS AND UNITS OF GOVERNMENT.....</b>  | <b>37</b> |
|            | <b>4.2 A CHARACTERIZATION OF INTERGOVERNMENTAL RELATIONS</b>  | <b>42</b> |
|            | <b>4.2.1 Formal Representation of the Regions in the Central Legislature.....</b>                       | <b>45</b> |
|            | <b>4.2.2 Selection of Regional Chief Executives .....</b>   | <b>49</b> |

|       |   |     |
|-------|---|-----|
| 4.2.3 | Assignment of Residual Powers .....                               | 50  |
| 4.2.4 | Fiscal Powers of Regional Governments.....                        | 52  |
| 5.0   | COLOMBIA’S FISCAL CONSTITUTION.....                               | 55  |
| 5.1   | DEVELOPMENT-RELATED GOVERNMENT FUNCTIONS .....                    | 55  |
| 5.1.1 | The Right to Education .....                                      | 55  |
| 5.1.2 | Locally Run, Demand-Driven Health Care .....                      | 59  |
| 5.1.3 | Prosperity and Fiscal Capacity Disparities .....                  | 64  |
| 5.2   | GOVERNMENT FINANCING INSTITUTIONS.....                            | 67  |
| 5.2.1 | Centralization of the Power to Tax .....                          | 67  |
| 5.2.2 | Intergovernmental Transfers, a Hallmark of the Constitution ..... | 73  |
| 5.2.3 | Public Borrowing, a Case of Rules-Based Control .....             | 79  |
| 6.0   | CANADA’S FISCAL CONSTITUTION .....                                | 82  |
| 6.1   | DEVELOPMENT-RELATED GOVERNMENT FUNCTIONS .....                    | 82  |
| 6.1.1 | Education, Meant to be a Provincial Affair.....                   | 82  |
| 6.1.2 | Health Care and the Federal Spending Power .....                  | 84  |
| 6.1.3 | A Form of Fiscal Equalization .....                               | 86  |
| 6.2   | GOVERNMENT FINANCING INSTITUTIONS.....                            | 87  |
| 6.2.1 | An Ample Multilevel Power to Tax.....                             | 87  |
| 6.2.2 | A Cohesive Role for Intergovernmental Transfers.....              | 95  |
| 6.2.3 | Federal and Provincial Borrowing as Self-Regulation .....         | 100 |
| 7.0   | SPAIN’S FISCAL CONSTITUTION .....                                 | 103 |
| 7.1   | DEVELOPMENT-RELATED GOVERNMENT FUNCTIONS .....                    | 103 |
| 7.1.1 | Education: Equalization of a Fundamental Right .....              | 103 |

|        |  |     |
|--------|--|-----|
| 7.1.2  | Devolution and Universal Access to Health Care .....                                   | 106 |
| 7.1.3  | In Search of a More Equitable Distribution of Regional Income.....                     | 108 |
| 7.2    | GOVERNMENT FINANCING INSTITUTIONS.....   | 110 |
| 7.2.1  | Geographical Partition of the Power to Tax.....  | 110 |
| 7.2.2  | Bottom-Up and Top-Down Intergovernmental Transfers.....                                | 118 |
| 7.2.3  | Intertwined Spanish and European Borrowing Regulations.....                            | 125 |
| 8.0    | CONSTITUTIONAL AMENDMENTS TO INTERGOVERNMENTAL FISCAL<br>RELATIONS IN COLOMBIA.....    | 127 |
| 8.1    | THE ORIGINAL 1991 INTERGOVERNMENTAL TRANSFER SYSTEM<br>128                             |     |
| 8.2    | AMENDMENTS TO THE <i>SITUADO FISCAL</i> .....  | 133 |
| 8.3    | AMENDMENTS TO THE <i>PARTICIPACIÓN MUNICIPAL</i> .....                                 | 134 |
| 8.4    | ARRIVAL OF THE <i>SISTEMA GENERAL DE PARTICIPACIONES</i> .....                         | 136 |
| 9.0    | MAIN SIMILARITIES AND DIFFERENCES BETWEEN FISCAL<br>CONSTITUTIONS.....                 | 138 |
| 10.0   | A QUANTITATIVE LOOK AT THE REGIONAL<br>ECONOMIC DISPARITIES AND FISCAL IMBALANCES..... | 146 |
| 10.1   | A COLOMBIAN MIXED STORY .....  | 147 |
| 10.1.1 | Levels and Trends.....   | 147 |
| 10.1.2 | Formal Models for Adaptation and Robustness .....                                      | 166 |
| 10.2   | INTERNATIONAL COMPARISON .....   | 174 |
| 11.0   | INTERVIEWS WITH COLOMBIAN POLICYMAKERS.....  | 184 |
| 11.1   | ON THE ROLE OF THE DEPARTMENTS IN DECENTRALIZATION.....                                | 187 |



|      |   |     |
|------|---|-----|
| 11.2 | FISCAL DISPARITIES AND ECONOMIC DEVELOPMENT .....   | 193 |
| 11.3 | POLITICAL AND FISCAL AUTONOMY .....   | 205 |
| 12.0 | CONCLUDING REMARKS .....  | 213 |
|      | APPENDIX A. SCORING OF INTERGOVERNMENTAL RELATIONS .....  | 231 |
|      | APPENDIX B. DISTRIBUTION OF COLOMBIA’S GENERAL PURPOSE TRANSFER<br>.....                        | 232 |
|      | APPENDIX C. TRANSFERS FROM THE BASQUE COUNTRY AND NAVARRE TO<br>SPAIN’S CENTRAL GOVERNMENT..... | 233 |
|      | BIBLIOGRAPHY .....  | 234 |

## LIST OF TABLES

|  |     |
|--|-----|
| Table 4-1: Major units of government, 2005 or most recent year available.....                                | 37  |
| Table 4-2: Area and population indicators by unit of government of the intermediate level, 2005<br>.....     | 40  |
| Table 10-1: Frequency distribution of Colombian departments' GDP per capita, selected years<br>.....         | 149 |
| Table 10-2: Level of taxation by tier of government in Colombia, selected years.....                         | 154 |
| Table 10-3: Panel models for Colombia's education transfers.....   | 168 |
| Table 10-4: Panel models for Colombia's health transfers.....  | 169 |
| Table 10-5: International comparison of levels of taxation by tiers of government, selected years<br>.....   | 176 |
| Table 10-6: Level of taxation of the intermediate tier of government by tax regime in Spain ..               | 177 |
| Table 10-7: Type of central government transfers to the intermediate level of government by<br>country ..... | 181 |
| Table 12-1: Changes in the tax burden of the intermediate level of government by country.....                | 223 |

## LIST OF FIGURES

|   |     |
|---|-----|
| Figure 3-1: General model .....   | 30  |
| Figure 3-2: Overview of relationships among variables.....  | 31  |
| Figure 3-3: GDP per capita by country, 2005.....  | 34  |
| Figure 3-4: Life expectancy at birth by country, 2005 .....   | 34  |
| Figure 3-5: Gross enrollment ratio by country, 2004 or most recent year available .....                   | 35  |
| Figure 4-1: Intergovernmental relations: A summary characterization.....                                  | 42  |
| Figure 4-2: Members of parliament and population by Canadian province. 38th Parliament, 2004<br>.....     | 48  |
| Figure 5-1: Colombia's health insurance system.....   | 62  |
| Figure 5-2: Assignment of revenue sources in Colombia, 2005.....  | 70  |
| Figure 5-3: Colombia's central government taxing schemes, 2004 or most recent year available              | 71  |
| Figure 5-4: Colombia's subnational taxing schemes, 2004 or most recent year available .....               | 72  |
| Figure 5-5: Colombia's intergovernmental transfers by purpose, Law 715 of 2001 .....                      | 75  |
| Figure 5-6: Intergovernmental links by type of transfers in Colombia, 2002-2008 .....                     | 77  |
| Figure 6-1: Assignment of revenue sources in Canada, 2004 or most recent year available .....             | 89  |
| Figure 6-2: Canada's federal taxing schemes, 2004 or most recent year available .....                     | 91  |
| Figure 6-3: Canada's provincial taxing schemes by tax source, 2004 or most recent year available<br>..... | 91  |
| Figure 6-4: Transfers to the intermediate level of government in Canada, 2005 .....                       | 96  |
| Figure 7-1: Assignment of revenue sources in Spain, since 2002 .....                                      | 113 |
| Figure 7-2: Spain: Central government taxing schemes, 2004 or most recent year available....              | 115 |

|   |     |
|---|-----|
| Figure 7-3: Taxing schemes in Spain's autonomous communities by tax source, 2004 or most recent year available .....                        | 116 |
| Figure 7-4: Direction of intergovernmental transfers in Spain.....  | 120 |
| Figure 7-5: Transfers to the intermediate level of government in Spain, .....   | 121 |
| Figure 8-1: Amendments to Colombia's 1991 fiscal constitution.....  | 128 |
| Figure 8-2: Original design of intergovernmental transfers in the 1991 Constitution.....  | 129 |
| Figure 8-3: Intergovernmental transfer flows in the original 1991 Colombian constitution.....   | 130 |
| Figure 9-1: Constitutional approaches to regional disparities by country and government functions.....                                      | 139 |
| Figure 9-2: Legal approaches to government financing by country and fiscal channel .....  | 142 |
| Figure 10-1: GDP per capita by Colombian department, 2005 .....   | 148 |
| Figure 10-2: Level of income and inter-regional income disparities in Colombia, 1990-2005 .   | 150 |
| Figure 10-3: Trend in the relationship between level of income and inter-regional income disparities in Colombia, 1990-2005 .....           | 151 |
| Figure 10-4: Inter-regional disparities in three dimensions of development in Colombia.....   | 152 |
| Figure 10-5: Colombia's intergovernmental transfers by purpose, departmental and local aggregate .....                                      | 155 |
| Figure 10-6: Colombia's intergovernmental transfers by level of government.....   | 156 |
| Figure 10-7: Colombia's intergovernmental health transfers by level of government, percentage share of the total in selected years .....    | 157 |
| Figure 10-8: Colombia's intergovernmental education transfers by level of government, percentage share of the total in selected years ..... | 158 |
| Figure 10-9: Level of taxation by departmental government in Colombia, 2005 .....   | 160 |

|  |     |
|--|-----|
| Figure 10-10: Departmental level of taxation and fiscal capacity by jurisdiction in Colombia.  | 161 |
| Figure 10-11: Subnational level of taxation and fiscal capacity by jurisdiction in Colombia....                                      | 162 |
| Figure 10-12: Health insurance coverage by type of financing in Colombia.....  | 163 |
| Figure 10-13: Colombia’s publicly funded health insurance: Regional disparities in coverage and in intergovernmental transfers ..... | 164 |
| Figure 10-14: Countrywide level and regional disparities in life expectancy in Colombia .....  | 165 |
| Figure 10-15: Access to education in Colombia: Countrywide level and regional Disparities..  | 166 |
| Figure 10-16: Robustness of Colombia’s health transfers in selected contingencies .....  | 172 |
| Figure 10-17: Robustness of Colombia’s education transfers in selected contingencies .....   | 172 |
| Figure 10-18: Per capita GDP disparities between regions by country .....  | 174 |
| Figure 10-19: Level of taxation disparities between regions by country.....  | 178 |
| Figure 10-20: Central government total transfers to the intermediate level of government by country .....                            | 179 |
| Figure 10-21: Life expectancy at birth disparities between regions by country.....   | 182 |
| Figure 10-22: Gross enrollment ratio disparities between regions by country .....  | 183 |
| Figure 11-1: Interviews of Colombian policymakers: Selected sample .....   | 185 |
| Figure 12-1: Dominant linkages between levels of government by country .....   | 214 |

For Toya, Daniel, and my parents

## PREFACE

I am indebted first to all the people from whom I have learned over the years, including educators, family and friends.

Special thanks go to Viviana Barberena and others, too many to name individually, for their help with the interviews for this study, as well as to the Colombian policymakers who agreed to be interviewed. I would also like to thank Ignacio Lozano and Laura Pabón for providing me the information I requested on the Colombian public finances and economic development, as well as Eduber Gutiérrez for making important official documentation from the *Federación Colombiana de Departamentos* available to me.

I acknowledge with gratitude institutional and financial support during my doctoral studies from the Fulbright Program, Colfuturo and my Colombian alma mater, the *Universidad Nacional*.

During my stay in Pittsburgh I was fortunate to meet some wonderful people whose friendship and hospitality I will always remember and appreciate.

Quotations from documents originally published in Spanish were translated into English by this author. One exception is the Spanish constitution: an official English version was used.

## 1.0 INTRODUCTION

This study examines the fiscal constitution of Colombia and explores the links between that particular type of institution and the country's regional disparities in economic development, mostly from 1990 to 2005. On selected issues, the fiscal constitutions of Canada and Spain are analyzed and compared with that of Colombia, along with some aspects of their regional economic geography. The term 'regions' is taken to mean the component jurisdictions of the intermediate level of government in each country (i.e., departments, provinces and territories, and autonomous communities). The Colombian case occupies central stage, with the cases of Canada and Spain serving as points of reference and sources of ideas on institutional design and change. Aided by the international comparative exercise and bearing in mind that there are similarities and differences between the legal traditions and systems of government of the three countries, the study seeks to identify institutional factors favoring or hindering the moderation of interregional economic inequalities (that is, inequalities within as opposed to between countries) and looks for ways to improve, by means of the legal system, the capability of the Colombian multilevel system of government to address such inequalities.

The concept of fiscal constitution is intended to embrace the fundamental rules governing the fiscal state. In general, the rules of interest here are legal rules ingrained in the written constitution or in hierarchically lower laws. For the purpose of this dissertation, the 1991 Colombian constitution, the Canadian Constitution Acts from 1867 to 1982 (the Canadian



constitution, for short) and the 1978 Spanish constitution, together with relevant developments by law, are, in their fiscal dimension, the primary legal objects of inquiry.

The idea that legislation matters for economic development was present in classical economics and is a centerpiece of institutional economics (Commons 1925; Commons 1931; Yifu Lin and Nugent 1995).<sup>1</sup> Constitutions and the law have the potential of deliberately furthering economic development insofar as they can be designed, as opposed to being unintentionally constructed. The question of how to materialize such potential becomes particularly important when economic development is considered a worthwhile public policy objective.

Colombia, Canada and Spain have all placed interregional inequality concerns in the constitution. In the Colombian case, the 1991 Constitution contains a mandate for state intervention to achieve “the equitable distribution of the opportunities and benefits of development,” and, more to the point, a provision to the effect that the state ought to intervene especially in order “to promote the harmonic development of the regions.”<sup>2</sup> Geographic fragmentation has been singled out, by Safford and Palacios (2002) among others, as a major factor in the development of Colombia as a historically “divided society,” with a relatively weak state. The marked unevenness of economic development across subnational jurisdictions, often taken as an expression of such geographic fragmentation, have long been a source of public concern in Colombia, although the issue appears to be more sensitive in some regions than in others (Posada-Carbó 1996; Rivera 2001). Indeed, according to a former member of the 1991

---

<sup>1</sup> . Adam Smith and John Commons were open to a joint intellectual enterprise between economic theory and ‘the science of legislation’.

<sup>2</sup> - COL. Constitution, 1991, art. 334.

Constituent Assembly , the ‘harmonic development of the regions’ provision made its way into the constitution as a response to “a heartfelt aspiration of the inhabitants of the country’s less developed regions.” (Perry 1996, p. 132)

Frequently described as a ‘country of regions’, Colombia has struggled to accommodate its regional and local features (or, from a related perspective, its subnational features) into the constitution and to translate the constitution into regional and local realities (Fals-Borda 1996; Bell 1998). The 1991 constitution defined Colombia as a “unitary decentralized state, with autonomy of its territorial entities,”<sup>3</sup> thus delineating the organizational structure meant to achieve the constitutionally instituted state goals, in what is widely seen as an attempt to reverse an enduring pattern of political and fiscal centralization. Voicing a pervasive opinion, Amilkar Acosta, a former speaker of the Colombian congress, maintains that such definition is “one of the most important steps forward of the 1991 Constitution,” part of its “quintessence,” while attaching a higher weight to decentralization and autonomy than to unity.<sup>4</sup> The Colombian 1991 Constituent Assembly adopted a multilevel government framework (e.g., a system of intergovernmental transfers; the popular election of governors) said to be consistent with the harmonic development of the regions or the decentralization of political and fiscal powers, or both (see, for instance, Parra 1992; Restrepo 1996).

Canada has been described as a group of regional societies that differ in their level of development (Harris 1998). According to Brooks (2004), economic disparities among provinces have fed regionalism, deemed one of the key axes of Canadian politics, along with the English-

---

<sup>3</sup> . COL. Constitution, 1991, art. 1.

<sup>4</sup> . Personal communication, May 16, 2007.

French divide. Under the heading “Equalization and regional disparities,” the Constitution Act, 1982 commits the federal and provincial levels of government, to “furthering economic development to reduce disparity in opportunities; and ... providing essential services of reasonable quality to all Canadians.”<sup>5</sup> In what is generally taken as a specific, program-oriented constitutional response to interregional economic disparities, under the same heading it also commits the Canadian federal government to making equalization payments to provincial governments. Fiscal equalization is at the core, in the eyes of many, of the fiscal configuration of Canadian federalism. Canada’s constitution deals with the assignment of tax powers and public expenditure responsibilities, as well as with the scope of provincial borrowing.

According to Newton and Donagh’s (1997) account, the rules for the establishment of Spain’s autonomous communities —the pillars of the spatial organization of the state— and their degree of autonomy were by far the most contentious issues during the gestation period of the 1978 Spanish constitution, which paved the way for the transition from the Francoist dictatorship to democracy. Perhaps this is not surprising considering that Spain has long strived, as Lawlor and Rigby (1998, p. 33) put it, “to blend the demands for recognition and autonomy from some of her regions with the need to maintain national unity.” A process that formally culminated in 1983, the establishment of 17 autonomous communities amounted to the creation a new level of government.

The inequalities in economic development between autonomous communities are a highly contested issue in Spanish politics (Magone 2004). Spain’s constitution sanctions state

---

<sup>5</sup>. CAN. Constitution Act, 1982, sec. 36(1).

intervention “to establish a fair and adequate economic balance between the different areas of the Spanish territory.”<sup>6</sup> And it contemplates at least one mechanism to counter such inequalities, the Interregional Compensation Fund. This Fund, foreshadowed in the constitution, has sought to lessen the economic imbalances among the regions by financing investment projects in the lagging autonomous communities (Newton and Donaghy 1997).

Instead of taking place in a vacuum, the design of a country’s legal system is likely to be rooted in a given legal tradition. The Colombian and Spanish legal systems are commonly taken to belong to the civil law tradition, which was passed on by Spain to Latin America as a result of colonization (Merryman 1985; Glendon, Gordon et al. 1999). According to Cifuentes (2003), the 1991 Colombian constitutional makers looked to the 1978 Spanish constitution for inspiration. A former Colombian president, the late Alfonso López Michelsen, went as far as to assert that the treatment given in the 1991 constitution to the regional question resulted from “the eagerness to imitate the new Spanish constitution.” (quoted by Buenahora, 1997, p. 64) Some traits of the Colombian legal system have been linked to the cultural influence of the colonial past.

The common law tradition largely, though not exclusively, informs the Canadian legal system at the federal level, including the country’s constitution. At the provincial level, as Katz (1986, p. 52) writes, “Canada has one of the most unusual legal systems in the world in that both the civil law (in Quebec) and the common law (in the other nine provinces) predominate today.” Canada’s current written constitution consists of a series of laws enacted between 1867 and 1982; constitutional conventions, understood as customary practices to which the participants in

---

<sup>6</sup> . SPA. Constitution, 1978, art. 138.1.

the political life generally conform, tend to be regarded as parts of the Canadian constitution (Brooks 2004). According to Brown (2002, p. 60), “fiscal relations among governments in Canada are shaped by the texts and conventions of the Canadian Constitution.”

Given the likely influence of many intermediary factors (e.g., the political process, the behavior of economic agents), I approach the relationship between the fiscal constitution and the geography of economic development more on heuristic than on strictly cause-effect terms. Among the dimensions of economic development, three are the focus of this study, namely: health, education and income. In addition to their intrinsic importance, health, education and income serve as the foundations of constitutionally mandated objectives of public policy in Colombia, and are the subject matter of the most commonly used indicators of human development.

The effects of the fiscal constitution on the economic geography of a country may occur through a variety of fiscal channels (e.g., taxation, intergovernmental transfers) and tools (e.g., income tax, education transfers). This study examines a selected set of channels and tools more from the perspective of the fiscal relations between and, at times, within levels of government, than from the perspective of the fiscal relations between governments, on the one hand, and persons, households or firms, on the other. A feature of the fiscal channels and tools dealt with here is their programmatic nature, their vocation of continuity; as a rule, they are not tactical or short term.<sup>7</sup> For example, a system of intergovernmental transfers usually belongs to the programmatic category, while the so-called pork-barrel projects approved in the annual budget

---

<sup>7</sup> . The distinction between programmatic and tactical programs is discussed by Dixit and Londregan (1996). See section 2.3 below.

process usually belong to the tactical or short-term category. The origin or destination of the economic resources mobilized through or by such fiscal channels and tools may be geographically labeled or ear-marked by legal mandate, where the relevant geographic units are sub-central (i.e., sub-national or sub-federal) government jurisdictions.

As the geographic distribution of economic development has a dynamic, evolving nature, the fiscal constitution requires, arguably, some built-in design features if it is to automatically counteract interregional economic disparities. Otherwise, it would be necessary to reform the constitution frequently to compensate for the shifts in the economic landscape. Considering this, two desirable design features of the fiscal constitution are its adaptability to the changes in a country's economic geography and its robustness of performance over a variety of localized contingencies. The study seeks ways to assess such design features with emphasis on the Colombian fiscal constitution.

By one count, Colombia has had nine constitutions throughout its history as an independent nation.<sup>8</sup> Their duration varies considerably, ranging from only two years (the 1830 constitution) to 105 years (the 1886 constitution).<sup>9</sup> Constitutional instability, as measured by the number of constitutions *in effect* per century, was considerably lower in the twentieth century (two constitutions) than in the nineteenth century (eight constitutions). A peculiarity of the current constitution, enacted in 1991, is its approval by a popularly elected Constituent Assembly (Buenahora 1997). It is worthwhile to mention that it has already been amended about twenty

---

<sup>8</sup>. A compilation of constitutional texts is offered by Restrepo Piedrahita, C. (1995). Constituciones políticas nacionales de Colombia. Bogotá, Universidad Externado de Colombia, Instituto de Estudios Constitucionales.

<sup>9</sup> / Though the long-lasting constitution of 1886 was amended about 69 times, it has been widely treated as a single constitutional body because many of its original features remained in place through the reform process (e.g., the unitary nature of the republic).

times, and that some of the fiscal-related amendments appear to be due to its lack of adaptability and robustness.

The research questions that the study attempts to shed light on can be summarized as follows:

- What factors in the Colombian 1991 fiscal constitution, if any, favor or inhibit the reduction of interregional inequalities in economic development? What factors, if any, intensify such inequalities? How do such factors operate?
- What could we learn from Spain, Canada and the theoretical literature on institutions, in terms of constitutional design strategies to deal with geographic disparities in economic development, especially those aimed at promoting the reduction of such disparities, taking into account the similarities and differences with the Colombian case as regards the legal traditions and systems of government?
- How could we assess the Colombian fiscal constitution's *adaptability* to changes in the country's geography of economic development, as well as its *robustness* of performance over a variety of plausible policy contingencies?
- If appropriate, what institutional design strategies could help to improve, reasonably, the Colombian fiscal constitution's *adaptability* to the country's geography of economic development, as well as its *robustness* of performance, with the object of furthering the capability of the Colombian multi-tier system of government to reduce interregional inequalities in economic development?

The study is organized as follows. Chapter 2 gives an account of theory-oriented insights on constitutional design, the concept of fiscal constitution and the geography of economic development. A brief graphical illustration of the model underlying the study is presented in chapter 3. As a whole, chapters 4 to 9 describe and analyze the design of the fiscal constitutions of Colombia, Canada and Spain. In particular, chapter 4 offers a comparative overview of the constitutional architecture of multilevel government in the three countries. With a regional

perspective in mind, the functions of government and the government financing institutions relevant for the provision of education and health care, as well as for the generation of income, are examined in the subsequent three chapters, one for each country. Chapter 8 is devoted to analyzing the amendments to the system of intergovernmental transfers embedded in the Colombian 1991 constitution. In chapter 9 the similarities and differences between the fiscal constitutions under scrutiny are discussed. From a quantitative perspective, chapter 10 is set up to explore in the case of Colombia major patterns of multilevel government finance under the current constitution, alongside major trends in regional disparities in income, education and health, with a tentative formal assessment of the adaptability and robustness of the system of intergovernmental transfers so far. A quantitative comparison with the cases of Canada and Spain on a selection of issues is included in this chapter too. Chapter 11 analyzes the interview material obtained, on the basis of a stratified sample design, from current or former heads of Colombian public sector organizations, belonging to different levels of government, with stakes in the policy making process in fields relevant for the study. Chapter 12 concludes the study, discussing the research questions in light of its findings.



## **2.0 CONSTITUTIONALISM AND ECONOMIC DEVELOPMENT IN THE THEORETICAL LITERATURE**

### **2.1 CONSTITUTIONAL DESIGN AND THE CONCEPT OF FISCAL CONSTITUTION**

Two leading proponents of the concept of fiscal constitution are Brennan and Buchanan (1980, p. 153), who define it as “the means of constraining government’s power to tax and to spend.” This definition is arguably incomplete. The means for enabling the use of such power are also essential for the working of the fiscal state.

In principle, the fiscal constitution would consist of all or some of the following building blocks: (a) conformation of fiscal tiers or levels of government, pillars of the organizational structure of the state from a geographic and fiscal perspective; (b) allocation of the power to tax and to raise other revenues between and within fiscal tiers; (c) assignment of spending powers and functions between and within levels of government; (d) establishment and design of intergovernmental transfers; and (e) scope and limits of public borrowing. Such building blocks, taken together, amount to the fiscal constitution of a multilevel system of government.

The odds are for the fiscal constitution to be at least partially embedded in a country’s written constitution, over its different sections. Following Gavison (2002), the standard content of written constitutions can be classified under a few headings, namely: Basic values and commitments; bill of rights; governmental arrangements and structures; enforcement

mechanisms; and amendment procedures. A ‘public policies’ heading can be added to account for the policy content found in some constitutions. Part of the fiscal constitution may be found in statutory or ordinary law.

Roughly following in the footsteps of Commons, who takes institutions to mean “collective action in control, liberation and expansion of individual action,” (1931, p. 649) and of North, who defines them as “the rules of the game in a society or, more formally, [...] the humanly devised constraints that shape human interaction,” (1990, p. 3) constitutions can be seen as a particular type of institutions. In North’s theoretical framework, constitutions, in conjunction with statutes and other legal instruments, belong to the family of formal institutions, which, to the degree that they are enforced, turn into sources of incentives under whose influence individuals and organizations, including central and lower level governments, act or operate.

Although institutions are all products of human action, a distinction can be made between institutions that are consciously designed and institutions that are by and large merely constructed (Goodin 1996; Reynolds 2002). In this regard, Popper (1961, p. 57) asserts that “Only a minority of institutions are consciously designed: the vast majority have just ‘grown,’ as the undesigned results of human actions.” Constitutions, particularly written constitutions, are generally taken as prominent examples of intentionally designed institutions. For instance, referring to the U.S. constitution, Simon (1996) describes it as a purposeful human design at a societal scale, an artifact devised to attain collective goals. Constitutions belong, in Simon’s conceptual framework, to the artificial world, as opposed to the natural world, and as such “they

are what they are only because of a system's being molded, by goals and purposes, to the environment in which it lives.” (p. xi) <sup>10</sup>

The purpose of written constitutions and the relative importance of their different components in achieving the given purpose have been the subject of a long lasting debate, which can be traced to the 1787 Philadelphia Convention. Thus, while the protection of rights is generally regarded as an overriding constitutional goal, disagreement prevails as to how best to protect them. Simplifying things somewhat, on the one hand there are those who believe that a bill of rights is the most suitable tool for achieving such a goal, whereas on the other hand there are those who argue, as Hamilton and Madison did, that the constitutional governmental structures, coupled with the enforcement mechanisms, are better than declarations as rights protecting devices. This latter position is well summarized by Sartori (1997, p. 196), who writes: “a constitution without a bill of rights is still a constitution, whereas a constitution whose core and center piece is not a frame of government is not a constitution.” Still, it is fairly common for constitutions to contain both a bill of rights and some sort of government framing provisions. Although in practice the issue does not manifest itself as a mutually excluding choice, the debate is a reminder that, when it comes to protecting rights, not all constitutional tools are equally up to the job.

As institutional construct, the fiscal constitution should not be seen as independent from the overall constitution. In identifying links between the two an open systems framework of

---

<sup>10</sup> The possibility that some constitutions, or parts of them, are not the product of design should not be written off. Horowitz (2002, p. 16) claims, for example, that “constitutions that have been *designed*, as opposed to merely constructed, are difficult to find. The sheer proliferation of participants makes it less, rather than more, likely that a design, with its consistent and interlocking parts, will be produced at the outset and adopted at the conclusion.” A utopian, perfectionist standard of design, where anything less than *entirely* ‘consistent and interlocking’ cannot be called design, looks to be an unpromising analytical avenue, however.

organizational design, such as the one presented by Harrison and Shirom (1999), is helpful. For example, the bill of rights can be seen as organizational goals (i.e., a country's collective goals), the fiscal tiers as organizational structure, and the powers to tax and spend as organizational inputs. The open systems framework allows the representation of a constitutional design from a means-and-ends perspective. Therein the fiscal constitution becomes a means of achieving collective goals. Yet, insofar as democracy is a valuable social goal in its own right, democratic institutions —of which the fiscal constitution may be an example— also become ends in themselves.<sup>11</sup> As far as developing countries are concerned, relatively little attention appears to have been paid to the assembly, as a system, of the fiscal constitution's building blocks, as Litvack, Ahmad et. al. (1998) suggest.

In the realm of constitutional design, different levels of choice can be identified for analytical purposes. The first level corresponds to the choice between some constitutional rules and *no* constitutional rules at all. As Brennan and Buchanan (1985) point out, this level of choice raises the fundamental question of the reason of rules. The second level is the choice *between* alternative constitutional rules. As Horowitz (2002, p. 19) writes, "If there is a subject called constitutional design, then there must be alternative constitutional designs." The third level refers to the choices available *within* a given set of constitutional rules, or, more specifically, within a fiscal constitution. These decision levels are interrelated. For example, decisions at the third level may be made to change the existing fiscal constitution, leading to the second level of choice.

More attention is paid here to the economic consequences of constitutional decisions than to the intentions of the constitution makers. Cooter (2000) argues in this respect that

---

<sup>11</sup> . Mill helped to plant the seeds of this line of argument by maintaining that "the ideally best form of government is representative government." Mill, J. S. (1991). Considerations on Representative Government. New York, Prometheus Books.

“constitutional theory should trouble itself less with literary analysis and arguments over founders’ intentions and focus much more on the real-world consequences of various constitutional provisions and choices.” Without subscribing to consequentialism as the only valid approach to judge a constitution, Cooter’s advice appears particularly pertinent for economic analysis.

As the nation-state remains the predominant legal jurisdiction, legal systems tend to be country-specific (e.g., the Colombian legal system, the Canadian legal system, the Spanish legal system). Nevertheless, constitutional design can be regarded as taking place in legal traditions that generally go beyond national borders. According to Merryman (1985, p. 2), a legal tradition is “a set of deeply rooted, historically conditioned attitudes about the nature of law, about the role of law in the society and the polity, about the proper organization and operation of a legal system, and about the way law is or should be made, applied, studied, perfected, and taught.” Glenn (2004) lists seven different legal traditions of the world, including the civil law tradition and the common law tradition. The other traditions are the Chthonic, the Talmudic, the Islamic, the Hindu, and the Asian legal traditions. In analyzing constitutions and in formulating strategies of constitutional design, the legal tradition in which a country’s legal system is embedded ought to be kept in mind.

Even as disagreement prevails on whether a constitution should be understood as a social contract, a bundle of conventions or something else, a degree of stability is generally considered a desirable feature of a constitution, provided that stability does not sanction tyranny or other forms of undemocratic rule. For example, for Rawls (1987, pp. 1 and 3) a country’s constitution is ideally “an overlapping consensus” over “the ‘basic structure’ of a [...] constitutional democracy”. Elster (2000, p. 88), building on many authors, sees constitutions as

precommitment devices, as leading examples of a variety of mechanisms created by societies “to protect [themselves] against [their] own tendency to make unwise decisions” No overlapping consensus or constitutional precommitment could yield fruit or be successful without an important degree of stability.

Adaptability and robustness are qualities of complex adaptive systems and the decision making process relevant for constitutional design. According to Axelrod and Cohen (1999, p. 7 ), adaptation occurs when the actions of agents seeking to adapt lead “to improvement according to some measure of success.” The incentives stemming from a constitution could be for or against adaptive improvement. Satori (1997) makes “the case for conceiving and building constitutions as incentive-based structures,” an approach claimed to be less commonly put into practice than would be desirable. For Lempert, Popper et. al. (2003), decision making should seek robust instead of optimal strategies, where robust strategies are those that “perform reasonably well compared to the alternatives across a wide range of plausible scenarios evaluated using many value systems held by different parties to the decision.” (p. *xiv*) Robustness in constitutional design is likely to lead to a more stable constitution.

## **2.2 ECONOMIC DEVELOPMENT AND ITS GEOGRAPHY**

The pioneers of economics in the 17<sup>th</sup> and 18<sup>th</sup> centuries devoted a good deal of attention to problems of economic development (Lewis 1988). The classical economists, including Smith, Ricardo and Marx, generally took development to mean regular progress and rising prosperity, as Sen (1988) points out. An essential element in their understanding of progress and prosperity

was, in turn, the improvement of the conditions of human life, with Ricardo and Marx particularly concerned with the distribution of wealth and income. By the mid-20<sup>th</sup> century a marked shift in the meaning of development had occurred. The shift is noticeable in the writings of Rosenstein-Rodan, Nurske, Lewis, and Rostow, generally regarded as the founders of modern development economics (for a compilation of such writings, see Kanth 1994). Although the creation of wealth is arguably a fundamental component of development, these authors went too far in equating economic development exclusively with economic growth and, oftentimes, industrialization.<sup>12</sup> The identification between economic growth and economic development reached new heights within conventional neoclassical economics, especially with the growth model set forth by Solow in the 1950s (Solow 1957).

In a way, the last two decades or so have witnessed a sort of revival of the classical economists' notion of development. Economic growth, industrialization and capital accumulation have all been questioned as exclusive or proper ultimate goals of economic development. These factors should be seen, it has been argued, as means rather than ends, or, in another scenario, as a partial set of objectives of development policy (e.g., Sen 1999). An early, important but frequently forgotten contributor to the redefinition of development is Dudley Seers, a British economist, who argued, for instance, that “[a] ‘plan’ that conveys no targets for reducing poverty, unemployment and inequality can hardly be considered a ‘development plan’.”

---

<sup>12/</sup> Economic growth was championed by many as the subject matter of development economics. For example, Lewis (1988, p. 36) wrote: “By development theory I mean those parts of economics that play crucial roles when one tries to analyze the growth of the economy as a whole.”

(Seers 1972, p. 24) Such views underlie the notion of human development, which since the early 1990s have become central to the United Nations' *Human Development Reports*.<sup>13</sup>

Notwithstanding its highly valuable insights into the meaning and ends of development, the human development approach is not free of limitations. Not particularly salient have been its contributions to the causal explanations of the development process, as Martinussen notes (1997). It does not say much, for instance, about the determinants of the provision of education and health care, not to mention the determinants of capital accumulation and technological change. Sen (1988, p. 11) at some point refers to this type of issues as “logistic and engineering problems.” To be sure, clarifying the goals of development is essential for the design of economic policy, but having the right ethical views on the nature of such goals does not by itself guarantee that we know how to get from here to there. For causal explanations of the development process, we would have to look elsewhere.

In assessing economic development in each or all of its dimensions, including health, education and income, the overall performance of a country matters, but the relative performance of the component units, whether they are defined as households, age groups or governmental jurisdictions, to name but a few possibilities, may be of interest as well.

Because it is intrinsically valuable, health is deemed one of the basic goals of development (Fukuda-Parr and Shiva Kumar 2003). Economic inequality and market failures offer a rationale for government intervention in the provision of health care (Stiglitz 1988).

---

<sup>13</sup> . According to Anand and Sen, the emphasis of the notion of human development is on “what people get from development,” more than on “what they put into it.” Anand, S. and A. Sen (2000). “The income component of the human development index.” *Journal of Human Development* 1(1): 83-106..



Individuals or households at the bottom of the economic scale may be unable to afford medical care, a situation that governments may seek to address. The inequality argument can be applied, with some qualifications, to the case of subnational jurisdictions. Uncertainty associated with the eventuality of illness, coupled with high treatment costs derived from its occurrence, leads, in all probability, to underprovision of health care by the market (Arrow 1963).<sup>14</sup> To compound matters further, the health insurance market is predisposed to adverse selection, a situation where the demand for insurance would disproportionately come from individuals likely to face high medical costs while the supply of insurance would disproportionately concentrate on healthy people. As health care provision is a composite activity, government intervention, which can be seen as a continuum from no intervention to complete statism, may take a variety of forms across and within the areas involved, including the regulation, financing and delivery of health services.

Education, above all the knowledge and skills acquired through it, is regarded as an end of development as well (Haq 1995). In addition, it is viewed as a form of human capital, and consequently a means of the development process, as the knowledge and skills of the labor force are fundamental ingredients in the generation of income and wealth (Schultz 1961). As Stiglitz (1988, p. 372) writes, “the primary justification for public support of education arises from concern about the distributional implications of the private financing of education.” A strong case can be made that the educational opportunities of a child should not entirely depend on luck, which materializes, as Stiglitz puts it, “on the wealth of his parents or the happenstance of the community in which his parents live.” Subnational government jurisdictions enter the scene

---

<sup>14</sup> . As Arrow (1963, p. 949) writes, “Illness is... not only risky but a costly risk in itself, apart from the cost of medical care.”

because they are a type of community, namely, political and fiscal communities. Most likely, the wheel of fortune would leave many children without schooling, contributing to the transmission of economic inequality across generations.

While broadly acknowledged to have a central place in economic development, the position of income and wealth creation, as well as the associated economic growth, in a means-ends framework stirs up controversy. According to the *Human Development Report* (1990), which first introduced the Human Development Index (HDI), a key component of economic development is the “command over resources needed for a decent living.” (p. 12) Income, a result, at a social scale, of economic activity, was chosen as the indicator of such dimension of development. Anand and Sen (2000, p. 86) argue that “there are many important capabilities which are critically dependent on one’s economic circumstances,” even though –these authors stress– commanding resources, which normally presupposes the creation of wealth, should not be considered an end in itself but only a means to achieve people’s ends. Some enthusiasts of the human development approach have taken this idea far afield, though, dismissing the importance of wealth creation and economic growth.

Regardless of whether or not the level and growth of aggregate income should be an objective of economic policy, governments, as Tobin (1964) observes, almost inevitably affect economic activity through, for instance, the spending budget and the tax code. Therefore, a neutral government with respect to the creation of income and wealth would be an impossibility at a practical level.

Economic development has, of course, a spatial expression. The geography of economic development encompasses the spatial distribution of income and wealth and of other dimensions

of development, including education and health. Theories in the field tend to focus on the spatial distribution of economic activity, or aggregate output. Classic models of the location of economic activities in national or regional spaces are due, or are derived from, Weber ([1909] 1969) and Christaller (1966). Weber's model, for instance, attempts to explain the location, or, perhaps more precisely, the causes of changes in the location of industries. Key factors in the location of industrial firms are, in this context, the availability of inputs, as well as the costs of labor and transportation. Forces for and against spatial agglomeration have been identified with the help of this model.

A more comprehensive theoretical approach to the location of economic activity has emerged in recent decades. Institutions, geography and trade have been hypothesized to be ultimate, as opposed to proximate, explanatory factors of the uneven distribution of economic activity among and within countries. Echoing the work of North, the role of institutions has been empirically examined, among others, by Acemoglu, Johnson and Robinson (2001), who attach particular significance to the different patterns of European colonial settlement in explaining the strength or weakness of both the rule of law and the security of property rights in Latin American and other countries, and by Hall and Jones (1999), who measure institutional development through a variable called social infrastructure. The role of geography is emphasized, for instance, by Krugman (1995) and Gallup, Sachs et al. (1999). In Gallup, Sachs et al. model, a country's GDP per capita is set to depend on the distance to core markets, the proportion of the population living in coastal regions, and the extent of the land area within the geographical tropics, among other geographical variables. One finding is that the majority of countries that are either landlocked or located in the geographical tropics (*or both*) are poor. The role of trade or, more

generally, the size of the market in determining the location of economic activity is highlighted in the work of Frankel and Romer (1999), to give one example. Rodrik, Subramanian et. al. (2004) focus on the interactions among institutions, geography and trade to explain the cross-country differences in per capita output, calling attention to how misleading it may be to consider the influence of these factors in isolation from one another.

### **2.3 LINKS BETWEEN THE FISCAL CONSTITUTION AND THE SPATIAL DISTRIBUTION OF ECONOMIC DEVELOPMENT**

As a field, the study of the economic effects of constitutions appears to be still in its infancy. Persson and Tabellini (2003) go as far as to state that the analysis of the impact of constitutions on policy making and the economy has been neglected in the theoretical and empirical literature, to the point of being “a missing link”.

While the overall constitution can be said to mold the spatial organization of the state, the fiscal constitution can be said to mold the spatial organization of the public finances. By doing so to some extent, the fiscal constitution sets the organizational conditions and structures through which it may influence the geography of economic development. The spatial organization of the public finances generally coincides or overlaps with the multilevel system of government, where such a system exists. No effects of the fiscal constitution upon the geography of economic development could materialize without the fiscal interactions between the system of government, multilevel or otherwise, and its outer environment (e.g., taxpayers, beneficiaries of public spending).

Some theoretical approaches deal with a multilevel system of government from a fiscal standpoint. Within neoclassical economics, for example, Tiebout's (1956) *A Pure Theory of Local Expenditures*, Musgrave's (1959) *The Theory of Public Finance*, and Oates's (1972) *Fiscal Federalism* are commonly considered ground-breaking works in the body of literature known as fiscal federalism, which examines, mostly from a normative viewpoint, the assignment of functions and revenue sources between levels of government. Following the classic statement by Musgrave (1959), the economic functions of government are classified in three branches: resource allocation, macroeconomic stabilization, and income and wealth redistribution. Contrary to what the fiscal federalism label suggests, such literature is frequently applied to both unitary and federal systems of government, or, for that matter, to any system of government integrated by a plural number of levels of government, loosely defined (Oates 1999). Such is distinctively the case when fiscal federalism is defined, as Bird (1999, p. 151) does, as "the analysis of the problems that gave rise to, and arise from, the existence of more than one level of government within the same geographical area." Certain assumptions employed in the fiscal federalism literature (e.g., perfect information and fully rational decision making), as well as the theoretical implications that follow therein, have been strongly and rightly criticized.

Differences in income and wealth between persons typically give rise to differences in income and wealth between regions in a given country. As income and wealth constitute the backbone of taxation, regional disparities in fiscal capacities (i.e., the potential capacity to generate tax revenues) and, under certain assumptions, in the provision of public goods arise. A central normative question in this regard is whether governments should seek to redress regional economic disparities. One approach holds that whatever the norms of distributive equity are, they

should apply to individuals, rather than to groups, regional or otherwise. For instance, Buchanan (1950) argues for the use of the principle of “equal fiscal treatment for equals” over the national scope, where individuals, instead of the sub-central government jurisdictions (e.g., states, departments), would be the appropriate units for the assessment of equity. This would be best implemented, according to Buchanan, by means of “geographically discriminatory central government personal income taxation,” with tax rates varying from jurisdiction to jurisdiction “so as to offset differences in state fiscal capacities.” (p. 595) But this policy option is judged by the author to be unfeasible, especially from a political standpoint.

An alternative view takes groups or collective entities, including sub-central jurisdictions or regions, as potentially valid, albeit not necessarily ideal, bearers of equity, however defined. If nothing else than for pragmatic reasons (i.e., political feasibility), Buchanan himself regards the units of the intermediate level of government as routes to the “equal fiscal treatment for equals”. A second best way of implementing this principle, Buchanan argues (1950, p. 586), would require an intergovernmental transfer system (particularly of an unconditional nature) from the central to the sub-central government units, tailored to “allow state units originally unequal in fiscal capacity to provide equal services at equal levels of taxation.” It is worth highlighting that for Buchanan the range of what should be equalized concerns the provision of public goods and the level of taxation only, rather than an overarching collection of sources of economic inequality.

The survival and stability of a country as a political community could well be compelling reasons, overlooked by Buchanan, why the reduction of economic or fiscal disparities among government jurisdictions or regions is a justifiable policy goal in its own right. Deep economic or

fiscal inequalities among regions, when left unaddressed, can become a source of social and political unrest, even to the point of threatening the very existence of the countrywide political community itself.

Transaction costs theorists distinguish between grand or programmatic redistribution and tactical redistribution conducted through the fiscal state (Dixit and Londregan 1996). The first type of redistribution, deemed to reflect the social beliefs about economic equality and to be relatively stable through time, is more likely to be the subject of regulation at the constitutional level or to be voted into relatively lasting laws.<sup>15</sup> The second type of redistribution takes place through ‘pork barrel’ politics and other similar mechanisms, and corresponds to the everyday play of the game within a given fiscal constitution or legal framework. The two levels of redistribution, which may have different determinants, can be placed in a multilevel government setting. Intergovernmental transfers, for instance, are prime candidates to belong to the grand or programmatic category of redistribution.

The following sections offer an overview of major programmatic channels through which the fiscal state is likely to shape the spatial distribution of economic development.

---

<sup>15</sup> / Dixit and Londregan (1996, p. 1132) describe grand redistribution as reflecting “the prevailing ideological beliefs about equality and is carried out using income taxes (sometimes and in some countries wealth taxes) and the general social welfare system. These redistributive programs are relatively fixed for large periods of time and change only when there is a major ideological shift in the population.”

### **2.3.1 Taxation and Other Revenue Sources**

A starting point here is the problem known as the assignment of taxes and other revenue sources. In the case of taxes, for instance, the problem would be to determine who taxes (*or* should tax), where and what, as Musgrave (1983) puts it. The ‘who’ refers to the level of government to which a tax source is assigned, the ‘where’ to the territorial scope of the tax, and the ‘what’ to the kind of economic activity (e.g., production, consumption) or, more specifically, the goods and services to be taxed.

An important issue is the degree of centralization/decentralization of the tax system, that is, the degree of control that the rules of taxation permit to subnational governments over the tax base, the rate structure, the tax rates, and the administration of taxes (Groenewegen 1990). Different degrees of tax centralization/decentralization mean different assignments of tax and spending powers in a world of multiple government jurisdictions, and therefore different policy making scenarios, each one with its own benefits and costs in terms of economic development.

### **2.3.2 Intergovernmental Transfers**

The separation of spending and taxation typically embodied in the assignment of revenue sources and functions between levels of government is at the heart of what is known in the literature on the subject as vertical fiscal imbalance, the monetary mismatch, before intergovernmental transfer payments, between the revenue potential, given the assignment of taxes, and the



expenditure responsibilities across levels of government (For a discussion of this issue, see Boadway 2005).<sup>16</sup>

A rationale for intergovernmental transfers is to close or narrow such vertical imbalance (on the rationales and design of transfers, see, for instance, Anderson 1994; Ahmad 1997). A situation of unlimited intergovernmental transfers would be avoided by defining the vertical imbalance with respect to standard or optimal differences, rather than with respect to the actual differences, between revenues and expenditures. Another rationale for intergovernmental transfers is to compensate for the disparities across jurisdictions in the potential to raise tax revenues or to provide a similar level of public goods and services. Again, if unlimited transfers are to be avoided, the level of taxation and the expenditure needs should be defined with respect to cross-jurisdictional benchmarks. Equalization transfers, as the transfers serving these purposes are called, tackle the horizontal fiscal disparities (or imbalances). An intergovernmental transfer system may be designed to correct in whole or in part both the vertical and the horizontal fiscal imbalances, so that the two rationales are not necessarily mutually exclusive.

When the territorial boundaries of subnational governments and those of the public goods they provide are the same, a case has been made for the application of the benefit principle, which entails, as Olson (1969, p. 483) writes, “a match between those who receive the benefits of a collective good and those who pay for it.” The benefit principle would apply here to each sub-central jurisdiction taken as a whole, which is not inconsistent with the use inside the given

---

<sup>16</sup>. Some authors use the expression ‘vertical fiscal gap’ to describe this phenomenon, leaving the expression ‘vertical fiscal imbalance’ to refer to a situation where intergovernmental transfers fail to close the vertical fiscal gap. In this study, I have opted for the usage described in the main body of the text.

jurisdiction of a mixture of taxation criteria, say, the ability to pay principle for the property tax, the benefit principle for the vehicle tax, and so on and so forth. But when there are externalities between jurisdictions in the provision of collective goods, the case for the benefit principle, applied in its pure form, weakens. As regards education, for instance, owing to migration the jurisdiction where a person goes to school and the jurisdiction where the person works after graduating may be different. As a result, the governments of net emigrating jurisdictions would face disincentives to provide enough funds for education, and, if they provided enough funds, their taxpayers would end up subsidizing the taxpayers of the net immigrating jurisdictions. Without rendering the monetary contributions of sub-central governments redundant, inter-jurisdictional externalities thus constitute grounds for the financing of education by means of transfers from the central government, as Olson argues.

The responses to the vertical fiscal imbalance and the horizontal fiscal disparities may, as the preceding example suggests, intensify or limit the inter-jurisdictional inequalities in economic development.

### **2.3.3 Public Borrowing**

The conventional wisdom among economists is that macroeconomic stabilization —the use of fiscal and monetary policy to smooth the business cycle— is a function of the state best carried out by the national (or federal) level of government (Musgrave 1959). Taking into account that budget deficits (one of the tools of fiscal policy) almost by definition mean financing public expenditure by debt, the conventional wisdom raises the question of whether, and how, borrowing at the sub-central level of government should be regulated. Some constitutions

contain debt regulations, as happens to be the case in the Colombian one. Regulations of subnational debt are likely to have non-negligible consequences for economic development. For instance, borrowing is known to be an important source of financing for the provision of public infrastructure in many developing-country cities, including those of Latin America (Bahl and Linn 1992). The availability and quality of public infrastructure have a bearing on the performance of the regional and local economies, on which the subnational governments' ability to pay to some extent depends.

Even if a written constitution does not contain explicit fiscal provisions, it may still have indirect consequences for the geography of both the public finances and economic development by way of the rules governing the policy making process, including the conformation of congress and other decision making bodies, as well as the decision rules laid down for such bodies. For example, fiscal redistribution has been modeled as the outcome of the interactions between central and sub-central politics with the constitution providing the rules of the game (Dixit and Londregan 1998). Moreover, voting procedures used by legislatures have been argued to be not neutral with respect to the geographical composition of the budget (Alesina and Perotti 1999). For the most part, such indirect consequences fall outside the scope of this study, however.

## **2.4 COLOMBIAN CONTRIBUTIONS AT A GLANCE**

The performance and structure of the Colombian regional economies have been gaining ground as a subject of study in recent years, with certain emphasis on regional income disparities and the

presence or absence of regional per capita income convergence. Examples of contributions in this area are Cárdenas (1993), and Bonet and Meisel (1999).

Different economic and fiscal aspects of the Colombian 1991 constitution have been the subject of analysis. At a general level, for example, Montenegro (1995) analyzes the transaction costs consequences for economic performance of the verbosity and lack of simplicity of the 1991 constitution, while Kalmanovitz (2002) and Uprimny and Rodríguez (2005), among others, have debated the question of whether or not there is an economic policy regime in, or sanctioned by, the constitution. Many studies have sought to examine the implications of the design of given fiscal institutions for the achievement of macroeconomic policy objectives, especially fiscal adjustment and public debt sustainability. Such is the case, for instance, of Junguito, Melo et. al (1995), Dillinger and Webb (1999), and Echavarría, Rentería et. al. (2002).

Subnational dimensions of a variety of aspects of the overall or fiscal constitution have been examined under the headings of '*ordenamiento territorial*', an expression that can be loosely translated as territorial ordering, and of fiscal and political decentralization. Four favorite issues are intergovernmental transfers, subnational taxation, oil royalties, and the budget procedures. Examples of this body of literature are Wiesner Durán (1992), Comisión de Racionalización de las Finanzas Públicas (1997), and Castro (1998).

### 3.0 UNDERLYING MODEL

Using the jurisdictions of the intermediate level of government (Departments in Colombia, including the Capital District of Bogotá; Provinces and Territories in Canada; and Autonomous Communities in Spain), or regions for short,<sup>17</sup> as the geographic units of analysis, the research problem that the study seeks to address can be graphically represented as follows:

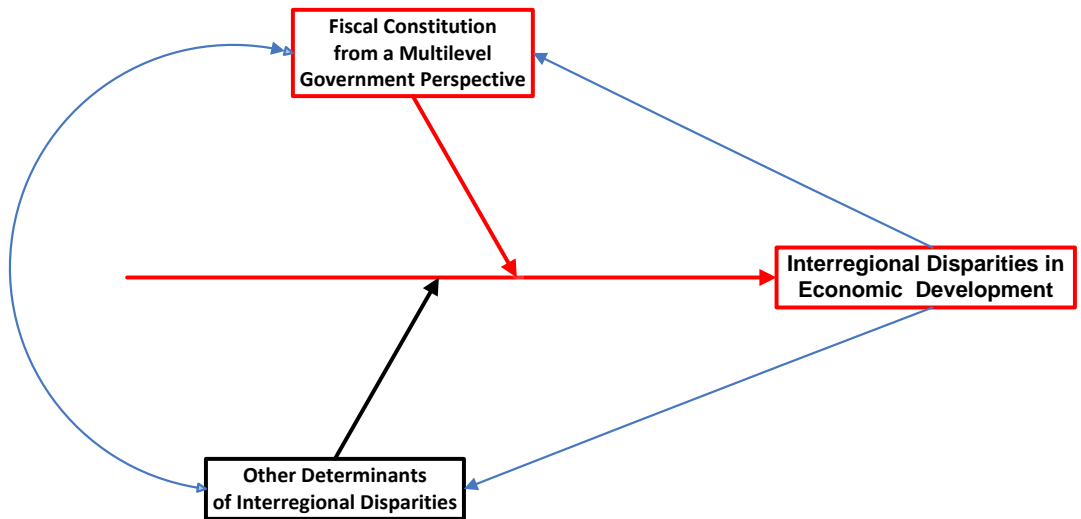


Figure 3-1: General model

---

<sup>17</sup> . Used generically to substitute for the country-specific denominations, the word region is given here a descriptive connotation and is not intended to validate or question the legitimacy of the nationalisms or regionalisms existing inside each country.

In Figure 3.1 the arrows represent causal relationships. The links from the fiscal constitution to the geography of economic development explored here are indicated by the red arrows, with the exploration having a heuristic character. It is recognized, however, that regional economic disparities may in turn shape the fiscal constitution, and that there are other determinants of interregional inequalities, such as trade, geography and non-fiscal institutions. It is also recognized that there may be causal connections, going both ways, between the fiscal constitution and the other determinants of interregional disparities. The indirect effects of the fiscal constitution will not generally be dealt with in this study.

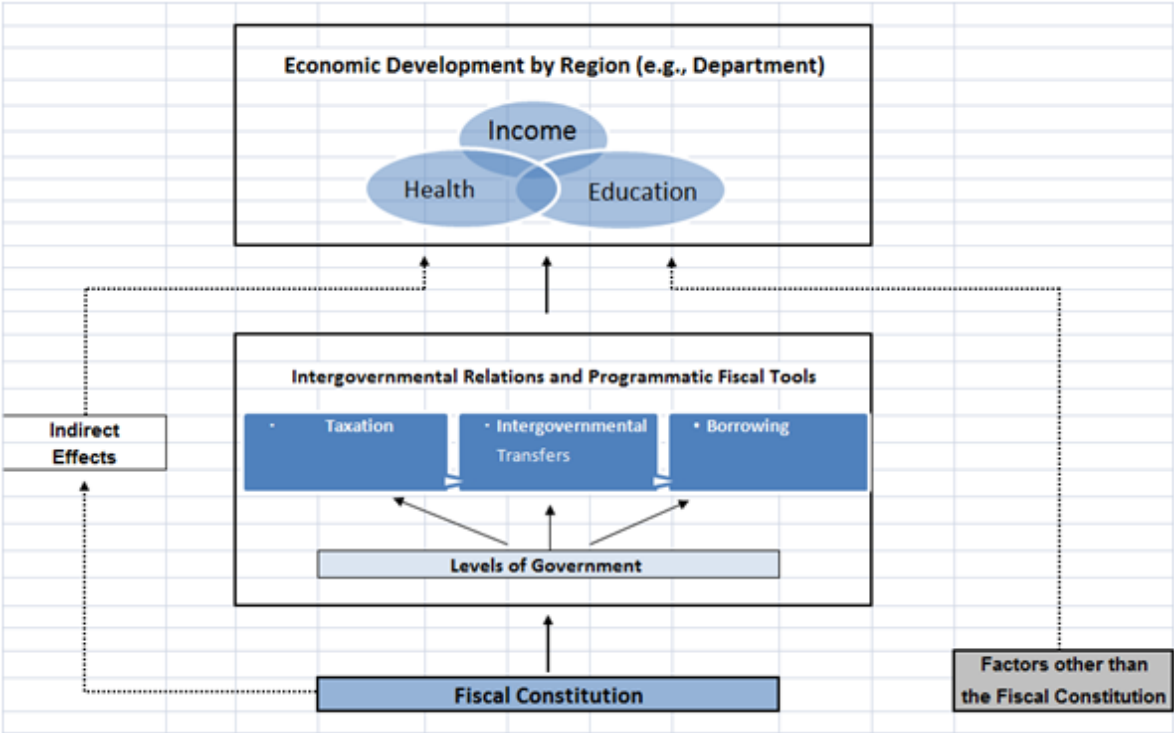


Figure 3-2: Overview of relationships among variables

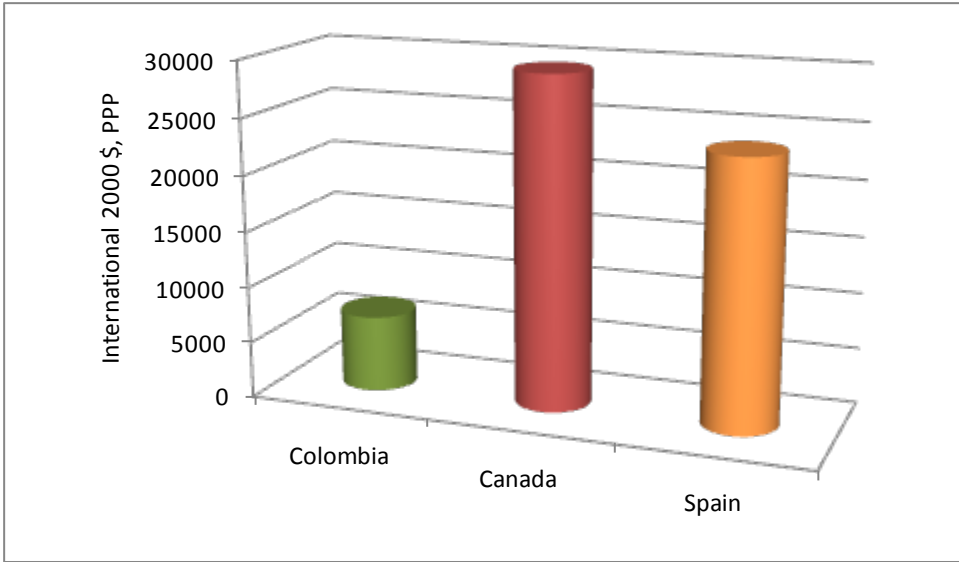
Figure 3.2 offers a more detailed representation of the study's subject matter. On the dependent variable side, economic development by region encompasses, for the purposes of the analysis, three components: health, education and income. On the independent variables side, three components of the fiscal constitution are highlighted: taxation, intergovernmental transfers, and borrowing. These components are seen as linked to the different levels of government. Attention focuses on fiscal tools considered to be programmatic and relevant for fiscal intergovernmental relations.

Even though the Colombian political and fiscal institutions of interest here are sanctioned by the 1991 constitution, their historical origins may precede the newly adopted constitutional charter, in some cases dating back to colonial times. A few examples may suffice to illustrate this point. At the beginning of the twentieth century, the government of General Reyes adopted a policy of partition of the former *Estados Soberanos* – the pivotal component units of the federal structure of government in place in the mid-nineteenth century– into smaller territorial units, giving rise to the current departments. Fears of political dissolution led the Reyes government to weaken the regional powers by way of the partition, according to Fals-Borda (1996). Some departments have been created since July, 1991, but what the new constitution essentially did in this respect was to revalidate the legal credentials of the jurisdictional units called departments as part of the spatial organization of the Colombian state. A good deal of the current division of the power to tax between levels of government gained legal currency in the 1886 constitution. As Alviar y Rojas (1985, p. 65) tell us, “The fiscal regime adopted by the constitution of Nuñez y Caro, whose main features are still alive, allocated the original power to tax to the central level of government.” Regarding taxation powers, as opposed to spending powers, the 1991 constitution in essence corroborated this situation. For its part, the intergovernmental transfer

system originally approved in the 1991 constitution finds its roots in the late 1960s, when the transfers known as *situado fiscal* and *cession del IVA* were first signed into legislation. On the word of Ocampo (1984, p. 365), “the nationalization of education and health services [was],” around the late 1970s, “the latest episode in the process of centralization of the Colombian state”. Fiscal centralization, in particular, is described by this author as a relatively “recent historical phenomenon,” starting at the end of the 1920s (*ibid.*, p. 359). All this indicates that the country’s political and fiscal history helped shaped the 1991 constitution. Still, history is not necessarily destiny and there were real choices between legal arrangements made by the 1991 Constituent Assembly, including choices in favor of the status quo. In this sense, the fiscal institutions associated with the 1991 constitution would meet a relative autonomy criterion to classify as potential candidates for causal factors in economic development.

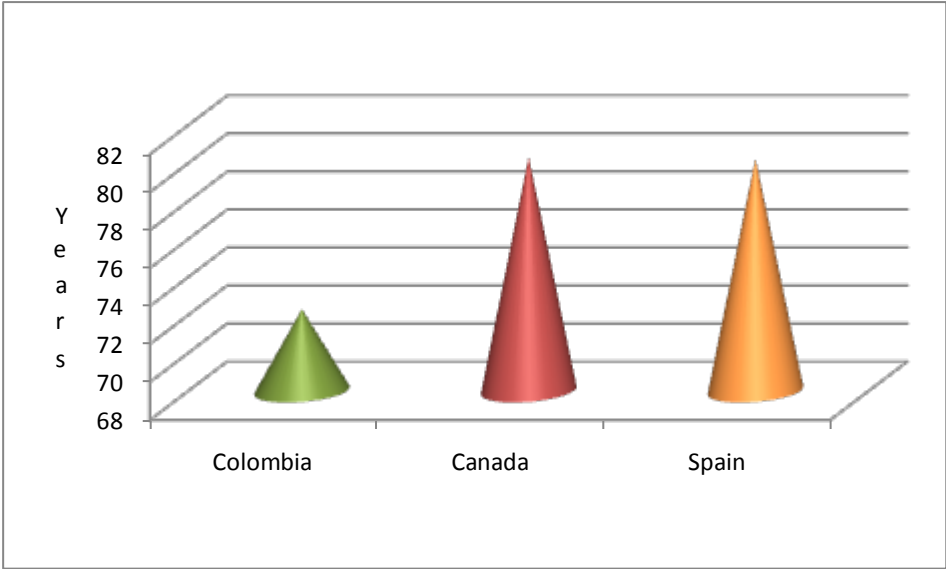
It should go without saying that Colombia differs significantly from Canada and Spain as to the overall level of economic development (it remains to be seen how they differ as to the spatial distribution of development within each country). Colombia’s per capita GDP lags well behind that of Canada and Spain. In 2005, for instance, it reached \$6,789 (2000 PPP international prices), amounting to 23 percent of Canada’s per capita GDP and 29 percent of Spain’s (Figure 3.3). In international per capita income rankings, such as that of the World Bank, Colombia is typically classified as a middle-income country, whereas Canada and Spain belong to the high-income category. An implication of this is, of course, that Colombia is more resource-constrained to offer a given level of education and health services than the other two countries. The quantity and quality of services deemed basic can, however, vary across countries.





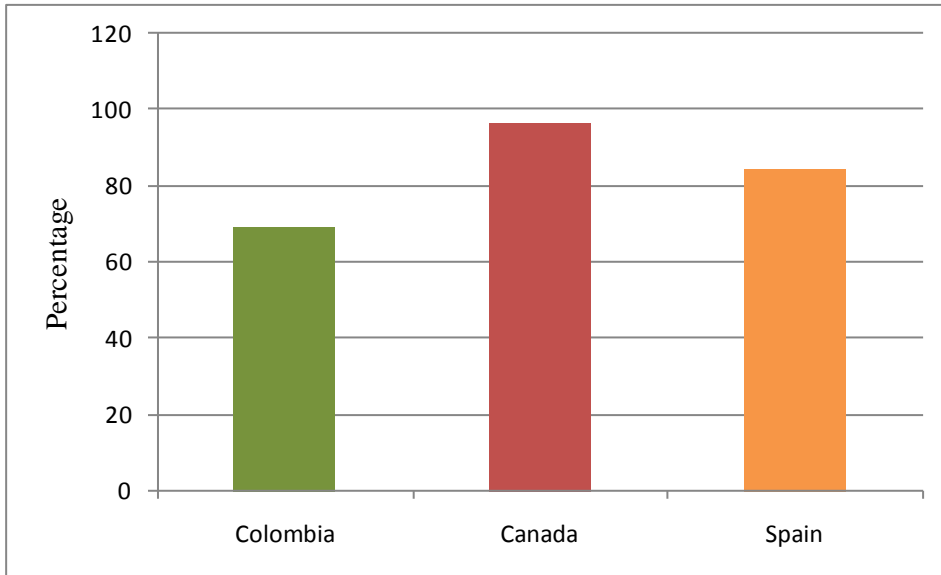
**Figure 3-3: GDP per capita by country, 2005**

*Source:* World Bank, World Development Indicators



**Figure 3-4: Life expectancy at birth by country, 2005**

*Source:* United Nations, Human Development Report, various years.



**Figure 3-5: Gross enrollment ratio by country, 2004 or most recent year available**

*Source:* Original data for Colombia, *Programa Nacional de Desarrollo Humano* DNP/PNUD database (available by request); for Spain, Herrero C., Soler A., Villar A. (2004); and for Canada, author's estimation based on enrollment and school-age population data from Statistics Canada, CANSIM, [www.statcan.ca](http://www.statcan.ca).

With life expectancy at birth slightly surpassing 80 years in both Canada and Spain in 2005, Colombia, with the corresponding figure at 72 years, has a long way to go (Figure 3.4). In the field of education, Colombia trails Canada and Spain as regards enrollment in the basic levels (Figure 3.5). In practical terms, Canada has achieved universal, or near universal, coverage in primary and secondary education, with an estimated gross enrollment ratio of not less than 96.5% since 1990, while in Colombia the same indicator has hardly surpassed 70% in a similar time interval. The most recent estimate for Spain by Herrero, Soler et. al. (2004) puts the gross enrollment ratio at 84.4%; the figure refers to 1999/00 and includes university enrollment.

#### 4.0 CONSTITUTIONAL ARCHITECTURE OF MULTILEVEL GOVERNMENT

This chapter offers an overview of the basic architecture of multilevel government in the three countries of our case study. Some clarification of terminology is first warranted. In Colombia the government with the countrywide jurisdiction is called the national government, in Canada the federal government and in Spain the state (*estado*). Even though the Spanish constitution calls Spain a nation, the expression national government is generally avoided in both academic and everyday parlance because the constitution also recognizes the existence of different nationalities within the country, the commonly named historic nationalities, as a result of a compromise formula to accommodate the Basque, Catalanian and Galician nationalisms within the constitutional framework (Newton and Donaghy 1997). To prevent confusion, we will refer to the countrywide government of Spain and, in some instances, of Colombia and Canada, as central government. In the three cases, our usage of the expression *level or tier* of government, applied to either the countrywide or a smaller jurisdiction, is meant to include the executive and, if present, the legislative (be it, for instance, Colombia's national congress, Canada's federal parliament, or Spain's *Cortes Generales*) and the judiciary branches.

## 4.1 LEVELS AND UNITS OF GOVERNMENT

In addition to the national level, two subnational levels of government are set forth in the Colombian constitution, the departmental level and the local level (Table 4.1). The departmental level consists of thirty two departments and the capital district of Bogotá, which for some purposes is endowed with typically departmental powers and functions, for a total of thirty three jurisdictions. Comprising the municipalities, the special districts, and, again in some respects, the capital district of Bogotá, the local level is made up of about 1,100 jurisdictions. The constitution allows for the creation of two new levels of government, but to date such a possibility has not gone beyond consideration stage.<sup>18</sup> Were the new levels to become reality, Colombia would end up having five constitutional levels of government.

**Table 4-1: Major units of government, 2005 or most recent year available**

|    | Level of Government | Colombia   | Canada                             | Spain   |
|----|---------------------|--|------------------------------------|---|
| 1. | <b>Countrywide</b>  | National Government  | Federal Government                 | Central Government  |
| 2. | <b>Intermediate</b> | Departments (32);<br>Capital District (1)                                | Provinces (10);<br>Territories (3) | Autonomous Communities (17)   |
| 3. | <b>Local</b>        | Municipalities (1094);<br>Capital District (1);<br>Special districts (3) | Municipalities (about 4,000)       | Municipalities (about 8,100);<br>Autonomous Cities (2);<br>Provinces (50) |

NOTE: Number of units in parenthesis.

www.dnp.gov.co; Canada, Mc Millan (2004); Spain, Ministerio de Administraciones Públicas, www.map.es

---

18. The constituent units of the potential tiers of government are referred to in the Colombian constitution as 'regions' and 'provinces'. The 'regions' would each consist of departments. Here the word region is used as common denominator of the existing, as oppose to the potential, government jurisdictions.

Only two levels of government are entrenched in the Canadian constitution: the federal and the provincial levels. Provinces currently number ten; the union originally consisted of four provinces (Stevenson 2004). There are also three territories, which, unlike the provinces, are not directly ingrained in the constitution but are the product of federal law. The difference in legal status enables substantially higher federal involvement in territorial affairs than in provincial affairs. Bearing in mind that the jurisdictions of the provinces and territories do not overlap, we can speak of the provincial/territorial level of government. A sort of local level can also be identified in practice, but the legal life of its constituent units, the municipalities, depends on the provinces (McMillan 2004). For this reason, municipalities are described as “creatures of the provinces”.<sup>19</sup> To a lesser extent, this is also true of the municipalities in the territories. Municipal governments in Canada number roughly 4,000.

In the Spanish constitution, along with the central level, a local level of government, composed of municipalities and provinces, and an intermediate level, integrated by autonomous communities (*comunidades autónomas*), are recognizable. The provinces are an organizational prolongation of the municipalities, so that they are not really a distinct level of government. The provinces typically served, however, as building blocks of the autonomous communities, created during the eighties as a result of a constitutionally regulated process (Gunther, Montero et al. 2004; Magone 2004). At the intermediate level of government, Spain is composed of seventeen

---

19. According to McMillan (2004, p. 5), “The authority of local government in Canada is derived entirely from the provinces. The Constitution only mentions municipalities to declare that they are the exclusive jurisdiction of the provinces. As ‘creatures of the provinces,’ their responsibilities and powers are only those delegated to them by the incorporating province and to which their actions must conform. The provinces have the power to modify those responsibilities and powers and, indeed, to create, change and abolish municipalities at the province’s will. The provinces have not been reluctant to ‘reform’ local government by changing boundaries, responsibilities, powers and funding. Besides, the provinces control their municipalities closely with a host of laws and regulations.”

autonomous communities. Locally, there are two autonomous cities (Ceuta y Melilla) and about 8,100 municipalities, which in turn are grouped in fifty provinces.

There are more regional governments in Colombia (33) than in Spain (17) or Canada (13). With jurisdictions that do not overlap (an exception is the city of Bogotá and the department of Cundinamarca in Colombia), the regions in each of the countries have general purpose governments, belong to the same level of government (i.e., the intermediate level) and are part of a system-wide institutional architecture.<sup>20</sup>

Data on the area and population of the units of the intermediate level of government by country is presented in Table 4.2 for 2005 or the most recent year available. On average, Canada's regions are by far the largest in terms of area, followed by Colombia's and Spain's, in that order. The area of the average Canadian region is, respectively, about 22 and 29 times as large as the area of their Colombian and Spanish counterparts. Some Canadian provinces and territories are as big as, or bigger than, Colombia or Spain, each taken as a whole. In terms of average population size, the Colombian departments are the smallest in the group, with the Spanish autonomous communities taking first place. In Canada, population is highly concentrated in just two provinces, Ontario and Quebec, which together account for about 63 percent of the country's inhabitants. The two largest Colombian jurisdictions in population size, Bogotá and Antioquia, jointly comprise about 28 percent of total population, while their Spanish equivalents, Andalusia and Catalonia, make up about 34 percent of the corresponding aggregate. Contrary to Spain, in Canada and Colombia the degree of variation across jurisdictions, as measured by the corresponding coefficient of variation, is higher for the population size than for

---

20. For a discussion of these and other organizational features of multilevel government systems, see Hooghe, L. and G. Marks (2001). "Types of Multi-Level Governance." *European Integration Online Papers* 5(11).

the area. Population density in Colombia reaches about 40 persons per square kilometer, compared to 86 in Spain and a mere 3.2 in Canada. The variability of population density is particularly high for Colombia (coefficient of variation of 4.4), compared to Canada and Spain (both 1.2).

**Table 4-2: Area and population indicators by unit of government of the intermediate level, 2005**

|  | Area *    | Population **       | Population Density |
|--|-----------|---------------------|--------------------|
|  | sq km     | Persons (thousands) | Persons / sq km    |
| <b>Colombia</b>  |           |                     |                    |
| Number of jurisdictions: 33, including Capital District              |           |                     |                    |
| <b>Total</b>   | 1.141.748 | 46.045              | 40                 |
| Average per jurisdiction   | 34.598    | 1.395               |                    |
| Standard Deviation   | 29.096    | 1.618               | 177 <sup>a</sup>   |
| Coefficient of Variation   | 0,8       | 1,2                 | 4,4                |
| Max  | 109.665   | 7.186               | 4.528              |
| Min  | 44        | 33                  | 0,6                |
| <b>Canada</b>  |           |                     |                    |
| Number of jurisdictions: 13, of which 10 provinces and 3 territories |           |                     |                    |
| <b>Total</b>   | 9.984.670 | 32.299              | 3,2                |
| Average per jurisdiction   | 768.052   | 2.485               |                    |
| Standard Deviation   | 621.871   | 3.743               | 3,8 <sup>a</sup>   |
| Coefficient of Variation   | 0,8       | 1,5                 | 1,2                |
| Max  | 2.093.190 | 12.559              | 24,4               |
| Min  | 5.660     | 30                  | 0,01               |
| <b>Spain</b>   |           |                     |                    |
| Number of jurisdictions: 17 autonomous communities                   |           |                     |                    |
| <b>Total</b>   | 505.151   | 43.968              | 87                 |
| Average per jurisdiction   | 29.715    | 2.586               |                    |
| Standard Deviation   | 30.456    | 2.342               | 108 <sup>a</sup>   |
| Coefficient of Variation   | 1,0       | 0,9                 | 1,2                |
| Max  | 93.814    | 7.850               | 743                |
| Min  | 4.992     | 301                 | 24                 |

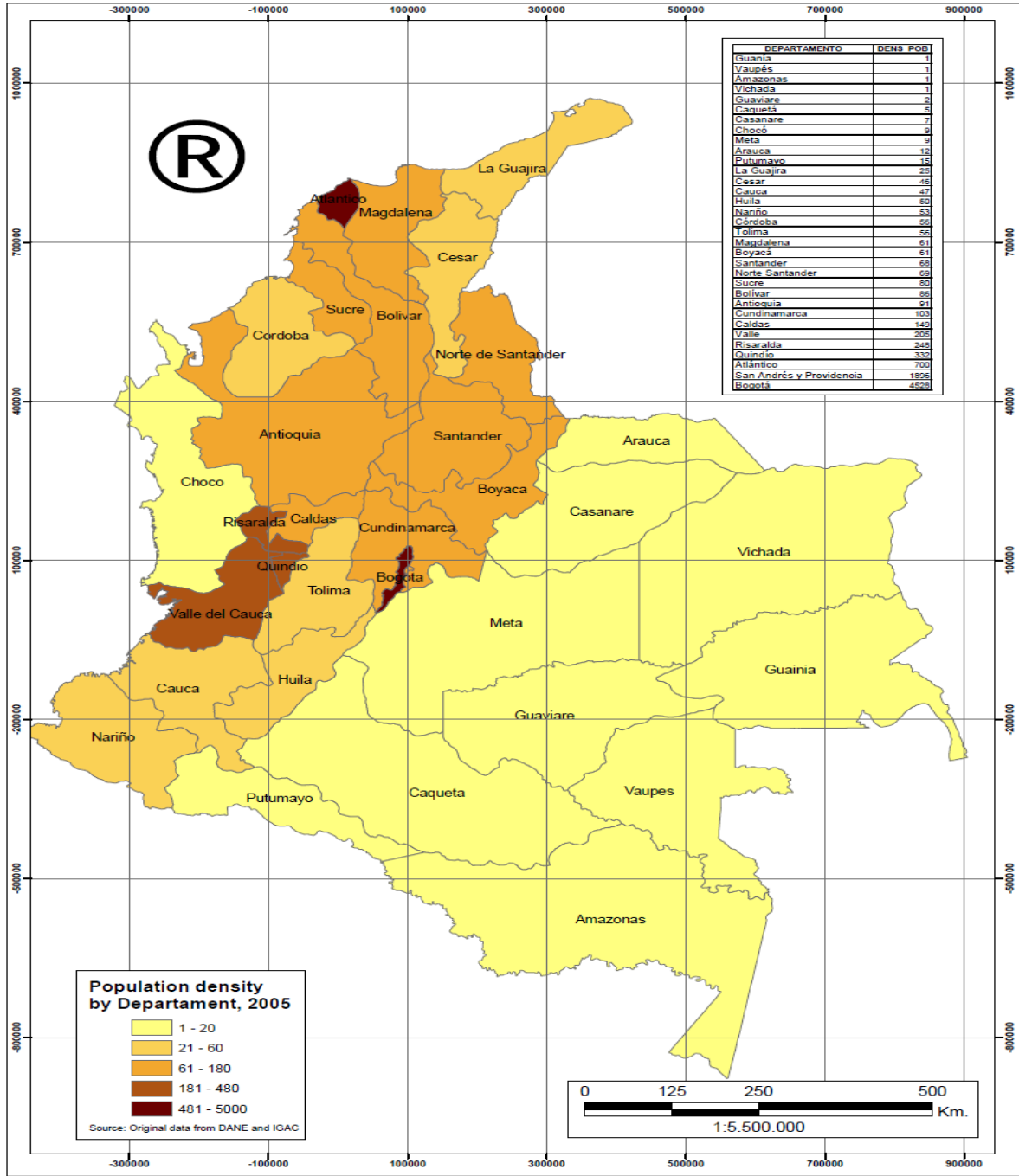
Source: Original data for Colombia from IGAG (\*) and DANE (\*\*); for Canada from Natural Resources Canada (\*) and Statistics Canada (\*\*); for Spain from Instituto Nacional de Estadística.

Note: In the Spanish case, excluding the autonomous cities of Ceuta y Melilla.

<sup>a</sup> Weighted.

The attached map displays population density (*inhabitants/km<sup>2</sup>*) in Colombia by department.

# Population density by Department, 2005





## 4.2 A CHARACTERIZATION OF INTERGOVERNMENTAL RELATIONS

Intergovernmental relations in the three countries of our study can be characterized using a two-dimensional coordinate system, where the horizontal axis represents the unitary/federal dimension and the vertical axis the centralization/decentralization dimension (Figure 4.1). This classificatory system conveys the idea that unitary and federal systems of government may exhibit varying degrees of centralization or decentralization of political and fiscal decision-making. Explanations of basic country-by-country features in the two dimensions of the coordinate system are offered below. For details of scoring decisions, see Appendix A.

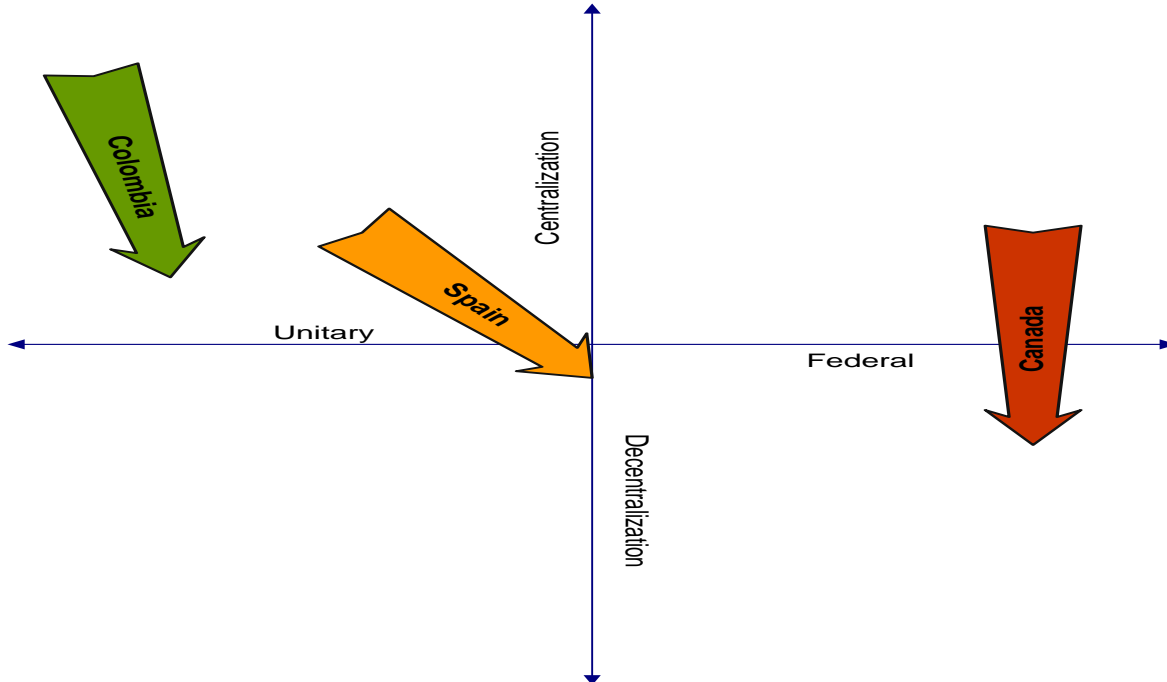


Figure 4-1: Intergovernmental relations: A summary characterization

Classifying Colombia and Canada in the unitary or federal quadrants is relatively straightforward. In fact, the Colombian constitution makes explicit reference to the unitary nature of the state.<sup>21</sup> Canada, as defined in the Constitution Act, 1867's preamble, is a federal country. Political authority in Colombia, including the constitutional authority to make laws, primarily resides in the national level of government, organized along the lines of a presidential system. Notwithstanding that the Colombian subnational levels of government are entrenched in the constitution, they are subordinates of the national level, which, among other things, is empowered, with a few limitations, to unilaterally create or abolish the constituent units of government at each level, as well as to redraw their boundaries.<sup>22</sup> Since the 1991 constitution came into effect, this power has been used in regard to the local level only. Although there are different paths for amending the constitution (e.g., legislative act, referendum, Constituent Assembly), the national congress plays a decisive role in determining which amending path to follow and in the case of the legislative act is the primary decision maker. Except for the authorization to introduce amendment bills, neither the departments nor the municipalities have a formal place in the amendment process.

In Canada, as a federation, the two levels of government are guaranteed independent powers in the constitution. Legislative authority in particular is divided between the federal and provincial levels. The federal level of government, which may be characterized as a parliamentary monarchy, is not allowed to unilaterally create new provinces, or to abolish or modify the existing ones. As to the amending procedure, the constitution calls for the approval of

---

<sup>21</sup>. COL. Constitution, 1991, art. 1.

<sup>22</sup>. The limitations apply in particular to Bogotá, Cartagena, Santa Marta y San Andrés, sub-national units of government which are explicitly mentioned in the constitution.

the federal legislature and the provincial legislatures, in the latter case following, at a minimum, a version of a decision rule known as double majority principle.<sup>23</sup>

Neither the term unitary nor the term federal is employed in Spain's constitution. As Agranoff and Ramos (1997 , p. 3) observe, "Both the Constitution and the governing institutions that emanate from this document establish a framework that is multilayered and interdependent. A look at the constitution of this parliamentary monarchy also reveals that it defies easy federal/unitary classification." It has been described, however, as a quasi-federation (Brooks 2004), as unfulfilled federalism (Beramendi and Máiz 2004), and as an emergent federation (Agranoff and Ramos 1997). For our purpose, the state of autonomies (*estado de las autonomías*), as the territorial organization of the state associated with the 1978 constitution is often called, may be located near the center of the unitary/federal axis, to indicate that there are some traits of each system. The autonomous communities (AC) are generically entrenched in the constitution, but the creation of a particular autonomous community is the result of a special law, called statute of autonomy, whose approval requires the concurrence of both the central level of government, organized as parliamentary monarchy, and the autonomous community to be. Nor is the central level empowered by the constitution to eliminate an autonomous community unilaterally. Nonetheless, the central legislative body (*Cortes Generales*) is entitled to amend the constitution, by qualified majority, with no formal participation of the autonomous communities, albeit they are given some initiative in the amending procedure.

To illustrate the degree of political centralization or decentralization in the three countries four criteria are used here, namely: the presence of formal representation of the regions in the

---

23. For certain issues, the amendment rule calls for the approval of "the legislative assemblies of at least two-thirds of the provinces that have, in the aggregate, according to the then latest general census, at least fifty percent of the population of all the provinces." (CAN. Constitution Act, 1982 Sec. 38(1.b)).

central legislative body, the type of rules for selecting regional chief executives, the constitutional assignment of residual power, and the allocation of fiscal powers to regional governments.

#### **4.2.1 Formal Representation of the Regions in the Central Legislature**

The presence of some type of formal territorial representation at the central legislature can be taken as an indicator of the degree to which political power is shared between the center and the constituent jurisdictions of a country (Breton 1996).<sup>24</sup> A marginal element of territorial representation is present in the Colombian central legislature, particularly in the lower chamber, the House of Representatives. Each department, as well as the capital district, is entitled to a minimum of two representatives. This minimum quota accounts for 40% (66 representatives) of a total of 165 representatives. The rest of the seats are allotted in proportion to the population of the regions. Formal territorial representation is entirely absent from the upper chamber, the Senate, as senators are elected in a countrywide electoral district, with seemingly negative consequences for public policy (Rodríguez 2001). In Spain, formal territorial representation has an important bearing on the composition of the Senate, the upper chamber, but its nature is more local than regional (see Box 4.1). Similar to the Senate, members of the lower chamber are

---

24. Two common rules for the apportionment of seats among sub-national jurisdictions in legislative bodies are known as the principle of popular representation and the principle of territorial representation. While under the former seats are allotted in direct proportion to the population, under the latter seats are distributed more or less equally among jurisdictions.

typically elected in provincial districts, with a minimum quota of seats per province and the remaining seats apportioned between the provinces in proportion to the population.<sup>25</sup>

---

<sup>25</sup> . SPA. Constitution, 1978, art. 68.

#### Box 4.1 Territorial representation in Spain's Parliament <sup>26</sup>

The Spanish central parliament (*Cortes Generales*) consists of two chambers, the House of Representatives (*Congreso de los Diputados*), mostly based on the principle of popular representation, and the Senate, called the chamber of territorial representation, invested with special legislative functions as to the economic development of the autonomous communities and regional and local policies. The districts for the selection of senators are both the provinces and the autonomous communities, but with the former having until now more weight than the latter. Senators are selected through a combination of methods: universal suffrage at the provincial level and appointment by the legislative or highest corporate body at the autonomous community level.

The number of senators *imputable* to a non-insular autonomous community,  $S_i$ , including those elected by its provinces, can be expressed as follows:

$$S_i = (4 \times N^{\text{PR}}_i) + (1 + (P_i / 1,000,000))$$

Where  $N^{\text{PR}}_i$  is the number of provinces belonging to the autonomous community  $i$ . The term  $(4 \times N^{\text{PR}}_i)$  yields

the number of senators elected at the provincial level.  $P_i$  stands for an autonomous community's population size. The term  $(1 + P_i / 1,000,000)$  yields the number of senators selected at the autonomous community level. By the end of 2004, taking the Senate as a whole, 208 out of 259 seats were elected in provincial or similar districts (80% of the total). Given that the rule for the apportionment of seats treats the provinces as equal, it can be stated that the territories represented in the Senate are more the provinces than the autonomous communities. And since the Spanish provinces are deemed local entities, the Senate looks more like the chamber of the local than of the regional.

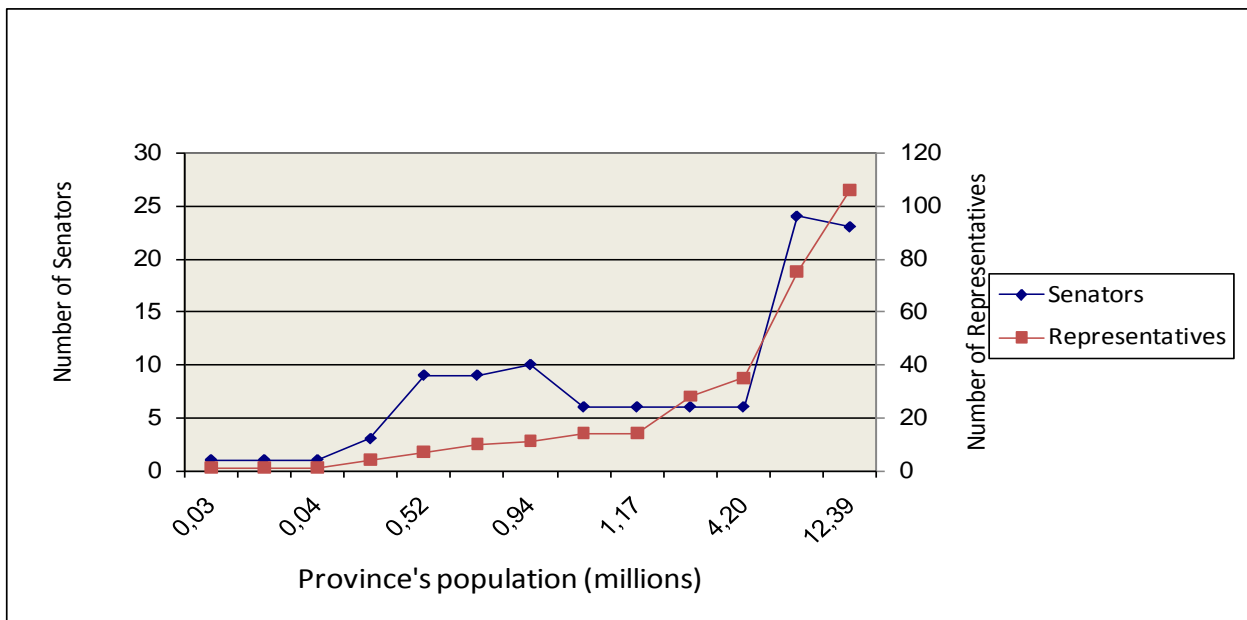
For the legislature beginning in 2004, the number of senators imputable to an autonomous community (other than Canarias and Baleares) fluctuated between 40 for Andalusia and 5 each for Cantabria, Navarre and la Rioja. The correlation between the number of senators and population size across regions reached 0.64. Thus, when the autonomous communities are taken as spatial references for assessing the composition of the Spanish Senate, the prevalence of the territorial principle of representation appears limited and largely unsystematic.

To sum up, while in the House of Representatives the weight of each province, as measured by the number of representatives, depends ultimately on population size, in the Senate the provinces, not the autonomous communities, are treated as equal, regardless of their population size.

---

<sup>26</sup>. In addition to the Spanish constitution, this section is largely based on information from the official websites of the Spanish parliament: [www.senado.es](http://www.senado.es) and [www.congreso.es](http://www.congreso.es).

According to Watts (1999 , p. 96), “Canada, as is the case with so much about its Senate, is unique among federations in basing Senate representation on regional groups of provinces with the four basic regions having 24 seats each, plus an additional 6 for Newfoundland and 3 for the Territories.” Notwithstanding the equality of representation by groups of provinces, in the 38th Parliament, elected in June, 2004, the number of seats attributable to individual provinces in the Senate appears to be largely based on population size, as is also the case in the House of Representatives (Figure 4.2).<sup>27</sup> As senators are appointed by the federal government, not to mention the supra-provincial geographical basis for their selection, the Senate is barely a chamber of provincial representation at the federal level.



**Figure 4-2: Members of parliament and population by Canadian province. 38th Parliament, 2004**

*Sources:* Original data on members of parliament from the Parliament of Canada, [www.parl.gc.ca](http://www.parl.gc.ca), and on population from Statistics Canada, [www.statcan.ca](http://www.statcan.ca).

<sup>27</sup>. The number of senators per province and territory showed a relatively high correlation with each jurisdiction’s population size (0.86), although lower than in the case of the House of Representatives, where the corresponding correlation is nearly perfect.

#### 4.2.2 Selection of Regional Chief Executives

Appointment by a higher level of government and popular election by the corresponding territorial electorate can be seen as the poles of a centralization-decentralization continuum for the selection of regional chief executives in a democracy. The popular election of governors, who were previously appointed by Colombia's president, was explicitly mandated by the 1991 constitution. Mayors had been popularly elected since the mid-eighties, but the constitution ratified this mode of selection. Even though a lieutenant-governor, the representative of the United Kingdom monarchy in a province, is, according to the Canadian constitution, the formal head of government in each province, his/her role is considered largely ceremonial.<sup>28</sup> Real provincial executive power is held by the premier, typically the leader of the biggest political party in a province's legislature. In the territories, a federal appointee, called the commissioner, performs functions similar to those of a lieutenant governor in the provinces. The premier is usually elected by the members of the territory's legislature. As for Spain, the constitution prescribes a model for the organization of the regional institutions of self-government for those autonomous communities following a particular route to autonomy, but in practice the model appears to have spread out to all autonomous communities (Ross 2002). According to the prescribed model, a prime minister (*presidente*), elected by the region's legislature, is the head of government.<sup>29</sup>

---

<sup>28</sup>. See CAN. Constitution Act, 1867 sec. 58. For updated information on Canada's government at the federal and provincial levels, see Canada's official website, <http://canada.gc.ca>, from which I have drawn for this description.

<sup>29</sup>. SPA. Constitution, 1978, art. 152.



Although the specifics vary, the chief executives of regional governments in the three countries are elected rather than appointed (this statement applies to the Canadian provincial premiers, not the lieutenant governors). In Colombia and, via the statutes of autonomy, in Spain, this mode of selection is ingrained in the written constitution.

### **4.2.3 Assignment of Residual Powers**

Residual powers are, Dickerson and Flanagan (1982, p. 175) write, “those powers of government that are not specifically enumerated in the [constitutional] text.” A constitution may assign residual powers to one or another level of government. As a rule of thumb, the more incomplete the enumeration of powers in the constitution is, the higher the number of powers corresponding to the holder of the residual powers clause.

In Colombia, the constitution dictates the internal organization of the national and subnational levels of government and enumerates the powers of each level. While there is no residual powers clause proper, the national congress is given original law-making powers, in contrast with the derived legislative powers granted to the departmental assemblies and local councils. In other words, congress is empowered to develop the constitution, whereas the subnational legislatures are only empowered to develop the laws enacted by the national congress, often insofar as the laws themselves authorize them to do so. It can be stated, then, that the national level of government is the holder of residual powers, loosely defined.

As regards Canada, the constitution enumerates the government functions falling exclusively under the legislative authority of the provinces.<sup>30</sup> It also provides a non-exhaustive list of the types of subjects falling under the federal parliament's jurisdiction.<sup>31</sup> Concurrent federal and provincial legislative authority holds over agriculture and immigration.<sup>32</sup> Regarding residual powers, the constitution says that the federal parliament's legislative scope extends to "...all matters not coming within the classes of subjects by this act assigned exclusively to the legislatures of the provinces."<sup>33</sup> According to Watts (1987), allocating the residual powers to the federal level puts the provinces in a subordinate position, at least for the standards of federalism.

A catalogue of the exclusive competences of the central level of government is found in the Spanish constitution, including matters such as immigration, defense, and administration of justice.<sup>34</sup> Autonomous communities' competences listed in the constitution are optional; it is up to the statute of autonomy to determine which competences from the list are assumed by a regional government; those competences not claimed by the statutes of autonomy belong to the central level.<sup>35</sup> Conversely, any competence not expressly assigned by the constitution to the central level of government may "fall under the jurisdiction of the [autonomous communities] by virtue of their statutes of autonomy."<sup>36</sup> It can be stated, then, that in Spain residual powers correspond to the regions rather than the center, subject to the approval of the statutes of autonomy (see Box 4.2).

---

<sup>30</sup>. CAN. Constitution Act, 1867, sec. 92 and sec. 93.

<sup>31</sup>. CAN. Constitution Act, 1867 sec. 91.

<sup>32</sup>. CAN. Constitution Act, 1867 sec. 95.

<sup>33</sup>. CAN. Constitution Act, 1867 sec. 91.

<sup>34</sup>. SPA. Constitution, 1978, art. 149.

<sup>35</sup>. SPA. Constitution, 1978, art. 148.

<sup>36</sup>. SPA. Constitution, 1978, art. 149.3

#### **Box 4.2 Spanish Statutes of Autonomy**

As there were different tracks for the creation of the autonomous communities, there were and are also different tracks for the approval of the statutes of autonomy. There is, however, a minimum common denominator: the approval of a statute of autonomy is a bilateral process involving the central level of government, on the one hand, and the corresponding autonomous community, on the other.

Generally speaking, by constitutional mandate the autonomous community prepares, through the pertinent bodies, a statute proposal or amendment. Here two broad paths have been followed. In the first one, available for most autonomous communities, the proposal must then be sent to the Spanish parliament, where, if approved by absolute majority voting, it becomes an organic law. In the second path, available for the Basque Country, Galicia and Catalonia (i.e., the nationalities), as well as for Andalusia (with some caveats), after passing through the Spanish parliament, the approved text must be submitted to a referendum of the electorate of the autonomous community. Note that in the first path a bottom-up approach to legislation prevails, with the final word resting with the Spanish parliament, whereas in the second path the legislative procedure does not stop at the top but goes down again, the autonomous community having the final word.

#### **4.2.4 Fiscal Powers of Regional Governments**

Subnational governments in Colombia are constitutionally entitled to have fiscal powers.<sup>37</sup> The extent of such powers is determined by national legislation. Although the degree of fiscal

---

<sup>37</sup> Colombian sub-national governments are entitled to “1. Govern themselves under their own authority; 2. Exercise the competences allocated to them; 3. Administer their resources and establish the taxes necessary for their operation; 4. Participate in national revenues.” See Constitution, 1991, art. 287.

decentralization has increased relative to the pre-1991 situation, subnational fiscal powers are highly vulnerable to changes in the legislation unilaterally made at the national level. In Canada, the constitution distributes the fiscal powers between the federal and provincial levels of government. Unlike Colombia, the fiscal powers of both levels of government may be said to be original. There is, however, a grey area, mainly involving intergovernmental relations, where the boundaries between the fiscal powers of the federal and provincial levels are hard to establish. Spain's 1978 constitution sanctions two main coexisting sets of government financing institutions across Spain's autonomous communities (Salinas 2002). The first one, known as *régimen foral* (special regimen), applies to the Basque Country and Navarre. By virtue of their constitutionally recognized historic rights and traditional charters (*fueros*), these two autonomous communities operate, with respect to the central government, as nearly independent tax jurisdictions. The second set of government financing institutions, called *régimen común* (common regime), applies to the other fifteen autonomous communities. Regional fiscal autonomy is considerably higher in the special regime than in the common regime.

\* \* \*

The position of a country along the unitary/federal dimension, as well as along the centralization/decentralization dimension, may well change through time. What the 1991 constitution did, for instance, was to move Colombia closer to the decentralization quadrant, while keeping the unitary nature of the country. It is not an accident that the very first article of the constitution describes the organization of the Colombian state as “unitary and decentralized, with autonomy of its subnational governments.” Likewise, Spain's 1978 constitution marked a departure from the highly centralized unitary institutions of the authoritarian Franco era and

signaled the transition to democracy in a slightly decentralized quasi-federal environment (Gunther, Montero et al. 2004). Canada, for its part, has remained federal since 1867, when it turned into a self-governing territory with ties to the British monarchy, but along the way has experienced waves of centralization and decentralization (Russell 2004; Stevenson 2004). In the fiscal realm, for example, the tendency appears to have been towards decentralization after World War II. In Figure 4.1 above, these broad trends are illustrated by arrows.

## 5.0 COLOMBIA'S FISCAL CONSTITUTION

### 5.1 DEVELOPMENT-RELATED GOVERNMENT FUNCTIONS

#### 5.1.1 The Right to Education

In the Colombian constitution, education is included among the social, economic and cultural rights, as opposed to the fundamental rights and the collective and environmental rights.<sup>38</sup> Yet, the Constitutional Court has tended to widen the circle of fundamental rights by including in that category some rights originally classified as social and economic rights (health care and, perhaps to a lesser extent, education), or at least by considering them intrinsically connected to fundamental rights. Education is also dubbed “a public service with a social function.” Comprising ten years of basic instruction, schooling is mandatory by law up to the age of 15. In the chapter on the social ends of the state, meeting the unsatisfied basic needs in education is made a fundamental objective of the Colombian state.<sup>39</sup> Moreover, the state is required to promote access to education services for rural workers and handicapped persons.<sup>40</sup>

---

<sup>38.</sup> COL. Constitution, 1991, art. 67. Nonetheless, the distinction between the alluded types of rights becomes somewhat blurred as education is itemized amongst the “children’s fundamental rights” in one of the provisions of the chapter on the social, economic and cultural rights (art. 44).

<sup>39.</sup> COL. Constitution, 1991, art. 366.

<sup>40.</sup> COL. Constitution, 1991, arts. 64 and 68.

How does the Colombian constitution envision, if at all, the protection or enforcement of the right to education? Constitutional mechanisms for the protection of rights may be generic, such as the separation of powers in democratic societies, as well as specific, such as a bill of rights (Tirado 1992). The enshrinement of the right to education belongs then to the category of specific mechanisms of protection. It should be taken into account, however, that the constitution enumerates what it calls rights of immediate application and that education, let alone other social, economic and cultural rights, is not listed in such a class of rights.<sup>41</sup> Only fundamental rights, and not all of them, were granted the status of rights of immediate application. The writ of protection (*acción de tutela*), “by virtue of which any person may directly request any judge in the country to protect his or her fundamental rights...” (Uprimny 2006, p. 4), would not in principle shelter social and economic rights, but the courts, by their powers of interpretation, have made it available for some instances of the rights to education and health. Although the full implications of all this remain unclear, judicial enforcement, as designed in Colombia, appears to be destined to play a limited role in achieving universal basic education, an outcome sought for in the constitution, as witnessed, among other things, by the status of right given to education. The writ of protection, for instance, can only be used when no other appropriate option remains and the rulings associated with it “only have an *inter partes* effect.” (ibid, p. 5)

In pursuit of universal basic education, the constitution allows for both public and private schooling, while calling for free education in government-funded schools.<sup>42</sup> An underlying assumption is that such an objective can be achieved by combining different modalities of delivering education services (i.e., publicly and privately-run schools). The Colombian state is

---

<sup>41</sup> . COL. Constitution, 1991, art. 85.

<sup>42</sup> . COL. Constitution, 1991, arts. 67 and 68.

presented with the governing power over education, including the power to regulate, inspect and supervise both the public and private delivery of services.<sup>43</sup> Although in a roundabout way, the constitution categorizes public expenditure on education as a type of social public expenditure, an item which is given priority over any other expenditure allocation.<sup>44</sup> By designating the departments and municipalities as the recipients of national government transfers for education, it hints at a role for the lower levels of government in the provision of education services, with little or no indications as to their individual functions.<sup>45</sup> Beyond that, the constitution leaves to the law, that is, to the national level of government, the division of government powers and functions between the national, departmental and municipal spheres.

In the situation preceding the 1991 constitution, the governing powers over education were highly centralized. The central government not only exercised the regulatory function but also carried out, in some instances in a spatially deconcentrated fashion, the heart of the management and administration (Misión de Finanzas Intergubernamentales 1984; Comisión Racionalización de las Finanzas Públicas 1997). For example, the management of funds, particularly those to cover the teachers' payroll, was carried out by the *Fondos Educativos Regionales*, at the time regionally deconcentrated branches of the National Ministry of Education. The new constitution signaled a move towards decentralization of powers in the sphere of education, as opposed to a mere functional de-concentration. Public funding for basic education had traditionally been oriented towards the supply of services (e.g., schools' facilities,

---

<sup>43</sup>. Ibid.

<sup>44</sup>. COL. Constitution, 1991, art. 52 reads: "Sports and recreation are part of education and constitute social public expenditure."

<sup>45</sup>. COL. Constitution, 1991, art. 356. Departmental assemblies are given an unspecified role in the regulation of the education sector, in cooperation with the municipalities (art. 300.10).



teachers' payroll) rather than their demand (e.g., vouchers), and it has continued to be so even as the legal framework has experienced big changes.

Under the prevalence of the 1991 constitution, the multilevel government framework for the provision of basic education has been supplied by two main laws, Law 60 of 1993 and Law 715 of 2001. As determined by the latter, the regulatory function corresponds to the national government. Such function includes the formulation and adoption of education policies and the enactment of organizational and pedagogic guidelines. For the departments, the law foresees a technical and administrative supporting role exercised with respect to the municipalities. No substantial regulatory function is assigned to the departments. In contrast, local governments are entrusted with many managerial responsibilities as regards publicly-funded basic education, such as the hiring and promotion of teachers and the distribution of personnel and national grants between the schools of the municipal jurisdiction.

Law 60 of 1993 and Law 715 of 2001 set a procedure, known as certification (*certificación*), for handing over national competences to the subnational governments, but ultimately envisioned that the main subnational role was to belong to local governments. Law 715, in particular, concluded the certification of all departments and districts and determined that by 2002 all municipalities of more than 100,000 inhabitants should have taken over the education responsibilities. Departments were authorized to assume administrative responsibilities in those municipalities with a population of less than 100,000 inhabitants, but the legislation allowed for their eventual certification. As the certification process goes ahead in the small municipalities, the role of the departmental governments would become more and more marginal.

In sum, the main governing powers over education are split between the national government (regulation and supervision) and the local governments (management and administration), with the departmental governments given a minor coordinating and technical advising role. Nonetheless, education used to be so centralized that even the role of departmental governments most probably has grown since 1991.

### **5.1.2 Locally Run, Demand-Driven Health Care**

In the original 1991 constitution, health care was one of the social, economic and cultural rights, by default a right of non-immediate application.<sup>46</sup> The constitutional standing of health care has changed, however, as a result of the exercise of the Constitutional Court's powers of interpretation. It is now deemed a fundamental right.<sup>47</sup> Health care also has the constitutional status of a public service, and meeting unsatisfied health needs is counted as a fundamental end of the state.<sup>48</sup> Universality is made one of the guiding principles for the exercise of the governing powers of the state in the health area. "The law will determine the limits within which basic health care for everyone will be free of charge and mandatory," the constitution says.<sup>49</sup> All things considered, there is a manifest aspiration of ensuring for everyone the access to at least a minimum level of health care services. Note that such desired outcome implies the interregional equalization of health care services, in terms of the minimum level.

---

<sup>46</sup> . COL. Constitution, 1991, arts. 49 and 85.

<sup>47</sup> . COL. Constitutional Court, pronouncement T-760/08.

<sup>48</sup> . COL. Constitution, 1991, art. 366.

<sup>49</sup> . COL. Constitution, 1991, art. 49.

The role of the state in the health sector is spelled out as follows:

“It is the responsibility of the state to organize, direct, and regulate the delivery of health services [...] to the population in accordance with the principles of efficiency, universality, and cooperation, and to establish policies for the provision of health services by private entities and to exercise supervision and control over them.”<sup>50</sup>

In practice, considering the allocation of powers to legislate, it is up to the national level of government, in particular up to congress, “to organize, direct and regulate the delivery of health services.” By virtue of such power, it may “establish the jurisdiction” of the public sector, both at the national and subnational levels, as well as the private sector, and determine “the share of their responsibilities.”<sup>51</sup> Nevertheless, the constitution gives directions to the effect that “health services will be organized in a decentralized manner, by levels of responsibility and with the participation of the community.”<sup>52</sup> This is reinforced by the directions given to confer priority to health care and other specified items in the allocation of intergovernmental transfers.<sup>53</sup>

Laws 60 and 100 of 1993, which embody a large-scale reform of the health sector in Colombia, provide, together with Law 715 of 2001, the bulk of the multilevel government legal framework for health care provision under the 1991 constitution [see, for example, Gaviria et. al. (2006) and Escobar et. al. (2003) for analyses of the reform].

The following ingredients are particularly relevant from an interregional viewpoint. First, health insurance was made mandatory for all the country’s inhabitants, regardless of the place of residence. Second, two mutually exclusive routes for getting health insurance coverage were put together, the contributive regime, available for those who have the ability to pay the insurance

---

<sup>50</sup> . COL. Constitution, 1991, art. 49, original in Spanish.

<sup>51</sup> . Ibid.

<sup>52</sup> . Ibid.

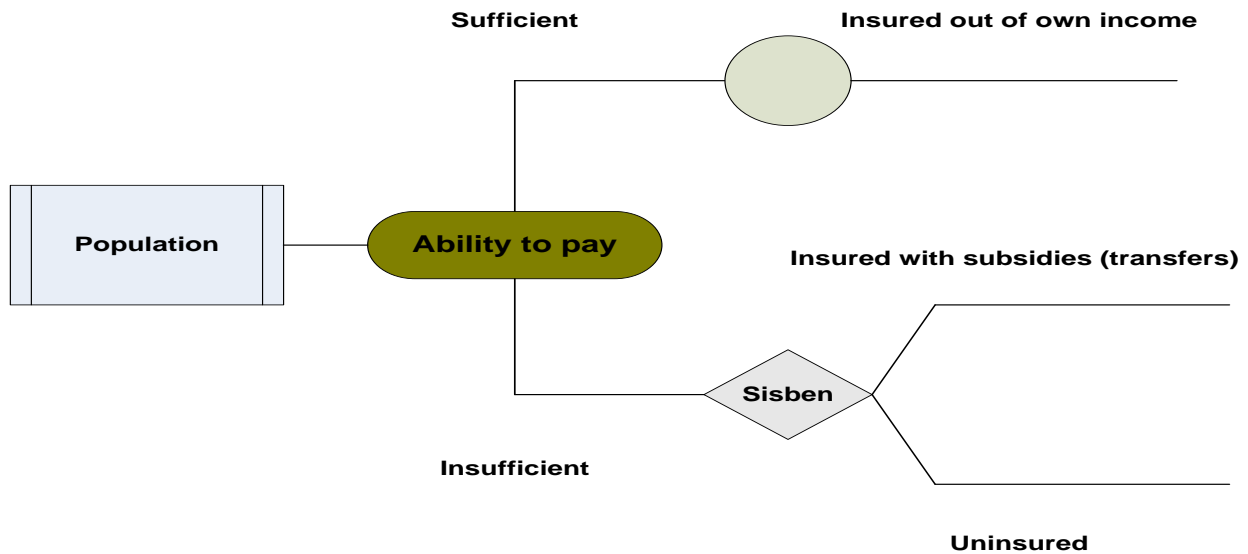
<sup>53</sup> . COL. Constitution, 1991, art. 356.

fees (*cotizaciones*), such as contract employees, public servants and pensioners, and the subsidized regime, available for those who lack the ability to pay the insurance fees, largely the poor (Figure 5.1). Affiliation to any of the two insurance regimes must be done through an insurance carrier, in general freely chosen by the insured, the *Empresas Promotoras de Salud* in the contributive regimen and the *Administradoras de Regimen Subsidiado* in the subsidized regime; the insurance carrier may be a private organization, a government agency or an organization of a mixed nature. Third, a basic benefit plan (*Plan Obligatorio de Salud*) for the insured was created, with the stated objective of making the services covered by the plan the same for the two insurance regimes. The costs of services under the basic benefit plan are officially standardized on a per capita basis.<sup>54</sup> If, as is by definition the case of the subsidized regime, the affiliate's insurance fees are lower than the standardized costs of the basic plan, the difference is largely covered by a public sector subsidy, with revenue coming from intergovernmental transfers and a fund called *Fosyga*.<sup>55</sup> Recipients of the insurance subsidy must satisfy a needs test based on income, among other selection criteria. This means-tested program is known as *Sysben*. In this regard, as Gaviria, et. al. (2006, p. 1) point out, "The reform attempted to radically change public provision of health services, by means of the transformation of subsidies to supply (direct transfers to hospitals) into a new scheme of subsidies to demand (transfers targeted at the poorest citizens)."

---

<sup>54</sup> . The basic benefit plan, and, therefore, the size of the insurance subsidies, is established by a central government-led organization, the *Consejo Nacional de Seguridad Nacional en Salud*.

<sup>55</sup> . If, as may be the case of the contributive regime, the affiliate's insurance fee payments are greater than the standardized costs of the basic plan, the difference is transferred to *Fosyga*.



**Figure 5-1: Colombia’s health insurance system**

Keeping in mind that health care providers may well be publicly or privately-owned organizations, the management and administration of the health sector is ultimately conceived of as a subnational matter, as the national government, which used to play that role, is required by Laws 60 and 100 of 1993 to hand over such responsibilities to the departments, and, for services of a certain level of complexity, the departments in turn to their respective municipalities.<sup>56</sup> Such handing over of responsibilities is commonly referred to as the health sector’s certification process. Nearly all departments and most of the larger municipalities have been certified. Local governments have the responsibility of running *Sysben*, the means-tested program for the selection of the subsidized regime’s beneficiaries. Within this general framework, the aforementioned 1993 and 2001 legislation grants regulatory powers to the national government in an assortment of issues from policy making, to technical assistance, to investment

---

<sup>56</sup>. For instance, COL. Law 60, 1993, arts. 15 and 16, and Law 100 of 1993, art. 174.

programming and project appraisal, and to supervision and control. The departments are also granted some regulatory powers with respect to their municipalities but the powers are subsidiary to those bestowed upon the national government.

A number of conditions for the Colombian health insurance system to yield universal coverage, and consequently to achieve interregional equality in terms of the basic benefit plan, can be identified. The total amount of public expenditure devoted to the subsidized regime must be large enough to subsidize the insurance fees of those who cannot fully afford health insurance. At least as important a condition is that the geographic distribution of such public expenditure must match, or be highly correlated with, the geographic distribution of the poor, broadly speaking the targeted population of insurance subsidies. Furthermore, all those in need of the insurance subsidy must actually get selected by the *Sysben* means-tested program. Finally, on the supply side, hospital and medical services should be sufficient and of an adequate quality to meet the demand in all the subnational governments jurisdictions. Finally, there should be no significant difference between the services offered by the basic benefit plan under either the contributive regime or the subsidized regime.

As we shall see, the 1991 constitution itself induced an increase in health public expenditure, large enough, it seems, for putting universal health insurance coverage within reach, at least financially. Other conditions for universal coverage (and interregional equalization) in basic health services are farther away, however. For instance, even though health insurance coverage has increased in the country as a whole, the *Sysben*'s selection rate has been shown to be rather uneven across municipalities, leading to marked inequalities in health care provision both within and, eventually, between departments (Sánchez 2006). This is likely to claim a heavier toll on the poorest regions, where there is a disproportional concentration of eligible

beneficiaries of the subsidized regime. A large slice of the health insurance revenues, in the form of both contributions and subsidies, ends up as insurance carriers' intermediation mark-up instead of doctor's and hospital's services, to the detriment of the quantity and quality of health care, a situation not necessarily spatially homogeneous (Escobar and Panapoulou 2003).<sup>57</sup> Additionally, the subsidized regime is widely acknowledged to lag behind the contributive regime in terms of the quantity and quality of services.<sup>58</sup> Although the design of the fiscal institutions create incentives that contribute to these results (e.g., a means-tested selection criteria incorporates the possibility of faulty selection), the influence of policy implementation shortcomings should not be ruled out.

### 5.1.3 Prosperity and Fiscal Capacity Disparities

In the section on fundamental principles of the 1991 constitution, the promotion of prosperity is made an essential aim of the state.<sup>59</sup> With income being one of the expressions of prosperity, this provision can be read as an income enhancing development goal. Contrasting with the cases of education and health care, however, no interpersonal or interregional equalization mandate is directly found in the constitution in terms of a minimum level of income (quite another matter is whether such kind of mandate *should* be in the constitution).<sup>60</sup> In principle, this is not

---

<sup>57</sup>. Insurance carriers face strong incentives to lobby for the official use of a high price, low service content, basic benefit plan, as well as to squeeze the fee-for-service paid to doctors and hospitals, as all of these factors enhance their profits.

<sup>58</sup>. The cost of the basic benefit plan of the subsidized regimen is about 40% that of the contributive regimen (Escobar y Panopoulou, 2003, p. 580).

<sup>59</sup>. COL. Constitution, 1991, art. 2.

<sup>60</sup>. Given the interrelations between education, health and economic growth, the promotion of prosperity is not really independent from the education and health care goals.

incongruent with the constitutionality of policies aimed at counteracting the disparities in fiscal capacity among regional governments, particularly the disparities in tax revenue potential, a restricted form of regional income-equalization, which could be grounded on the mandate for state intervention to promote the harmonic development of the regions, in conjunction with the prosperity goal, among other constitutional provisions. There are many pronouncements of the Colombian Supreme Court alluding to this issue, but a forthright, explicit treatment of it has not been produced thus far. In this sense, the issue can be said to remain constitutionally unsettled.

Another constitutional mandate is for the state to intervene in the economy with the objective of attaining full employment,<sup>61</sup> found in the section on the economic regime and public finance.<sup>62</sup> Given the link between the level of employment and the level of income, classically examined by Keynes (1936) and Okun (1962), such mandate could be connected to the prosperity goal as well. References to monetary and fiscal policy, the means of greater potential effectiveness for macroeconomic stabilization (i.e., the government function of attaining high levels of employment, along with low levels of inflation) according the conventional economic wisdom, are plenty in the 1991 constitution. Monetary policy is by constitutional mandate in the hands of an independent central bank, and that policy is designed and evaluated mainly through national aggregates.<sup>63</sup> In contrast, all the levels of government have some influence on tax revenues and public expenditure. Fiscal policy is not, therefore, an exclusively national level of government's attribution. How well, if at all, the existing fiscal division of labor between the

---

<sup>61</sup> . COL. Constitution, 1991, art. 334.

<sup>62</sup> . There is a right to work as well, listed among the fundamental rights; its judicial enforcement has a vague nature. COL. Constitution, 1991, art. 25.

<sup>63</sup> . The chapter on central banking sets "the preservation of the purchasing power of money" as primary (not exclusive) objective of monetary policy, in coordination with the overall economic policy.



national and subnational governments copes with varying levels of employment and per capita income across regions while overall macroeconomic stabilization is pursued is far from inconsequential for regional development.

## 5.2 GOVERNMENT FINANCING INSTITUTIONS

### 5.2.1 Centralization of the Power to Tax

Even though the 1991 constitution confers some power to levy taxes to departmental assemblies and local councils, the original power is primarily delegated to the national level of government, particularly to congress.<sup>64</sup> Leaving the generic limitations of power aside (e.g., separation of powers, judicial review), congress' power to tax is specifically limited by the constitution itself in a variety of ways. Thus, it not only provides principles to which the tax system ought to bond (i.e., equity, efficiency, and progressiveness) but also provides the design, or shapes the design of, some aspects of the tax system.<sup>65</sup> As a case in point, subnational tax assignment, particularly the one prevailing when the constitution came into effect, is frozen, or, at the very least, made difficult to change: "Departmental and municipal taxes enjoy constitutional protection and consequently the law may not transfer them to the [the central government], except temporarily in case of a foreign war," the constitution reads.<sup>66</sup> In a similar vein, local governments are made the only authorized governments to tax real estate, while subnational governments, both local and departmental, are granted the exclusive entitlement to royalties for the exploitation of non-

---

<sup>64</sup> . See, for instance, COL. Constitution, 1991, arts. 150, 287 and 338.

<sup>65</sup> . The adopted principles of taxation are spelled out in COL. Constitution of 1991 art. 363.

<sup>66</sup> . COL. Constitution, 1991, art. 362.

renewable natural resources in their territory.<sup>67</sup> Congress is directed to pass legislation allocating royalties between producing and non-producing subnational jurisdictions, on the one hand, and within each of these groups, on the other.

Quite the opposite, the central government is not assigned particular tax revenue sources in the constitution. In some regards, the constitution tells congress what to do and what not to do in matters of tax design. On the ‘to-do’ side, congress must directly determine the legal bearers of the tax liability, the tax base and the tax rates (at the very least, the tax rate structure), among other things.<sup>68</sup> On the ‘not to-do’ side, congress is told “not to concede exemptions or preferential treatment in relation to taxes belonging to [subnational governments],”<sup>69</sup> and is forbidden from ear-marking central government’s revenues, with the main exception of revenues allocated to intergovernmental transfers and social public expenditure.<sup>70</sup>

In matters of revenue, the relationship between the department of Cundinamarca and the city of Bogotá, the latter at the same time the capital of the department and of the country, is constitutionally regulated, with Bogotá having a share of Cundinamarca’s revenues.<sup>71</sup> This arrangement does not create legal asymmetries with other departments as it covers Cundinamarca’s jurisdiction only.

Subnational governments are given autonomy to “establish the taxes needed for fulfilling their functions,”<sup>72</sup> but such autonomy is confined to what national-level legislation chooses it to be, within the constitutional limitations to the power of congress. In practice, departments and

---

<sup>67</sup> . COL. Constitution, 1991, arts. 317 and 360.

<sup>68</sup> . COL. Constitution, 1991, art. 338.

<sup>69</sup> . COL. Constitution, 1991, art. 294.

<sup>70</sup> . COL. Constitution, 1991, art. 359. The constitution also provides principles to which the tax system ought to bond, in particular the principles of equity, efficiency, and progressiveness (art. 363).

<sup>71</sup> . COL. Constitution, 1991, art. 324.

<sup>72</sup> . COL. Constitution, 1991, art. 287.

municipalities frequently adopt the corresponding subnational taxes as sanctioned by congress, even using the same wording as national legislation. Such procedure is in many cases little more than a formality, since subnational governments are generally not allowed to opt out of national legislation. A more meaningful autonomy arises when congress authorizes the departments and municipalities to set the tax rates within a predefined tax rate structure, a practice of particular importance as regards the local level.

Assignment of tax sources between the Colombian levels of government is presented in Figure 5.2. The data refers to 2005, but the core of tax assignment has changed only marginally in the last two decades or so. Major taxes assigned by congress to the national government are the income tax, both in its corporate and personal forms, the valued-added tax (VAT), and the financial transactions tax. Departments get their tax revenues from an array of taxes which can be classified in four groups: excise taxes (beer, liquor and cigarettes), vehicle and gasoline taxes, registration tax, and other taxes (gambling taxes, slaughter tax). Notwithstanding that local governments levy several taxes, the pillars of local tax finance are the business tax and the property tax.

| Major revenue sources        | Central | Departmental | Local |
|------------------------------|---------|--------------|-------|
| 1 Income taxes               |         |              |       |
| Personal income tax \        | ✓       |              |       |
| Corporate income tax         | ✓       |              |       |
| 2 Value added tax            | ✓       |              |       |
| 3 Financial transactions tax | ✓       |              |       |
| 4 Excise taxes               |         | ✓            |       |
| Beer                         |         | ✓            |       |
| Cigarettes                   |         | ✓            |       |
| Spirits                      |         | ✓            |       |
| 5 Registration tax           |         | ✓            |       |
| 6 Vehicle tax                |         | ✓            | ✓     |
| 7 Gasoline tax               |         | ✓            | ✓     |
| 8 Gambling tax               |         | ✓            |       |
| 9 Property tax               |         |              | ✓     |
| 10 Business tax              |         |              | ✓     |

**Figure 5-2: Assignment of revenue sources in Colombia, 2005**

Source: Original data from Colombia's tax legislation.

Figure 5.3 depicts the main design features of Colombia’s national taxes, as set by law, for 2004 or the most recent year available. Personal income taxation has long had a graduated tax rate schedule, with the number of brackets and the degree of tax rate progressivity varying over time (González and Calderón n.a.).<sup>73</sup> Income tax statutes in Colombia have been shown to be fraught with exemptions and deductions, along with non-taxable income provisions, leading the taxes to perform badly on vertical and horizontal tax equity criteria (Hernández, Soto et al. 2000; Parra, León et al. 2005). Although most corporate tax exemptions and deductions are nationwide, economic activity-tailored, there are some sub-nationally circumscribed exemptions and

---

<sup>73</sup> . Personal and corporate taxes are harmonized by using the former’s top marginal rate as the latter general flat rate and by taxing profits at the corporate level only (in other words, dividends paid to shareholders are not taxed).

deductions of some importance in terms of coverage and revenue impact in recent years, benefiting, for example, the Paez zone, the tax and duty free industrial exporting zones, and the coffee growing area neighboring Armenia.

| Tax source                           | Tax base                          | Tax rate structure                 | Tax rate levels   | Notes  |
|--------------------------------------|-----------------------------------|------------------------------------|---|--|
| <b>1. Income taxes</b>               |                                   |                                    |   |  |
| Personal income tax                  | Taxable income, four tax brackets | Progressive marginal tax rates     | 0% on the first \$22,7 million of taxable income; 20% between \$22.7 and \$36.1 million of taxable income; 29% between \$36.1 and \$86.9 million of taxable income; 35% of taxable income over \$86.9 million | The individual is the tax-paying unit. Tax exemptions apply. |
| Corporate income tax                 | Taxable income                    | Flat rate<br>Temporary surcharge   | 35%<br>10% of tax liability between 2004 and 2006   | Tax exemptions apply for capital income.                     |
| <b>2. Value Added Tax (VAR)</b>      | Final consumption                 | General rate<br>Differential rates | 16%<br>20%,10%,5%,3%,2%   | Zero-rated and exempt goods and services                     |
| <b>3. Financial transactions tax</b> | Fund withdrawals                  | Flat rate                          | 4‰  |  |

**Figure 5-3: Colombia's central government taxing schemes, 2004 or most recent year available**

*Source:* Original data from Colombia's tax legislation.

The Colombian VAT is, from an aggregate perspective, a tax on final consumption (gross investment expenditure is excluded from the tax), implemented under the destination principle (i.e., imports are taxed but exports are not). Tax exemptions and differential tax rates, including zero-rating, are typically nationwide and designed on a type-of-goods-and-services criterion. The financial transaction tax has a single tax rate (i.e., 4 per mil), as a rule with no subnational exemptions or tax rating.

Figure 5.4 summarizes the taxing arrangements at the departmental level for 2004 or the most recent year available, partly resulting from the 1995 and 1998 reforms. In nearly all cases departmental tax bases come from national legislation and are uniform across departments.

Excluding the registration tax and the gasoline tax, departmental authorities have no say on tax rates, which are fixed at the national level as well. Tax rates set by national legislation for excise taxes are generally the same for all departments, the major exceptions being La Guajira and San Andrés, where tax rates are lower than elsewhere in the country in an attempt to discourage smuggling. In both the registration and the gasoline tax, the range within which departments are permitted to choose the tax rate applicable in their respective jurisdiction is quite narrow. Determination by the national level of departmental tax bases and rates entails a reduction of the departments' autonomy, but it also may be seen as a response to the need of coordination of a multilevel government tax system. Homogenous tax bases and not so dissimilar tax rates may be advantageous when the taxed goods are highly mobile between jurisdictions, as happens, for example, with cigarettes and beer.

| Major revenue sources    | Tax collection         | Tax base | Tax rate                          |
|--------------------------|------------------------|----------|-----------------------------------|
| <b>Departments</b>       |                        |          |                                   |
| 1 Excise taxes           |                        |          |                                   |
| Beer                     |                        | Central  | Central                           |
| Cigarettes               | Departments (domestic) | Central  | Central                           |
| Spirits                  | and Central (imports)  | Central  | Central                           |
| 2 Registration tax       | Departments            | Central  | Departmental within central range |
| 3 Vehicle tax            | Departments            | Central  | Central                           |
| 4 Gasoline tax           | Departments            | Central  | Departmental within central range |
| 5 Gambling taxes         | Departments            | Central  | Central                           |
| <b>Local Governments</b> |                        |          |                                   |
| 6 Property tax           | Local                  | Central  | Local within central range        |
| 7 Business tax           | Local                  | Central  | Local within central range        |

**Figure 5-4: Colombia's subnational taxing schemes, 2004 or most recent year available**

*Source:* Original data from Colombia's tax legislation.

Liquor, beer, gasoline and gambling tax revenues are partially or totally earmarked by national legislation for uses such as health care and road construction and maintenance. In the

remaining tax sources departmental authorities are free to choose between alternative revenue uses, as long as the uses fit the departments' nationally established expenditure functions. Most departmental taxes are collected by the departments themselves. Departments are endowed with major authority for controlling tax evasion in nearly all of their own taxes.

A distinctive feature of the main local taxes, the business tax and the property tax, is that the range with which local authorities are allowed by national legislation to set the tax rates is comparatively wider than in the case of departmental taxes. Moreover, their income elasticity tends to be higher than that of excise taxes, the main departmental taxes, resulting in more room of maneuver to adjust tax revenues to local public expenditure needs (see, for instance, Gutiérrez and Ospina 1996).

### **5.2.2 Intergovernmental Transfers, a Hallmark of the Constitution**

A hallmark of the 1991 constitution is the attention devoted to intergovernmental transfers. The product of the latest in a series of transfer-related constitutional amendments, the current intergovernmental transfer system, known as *Sistema General de Participaciones*, dates back to 2001.<sup>74</sup> By constitutional mandate, transfers from the national government to the subnational governments, both departmental and local, originate from a single pie, so to speak. A new pie is created every year. What the constitution does, to begin with, is to provide a rule for determining the size of the annual pie. For the year 2001, it even provides its precise measures

---

<sup>74</sup> . At the time of writing a new transfer-related constitutional amendment (Acto Legislativo No. 4 de 2007) had been passed, but the essential design features of the Sistema General de Participaciones remained untouched.



(\$10,962 trillion pesos, in the U.S. system for naming large numbers).<sup>75</sup> Taking the 2001 pie as the baseline, between 2002 and 2008, deemed a transition period, the pie size is linked to the growth rate of nominal GDP.<sup>76</sup> Next follows the uses of transfers. Education and health care should be given priority, the Constitution says, leaving to the law the determination of what “priority” means in this context. When it comes to the distribution of the pie pieces between subnational units of government, the constitution furnishes congress with joint distributive criteria for education and health, namely, the population covered and uncovered by the respective service, the proportion between urban and rural population, as well as “administrative and fiscal efficiency” and “equity”. The constitution, at least in its 2001 amendment, is silent as to whether the transfers’ recipient jurisdictions should be the departments or the municipalities, or both.

In developing such constitutional framework, Law 715 of 2001 cuts the overall transfers pie into three pieces, depending on the designated use: an education transfer, a health transfer, and a general purpose transfer, with respective shares of 58.5%, 24.5% and 17% of a slightly adjusted total (Figure 5.5). These shares are tantamount to the operating definition of priority for education and health mandated by the constitution. As determined by Law 715, the default recipient jurisdictions of the education transfer are the “certified municipalities,” that is, the municipalities that have assumed the responsibilities in the field of education, typically the larger

---

<sup>75</sup> . COL. Constitution, 1991, art. 357.

<sup>76</sup> / In subsequent years the pie size would change with a moving average of the growth rate of the national government’s current revenues. The moving average is calculated for a four year-span.

municipalities in population size.<sup>77</sup> Departments become designated recipients on behalf of the still uncertified municipalities, typically the smaller municipalities. As regards the health care transfer, the designated recipient jurisdictions are the municipalities (including the special districts) in nearly all cases.

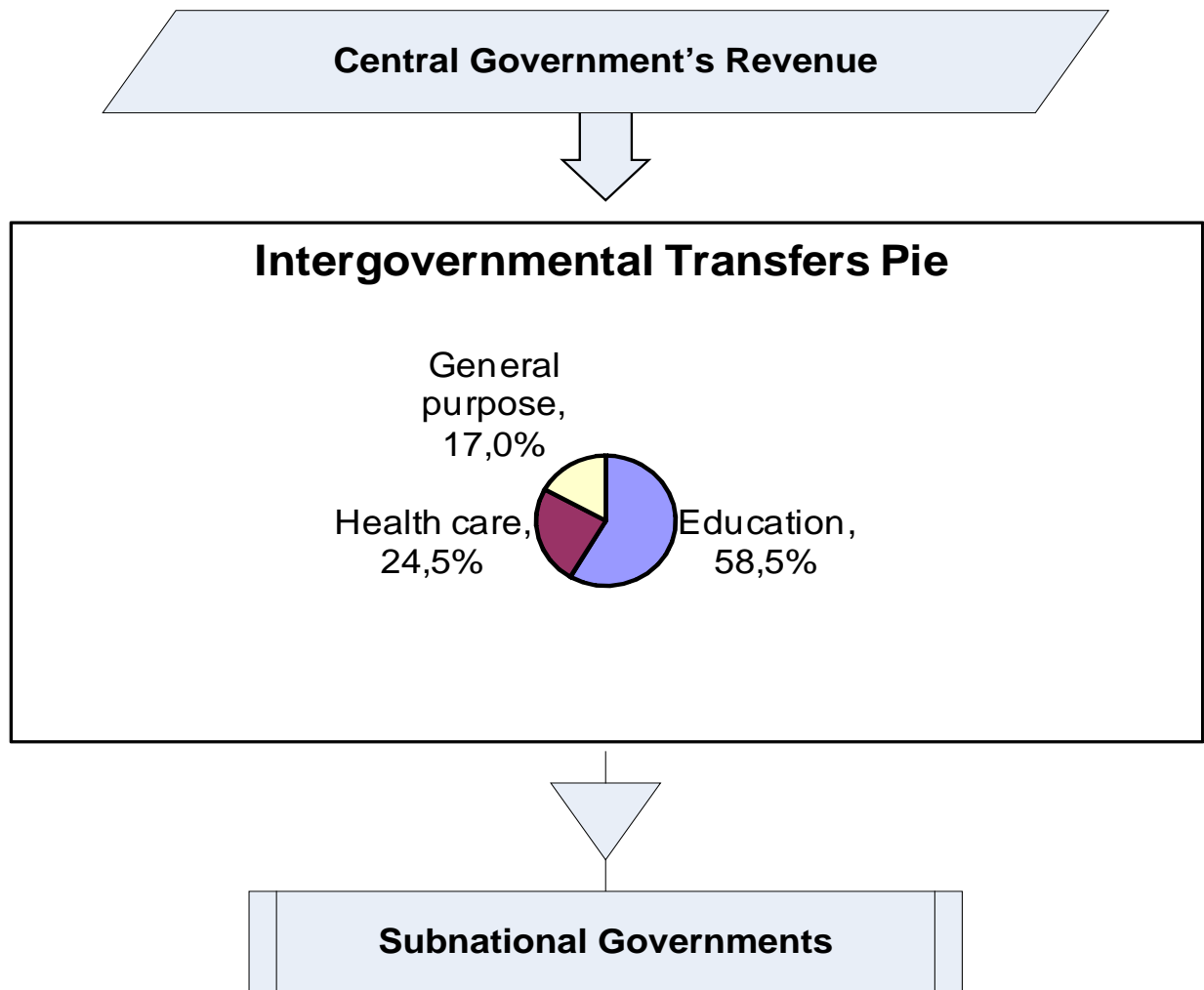


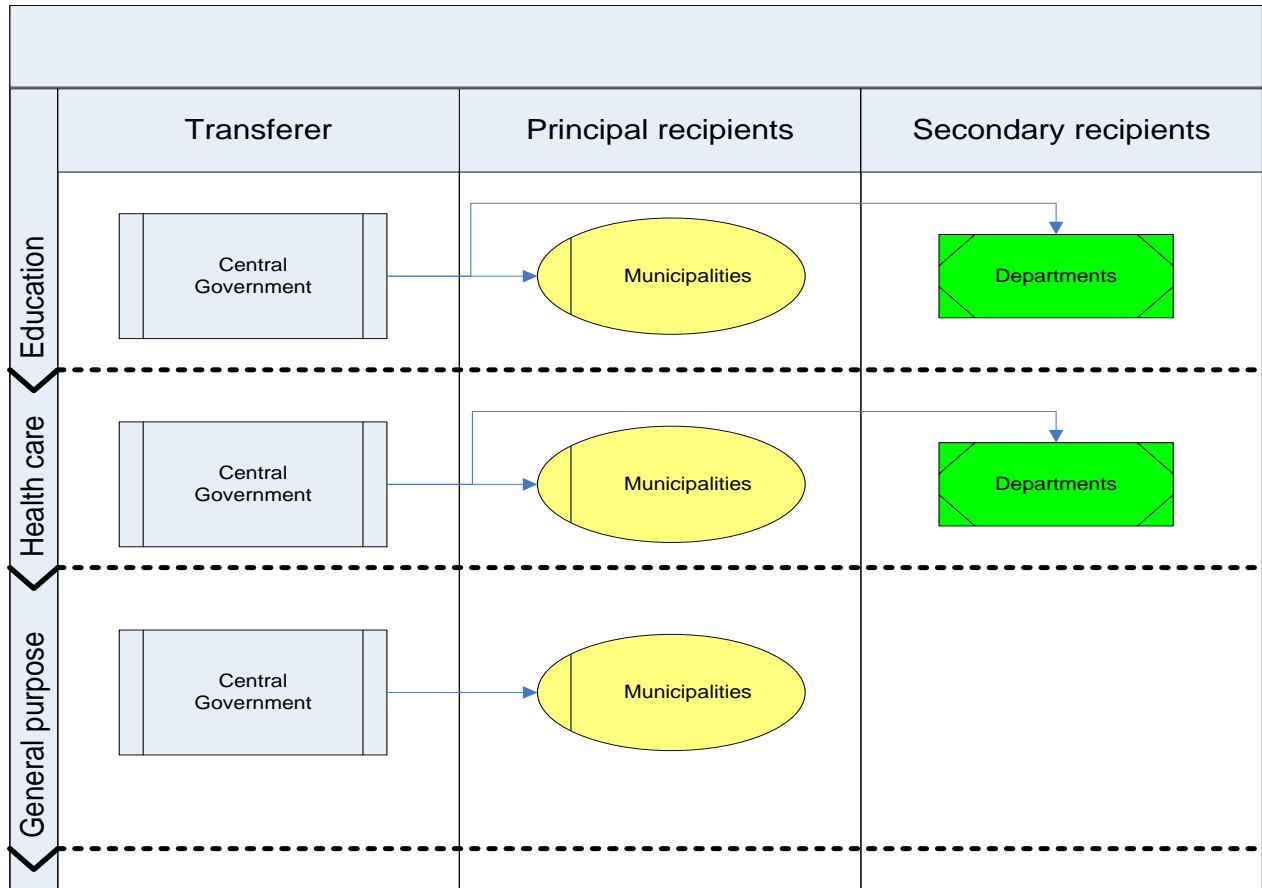
Figure 5-5: Colombia's intergovernmental transfers by purpose, Law 715 of 2001

<sup>77</sup>. According to Dirección de Desarrollo, T. (2004). Evaluación del Sistema General de Participaciones 2003. Bogotá, Departamento Nacional de Planeación., 42 municipalities out of a total of 1,098 have been certified. These municipalities account for 30% of basic education enrollment in the country as a whole.

In the case of education, the population covered by the service, defined as the number of students in the different levels of basic schooling (i.e., pre-school, school, and high school) whose enrollment has been financed out of intergovernmental transfers, is taken by Law 715 as the starting distributive criterion. The transfer for a given jurisdiction is obtained by multiplying the number of students covered at each level of schooling by a standardized allocation per student. Noticeably, the remaining distributive criteria operate at the margin, that is, over what is left once the preceding criteria has been applied to all relevant subnational jurisdictions. For example, equity, which is measured by an indicator of poverty, comes last in the distributive criteria queue.

The distributive strategy in the case of the health transfer shows striking similarities with that of the education transfer, particularly concerning the driving role of the covered population and the residual role of all other criteria. By covered population, Law 715 means the number of poor people that in the preceding year received health insurance through the subsidized regime. The health transfer corresponding to a given municipality in a given year is equal to the number of subsidized people in the jurisdiction, times the nationwide per capita allocation to the subsidized regime out of the transfer in the preceding year. If after summing up the allocation to the subsidized regime across municipalities there is something left out of the health transfer, the residual is devoted to finance the implementation of public health actions and the provision of health services to uninsured poor people, in that order. It is in these two cases that the

constitutional distributive criteria other than the covered population (e.g., uncovered population, equity) are applied.<sup>78</sup>



**Figure 5-6: Intergovernmental links by type of transfers in Colombia, 2002-2008**

78. A transition period of two years was set by Law 715 for the health transfer (art. 69). During the transition period the population to be covered in each jurisdiction is estimated by deducting the insured population under all regimes (e.g., contributive and subsidized) from total population (art. 71).

Note that the intergovernmental relationship embodied in the design of the education and health transfers is fundamentally one between the national government, as the transfer deliverer, and the larger municipalities, as the transfer recipients, with the role of the departments confined to the case of small, non-yet-certified, municipalities, as illustrated in Figure 5.6. Note also that the 1991 constitution allowed for this arrangement, but it did not directly set it forth (it was the product of ordinary legislation instead). If, and when, all municipalities come to be certified, there would be, as determined by the legislation, a relatively minor role for the departments in the education transfers and virtually no role in the health care transfers. In other words, the departments are largely sidestepped by the system of intergovernmental transfers for education and health care, insofar as the larger municipalities are concerned. Departments cannot fully be, therefore, active players in the reduction of interregional inequality by way of such transfers. To a certain extent, interregional distributive patterns of transfers should be seen then as a byproduct of the corresponding inter-municipal patterns. It is also noteworthy that, by giving strong priority to the population already covered among the distributive criteria, the two transfers in principle favor the preservation of the status quo in the interregional distribution of funding for education and health care. Of course, the population covered by department, expressed as a proportion of the corresponding total population, may vary across jurisdictions.

Lastly, given the logic with which the two intergovernmental transfers are designed, achieving interregional equality in the funding of a basic level of education and health services requires that the size of each transfer to be large enough to residually finance the provision of services to the uncovered population, at the prevailing levels of per capita allocations.

Recall that the third component of the intergovernmental transfer system is a general purpose transfer. Paradoxically enough, Law 715 partially earmarks the general purpose transfer

to some specific purposes (e.g., in the smaller municipalities, up to 28% of the transfer for operating expenditures). By directly linking the national government and the municipalities, as the transfer deliverer and the recipients, respectively, here again the departments are circumvented. (The distribution formula is described in Appendix B). Whatever the general purpose transfer does for the amelioration of interregional inequality, it is best regarded as a side effect of its primarily municipal incidence.

### **5.2.3 Public Borrowing, a Case of Rules-Based Control**

A few rules concerning public sector borrowing made their way into the 1991 constitution. Overall regulatory power over public indebtedness was bestowed upon the national level, dividing it between congress and the executive.<sup>79</sup> Subnational governments were authorized to issue bonds and debentures, both in the domestic and foreign financial markets, but subject to congressional legislation.<sup>80</sup> The amount of debt that can be issued by the central, departmental and local governments was tied to the issuer's ability to pay, while opening the way for congress to legislate the specifics of such constraint.<sup>81</sup> The main rationale of this provision was to keep overall public indebtedness, including subnational indebtedness, at a sustainable level, a condition deemed to favor the conduction of fiscal policy by the central government for macroeconomic stability objectives (Perry and Huertas 1997). The newly independent central bank was banned by the constitution from directly providing debt financing to both the central

---

<sup>79</sup>. COL. Constitution, 1991, arts. 150.19 and 189.25.

<sup>80</sup>. COL. Constitution, 1991, art. 295.

<sup>81</sup>. COL. Constitution, 1991, art. 364.

and subnational governments, except when the members of the central bank board give their unanimous approval.<sup>82</sup>

Congress has focused more on regulating subnational than national public indebtedness. Law 358 of 1997 determined that, with a handful of exceptions, departments and municipalities could borrow only for financing investment, as opposed to current expenditure, a rule known as the golden rule (Ter-Minassian and Craig 1997). A set of numeric rules whose operation mimics a traffic light regulates the maximum amount that may be borrowed. The rules are based on two or three indicators of a subnational government's fiscal standing meant to reflect its ability to pay, namely, *i*) the ratio of interest payments to operational savings, *ii*) the ratio of the debt's outstanding balance to current revenues and, in some cases, *iii*) the growth rate of such outstanding balance. When the indicators are below certain limits, the department or municipality can borrow with little higher level government intervention, meaning, metaphorically speaking, that the traffic light is green. No further borrowing is authorized when the indicators exceed certain levels, a situation amounting to a red light. In between, where the traffic light turns yellow, departments and municipalities are required to sign a fiscal performance plan before getting higher level government's authorization to run into additional debt. The fiscal performance plan is formalized in a blueprint agreed with, and supervised by, the Ministry of Finance and other national authorities. When a small municipality adopts a fiscal performance program, the departmental government is required to carry out certain supervision tasks, but in general it does not play a significant role in the negotiation and application of the program by its own municipalities.

---

<sup>82</sup>. COL. Constitution, 1991, art. 373.

In addition, a program aimed at allowing and promoting the restructuring of the subnational governments' unfulfilled obligations of different kinds was signed into law, i.e., Law 550 of 1999 (Restrepo 1999 and 2000). Tailored after a similar program for the private sector, the restructuring program gives priority to pension, wage and salary liabilities over debt liabilities.

Available evidence indicates that the number of subnational governments experiencing fiscal stress grew considerably in the second half of the 1990s, and that some of them slipped into a deep fiscal crisis as a result of the 1999 economic recession (Rodríguez 1999; Restrepo 1999 and 2000). The fiscal performance plans and the restructuring program were made available for all departments and municipalities, provided they meet the corresponding requirements. By their nature, the mechanisms of regulating subnational finances benefit some governments more than others, but, on the whole, they appear to have played a positive overall role. Part of the policy response to the growing incidence of fiscal crises was to bail-out the affected subnational governments, with the direct or indirect backing of the national government's budget (Echavarría, Rentería et al. 2002).



## **6.0 CANADA'S FISCAL CONSTITUTION**

### **6.1 DEVELOPMENT-RELATED GOVERNMENT FUNCTIONS**

#### **6.1.1 Education, Meant to be a Provincial Affair**

Although not explicitly so stated, education and health care are generally taken to be among the “opportunities” and “essential services” the Constitution Act, 1982 commits the Canadian state to reduce the regional disparities of, or to make available to everyone. But taking into account that the same Constitution Act calls for such commitment to be carried out “Without altering the legislative authority of Parliament or of the provincial legislatures, or the rights of any of them with respect to the exercise of their legislative authority,” the role of the federal government, more than the role of the provincial governments, is a matter of dispute, for reasons made clear below.

Education is one of the classes of subjects over which provincial legislatures have exclusive powers, according to the Canadian constitution.<sup>83</sup> The exercise of provincial authority over education is subjected, however, to certain constitutional limitations, related, for instance, to the rights and privileges of denominational schools and the status of English and French in

---

<sup>83</sup>. CAN. Constitution Act, 1867, sec. 93.

government affairs.<sup>84</sup> Nevertheless, using an expedient known as the federal spending power, characterized by Bird and Vaillancourt (2006, p. 193) as “the power of the federal government to pay money to people or institutions for purposes with respect to which the federal Parliament does not have the power to legislate,” the federal government has become involved in some matters of education, particularly at the post-secondary level (Smart and Bird 1996).

Arrangements for the provision of education vary across provinces. Yet, some trends have been identified as to how the provinces use their legislative authority. According to McMillan (2004, p. 5), until the late 1980s “the conventional arrangement for schooling could be described as shared local and provincial responsibility in that the province provided (usually) most of the funding (on an equalizing basis) with the local school board generating additional funds as required from a local property tax levy.” Since the early 1990s, in most provinces funding became an entirely provincial affair, abandoning the shared provincial-local funding arrangement. Provincialization of schooling funding occurred at the expense of the taxing powers of local school boards. In general, local school property taxes became provincial property taxes. McMillan (2004, p. 6) describes the resulting state of affairs as follows:

“Now, only the provincial government decides on the level of school expenditures. Within the bounds of the provincially provided funding, school boards have discretion in spending to deliver schooling subject to substantial oversight by the provincial ministries of education. Provincial oversight includes, for example, defining curriculum, requirements for common exams, teacher qualifications, requirements for the schooling of challenged students, etc.”

In Canada, provincial-local relations in the area of education resemble the hierarchical relations characteristic of unitary countries between the central and lower levels of government.

---

<sup>84</sup>. CAN. Constitution Act, 1867, sec. 93; Constitution Act, 1982, sec. 16 and sec. 23.

### 6.1.2 Health Care and the Federal Spending Power

The word ‘health’ does not appear in the text of the Canadian constitution. Yet, on the basis of the division of powers set up in sections 91 and 92 of the Constitution Act, 1867, including the residual power clause, health care is generally taken as a jurisdiction of the provinces. As Braën (2002, p. 18) writes, “from a constitutional standpoint, primary responsibility for health services and care belongs to the provinces.” A key constitutional provision in this regard grants the provinces the power to legislate over “the establishment, maintenance, and management of hospitals, asylums, charities, and eleemosynary institutions in and for the province, other than marine hospitals.”<sup>85</sup> In a study of the constitutional jurisdiction over health care in Canada, Leeson (2002, p. 4) observes that federal involvement in the area of health care has become significant, especially after World War II and relative to the situation in 1867, when many social issues, including health care and education, were considered “private, charitable or religious matters.” As in the case of education, the constitutional foundations for the role played by the federal level are controversial, however.

Federal involvement in matters of health care, an issue that seems particularly sensitive for Québec, has been justified invoking the federal spending power and, more generally, the courts’ interpretation of the constitutional text, but has also been called into question as a non-constitutionally established federal intervention in fields of provincial jurisdiction (Commission on Fiscal Imbalance 2002). Changes in the conceptions of the economic responsibilities of the different levels of government, as well as in the meaning attributed to health, appear to have

---

<sup>85</sup>. CAN. Constitution Act, 1867, sec. 92.7. Jurisdiction over quarantine stations and marine hospitals is explicitly attributed to the federal level (sec. 91.11).

notably shaped the role of the state in the health care area. Referring to the Great Depression of the 1930s, Leeson (2002, p. 4) points out in this respect:

“The lesson of the depression was that the provinces had the constitutional power with regard to matters like unemployment, pensions, and social services, but lacked the fiscal capacity to cope with the problems. By contrast, the federal government had the plenary taxing power and the fiscal capacity, but no constitutional jurisdiction in relation to these costly areas of social welfare. This led to intense pressure from Canadians for the federal government to get involved in areas of provincial responsibility.”

Underlying the allocation to the provinces of the jurisdiction over hospitals and psychiatric organizations was, according to Leeson (2002), a conception of health whose emphasis was on curative medicine. With the modern expansion of the meaning of health to include a preventive dimension, and particularly to include, as the cited author writes (*ibid*, p. 2), “such things as genetic factors, lifestyle, social and economic status, occupational and environmental conditions, and even race or gender,” judicial interpretation, on the basis of the residual power clause that governs the division of legislative powers, opened the way or endorsed the growing role of the federal level, above all in issues deemed “beyond the power of the provinces to deal with.”<sup>86</sup>

Federal legislative action to promote national standards in the provision of health care services is crystallized in the *Canada Health Act*, in effect since the mid-eighties. From an economic standpoint, its essence is the provision of financial incentives to the provinces and territories, by means of the intergovernmental transfer system (esp., Canada Health Transfer), for meeting countrywide standards. For instance, according to the *Canada Health Act*, every province is required to provide free and universal access to health insurance “on uniform terms and conditions.” Besides, the provincial health insurance plans “must be administered and

---

<sup>86</sup>. Hogg quoted by Leeson (2002, p. 6).

operated on a non-profit basis by a public authority...” Insured health care is meant to comprise all medically necessary services, a sort of basic basket of services. As reported by Ramsay (2002, p. iv), the concept of medical necessity “has not been officially determined,” at least nationally, so that “...the extent of public insurance varies from province to province.” Hospital and physicians services judged by each province “medically necessary” are, however, typically covered by the provincial insurance plan.

But how is the insured health care financed and delivered? While practically all possible combinations of public/private financing and public/private delivery of services are found in the provinces, “In Canada,” according to Deber (2002 p. v), “most health care delivery is already private. Although about 70% of Canadian health care is financed publicly, almost all of this care is already delivered by private [usually not-for-profit] providers.” Public financing and private delivery can be taken then as the predominant combination in the North American country. The fact that public financing occurs in a multilevel government setting and that most private delivery is not-for-profit should not be overlooked, though.

### **6.1.3 A Form of Fiscal Equalization**

The Constitution Act, 1982 commits the Canadian federal government and parliament to “the principle of making equalization payments to ensure that provincial governments have sufficient revenues to provide reasonable comparable levels of public services at reasonable comparable levels of taxation.”<sup>87</sup> Equalization payments had been made at least since 1957, but this

---

<sup>87</sup>. CAN Constitution Act, 1982, sec. 36(2).

provision strengthened the legal grounds for the fiscal equalization program that is now a distinguishing trait of Canadian federalism (Clark 1997).

The equalization program in place in Canada is a form of revenue equalization across provincial governments. It does not attempt to equalize the actual regional provision of public services. Neither does it attempt to directly reduce regional income disparities, as Clark (1997, p. 86) rightly notes. What it seeks is to reduce the disparities in the income of regional governments (especially tax income) or, from another perspective, in the provinces' potential to finance the provision of "comparable levels of public services." An essential requirement of this restricted form of regional income equalization is for the provinces to make a comparable level of tax effort (aka level of taxation). The specifics for the equalization program are explained in section 6.2.2.

## **6.2 GOVERNMENT FINANCING INSTITUTIONS**

### **6.2.1 An Ample Multilevel Power to Tax**

Under the constitution, Canada's federal level enjoys an ample power to tax. The legislative authority of the federal parliament covers, in effect, "the raising of money by any mode or system of taxation."<sup>88</sup> Both direct and indirect taxes may thus be imposed federally. For their part, the provincial legislatures may exclusively make laws concerning only "direct taxation

---

<sup>88</sup> . CAN. Constitution Act, 1867, sec. 91.3.

within the province in order to the raising of a revenue for provincial purposes.”<sup>89</sup> According to Thirsk (1983), the direct taxation restriction was enacted with the initial objective of preventing the provinces from using indirect taxation to create inter-provincial trade barriers. The history of tax assignment in Canada has been marked by this provision.

Given its bearing on the scope of the provincial powers of taxation, the meaning of direct taxation has historically been a contested issue, requiring the recurring exercise of the Supreme Court’s powers of official constitutional interpretation. The Supreme Court’s rulings have been such that, according to Bird and Vaillancourt (2006), “Provinces in Canada are constitutionally able to tax anything they want to tax (except international and inter-provincial trade)...” Even if formally limited, provincial powers of taxation are ample as well. To this it should be added that the provinces are constitutionally authorized to impose taxes, within their respective jurisdictions, on natural resources “by any mode or system of taxation”.<sup>90</sup>

A striking feature of Canada’s tax system is that all major tax sources are shared between the federal and provincial levels of government. Figure 6.1 depicts the assignment of taxes. Major revenue sources common to both levels of government are the personal income tax, the corporate income tax, certain sales taxes, the payroll tax, and a number of excise taxes and duties (for a snapshot of the evolution of tax sharing in the personal income tax, see Box 6.1). While the use of the independent taxing powers of the two levels of government enabled the development of this tax arrangement, it also had the potential of leading to a ‘tax jungle’. Tax harmonization and tax-collection agreements between the federal government and most

---

<sup>89</sup>. CAN. Constitution Act, 1867, sec. 92.2.

<sup>90</sup>. CAN. Constitution Act, 1867, sec. 92A(4).

provinces, signed in the post World War II era, have sought to avoid such an outcome, which was actually observed in the interwar years (Lazar 2000). Within most provinces tax assignment is characterized by the allocation to municipalities of a separate tax revenue source, namely, the property tax (Bird and Tassonyi 2003).

| Major Revenue Sources                                 | Federal | Provincial |
|---|---------|------------|
| <b><i>Federal and provincial revenue sources</i></b>  |         |            |
| 1. Income taxes                                       | ✓       | ✓          |
| Personal income taxes                                 | ✓       | ✓          |
| Corporate income taxes                                | ✓       | ✓          |
| 2. Sales taxes  | ✓       | ✓          |
| 3. Payroll taxes                                      | ✓       | ✓          |
| 4. Excise taxes                                       | ✓       | ✓          |
| <b><i>Exclusive federal revenue sources</i></b>       |         |            |
| 1. Customs import duties                              | ✓       |            |
| 2. Taxes on non-residents                             | ✓       |            |
| <b><i>Exclusive provincial revenue sources</i></b>    |         |            |
| 1. Resource royalties within provincial jurisdiction  |         | ✓          |
| 2. Property taxes (mostly assigned to municipalities) |         | ✓          |

**Figure 6-1: Assignment of revenue sources in Canada, 2004 or most recent year available**

Sources: Original data from Department of Finance Canada, [www.fin.gc.ca](http://www.fin.gc.ca).



## Box 6.1 Personal Income Tax Sharing in Canada

Joint federal and provincial occupancy of the personal income (PI) tax field began in 1917. It was interrupted in the early 1940s, when the provinces agreed to vacate the income tax field, both personal and corporate, in favor of the federal government in order to enable it to finance the Second World War effort; the provinces received in returned financial compensation, as established in a series of *Rental Tax Agreements*. In 1954 Quebec implemented its own PI tax. In the early sixties, with the introduction of the *Tax Collection Agreements*, the sharing of the income tax field between the two levels of government became the rule again. For details, see Sheikh and Carreau (2002), on which this description is based.

Basic characteristics of the taxing schemes employed at the federal level are depicted in Figure 6.2, and those of the provincial level in Figure 6.3, for the fiscal year 2005. The federal personal income (PI) tax is designed following a progressive pattern.<sup>91</sup> Kesselman and Cheung (2004) and Martineau (2005) discuss the nominal and actual progressivity of the federal PI tax. This taxing scheme, particularly due to the graduated tax rate schedule, is in principle expected to generate an automatic compensatory effect of provincial business cycles. Because the economic incidence of a tax may differ from its legal incidence, the actual compensatory effect can, however, be smaller than the one implied by the nominal tax rates.

---

<sup>91</sup> . Non-refundable tax credits are used, according to Treff and Perry (2004), for exempting from the tax what can be described as basic living income.

| Federal tax source                         | Tax base                          | Tax rate structure  | Tax rate levels  | Observations  |
|--|-----------------------------------|---|--|---|
| <b>1. Income taxes</b>                     |                                   |   |  |   |
| Personal income tax                        | Taxable income, four tax brackets | Progressive marginal tax rates                                    | 16% on the first CA \$35,000 of taxable income; 22% on the next CA \$35,000 of taxable income; 26% on the next CA \$43,804 of taxable income; 29% of taxable income over CA\$113,804 | The individual is the tax-paying unit<br><br>The combined federal and provincial marginal tax rates are 24.32; 33.44; 39.52; and 44.08, respectively. (?) |
| Corporate income tax                       | Taxable income                    | Flat rates by business type                                       | General: 28%<br>Manufacturing: 21%<br>Small business: 12% up to an income threshold  | Corporate rates after federal abatement<br>General rate before abatement: 38%   |
| <b>2. Goods and service tax</b>            | Final consumption                 | Flat general rate   | 7%   | A type of value-added tax; zero-rated and exempt goods and services   |
| <b>3. Selected excise duties and taxes</b> |                                   |   |  |   |
| Distilled spirits duty                     | Quantity of product               | Fixed amount per unit   | CA\$11.066/liter of alcohol  |   |
| Beer duty                                  | Quantity of product               | Fixed amount per unit, according to percentage of alcohol content | Up to 1.2% alcohol, CA\$2.591/hectoliter<br>1.2% to 2.5% alcohol, CA\$13.990/hectoliter<br>Over 2.5% alcohol, CA\$27.985/hectoliter  |   |
| Cigarettes duty                            | Quantity of product               | Fixed amount per unit   | CA€39.6255/5 cig.  |   |

**Figure 6-2: Canada's federal taxing schemes, 2004 or most recent year available**

Source: Original data from Canada Revenue Agency, [www.cra-arc.gc.ca](http://www.cra-arc.gc.ca), for the personal income tax; Canadian Tax Foundation, *Finances of the Nation 2004* for the remaining taxes.

| Major Tax Sources                              | Taxing arrangements |                    |              |                                  |
|--|---------------------|--------------------|--------------|----------------------------------|
|  | Number of Provinces | Tax administration | Tax base     | Tax rate                         |
| <b>1. Income tax</b>                           |                     |                    |              |                                  |
| Personal income tax                            |                     |                    |              |                                  |
| Most provinces                                 | 9                   | Federal            | Federal base | Own rate on federal base         |
| Other provinces (Quebec)                       | 1                   | Provincial         | Own base     | Own rate on federal base         |
| Corporate income tax                           |                     |                    |              |                                  |
| Most provinces                                 | 7                   | Federal            | Federal base | Own rate on federal base         |
| Other provinces (Alberta, Ontario, and Quebec) | 3                   | Provincial         | Own base     | Own provincial rate              |
| <b>2. Sales tax</b>                            |                     |                    |              |                                  |
| Most provinces                                 | 5                   | Provincial         | Own base     | Own provincial rate              |
| Other provinces                                | 3                   | Federal            | Federal base | Uniform rate for the 3 provinces |
| <b>3. Excise taxes and duties</b>              |                     |                    |              |                                  |
| Cigarette taxes                                |                     |                    |              |                                  |
| All provinces                                  | 10                  | ...                | Own base     | Own provincial rate              |
| Gasoline Taxes                                 |                     |                    |              |                                  |
| All provinces                                  | 10                  | ...                | Own base     | Own provincial rate              |
| <b>4. Payroll tax</b>                          |                     |                    |              |                                  |
| Most provinces                                 | 10                  | Provincial         | Own base     | Own provincial rate              |

**Figure 6-3: Canada's provincial taxing schemes by tax source, 2004 or most recent year available**

Source: Karin Treff and David B. Perry, *Finances of the Nation 2004*, Canadian Tax Foundation.

Note: The sale tax here covers the General Sales Tax and the Harmonized Federal-Provincial sales tax. Sales taxes are not levied in some provinces (e.g., Alberta).

The federal personal income (PI) tax is nominally blind from a spatial perspective, in that it applies to all taxpayers in all jurisdictions, with some exceptions. One major exception relevant for fiscal intergovernmental relations is that taxpayers in Quebec are allowed to reduce 16.5 percentage points of federal PI tax, an arrangement known as the Quebec abatement.<sup>92</sup> Accordingly, the federal PI tax is lower in Quebec than elsewhere in the country, other things being equal. The PI tax room thus freed by the federal government is occupied by Quebec by a higher provincial PI tax. On the word of Perry (2001), “Quebec residents receive an abatement of federal personal income tax because Quebec opted out of a number of joint programs in the 1960s and accepted income tax room instead of cash payments from Ottawa. Thus Quebec’s provincial tax burden is higher, but the federal burden is lower.” From the perspective of the federal government, the Quebec abatement is intended to be fiscally neutral, as the lower collection of federal PI tax in Quebec’s jurisdiction is offset by lower transfers to the province.

At least since the early 1970s an essential element of the provincial PI taxing scheme has been the provinces’ and territories’ autonomy to choose their respective tax rates. “As of the 2004 taxation year,” (Treff and Perry 2004 p. 3:9) point out, “all the provinces and territories calculate provincial or territorial tax as a percentage of federally defined taxable income...” This holds true for 2005 as well. In other words, the provincial PI tax operates as a tax on federally defined taxable income (i.e., tax on income), instead of a surcharge on the federal tax liability (i.e., a tax on tax), as was previously the case. PI tax rate schedules of three or four income brackets are used by most the provinces and territories (Treff and Perry 2004).

---

<sup>92</sup>. Under another major exception, most residents of the Canadian territories and the residents of some prescribed zones in the provinces are entitled to “[a] location-based deduction [which] is allowed to offset the cost of living in northern Canada,” Treff and Perry Treff, K. and D. B. Perry (2004). *Finances of the Nation 2004*. Toronto, Canadian Tax Foundation.

The provincial PI taxing schemes allow for either a centralized or a decentralized tax administration. In fact, nine provinces have opted for delegating the tax collection function, as regards the personal income tax, to the federal tax agency (Treff and Perry 2004). The delegation takes the form of a tax collection agreement between the federal government and the provinces. For the federal government to enter into such an agreement, the provinces must, as stated by Broadway and Kitchen (1999 p. 139), “accept the federal tax base and rate structure.” Quebec is the only province with a decentralized PI tax administration in place.

Similarly to the PI tax, the corporate income tax works as a tax room jointly occupied by the federal and provincial governments. The definition of taxable income, the tax base, is essentially the same at the two levels. At the federal level, the tax rate structure is set in such a way as to leave some tax room for the provinces, taking into account the desired overall tax burden of the country (Boadway and Kitchen 1999). As of 2004, the federal tax structure consisted of a small group of flat rates by business type. In general, the rate structure itself looks nominally neutral across jurisdictions.

Imposed by every province and territory, the subnational corporate income tax raises important questions of horizontal coordination. Given the difficulty of determining the geographical origin of income, a formula for allocating taxable income among provinces has been adopted. As described by Broadway and Kitchen (1999, p. 179), “[T]he proportion of taxable income that the formula allocates to a province is an average of the proportion of the firm’s sales in the province and the proportion’s of the firm’ payroll in the province.” The federal tax administration agency collects the tax on behalf of the majority of provinces by virtue of tax collection agreements, with the minority (e.g., Ontario and Quebec) collecting the tax on its own (Treff and Perry 2004).

Sales are taxed at both the federal and provincial levels of government. The federal sales tax, known as the Goods and Service Tax (GST), is a variant of the value-added tax (VAT), particularly a consumption type-VAT operating under the destination principle. In Quebec the federal GST is collected by the province. In the rest of Canada the federal tax agency is in charge of administering the GST. With the exception of Alberta, all provinces impose a sales tax of their own. None of the territories have such a tax.

Bird and Gendron (2001, p. 9) summarize the sales taxes landscape as follows: “Canada (...) offers a variety of interesting situations: separate federal and provincial VATs administered provincially, joint federal and provincial VATs administered federally, and separate federal VAT and provincial RTSs administered separately.” Although this variety of sales tax arrangements induces tax arbitrage and raises the administrative and compliance costs of inter-provincial trade, as noted by Bird and Gendron, the Canadian case can be taken as a testimony of the plausibility of subnational sales taxation.

Concerning property taxes, Treff and Perry (2004, p. 6:2) tell us that “Real property taxes and other property-based taxes are imposed by both provincial and local governments. They represent only a small part of provincial revenue but are the single most important source of municipal revenue.” Lastly, a variety of excise taxes and duties (e.g., alcohol, gasoline and tobacco) products are imposed by both the federal and provincial levels of government in Canada.

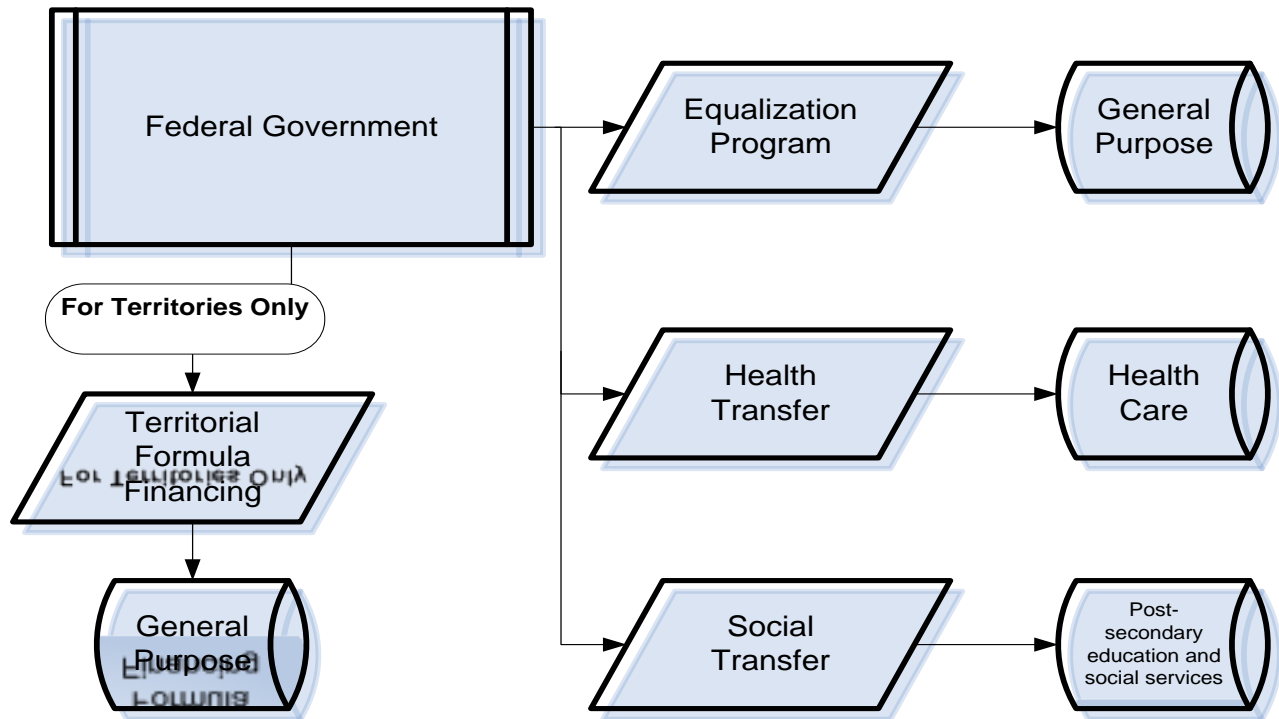
## 6.2.2 A Cohesive Role for Intergovernmental Transfers

Currently, Canada's transfer system consists of four main components: the fiscal equalization program, the Canada Health Transfer (CHT), the Canada Social Transfer (CST) and the territorial formula financing (TFF), as shown in Figure 6.4. The fiscal equalization program, which has been described as "an important element of national cohesion" and even as "the glue that holds [the] federal state together"<sup>93</sup>, is embedded in the constitution, specifically in the equalization payments commitment. The constitutional standing of the health and social transfers is controversial. No explicit reference to such transfers is found in the constitution. While the CHT and the CST could find ground in the commitment to reduce economic development disparities and to provide essential services to everyone, they are commonly regarded as resulting from the exercise of the commonly called federal spending power.<sup>94</sup> Transfers to the territories, being federal creatures, may be made under the umbrella of federal legislation.

---

<sup>93</sup>. See MacNevin (2004, p. xv).

<sup>94</sup>. By virtue of the federal spending power, Leeson (2002, p. iv) argues, "the federal government can make transfer payments to provinces for health care purposes and attach conditions to those transfers, even if they appear to invade provincial jurisdiction." Others question the constitutional grounds of the federal government to ear-mark intergovernmental transfers and even to make such payments altogether.



**Figure 6-4: Transfers to the intermediate level of government in Canada, 2005**

Although the historical origins of the modern equalization program can be traced to 1867, it formally began in 1957 and became constitutionally protected in 1982 (Russell 2004; Stevenson 2004). Equalization payments to the beneficiary provinces are determined by a formula set in the Federal-Provincial Fiscal Arrangements Act. The essential logic of the formula is as follows: The standardized tax revenue of a selected group of provinces operates as the yardstick against which the standardized tax revenue of a given province is compared, both calculated on a per capita basis. A province receives equalization payments if its standardized tax revenue is lower than the standardized tax revenue yardstick, again in per capita terms. No transfer is made otherwise, so that negative transfers are ruled out. The amount of the equalization transfer to a province is in principle obtained by multiplying its gap in standardized

per capita tax revenue by its population. For a detailed account of the characteristics of the Canadian equalization system, see MacNevin (2004). What the formula seeks is to ensure that every province gets at least a minimum level of revenue (per capita), where the minimum corresponds to the selected-group-of-provinces yardstick. By doing so, it in some degree offsets the disparities in provincial fiscal capacity and equalizes the *potential* to provide a minimum standard of public goods and services across provinces. Following Bird and Villancourt (2006), the equalization entitlement of province  $p$  can be expressed in this form:

$$\text{Equalization entitlement of province } p (>0) = \left[ \begin{array}{cc} \text{Standardized} & \text{Standardized} \\ \text{per capita} & \text{per capita} \\ \text{tax revenue} & \text{tax revenue} \\ \text{yardstick} & \text{province } p \end{array} \right] \times \text{Population province } p$$

Because of the use of a common basket of provincial revenue sources, this method of estimating fiscal capacity is known as the *Representative Revenue System Approach*. The degree of tax equalization provided by the formula is calibrated for similar levels of taxation or tax effort across provinces by using a single tax rate for each revenue source. The equalization formula has been the subject of periodic revisions, so that its specifics have varied over time. The provinces serving as yardstick and the tax sources used for the calculation of the standardized per capita tax revenue are a case in point. For the period beginning in April, 1999 and ending in March, 2004, five provinces entered in the yardstick, namely, British Columbia, Manitoba, Ontario, Quebec and Saskatchewan, considered to be “middle” provinces, while some 33 tax sources were employed in determining the standardized tax revenue.

A ceiling and a floor to the total amount of equalization payments were introduced in 1982. Payments to the provinces were adjusted downward when the aggregate equalization



entitlements obtained by applying the formula surpassed the ceiling, set, at a time, as a percentage of GNP. MacNevin (2004, p. 195) reports, however, that “the federal government (...) eliminated the ceiling permanently beginning in 2002-03.” A floor provision has also been in place to make sure that equalization payments do not fall below a certain level.

The equalization scheme has a number of key features. First, neither provincial expenditure needs nor the cost of providing government services enter into the formula; the degree of equalization provided applies to tax capacities only. In other words, the scheme focuses on the revenue side rather than on the expenditure side of the provincial budgets. Second, equalization transfers are general-purpose transfers, so that they are given the use autonomously determined by the provinces. As a result of these two features, the scheme contains no guarantee that the level of public services actually provided by the provinces would be equalized. By virtue of the scheme the provinces have a floor-level of financial resources but what they do with them is quite another matter (hence the *potential* to provide a similar level of basic services). Third, equalization payments are financed out of the federal purse. Provinces above the five-equalization yardstick are neither entitled to equalization transfers nor are they required to make direct contributions to cover the equalization payments. The transfers are vertical (federal-provincial) rather than horizontal (province to province). Note, however, that federal taxpayers are, generally speaking, provincial taxpayers as well, so that the taxpayer is in the final analysis the pillar of the scheme.

The equalization scheme in Canada is, or can be seen as, split into two branches, differentiated by the type of subnational units of government involved. The first is the Equalization Program, which is federal-provincial in coverage. The second is the Territorial Formula Financing (TFF), whose scope is federal-territorial, as its name suggests. In setting up

these two equalization branches, a key factor was the wide divide between the provinces and the territories as regards the natural and socio-economic environment (e.g. the implications of extreme climate for human settlements). And the level of economic activity in the territories is much lower than in the rest of Canada. As a result, Rayner and McLarnon (2001 , p. 1) note,

“The North has unique needs that must be reflected in federal transfers to the territories. Territorial infrastructure and socio-economic needs cost significantly more than elsewhere in Canada. Canada’s territories face several distinct challenges in this respect, the fundamental challenge being their limited capacity for generating revenues. This limited capacity is primarily due to their limited degree of economic activity and small tax base, a product of their small population and low tax rate.”

Both expenditure needs and revenue-raising capacity are incorporated into the Territorial Formula Financing (Slack 2005), unlike the Equalization Program, which focuses merely on the revenue dimension. This is a fundamental difference between the two equalization branches. Expenditure needs enter into the allocation formula in a very rough way, though. TFF is regulated by agreements between the federal government and the territories. The agreements are periodically renewed. Similar to the provincial equalization transfer, the TFF is an unconditional block transfer.

The Canada Health Transfer (CHT) and the Canada Social Transfer (CST) began operating in 2004 in replacement of the former Canada Health and Social Transfer (CHST), which in turn resulted from the consolidation, in 1996, of a group of federal conditional transfer programs.<sup>95</sup>

In understanding the working of the current transfers, it may be helpful to see how the CHST operated. For a detailed description, see Smart and Bird (1996) and MacNevin (2004). By means of the CHST the federal government provided funding to the provinces in support of

---

<sup>95</sup>. Department of Finance website, [www.fin.gc.ca](http://www.fin.gc.ca), viewed on July 7, 2006.

health care and post-secondary education, as well as social assistance and services, including early childhood development. Allocation of the CHST among the provinces was made on a per capita basis, with the amount transferred determined by the federal government. The CHST took the form of a block grant, that is, a grant which must be spent in the predetermined areas of social expenditure, while giving the recipients (e.g., provinces) the freedom to choose how to spend within such broad areas. According to Smart and Bird (1996, p. 2), “Payments to provinces under CHST [were] a combination of direct cash transfers and ‘tax point transfers,’ through which the federal government (...) agreed to reduce its levies on personal and corporate income, leaving additional tax ‘room’ to be occupied by the provincial governments if they so choose.” In terms of design, the most significant change introduced in the 2004 CHST restructuring was the separation of the health care component of the CHST from the other components. The health care component became the Canada Health Transfer (CHT), whereas the post-secondary education, social assistance and social services component turned into the Canada Social Transfer (CST). Other features remained unchanged: Both are federal block transfers to the provinces and territories, both are allocated on a per capita basis (equal for every province), and both consist of a cash transfer and a tax transfer.

### **6.2.3 Federal and Provincial Borrowing as Self-Regulation**

The Canadian constitution gives each province exclusive legislative powers over the “borrowing of money on the sole credit of the province.”<sup>96</sup> Meanwhile, exclusive legislative authority over

---

<sup>96</sup>. CAN. Constitution Act, 1867, sec. 92(3).

public debt at the federal level is attributed to the Parliament of Canada.<sup>97</sup> The powers of the two levels of government to regulate borrowing thus run in parallel. In this constitutional setting, the federal level has no prerogative to impose rules aimed at controlling provincial borrowing. Provincial access to credit markets, either domestic or foreign, is (and appears to have been) centrally unrestricted.<sup>98</sup>

Bird and Tassonyi (2003) offer an interesting analysis of the regulatory conditions of sub-central public indebtedness in Canada, which runs along the following lines. As the Canadian provinces do not have constitutions, there are no restrictions on the legislative powers of provincial parliaments other than those set by the federal constitution. Provinces may use their legislative authority over their own borrowing in two main ways. On the one hand, they may opt for setting out rules to control it. (Beginning in 1993 with Alberta, a trend toward the self-imposition by the provinces and territories of balanced budget and/or debt-reduction rules became apparent, Millar (1997) shows. By 1997 six out of the ten provinces, together with the two territories, had enacted such type of legislation). A provincial parliament may use, however, its exclusive legislative authority to modify any self-imposed budget and borrowing rules in any legislature. The self-imposed constraints are in this sense soft. On the other hand, the provinces may opt for leaving their own access to borrowing unrestricted.

Unlike the provincial case, municipal borrowing tends to be heavily controlled by the provincial level.

---

<sup>97</sup>. CAN. Constitution Act, 1867, sec. 91(1A).

<sup>98</sup>. According to Bird and Tassonyi (2003, p 92), “Provinces may borrow money for any purpose, whenever, wherever, and however they wish. There are no federal controls at all over provincial borrowing...”

Notwithstanding the different legal approaches to borrowing found in the federal-provincial and provincial-municipal settings, the result in both cases would have been one of fiscal discipline, Bird and Toyanssi go on to point out. This outcome is attributed to the workings of a deeply rooted culture of fiscal prudence, coupled with the discipline imposed by the market. In the words of Bird and Tassonyi (2003, p. 112), “it may be that if Canada has any lesson in this respect it is that what matters most may be not the method by which ‘hardness’ is sought but the setting (or, if one will, ‘culture’) within which it is sought.” And there would be still another manifestation of such culture: In Canada a rule has it that provinces in fiscal crises are not rescued by the federal government. This rule would not take the form of a legal mandate but of a social and political convention. Subnational debt default appears to have been a rare episode, as would have been the practice of subnational bail-outs by the federal government. It is an open question whether the acceptance of the no federal bailing-out informal rule operates as an incentive for designing better multilevel fiscal institutions.

## 7.0 SPAIN'S FISCAL CONSTITUTION

### 7.1 DEVELOPMENT-RELATED GOVERNMENT FUNCTIONS

#### 7.1.1 Education: Equalization of a Fundamental Right

The 1978 Spanish constitution gives education the status of a fundamental right for everyone,<sup>99</sup> standing in the same category as, say, the right to life and the right to freedom. “Elementary education is compulsory and free,” the constitutional charter reads.<sup>100</sup> As a fundamental right, the right to education is binding on all public authorities; any citizen may ask for the protection of such right “by means of a preferential and summary procedure before the ordinary courts and, when appropriate, by lodging an individual appeal for protection (*recurso de amparo*) to the Constitutional Court.”<sup>101</sup> The Constitutional Court is entitled to hear appeals against the constitutionality of laws and other legal acts which allegedly fail to recognize the condition of fundamental right granted to education.<sup>102</sup> Education is not mentioned among the rights that

---

<sup>99</sup> SPA. Constitution, 1978, art. 27.1.

<sup>100</sup> SPA. Constitution, 1978, art. 27.4.

<sup>101</sup> SPA. Constitution, 1978, art. 53.

<sup>102</sup> SPA. Constitution, 1978, art. 161.

“may be suspended when a state of emergency or siege (martial law) is declared under the terms provided in the Constitution.”<sup>103</sup>

Within the list of functions over which the central level of government is assigned exclusive competence by the constitution, education is not enumerated. Neither is it enumerated among the “matters” over which the autonomous communities “may assume competences.”<sup>104</sup> Yet, given the constitution’s residual powers clause, education in a particular autonomous community may remain within the central government’s scope of competences or, if the corresponding statute of autonomy so establishes, it may become a function of the autonomous community. Therefore, the level of government responsible for educational affairs may, in principle, vary across autonomous communities. It should be kept in mind, however, that the central level of government is authorized to regulate the “basic conditions guaranteeing the equality of all Spaniards in the exercise of their rights,” and that education is one of those rights.<sup>105</sup> Indeed, as maintained by Monasterio (2002 p. 16), the scheme for the provision of education services, let alone health services, is one of “shared competences, in the sense that the central government defines the access conditions and the catalog of services offered, as well as the standard level of provision, while the autonomous communities are in charge of managing the services and delivering them to the final users.”

According to the constitution, “An allocation may be made in the [central government’s] budget to the [autonomous communities]... to guarantee a minimum level of basic public

---

<sup>103</sup> . See SPA. Constitution, 1978, art. 55.

<sup>104</sup> . SPA. Constitution, 1978, art. 148.

<sup>105</sup> . SPA. Constitution, 1978, art. 149.1.

services throughout the Spanish territory.”<sup>106</sup> Down in the legal scale, in the Organic Law of the Autonomous Communities Financing Framework, enacted in 1980 and known as LOFCA, education and health care are identified as the basic public services whose minimum level should be guaranteed.<sup>107</sup> This amounts, it has been rightly claimed, to a mandate to reduce interregional inequalities in the provision of basic education (de la Fuente 2005). In 1990, compulsory schooling was set at 10 years. An autonomous community is considered, by virtue of the aforementioned organic law, to be below the target when the provision of education, defined in terms of the minimum level, falls below the country average by a given percentage. Once certain administrative requirements have been fulfilled, the central government is directed to provide complementary financial assistance to the lagging autonomous communities.

In a process initiated in 1980 with the Basque Country and, in a way, practically completed in 1999 with Madrid, the central government transferred an array of competences and functions in education over to the autonomous communities (Ministerio de Economía y Hacienda de España 2006a; 2006b). Nowadays the management and provision of education services to the final users in Spain’s territory is fundamentally a sub-central affair. Nonetheless, the prevailing assignment of functions between levels of government should not be seen as permanently frozen.

Although currently the autonomous communities of both the common and the special regimes are the official holders of the governing competences for the provision of education in their respective jurisdictions,<sup>108</sup> a peculiarity of the Basque Country and Navarre (i.e, the special regime) is the legal foundation for the exercise of such competences, namely, their

---

<sup>106</sup> SPA. Constitution, 1978, art. 158.1.

<sup>107</sup> SPA. Ley Orgánica de Financiación de las Comunidades Autónomas, 1980, art. 15.

<sup>108</sup> For the Basque Country, see *Estatuto de Guernica*, Organic Law 3/1979, art. 16; for Navarre, see *Reintegración y Amejoramiento del Régimen Foral de Navarre*, Organic Law 13/1982, art. 47.



constitutionally protected historic rights as territories with traditional charters,<sup>109</sup> which in practice favors the exercise of a substantially higher degree of autonomy. On the financing side of education there are also important differences between the common and the special regimes, as we shall see. To be sure, the statutes of autonomy of the Basque Country and Navarre explicitly acknowledge the fundamental right character of education, as established by the Spanish constitution.

### **7.1.2 Devolution and Universal Access to Health Care**

“The right to health protection,” reads Spain’s constitution, “is recognized,”<sup>110</sup> but this recognition is of a somewhat different legal nature than the recognition of the right to education. Health care, unlike education, is not enumerated among the fundamental rights. It is listed instead in a chapter titled “Principles governing economic and social policy.” As the constitution makes clear, such principles “shall guide legislation, judicial practice and actions by the public authorities. They may only be invoked before the ordinary courts in accordance with the legal provisions implementing them.”<sup>111</sup> In comparison with education, the envisioned enforcement mechanisms for the “right to health protection” would be in any case of a lower legal status. Central level legislation has, however, sought to make the access to health services universal across regions.

---

<sup>109</sup> . SPA. Constitution, 1978, First Additional Provision.

<sup>110</sup> . SPA. Constitution, 1978, art. 43.

<sup>111</sup> . SPA. Constitution, 1978, art. 53.3.

Similar to the case of education, health care is not listed in the Spanish constitution among the “matters” over which the central level of government “shall have exclusive competence.”<sup>112</sup> On the contrary, the constitution names “health and hygiene” as one of the matters over which the autonomous communities “may assume competences,” the choice being up to the corresponding statute of autonomy.<sup>113</sup> When an autonomous community forsakes this option, the central level of government is entitled to step in and assume the competences.

A commitment to ensure the availability of at least a minimum level of health services in all the Spanish territory is enshrined in the Organic Law of the Autonomous Communities Financing Framework, by giving health care the legal rank of a basic public service. The rules for determining when an autonomous community has fallen behind the minimum level target and for providing central government equalization aid are very much alike to those applied in the case of education.

The Health Care General Law (*Ley General de Sanidad*), issued in 1986, articulates the multilevel government system aimed at achieving universal access to basic health services, a system characterized by the combination of public funding, predominantly central government funding, and decentralization of governing powers to the autonomous communities (Lopez-Casasnovas, Costa-Font et al. 2004). At the end of the Francoist era, health care government functions were highly centralized. The eighties and nineties witnessed the transfer, envisioned in the constitution,<sup>114</sup> of a core of such functions from the central government to the different autonomous communities, more or less running simultaneously with the transfer in the education ambit (Ministerio de Economía y Hacienda de España 2006a; Ministerio de Economía y

---

<sup>112</sup> . SPA. Constitution, 1978, art. 149.

<sup>113</sup> . SPA. Constitution, 1978, art. 148.

<sup>114</sup> . SPA. Constitution, 1978, art. 148.21.

Hacienda de España 2006b). “Access to health care,” Lopez-Casasnovas, Costa-Font et al. tell us (2004 , p. 6), “is free at the point of use to all residents (including illegal immigrants) and user copayments are restricted to pharmaceuticals.” Wealthy families tend to buy extra health insurance “as a means for ‘waiting lists avoidance’...” These authors also report that “Health care delivery is mainly undertaken through a network of publicly owned, staffed and operated inpatient and outpatient centers, with significant geographical differences in the way services are contracted out to the private sector.” (ibid., p. 6) General coordination of the health care system remains exclusively a central government function.<sup>115</sup> As in the case of education, the governing powers of the Basque Country and Navarre over health care provision are higher than those of other autonomous communities, as a result of their historical rights and traditional charters.

### **7.1.3 In Search of a More Equitable Distribution of Regional Income**

Regional income disparities are a constitutional issue in Spain. In the chapter devoted to the principles governing economic and social policy, public authorities are urged to “promote favorable conditions for... a more equitable distribution of regional and personal income within the framework of a policy of economic stability. They shall in particular carry out a policy aimed at full employment.”<sup>116</sup> Akin to the case of health care, this provision has the legal status of a constitutional guiding principle for “legislation, judicial practice and actions by the public authorities.”

---

<sup>115</sup>. SPA. Constitution, 1978, art. 149.16.

<sup>116</sup>. SPA. Constitution, 1978, art. 40.1.

Elsewhere in the constitution, under the heading “Economy and public finance”, state planning of economic activity is sanctioned with a view not only to “balance and harmonize regional and sectoral development” but also to “stimulate the growth of income and wealth and their more equitable distribution.”<sup>117</sup> Wisely enough, given, among other things, the controversial nature of the matter, the criteria to determine whether a given distribution of income and wealth is equitable are not spelled out in the constitution.

As shown by de la Fuente and Vives (2003), Spain’s public finances influence the distribution of income throughout the country by a variety of fiscal tools, but only a number of them explicitly target territories, as opposed to individuals and households, with the latter falling beyond the scope of this study.<sup>118</sup> The Interregional Compensation Fund, foreshadowed in the constitution, aims at “redressing interterritorial economic imbalances and implementing the principle of solidarity ...”<sup>119</sup> By constitutional mandate, the fund’s resources are earmarked to investment projects in the beneficiary autonomous communities (AC), so that it is via the financing of such projects that the reduction of interregional income disparities may come about. Legislation has sought to fulfill the fund’s objectives “by means of positive discrimination in favor of the less developed areas,” Newton and Donaghy (1997, p. 127) report. Note that

---

<sup>117</sup>. SPA. Constitution, 1978, art. 131.

<sup>118</sup>. For instance, on the basis of the public social security system envisioned by the 1978 constitution (i.e., art. 41), central level of government legislation (e.g., the 1980 Ley Básica de Empleo) instituted an unemployment subsidies and insurance scheme, creating a financial flow from the central administration to the unemployed throughout the country (Ayala, 2003). Its impact on interregional inequality is therefore a byproduct of its original individual impact.

<sup>119</sup>. SPA. Constitution, 1978, art. 158.2.

whatever income equalization occurs here, it occurs by way of the central government, as the Interregional Compensation Fund is part of its budget.

Meanwhile, the autonomous communities have independently from one another set up basic income maintenance programs, on the basis of a constitutional provision which grants them competences over social assistance,<sup>120</sup> according to Ayala (2003). “The basic income maintenance programs,” Ayala (2003, p. 273) tells us, “are... the most extreme manifestation of territorial decentralization of redistributive policies in Spain, since their design, management and financing depend entirely on the autonomous communities.” Such programs are designed for intraregional, rather than interregional, redistribution of income.

## 7.2 GOVERNMENT FINANCING INSTITUTIONS

### 7.2.1 Geographical Partition of the Power to Tax

“The primary power to raise taxes is vested exclusively in the State by means of law,” reads Spain’s constitution.<sup>121</sup> It has already been noted that the word *state* (*estado*, in Spanish) is by official constitutional interpretation generally taken to mean central level of government.<sup>122</sup> Autonomous communities and local governments are allowed to “impose and levy taxes, in

---

<sup>120</sup> . SPA. Constitution, 1978, art. 148.

<sup>121</sup> . SPA. Constitution, 1978, art. 133.1.

<sup>122</sup> . See Ross (2002, p. 20).

accordance with the Constitution and the laws.”<sup>123</sup> Thus, the power to tax of the central level of government, a power exercised by the Spanish parliament (*Cortes Generales*) in conjunction with the executive, can be said to be original in the sense that it is limited merely by the constitution. Meanwhile, the power to tax of the autonomous communities and local governments can be said to be derivative in that it is subject to the law, besides the constitution (Yebra 2004).<sup>124</sup>

It should be taken into account, nonetheless, that the 1978 constitution, by recognizing their historic rights and traditional charters, gives the Basque Country and Navarre a special fiscal status. The specifics of the special regime’s tax institutions are the product of agreements, sanctioned by law, between the central level of government, on the one hand, and each pertinent autonomous community, on the other (i.e., *Concierto Económico* for the Basque Country and *Convenio Económico* for Navarre). As established in the *Concierto* and the *Convenio*, these two autonomous communities are entitled to levy and collect practically all taxes, including taxes that elsewhere in Spain are levied and collected by the central government, the exception being custom duties and the taxes on imports. As far as the Basque Country is concerned, the tax competences are directly assigned to its provinces (i.e., Alava, Guipúzcoa y Vizcaya). In the other 15 autonomous communities prevails the common regime, grounded, in addition to the constitution, in an organic law (i.e., the LOFCA), whose approval and modification requires absolute majority voting in the Spanish House of Commons (*Congreso de Diputados*). Within

---

<sup>123</sup> SPA. Constitution, 1978, art. 133.2.

<sup>124</sup> . In a provision devoted to the rights and duties of citizens (i.e., art. 31.1), the constitution sets the duty to contribute to the public purse and establishes that the tax system should conform to the ability to pay principle, in the form of equality among equals (horizontal equity) and progressivity (vertical equity).

the common regime, the tax jurisdictions of the central government and the autonomous communities tend to intersect, in the way outlined below.

No particular taxes are assigned by the Spanish constitution to the central level of government or the autonomous communities. It lists, however, the types of revenue sources corresponding to the autonomous communities.<sup>125</sup> The list includes taxes, surcharges on central government taxes, shares of central government revenue, transfers from an inter-territorial compensation fund and other intergovernmental transfers, government property income, and interests from loan operations. For all autonomous communities but the Basque Country and Navarre, a legal distinction is made between the autonomous communities' own taxes and central level of government's taxes totally or partially ceded to them (*impuestos cedidos* in the Spanish legal jargon).

Figure 7.1 displays the tax assignment between levels of government in Spain. Regarding the special regime (*Régimen foral*), the tax sources corresponding to the Basque Country and Navarre include the personal and corporate income tax, the valued added tax (VAT), the wealth tax, the inheritance and donations tax, and the taxes on gambling. The power to levy and collect user charges (*tasas*) corresponds to the two communities as well. Major taxes assigned to local governments in the Basque Country and Navarre are the land and building tax, the business tax, and the vehicle tax. In exercising their tax powers, the Basque Country's and Navarre's authorities, both at the intermediate and local levels of government, are required to coordinate and harmonize the tax system with that of the central government. Thus, their tax systems should not discriminatorily interfere with the free circulation of persons, capital and goods in the

---

<sup>125</sup>. SPA. Constitution, 1978, art. 157.

Spanish territory; moreover, the tax burden in each community should be equivalent to the tax burden elsewhere in Spain.

| Major Revenue Sources                     | Common Regime                  |                        |                | Special (Foral) Regime |                        |                | Local Governments |
|---|--------------------------------|------------------------|----------------|------------------------|------------------------|----------------|-------------------|
|   | Exclusive revenue <sup>a</sup> |                        |                | Exclusive revenue      |                        |                |                   |
|   | Central Government             | Autonomous Communities | Shared revenue | Central Government     | Autonomous Communities | Shared revenue |                   |
| 1. Income taxes                           |                                |                        |                |                        |                        |                |                   |
| Personal income tax                       |                                |                        | ✓              |                        | ✓                      |                |                   |
| Corporate income tax                      | ✓                              |                        |                |                        | ✓                      |                |                   |
| 2. Value added tax                        |                                |                        |                |                        |                        |                |                   |
| Domestic                                  |                                |                        | ✓              |                        | ✓                      |                |                   |
| Imports                                   |                                |                        | ✓              | ✓                      |                        |                |                   |
| 3. Especial taxes                         |                                |                        |                |                        |                        |                |                   |
| Alcohol and spirits                       |                                |                        | ✓              |                        | ✓                      |                |                   |
| Beer                                      |                                |                        | ✓              |                        | ✓                      |                |                   |
| Electricity                               |                                | ✓                      |                |                        | ✓                      |                |                   |
| Petroleum products tax                    |                                |                        | ✓              |                        | ✓                      |                |                   |
| Transportation means                      |                                | ✓                      |                |                        | ✓                      |                |                   |
| Tobacco and cigarettes tax                |                                |                        | ✓              |                        | ✓                      |                |                   |
| 4. Levy on insurance fees                 | ✓                              |                        |                |                        | ✓                      |                |                   |
| 5. Taxes on non-residents                 | ✓                              |                        |                | ✓                      |                        |                |                   |
| 6. Customs import duties                  | ✓                              |                        |                | ✓                      |                        |                |                   |
| 7. Wealth tax                             |                                | ✓                      |                |                        | ✓                      |                |                   |
| 8. Property transfer and registration tax |                                | ✓                      |                |                        | ✓                      |                |                   |
| 9. Inheritance and donations tax          |                                | ✓                      |                |                        | ✓                      |                |                   |
| 10. Gambling tax                          |                                | ✓                      |                |                        | ✓                      |                |                   |
| 11. Retail tax on petroleum products      |                                | ✓                      |                |                        | ✓                      |                |                   |
| 12. Wine tax                              |                                | ✓                      |                |                        | ✓                      |                |                   |
| 13. Land and buildings tax                |                                |                        |                |                        |                        |                | ✓                 |
| 14. Business tax                          |                                |                        |                |                        |                        |                | ✓                 |
| 15. Vehicle tax                           |                                |                        |                |                        |                        |                | ✓                 |

**Figure 7-1: Assignment of revenue sources in Spain, since 2002**

Source: Original data from Ley 21 de 2001, Concierto Económico and Convenio Económico.

<sup>a</sup> Exclusive autonomous communities revenues consist of own taxes and ceded taxes, with 100% of revenue ceded.

The tax sources employed in the common and special regimes are virtually the same. What varies between one area and the other is the assignment of taxes between levels of government.<sup>126</sup> While in the special regime the revenues of the vast majority of taxes accrue to the autonomous communities, in the common regime, in addition to taxes whose revenue go entirely to the autonomous communities (e.g., wealth tax, inheritance and donations tax,

<sup>126</sup> . An important feature of the current financing system of the autonomous communities of the common regime is that it was adopted by law –Law 21/2001– for the first time in the 1978 constitution era. Previously, the autonomous financing system was sanctioned by an intergovernmental body and had to be revised periodically. The new system is intended to be permanent in the sense that there are no mandated periodic revisions.



gambling taxes), the revenues of a number of taxes are shared between the central government and the autonomous communities (Ministerio de Economía y Hacienda de España 2006a; Ministerio de Economía y Hacienda de España 2006b). Such is the case, for instance, of the personal income tax, the value added tax, and the special taxes on petroleum products and alcoholic beverages. The percentage of revenue accruing to the autonomous communities varies between 33 and 40 percent depending on the tax, with the remainder going to the central government. Within the common regime, only a handful of revenue sources belong exclusively to the central government, as the corporate income tax and the customs import duties. Major local taxes are virtually the same in both regimes.

Although the taxing arrangements (e.g., tax base, tax rate schedule, collection) of the different revenue sources are intricate, some broad features can be identified (See Figures 7.2 and 7.3). As far as the common regime is concerned, the central government generally collects those taxes not shared with the autonomous communities (e.g., corporate income tax) as well as those *partially* shared (e.g., personal income tax, value added tax). Taxes whose revenues have been entirely ceded to the autonomous communities (e.g., wealth tax, inheritance and donations tax) are collected by AC agencies. The taxing schemes of unshared central government taxes are determined, as expected, by central level of government's legislation. As a rule, the tax bases of ceded taxes, both partially and entirely ceded, are established by central level legislation. Autonomous communities of the common regime enjoy an important degree of autonomy to set their corresponding tax rates schedules in a number of cases, including the personal income tax, the wealth tax, and the inheritance and donations tax. As regards the personal income tax, they are required by central level legislation to employ the same number of income brackets used countrywide and to apply a progressive tax schedule, which complements the central level's tax

schedule. We have already referred to this type of scheme as tax base sharing. If a given autonomous community fails to adopt its own personal income tax schedule, a default tax schedule, given by central level legislation, applies.

| Central tax source   | Tax base                             | Tax rate structure             | Tax rate levels  | Observations   |
|----------------------|--------------------------------------|--------------------------------|--|--|
| 1. Income taxes      |                                      |                                |  |  |
| Personal income tax  | Taxable income,<br>five tax brackets | Progressive marginal tax rates | 9% on the first €\$4,161<br>of taxable income<br>15.8% on the next €\$10,196<br>of taxable income<br>18.7% on the next €\$12,485<br>of taxable income<br>24.7% on the next €\$19,976<br>of taxable income<br>29.2% of taxable<br>income over €\$46,818 | The default marginal tax rates applicable<br>by autonomous communities of the<br>common regime range between 5.9% and<br>15.8% of taxable income |
| Corporate income tax | Taxable income                       | Flat rates                     | General: 35%<br>Differential rates<br>of 25% and 1%  |  |
| 2. Value added tax   | Final consumption                    | Flat general rate              | 16%  | Differential rates apply   |

**Figure 7-2: Spain: Central government taxing schemes, 2004 or most recent year available**

*Source:* Original data from Spain's tax legislation, Ministry of Finance, [www.meh.es](http://www.meh.es).

The configuration acquired by Spain's tax assignment in recent years is the result of a process that took place largely during the eighties and nineties, whereby the autonomous communities gained control, under the legal form of totally ceded taxes in the case of the common regime, over a group of tax revenue sources previously controlled by the central government (Monasterio 2002). Such reallocation of revenue sources between levels of government was meant to provide the financial leverage for the transfer of public expenditure functions which was occurring at the time (Salinas and Alvarez 2003). The whole process appears to have been conceived as a zero-sum game from an intergovernmental perspective, where the newly acquired expenditure responsibilities of the autonomous communities were

expected to be matched by the reassigned tax revenues, together with the intergovernmental transfers.

| Major Tax Sources                         | Number of AC | Taxing arrangements <sup>a</sup> |  |  |                 |
|---|--------------|----------------------------------|--|--|-----------------|
|   |              | Tax collection                   | Tax base                                   | Tax rate   | Revenue sharing |
| 1. Income taxes                           |              |                                  |  |  |                 |
| Personal income tax                       |              |                                  |  |  |                 |
| Common Regime                             | 14           | Central                          | Central                                    | AC. own rates  | 33% ceded       |
| Foral Regime (Basque Country and Navarre) | 2            | AC                               | Own base                                   | Own rates  |                 |
| Corporate income tax                      |              |                                  |  |  |                 |
| Foral Regime (Basque Country and Navarre) | 2            | AC                               | Own base                                   | Own rates  |                 |
| 2. Value added tax (domestic component)   |              |                                  |  |  |                 |
| Common Regime                             | 14           | Central                          | Central                                    | Central  | 35% ceded       |
| Foral Regime (Basque Country and Navarre) | 2            | AC                               | Central                                    | Central  |                 |
| 3. Special taxes                          |              |                                  |  |  |                 |
| Common Regime                             | 14           |                                  |  |  |                 |
| Alcohol and spirits                       |              | Central                          | Central                                    | Central  | 40% ceded       |
| Beer                                      |              | Central                          | Central                                    | Central  | 40% ceded       |
| Electricity                               |              | Central                          | Central                                    | ...  | 100% ceded      |
| Petroleum products                        |              | Central                          | ...  | ...  | 40% ceded       |
| Transportation means                      |              | AC                               | Central                                    | Own rates by central authorization                       | 100% ceded      |
| Tobacco and cigarettes                    |              | Central                          | ...  | ...  | 40% ceded       |
| Foral Regime (Basque Country and Navarre) | 2            | AC                               | Central                                    | ...  |                 |
| 4. Wealth tax                             |              |                                  |  |  |                 |
| Common Regime                             | 14           | AC                               | Central                                    | Own rates by central authorization                       | 100% ceded      |
| Foral Regime (Basque Country and Navarre) | 2            | AC                               | Own base                                   | Own rates  |                 |
| 5. Inheritance and donations tax          |              |                                  |  |  |                 |
| Common Regime                             | 14           | AC                               | Central                                    | Own rates  | 100% ceded      |
| Foral Regime (Basque Country and Navarre) | 2            | AC                               | Own base                                   | Own rates  |                 |
| 6. Property transfer and registration tax |              |                                  |  |  |                 |
| Common Regime                             | 14           | AC                               | Central                                    | Own rates  | 100% ceded      |
| Foral Regime (Basque Country and Navarre) | 2            | AC                               | Own base                                   | Own rates  |                 |
| 7. Gambling tax                           |              |                                  |  |  |                 |
| Common Regime                             | 14           | AC                               | Central, but authorization to set own base | Own rates  | 100% ceded      |
| Foral Regime (Basque Country and Navarre) | 2            | AC                               | Central                                    | ...  |                 |
| 8. Retail tax on petroleum products       |              |                                  |  |  |                 |
| Common Regime                             | 14           | AC                               | Central                                    | Central, but authorization to set own rates within range | 100% ceded      |
| Foral Regime (Basque Country and Navarre) | 2            | AC                               | Central                                    | Central, but authorization to set own rates within range |                 |
| 11. Levy on insurance fees                |              |                                  |  |  |                 |
| Foral Regime (Basque Country and Navarre) | 2            | AC                               | Central                                    | ...  |                 |

**Figure 7-3: Taxing schemes in Spain's autonomous communities by tax source, 2004 or most recent year available**

Source: Author's elaboration based on Law 21/2001, *Concierto Económico*, *Convenio Económico* and other Spanish legislation. Spain's Ministry of Finance, www.meh.es.

<sup>a</sup> Some exceptions may apply.

Notes: Due to peculiarities in its tax system, the Canary Islands are not included. In the Basque Country, *Diputaciones Forales* of the Basque historic territories.

Given that the constitution does not go into the specifics of what level of government should tax what, the constitutional provisions on taxation seem in principle consistent with a variety of tax assignments between levels of government. It would be misleading, however, to believe that tax assignment is unconstrained. The history of tax assignment operates as a legal constraint in at least two main ways. First, in the special regime area, as a result of the constitutional recognition of the historic rights of the Basque Country and Navarre, tax assignment is more legally frozen than not. Second, in the common regime, once a particular tax revenue source has been declared by Spanish law to be part of the autonomous communities' own taxes, it comes under the umbrella of the constitutional provisions protecting such taxes. It can hardly be reassigned to another level of government. No equivalent protection is in place for the taxes of the central level of government. A given central government tax can be made over to the autonomous communities or, if the central government keeps the property title of the tax, the tax revenues can be in whole or in part ceded to them. The ceded tax revenues could eventually be reallocated to the central government by legal mandate. But legal constraints are not the only ones in place. Financial and political constraints are also likely to play a role. In any case, tax assignment in Spain, specifically as concerns the intermediate level of government, is path dependent, not only because of the sheer weight of history but also because of constitutional design.

To illustrate the workings of tax coordination in the exercise of the tax powers between levels of government in the common and special regimes, consider the case of income taxes as of 2005. With reference to the personal income tax, the tax rates schedule of the common regime is a progressive one with five taxable income brackets and marginal tax rates ranging between 9%

and 29.2%. Conversely, in the Basque Country, six income brackets are in place, with marginal tax rates varying between 15% and 48%. A similar taxing scheme is found in Navarre: six income brackets and the bottom and top marginal tax rates at 14% and 44%. To be sure, the income brackets differ from one place to the other. It could be shown, however, that the personal income tax rates in the Basque Country and Navarre are substantially higher than in the common regime area for comparable levels of income. By setting the tax rates at a relatively low level, the central level of government leaves some personal income tax room for the autonomous communities of the common regime to levy their own personal income rates (García 2005). Using the default tax schedule applicable to such communities as a point of reference, the combined marginal tax rates in the common regime (i.e., central plus autonomic) fluctuate between about 15% and 46%, a range quite similar to the one observable in the Basque Country and Navarre.

Concerning the corporate income tax, a general flat rate of 35% applies in the common regime area. Navarre employs the same general rate, whereas the Basque Country levies a rate of 32.5%. Here there is no need to leave tax room for the autonomous communities of the common regime, for in such tax area the corporate income tax entirely belongs to the central level of government. The mobility of capital across jurisdictions is likely to operate as a barrier against the adoption of widely different tax rates.

### **7.2.2 Bottom-Up and Top-Down Intergovernmental Transfers**

Mirroring the geographical partition of the power to tax, two intergovernmental transfers systems coexist in Spain, one for the Basque Country and Navarre (i.e., special regime) and the other for

the remaining autonomous communities (i.e., common regime).<sup>127</sup> The flow of transfers within the special regimen (*régimen foral*) follows a bottom-up direction, from the autonomous communities to the central government (Figure 7.4). Conversely, within the common regime it is the central government which makes transfers to the autonomous communities. Here the flow of transfers runs top-down. That intergovernmental transfers in the two systems go in opposite directions is anything but accidental. It is the result, instead, of the common/special regimes divide in the assignment of taxes and functions between levels of government. The Basque Country and Navarre carry out many government functions that in the rest of Spain are performed by the central government. Through their provinces, they also levy taxes that elsewhere are levied by the central government.

---

<sup>127</sup> . See, for instance, Ministerio de Economía y Hacienda (2006a and 2006b).

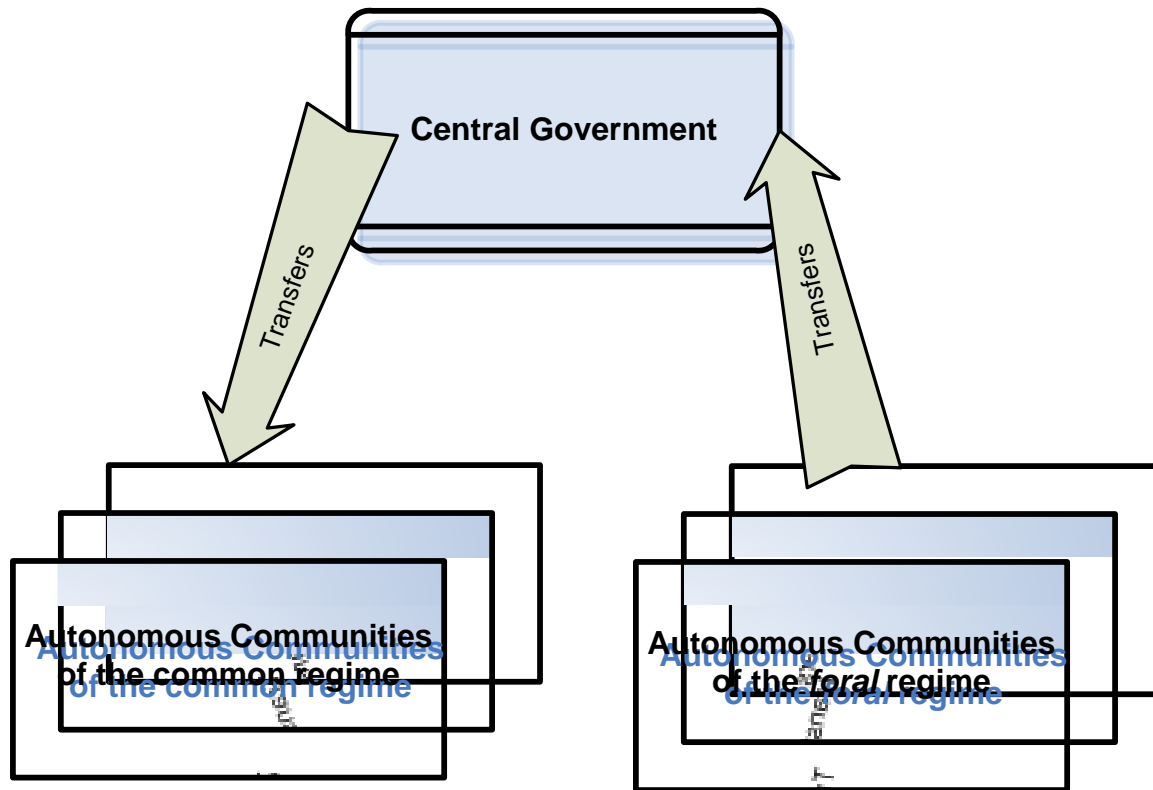
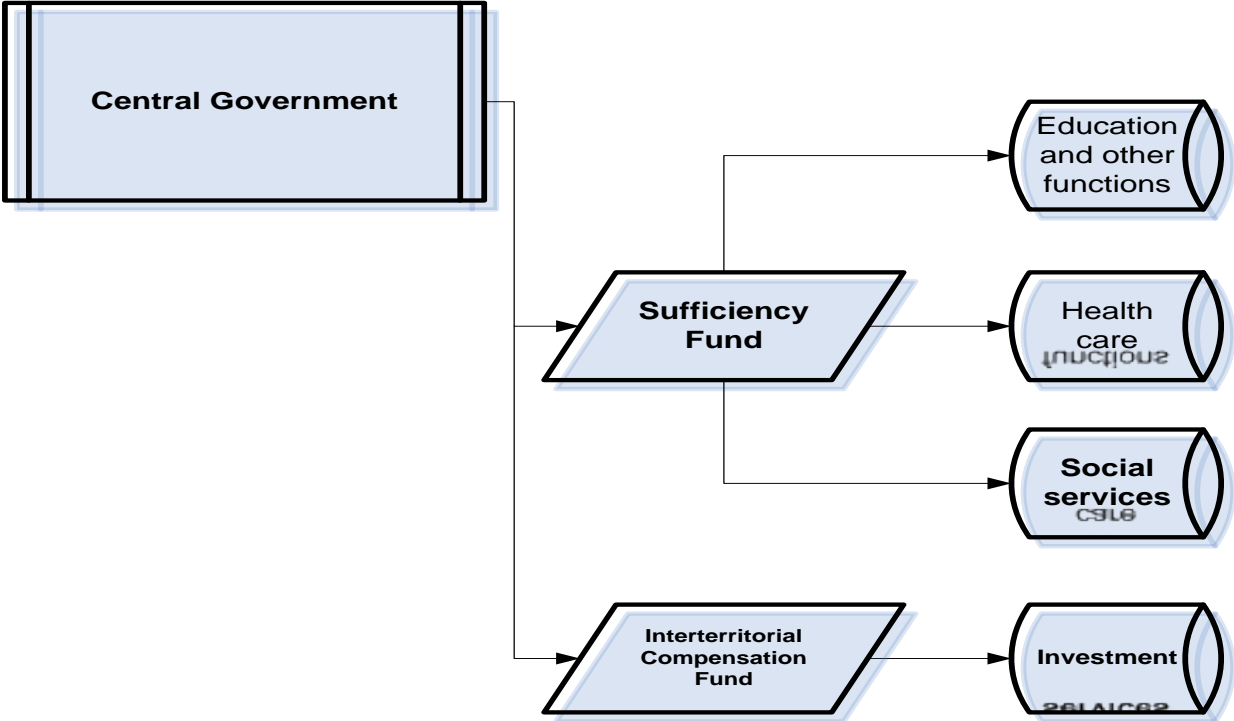


Figure 7-4: Direction of intergovernmental transfers in Spain

In terms of design, the intergovernmental transfer system of the special regime is relatively straightforward. The underlying governing rule of the system is that the Basque Country and Navarre should contribute to the financing of central government functions in direct proportion to their respective aggregate income (see Appendix C).

In comparison, the intergovernmental transfers system of the common regime appears cumbersome. Leaving aside many nuances, it can be described as follows. Two transfers integrate the system, the Sufficiency Fund (*Fondo de Suficiencia*) and the Interterritorial Compensation Fund (See, for instance, Gómez-Pomar 2002; Monasterio 2002; García 2005), as depicted in Figure 7.5. The Sufficiency Fund covers in turn three types of expenditure functions, namely, *i*) a pool of homogeneous functions across autonomous communities (*Bloque de*

*competencias comunes*), which includes education, *ii*) health care (*Bloque de servicios de asistencia sanitaria*), and *iii*) social services, including services for the elderly (*Bloque de servicios sociales*). For each autonomous community, the size of the Sufficiency Fund transfer is equal to the difference between the jurisdiction’s expenditure needs in the three types of functions and its own government revenues, including those taxes totally or partially ceded to it (a negative outcome entails no compensation).



**Figure 7-5: Transfers to the intermediate level of government in Spain,**

As regards the pool of homogenous functions, expenditure needs are first estimated for each type of function for the autonomous communities of the common regimen as a whole,



taking the 1999 budget allocations as the base line.<sup>128</sup> Next, expenditure needs by type of function are apportioned among the autonomous community using one or more, generally complex, distribution formulas.<sup>129</sup> For Monasterio (2002, p. 47), the complexity of the distribution formulas serves as “ ‘technical cover’ to conceal political agreements...”

Health care expenditure needs are apportioned among autonomous communities using a more straightforward distribution formula. The population protected by health care services in an autonomous community, relative to the population protected in all the autonomous communities of the common regime, accounts for three quarters of the distribution. As in the case of the pool of homogenous functions, the base line is 1999. A bit less than a quarter of the distribution is made in proportion to the relative size of the population aged over 65 years.

Within the range of the Sufficiency Fund, expenditure needs are standardized across units of government by way of the distribution formulas. Given the relatively high weight attached to the population size in the distribution formulas, this standardization procedure may be open to the criticism that it does not properly reflect the differences in expenditure needs across autonomous communities. In a way, it is as if expenditure needs, expressed in per capita terms, were the same everywhere.<sup>130</sup> Considering the difficulties of accurately estimating expenditure needs, the Spanish approach to standardizing such needs may well prove to be satisfying. On the

---

<sup>128</sup> / According to García (2005, p. 98), the estimation of expenditure needs is a mixture of the effective cost of services and political bargaining.

<sup>129</sup> . Part of the estimated expenditure needs (i.e., Fondo General) is allotted with a formula that gives the community's relative population size a weight of 94%. A minimum amount to each autonomous community is guaranteed. Still another part of the alluded expenditure needs, covered by a fund known as *Fondo de Renta Relativa*, is allotted according to an income-weighted index of the autonomous community's relative population size, with the weight favoring those autonomous communities with below- the-average per capita income. A floor and a ceiling to the increase in the valuation of expenditure needs regulate the growth of homogeneous functions grants to a given autonomous community.

<sup>130</sup> . By favoring the autonomous communities with below average per capita income, where presumably expenditure needs are higher, the *Fondo de Renta Relativa* may help counteract such shortcoming. The extent of the counteracting effect depends, of course, on the size of the *Fondo de Renta Relativa*.

contrary, no attempt whatsoever appears to have been made to standardize an autonomous community's own revenues for determining the Sufficiency Fund transfer. Actual revenues would be used instead. If so, autonomous communities with low tax effort would be rewarded, while those with high tax effort would be punished.

Since the early nineties, the beneficiaries of the Interterritorial Compensation Fund, the second piece of the intergovernmental transfers system of the common regime, have been limited, by legal mandate (e.g., *Ley 29/1990*), to the less developed autonomous communities in terms of per capita income. More precisely, the pool of beneficiaries consist of the autonomous communities whose GDP per head is at or below 75% of the European Union average. This selection rule in itself signals to the equalizing objective of the Interterritorial Compensation Fund. Formerly, all autonomous communities were potential beneficiaries. The Fund has two components, one aimed at financing investment and the other at temporarily covering the associated operating costs. On the whole, the investment component is equal to a percentage (22.5%) of an *ad hoc* definition of the central government investment budget, a definition that ultimately amounts to a share of the recipient autonomous communities in such a budget. The criteria to distribute the investment component among the beneficiaries include population size, per capita income, interregional migratory flows, unemployment, and territorial area. Periodically, the Spanish parliament establishes, by simple majority in each chamber, the precise distribution formula.

It has already been noted that the low-income autonomous communities as a whole are the only beneficiaries of the investment component, also taken as a whole. Yet it is one thing to name a group as the pie owner and quite another to allocate the slices among the members of the group. Most of the investment component (about 87%) is allocated according to the

beneficiaries' relative population size, inversely weighted by the relative size of their economies' income. The specifics of the distribution formula are fairly complicated, though.

The remainder of the Interterritorial Compensation Fund, set by law at 33% of the investment component, is meant to cover the operating costs generated by the investment projects. Autonomous communities may use the proceeds for that purpose for two years only.

From an institutional design perspective, what differences, other than the direction of grants, can be identified between the intergovernmental fiscal relations of the common and special regimes? One way to think about this issue is to compare the two regimes on a common notional ground. What would the situation look like, for instance, if the multilevel government fiscal rules of the special regime were applied to the common regime as well? In this case all the autonomous communities would levy and collect, within their respective jurisdictions, practically all the taxes existing in Spain, with an important degree of tax coordination among them, and each community would make transfers to the central government in proportion to the size of its economy. No interregional redistribution would occur through first-round intergovernmental transfers, let alone the personal income tax or other taxes; second-round interregional redistribution might take place via the central government's public expenditure as approved in the annual budget, though. No presumption can be made as to what patterns, if any, such second-round interregional redistribution would follow.

Now, what would the situation look like if the multilevel government fiscal rules of the common regime were applied to the special regime too? Here the central government would get the largest share of the most important revenue-yielding taxes across all the Spanish territory (the remaining share would accrue to the autonomous communities). Interregional redistribution would occur via central level taxation and the expenditure side of the annual central budget,

including intergovernmental transfers, in this case from the center to the autonomous communities.

So, from an equalization perspective, the essential difference between the special and common regimes is that the former tends to rule out any meaningful interregional redistribution by means of taxation and first-round intergovernmental transfers, whereas such redistribution is at the heart of the latter. Quite another matter is how well-crafted are the tools of such redistribution.

### **7.2.3 Intertwined Spanish and European Borrowing Regulations**

The central level of government is empowered by the 1978 constitution to self-regulate by ordinary law its access to borrowing,<sup>131</sup> as well as to regulate the indebtedness of the autonomous communities, this time through organic law.<sup>132</sup> That is in fact what the organic law known as the 1980 LOFCA, together with more recent legislation, does for the autonomous communities of both the common and special regimes (Monasterio 2002; Vallés 2002).<sup>133</sup>

As established by LOFCA, short term debt (normally, maturity of less than a year) can be issued by the autonomous communities for liquidity purposes exclusively. Echoing the so-called golden rule, the purpose for which medium and long term debt (i.e., maturity of more than a year) can be placed is to finance capital expenditures (investment). A maximum level of indebtedness is set forth: Annual debt service payments (i.e., principal plus interest payments)

---

<sup>131</sup> . SPA. Constitution, 1978, art. 135 and art. 149.1.14.

<sup>132</sup> . SPA. Constitution, 1978, art. 157.

<sup>133</sup> . See *Ley Orgánica de Financiación de las Comunidades Autónomas*, 8/1980, art. 14 and *Ley Orgánica* 5/2001.

ought not to surpass 25% of the autonomous community's current revenues. Foreign indebtedness requires authorization of the central government (i.e., Ministry of Finance). The Council of Fiscal and Financial Policy, with representatives of both the central government and the autonomous communities, is given the role of coordinating the debt policies of the different levels and units of government. Other aspects of sub-central government debt financing, such as the types of debt that can be issued, are subject to the same conditions that apply to the central government. It should be taken into account that Spain, as a member of the European Union, has subscribed to the Stability and Growth Pact, which sets an upper limit to the government debt (60% of GDP) and budget deficit (3% of GDP) during normal cyclical fluctuations (Vallés 2002). Unsurprisingly, Ahmad, Albino-War et al (2006, p. 416) classify Spain among the countries with "fiscal rules targeting the overall fiscal deficit..." The commitment to enforce fiscal discipline in practice involves, to varying degrees, all levels and units of government.

Singh and Plekhanov describe the operation of Spain's sub-central borrowing controls since the early nineties as one of intergovernmental cooperation, in contrast to the central rule that had previously prevailed. According to the authors, the country has a history of bailing out sub-central governments.

## 8.0 CONSTITUTIONAL AMENDMENTS TO INTERGOVERNMENTAL FISCAL RELATIONS IN COLOMBIA

Between July, 1991, and December, 2005, the Colombian constitution was amended 20 times, an annual average of nearly 1.4 times.<sup>134</sup> The amendments referred to a wide variety of issues. For example, the possibility of expropriating private property without indemnification, previously sanctioned by the constitution, was closed in 1999. To substitute the old written inquisitorial system of criminal justice, an oral accusatory system was authorized in 2002. As regards the executive branch, the ban on the reelection of the president was lifted in 2003, albeit limiting it to one extra term. Major changes were introduced to political parties' regulations, as well as to the electoral system, aimed at discouraging political fragmentation. Formally, some of the articles amended fall under a heading called territorial ordering of the state, but their specific content is unessential or irrelevant for the purpose of this study, as is the case of the change of name of the country's capital from Santafé de Bogotá to Bogotá. Practically all the main components of the constitution, from the bill of rights to the structure and functions of the state to the enforcement mechanisms, experienced changes of one sort or another.

---

<sup>134</sup> . In one occasion, the Constitutional Court declared the whole intended amendment invalid (i.e., *Acto Legislativo 2 de 2003*).

| Year | Legislative Act Number | Amended article | Article's subject   |
|------|------------------------|-----------------|---|
| 1993 | 1                      | 356             | System of intergovernmental transfers   |
| 1993 | 2                      | Transitory 60   | National Development Plan   |
| 1995 | 1                      |                 | 357   |
| 2000 | 2                      | 52              | Classification of sports and recreation as social spending in education; right to recreation. |
| 2001 | 1                      | 347             | Scope of the budgetary principle of universality. Cap on expenditure growth.                  |
|      |                        | 356             | System of intergovernmental transfers.  |
|      |                        | 357             | System of intergovernmental transfers.  |
| 2005 | 1                      | 48              | Right to social security; role of the state and the private sector; pension system.           |
| 2007 | 4                      | 356             | System of intergovernmental transfers.  |
|      |                        | 357             | System of intergovernmental transfers.  |

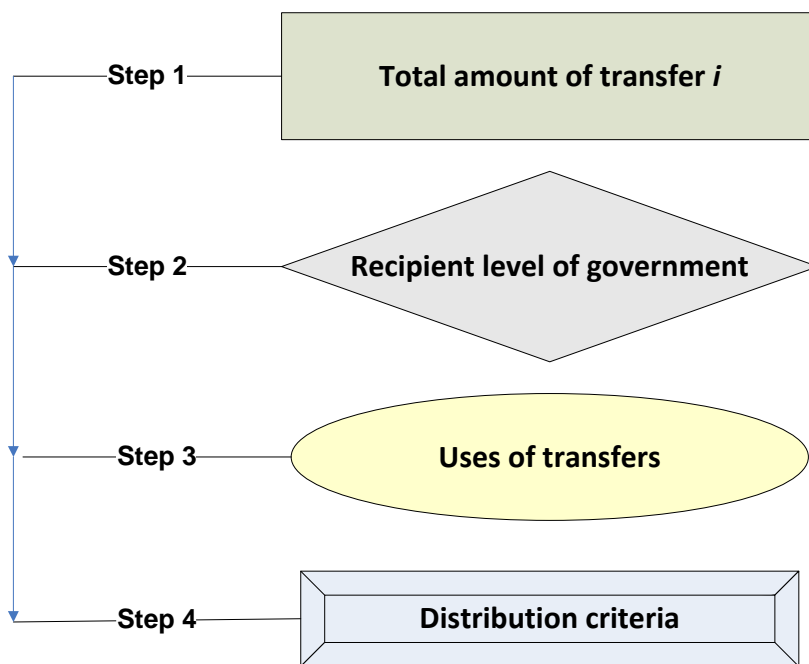
**Figure 8-1: Amendments to Colombia's 1991 fiscal constitution**

What we have termed the fiscal constitution has not escaped the reformist wave. With the main exceptions of a transitory cap on the growth of national government’s expenditure and a detailed regulation of the country’s pensions system, the amendments to the fiscal constitution deal with the system of intergovernmental transfers (Figure 8.1). Before analyzing the amendments, an overview of the system of intergovernmental transfers originally adopted in 1991 is warranted.

**8.1 THE ORIGINAL 1991 INTERGOVERNMENTAL TRANSFER SYSTEM**

The original design of the 1991 intergovernmental transfer system is illustrated in Figure 8.2. There were two transfers, the *situado fiscal* and the *participación municipal*. The first issue dealt with by the constitution was the size of each transfer. In the case of the *situado*, the constitution defined it as a percentage of the national government’s current revenues, adding that such a

percentage ought to increase annually starting in 1992 from a predetermined floor.<sup>135</sup> The *participación* was also defined as a percentage of the national government's current revenues, but in this case the constitution provided a more detailed schedule for its increase, namely, the *participación* ought to pass from 14% in 1994 to 22% in 2001 of the corresponding liquidation base. In sum, the 1991 Constituent Assembly clearly signaled towards an increase in the size of the two intergovernmental transfers.



**Figure 8-2: Original design of intergovernmental transfers in the 1991 Constitution**

---

<sup>135</sup> . COL. Constitution of 1991 as originally approved, art. 356 and transitory art. 44.



In terms of design, the second issue the original 1991 constitution addressed was the determination, for each transfer, of the recipient levels and units of government, resulting in the flows shown in Figure 8.3. Although the intermediate level of government, and particularly the departments, can be said to have been the chief recipients of the *situado*, the constitution also granted such entitlement to a number of units of the local level of government (e.g., Cartagena and Santa Marta). By doing so, a degree of asymmetry in the membership by level of government of the recipients was introduced into the *situado*. In contrast, all the recipients of the *participación* belonged to the local level of government (i.e., municipalities, special districts). Note that by way of the transfers a direct link operated between the national government (i.e., the transferer) and each of the subnational levels of governments (i.e., recipients). A similar type of link was in existence before 1991.

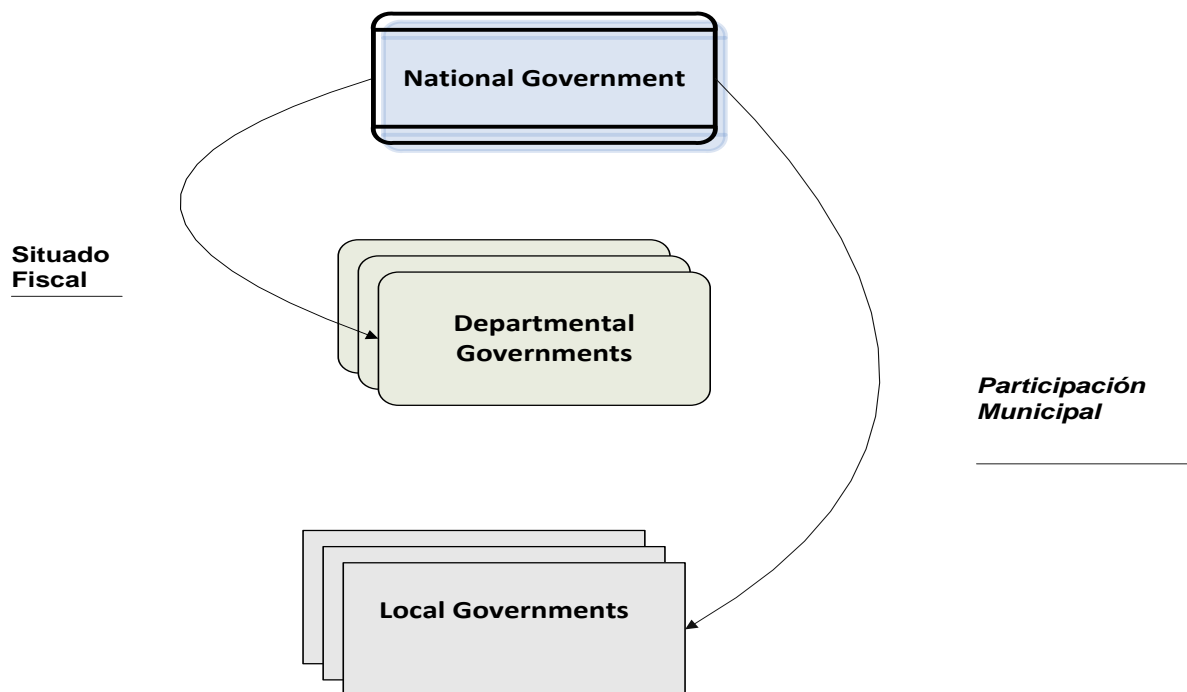


Figure 8-3: Intergovernmental transfer flows in the original 1991 Colombian constitution

The next issues in the design of intergovernmental transfers addressed by the original 1991 constitution turn out to be the uses of the revenues transferred, on the one hand, and the distribution formulas, on the other. No particular sequence between these two issues was set forth in the constitutional text. While the *situado* was ear-marked for education (e.g., pre-school, primary and secondary education) and health care, the *participación* was reserved for social investment, a category that the constitution explicitly left for the law to define. Although Law 60 of 1993 came up with a broad list of public expenditure categories to be counted as social investment, the largest share was allotted to education and health. Thus, the financing of education and health services was crafted, in part by the constitution, in part by the law, as a shared responsibility of the departmental and local governments. By earmarking in the constitution all the *situado* for education and health care, the possibility of establishing a general purpose component into the system of transfers for the departments was ruled out. This contrasts somewhat with the case of the local governments where the concept of social investment appears broad enough to permit uses other than those of education and health, a route that congress actually followed when crafting the *participación* into law.

As for the rules of distribution, what the Constituent Assembly essentially did with respect to the *situado* was to divide the transfer pie into two pieces, equivalent to 15% and 85% of the total, and then to establish the criteria for allocating each piece to the corresponding subnational governments. An aliquot portion of the first piece (i.e., the 15%) ought to be transferred to the departments and those local governments entitled to the *situado*, the constitution stipulated. For the remaining piece (i.e., the 85%), it listed the criteria that congress ought to use in specifying the distribution formula, namely, the number of current and potential users of the education and health services in each jurisdiction, together with the jurisdiction's tax

effort and administrative efficiency. The only room left for congress to tailor the distribution formula, other than amending the constitution, was, therefore, confined to the meaning and weights attached to the specified criteria.

Similar to the case of the *situado*, the *participación* was divided by the 1991 constitutional makers into two main pieces for distribution purposes, depending on the distributive criteria used. The first piece, amounting to 60% of the total, would be allocated among the municipalities in direct proportion to their level of poverty, as measured by the absolute and relative number of inhabitants with unmet basic needs. For the second piece, equivalent to the remaining 40% of the transfer, a number of distributive criteria were spelled out in the constitution, specifically population size, fiscal and administrative efficiency, and “the demonstrated progress in the quality of life,” allowing for a bonus to small municipalities (i.e., 5,000 inhabitants or less). A call for the law to specify the scope and definition of the *participación*’s distributive criteria was included in the original 1991 constitution.

In the law the logic of the design of both transfers to a good extent became one of ‘distribute first, determine the uses of the transfer next,’ a sequence that was neither explicitly required nor explicitly prohibited in the constitution. Thus, Law 60 of 1993 first determined how, specifically, the *situado* and the *participación* should be distributed between the corresponding subnational governments and then how the resulting amount transferred to each government should be allocated between education, health care and, when appropriate, other designated uses. Such design strategy opened the way to the eventual conflict between the rules of distribution and the designated uses of the transfers.

Take, for example, the case of the *situado*. Probably on an ad hoc basis, Law 60 of 1993 required that of the total amount of the *situado* allotted to *each* recipient government at least 60

percent be devoted to education and 20 percent to health care, with the remaining 20 percent freely allocated, by the recipient government, between the two sectors. As a result, for each and every department some allocations of the transfer between education and health care were ruled out from the outset, regardless of the jurisdiction's expenditure needs (e.g., no department could legally allocate 50 percent of the *situado* to health care).

Moreover, allocating the largest *situado* piece among the departments mainly on the basis of the actual expenditures in the education and health services in each jurisdiction invited the continuation, if not the deepening, of the existing regional inequalities in the distribution of the transfer, when assessed in per capita terms, with all the eligible beneficiaries counted. Meanwhile, for the smallest *situado* piece, being allocated among the departments in equal parts (aliquots), the connection between the rules of distribution and its designated uses appears remote. But because as a result of the aliquot the recipient jurisdictions were treated as equals (when in fact, they were not), it benefited the smallest jurisdictions in terms of population and fiscal capacity, allowing them to offset somewhat their disadvantages for the provision of education and health services.

A design directly linking the transfer uses to the distributive criteria while allowing for an equalization effect appears preferable.

## **8.2 AMENDMENTS TO THE *SITUADO FISCAL***

Just over two years after the 1991 constitution came into effect, it was amended for the first time. And the very first amendment was all about the fiscal constitution, particularly the *situado fiscal*,

one of the two constitutional intergovernmental transfers.<sup>136</sup> The amendment referred to the recipient governments. Barranquilla, a city on the Caribbean coast, was added to the list of recipients. The *situado* had traditionally been assigned to the departments and the country's capital, Bogotá, but the new constitution created the special districts of Cartagena and Santa Marta, as types of units of the local level, and entitled them as recipients of the *situado*. As a result of the amendment, Barranquilla, previously a municipality, became a special district as well, making it to the list of *situado*'s recipients. That the aliquot portion of the *situado* provided an incentive for municipalities to pursue the status of special districts, due to the associated increase in the transfer share, is witnessed by the subsequent flood of constitutional amendment proposals presented to congress with such a status-changing purpose.

### 8.3 AMENDMENTS TO THE *PARTICIPACIÓN MUNICIPAL*

In 1995 the *participación* was amended to widen the authorized uses of the transfer, allowing for a general purpose use principally in the case of small municipalities, while keeping the transfer's total size unchanged.<sup>137</sup> Recall that the *participación* in its original constitutional design was designated for social investment. Although Law 60 of 1993 took social investment principally to mean education and health care, it also stipulated that local governments could use a portion of the *participación* to finance their own operating costs, with the portion decreasing with the size of the municipality, as measured by the population and the rate of tax revenue growth. By the

---

<sup>136</sup> . COL. Legislative Act # 1, 1993.

<sup>137</sup> . COL. Legislative Act. # 1, 1995.

time the Constitutional Court ruled against the categorization of the local governments' operating costs as a type of social investment, it was already clear that many of the smaller municipalities could not afford their administrative expenses out of their own tax revenues, as a result of a combination of relatively low fiscal capacity and tax effort, let alone unfunded national mandates concerning the organization of local governments. Without a general purpose portion of the *participación* even their sheer existence as municipalities appeared in jeopardy. Proposals to encourage the consolidation, with their neighbors, of those small local jurisdictions experiencing fiscal stress did not go beyond consideration stage. In these circumstances, the national government opted for supporting the constitutional amendment which introduced the previously alluded to general purpose portion into the *participación*, thus authorizing the application of the transfer to cover administrative expenses, among other uses.

Another issue dealt with by the 1995 *participación* amendment relates to the rules for distributing the transfer among the recipient governments. The original 1991 distributive criteria we have referred to above was intended to come into full effect beginning in 1996. Between 1992 and 1995, deemed a transition period, a minimum share for each local government was sanctioned, where the minimum corresponded to the disbursement of a pre-1991 transfer known as *cesión del IVA*, measured in 1992 real terms.<sup>138</sup> During the transition period most of the *participación* was distributed applying the rules of the old transfer. Because the change of distribution rules, scheduled to take place in 1996, came to be considered too abrupt, the national and local governments (or at least many local governments hurt by the then approaching change) pushed for the prolongation of the transition period. The 1995 constitutional amendment set a

---

<sup>138</sup> . COL. Constitution, 1991, transitory art. 45.

new date for the full application of the new distributive criteria, i.e. the year 2000, while making an allowance for a smoother transition between the two sets of distribution rules.

#### **8.4 ARRIVAL OF THE *SISTEMA GENERAL DE PARTICIPACIONES***

What is probably the most far-reaching reform of the system of intergovernmental transfers originally adopted in 1991 took place in 2001. We have already described the *Sistema General de Participaciones* (SGP), as the product of the 2001 amendment was labeled, in chapter 5. Here some comments aimed at putting the SGP in the context of the amendments may suffice.

No longer was the overall size of the intergovernmental transfers determined, as it used to be, as a percentage of the national government's current revenues. By linking the size of the transfers to a moving average measure of the country's economic performance, the amendment immediate objective was to moderate the growth of the transfers with respect to the one envisioned in the original 1991 constitution, whose full effect in this particular regard was scheduled to take place starting in 2001. As intergovernmental transfers are accounted as central government' disbursements, the national budget deficit would be reduced as a result of the amendment. Indeed, the national government framed the rationale for the amendment in terms of fiscal and macroeconomic stability. Subnational governments and other stakeholders in the reform tended to counter that intergovernmental transfers were just a secondary determinant factor of the national budget deficit.

It would probably be correct to say that most of the attention paid to the 2001 amendment focused on the size of transfers. Yet, the amendment went far beyond this issue. In contrast to

the previous situation, where each level of government was constitutionally entitled to an individual transfer, the amendment did not specify the transfer entitlements by subnational level of government. By referring to the recipients generically as “territorial entities”, it made possible for the law to choose any combination of recipients between the departments and municipalities. As potential recipients, the departments and municipalities were put on equal footing. When congress opted for making the municipalities the default recipients of intergovernmental transfers, by means of Law 715 of 2001, it set the conditions for the departments to become little more than a broken link in the realm of fiscal intergovernmental relations. On the other hand, however, the 2001 amendment tended to reconcile the transfers’ distribution with their authorized uses, by mandating the application of distributive criteria more directly related to the jurisdictional expenditure needs in the education and health care sectors, as is the case of the size of the population covered and uncovered by the services. Whether or not congress (i.e., Law 715 of 2001) translated such criteria into a distribution formula capable of countering inter-jurisdictional inequality is another matter. Lastly, the 2001 amendment opened the way for the creation of a general purpose transfer (meant, apparently, for uses other than education and health care), which until then had not been constitutionally authorized.

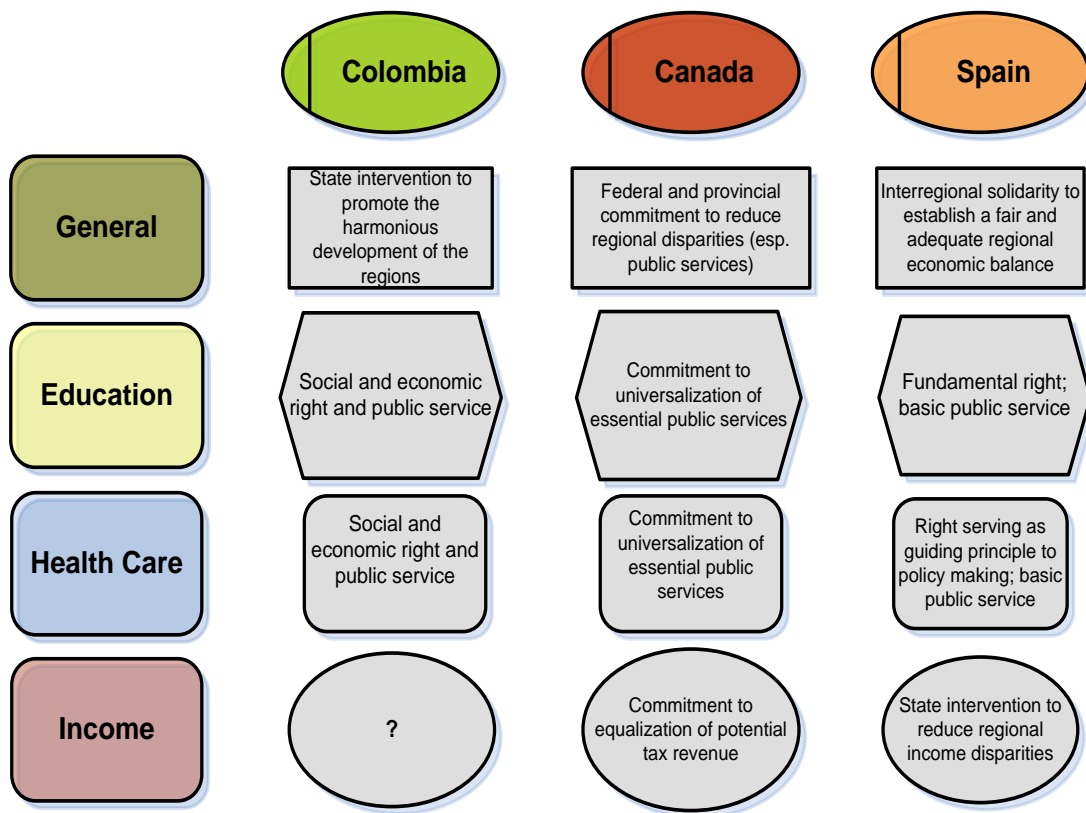


## **9.0 MAIN SIMILARITIES AND DIFFERENCES BETWEEN FISCAL CONSTITUTIONS**

The fiscal constitutions of Colombia, Canada and Spain assign core government responsibilities in the provision of education and health services to sub-central levels of government. But although decentralization of government responsibilities is, or has become, a common feature, Colombia is the only country in the group where a large share, if not the bulk, of such responsibilities has been assigned to the local level of government. The Colombian departments are called to play a subsidiary role. Unlike Colombia, in Canada and Spain the primary role in this regard belongs to the intermediate level of government.

In all three countries, universal coverage in basic education and health care is a declared public policy goal. But the legal status and form given to such goals differ between countries along legal tradition lines (Figure 9.1). In Colombia and Spain, two civil law tradition countries, education and health care rights are explicitly recognized in the respective written constitutions. In both cases these rights are in essence individual rights (in Colombia, for some purposes, such rights apply to households). In both cases, basic education is compulsory and free. In both Colombia and Spain, basic education and health care are deemed, by constitutional or other law, basic public services, again signaling their importance. Further to this, in Colombia public spending in these two areas has, according to an organic law, the status of social public spending, which gives it priority over other

types of spending. In Canada, where the common law tradition predominates, there is a constitutional commitment to reducing disparities in opportunities and to making essential services available to everyone. This commitment is contained in a section titled "equalization and regional disparities." While the constitution does not say it explicitly, it is generally acknowledged that education and health care, at least in their basic levels, are among the alluded opportunities and essential services.



**Figure 9-1: Constitutional approaches to regional disparities by country and government functions**

Judicial enforcement is enshrined in the written constitutions of both Colombia and Spain as a specific means to protect certain rights. In the Spanish case, this type of enforcement applies, for instance, to the right to education, a fundamental right. In the Colombian case, the written constitution

reserves the writ of protection (*acción de tutela*), a judicial enforcement instrument of last resort, for fundamental rights, which originally excluded, in principle, health care and education. However, pronouncements of the Colombian Constitutional Court have made such expedient available for the protection of education and health rights as well. At least in the case of health care it has done so by declaring it a fundamental right.

While in Colombia the transfers from the central to the intermediate level of government are specifically designated, largely by constitutional mandate, for education and health, in Canada and Spain, in addition to the transfers specific for social services (e.g., health transfer in Canada and the *Fondo de Suficiencia* in Spain), there are, as a result of explicit constitutional mandates, transfers to address interregional economic disparities. These are general purpose, fiscal equalization transfers in the Canadian case; their uses are limited to public investment in Spain. No such type of regional equalization transfer exists in Colombia. This is a big difference between the countries studied that transcends legal tradition and system of government boundaries.

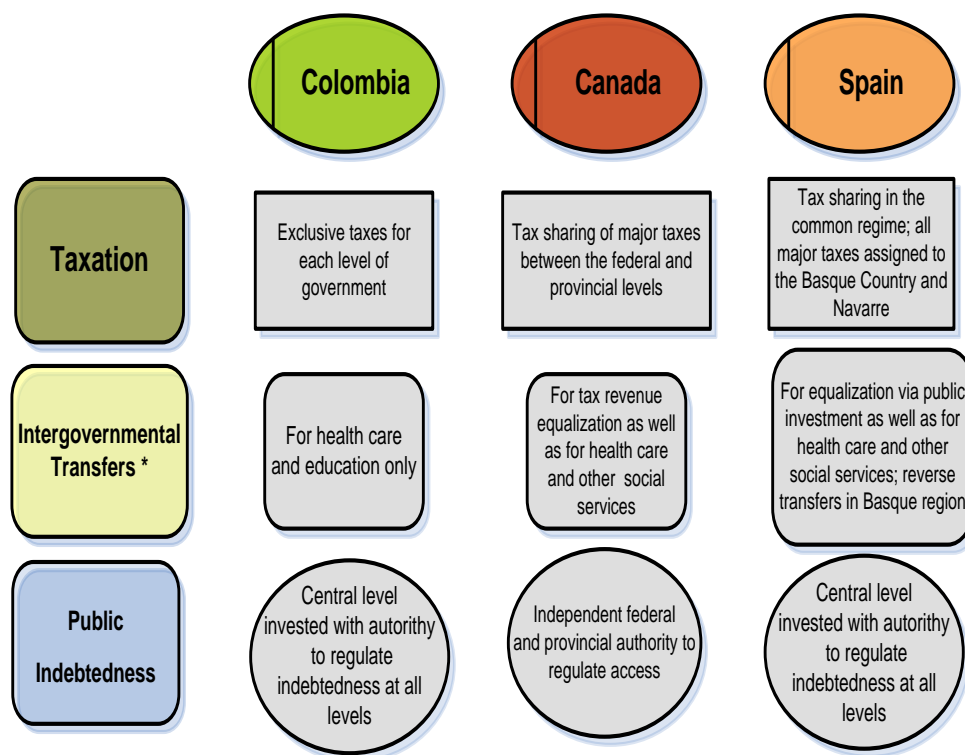
In Canada, in particular, the commitment to fiscal equalization has in practice taken the form of a program of revenue potential equalization for similar levels of tax effort, which benefits only the provinces that are below certain benchmarks in terms of fiscal capacity. In the Spanish case, the referred equalization role corresponds to the Interterritorial Compensation Fund, intended to finance public investment in the regions. The beneficiaries of the Compensation Fund are only economically lagging regions.

The central level of government is constitutionally endowed with the original power to tax in both Colombia and Spain (exceptions apply to the Basque Country and Navarre in the latter case). At the lower levels of government the power to tax is derived, that is, determined within limits by what the central level allows it to be. In contrast, in Canada the power to tax is constitutionally divided

between the federal and provincial levels of government. In other words, both levels are originally endowed with powers to tax.

Although not generally spelled out in the written constitutions, tax assignment, being a keystone of the fiscal state, can be thought of as part of the fiscal constitution, broadly understood. The type of taxes employed by the three countries is strikingly similar, particularly the ones of greatest revenue potential (e.g., income taxes, sales or value added taxes). But beyond the general point that all three countries have taxes assigned to each of their levels of government, there are significant differences between Colombia, on the one hand, and Canada and Spain, on the other, as regards the assignment of taxes.

While Colombia has tended to assign exclusive tax revenue sources to each level of government (e.g., income tax for the national level, registration tax for the intermediate level, the property tax for the local level), both Canada and Spain have in place tax sharing schemes between the central and intermediate levels of government (Figure 9.2). Tax base sharing is commonly found in Canada; in Spain there are instances of revenue sharing. It is important to note that such tax sharing schemes are different from intergovernmental transfers.



\* Between the central and the intermediate levels of government

**Figure 9-2: Legal approaches to government financing by country and fiscal channel**

Among the three countries surveyed, Spain exhibits the greatest asymmetry in the assignment of taxes within the intermediate level of government. The taxing powers of the autonomous communities of the common and special regimes differ substantially. The Basque Country and Navarre are by and large entitled, directly or through some of their component units, to the taxes that in the rest of Spain belong to the central level. In Canada, an important degree of asymmetry in the taxing powers and arrangements prevails between Quebec, on the one hand, and the rest of the provinces, on the other. In Colombia, tax assignment within the intermediate level of government is only marginally asymmetrical, compared with the Spanish and Canadian cases.

By constitutional mandate, in Colombia royalties on natural resource exploitation belong mainly to the producing subnational jurisdictions, both of the intermediate and local levels of government, while in Canada royalties belong to the provinces, that is to say, the intermediate level of government.

Income taxes in the three countries follow a nominally progressive pattern (i.e., a progressive tax rate schedule), tailored around the personal income tax. In theory, by virtue of this design the income tax can help offset regionally idiosyncratic economic cycles. However, the countercyclical potential of the Colombian income tax is likely to be greatly eroded by its relatively narrow coverage, compared with that of its Canadian and Spanish counterparts, resulting from the combination of tax exemptions, tax loopholes and tax evasion.

Each of the three countries has in place an intergovernmental health transfer. The Colombian and Spanish intergovernmental transfer systems provide funding for basic education. No specific transfer for basic education seems to exist in Canada. Colombia is the only country in the sample that does not have an intergovernmental transfer explicitly devoted to the moderation of the fiscal or income-related disparities between regions, other than those directly associated with health care and education.

In all three countries intergovernmental transfers originate in the respective central government (again, in Spain the exception being the Basque Country and Navarre). But there are differences as to the recipient governments. In Canada and Spain transfers flow to regional governments, whereas in Colombia transfers are divided among regional and local governments. The Basque Country and Navarre are a peculiar case, because they are the transferers to the central government. These reverse transfers of the Spanish autonomous communities of the special regime are, in essence, directly

proportional to the size of their economies, in effect precluding the possibility of first-round interregional redistribution, at least as far as the regional origin of the transfers is concerned.

A central formal objective given to health transfers in each of the three countries is to contribute to the provision of basic health services to all the inhabitants, regardless of their place of residence, an objective that implies but goes beyond inter-regional equalization in terms of such basic services.

The Colombian health transfer financially sanctions the operation of two parallel systems of health care delivery, created by legislation, one for those with sufficient and one for those with insufficient ability to pay health insurance. Health transfers are designed to subsidize those with insufficient ability to pay, if selected by a means-tested program, which entails the possibility of excluding eligible beneficiaries. Besides, the scope and quality of health services differ sharply under the two systems, being better for those with sufficient ability to pay. In contrast, in Canada and Spain the design of health transfers does not distinguish between beneficiaries by their ability to pay. In principle, the Canadian health transfer, like the social transfer, is allocated on an equal per capita basis among jurisdictions. Nonetheless, in Canada the definition of basic health services can vary between provinces.

Strikingly, unlike the Colombian case, where private health insurance is permitted, in Canada regulation calls for health insurance to be, as a rule, publicly administered, in a not-for-profit fashion, at least as far as basic health services are concerned. Moreover, in Canada hospitals and clinics are generally non-profit organizations. Yet all three countries rely on a combination of public, private and mixed ownership of hospitals and clinics for the delivery of basic health services.

Derived from the constitution, albeit not explicitly mentioned in it, Spain's Sufficiency Fund provides funding for a number of common competences of the autonomous communities, which

include but are not limited to education and health care. It is worth noting that the Inter-Territorial Compensation Fund and the Sufficiency Fund in principle cover only the regions of the common regime, that is, all regions except the Basque country and Navarre.

Regarding public indebtedness, in Colombia and Spain the central level of government is constitutionally vested with the power to regulate it for all levels of government, central and sub-central. Similar to the power to tax, in Canada this power is constitutionally divided between the federal and provincial levels, so that the federal level lacks the power to control provincial indebtedness. Colombian and Spanish law regulate the access of regional governments to credit through the golden rule (i.e., credit only for investment) and numerical limits, in terms, for example, of the debt service, as well as through administrative procedures in the case of foreign credit. In Canada, some provinces self-regulate their governments' access to loans.



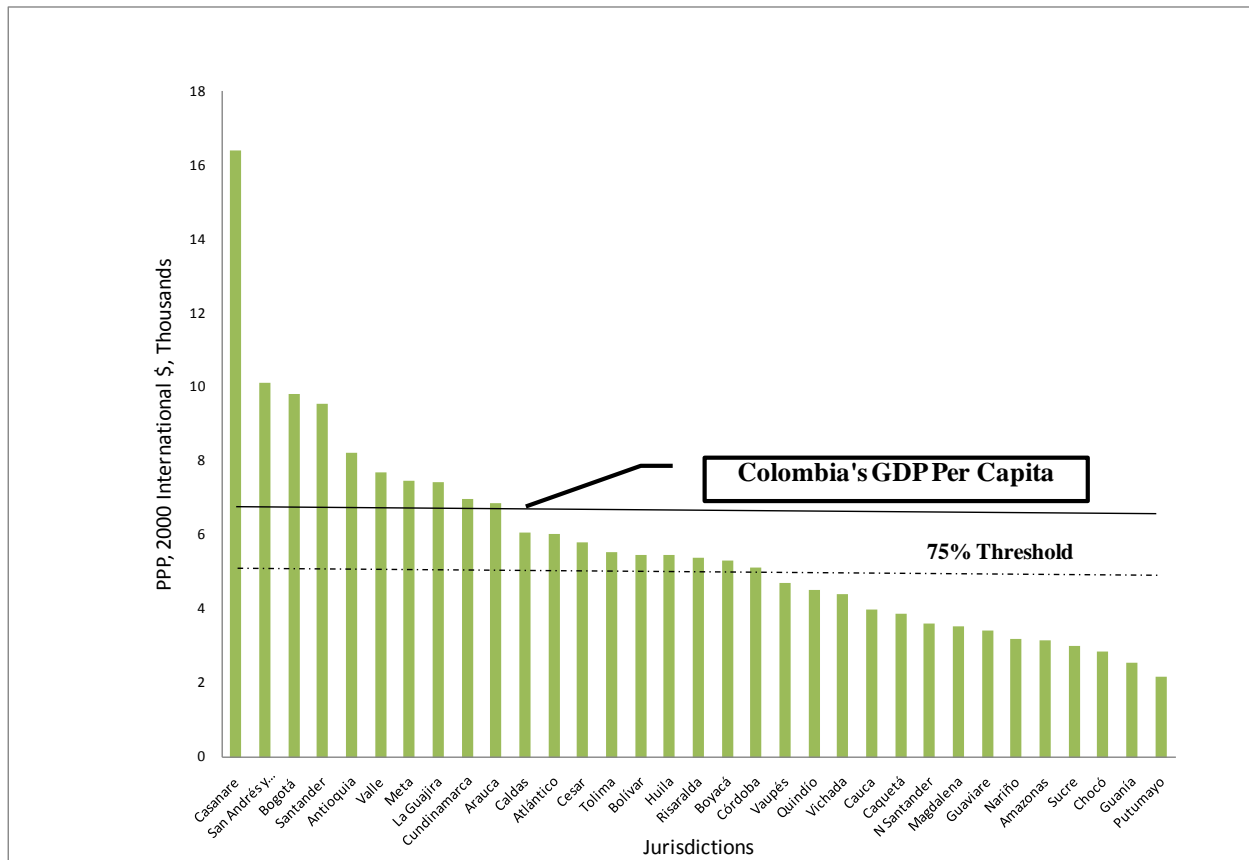
## **10.0 A QUANTITATIVE LOOK AT THE REGIONAL ECONOMIC DISPARITIES AND FISCAL IMBALANCES**

Besides providing a glimpse of how large the economic and fiscal disparities between regions in Colombia are, as well as of the size and composition of the country's tax and intergovernmental fiscal flows, this chapter takes a look at how such disparities and flows have evolved since the 1991 constitution came into effect and at the links connecting them. It also compares Colombia with Canada and Spain on a similar set of issues. One finding is worth reporting at the outset: Unlike what occurs in the Canadian and Spanish cases, fiscal disparities between the departments in Colombia or, more generally, the regional economic disparities other than those associated with education and health, have gone largely unaddressed by the 1991 constitution or, for that matter, the legal system in general. Further to this, if the Colombian intergovernmental transfer system has contributed to the reduction of interregional disparities in the provision of education and health services, it has done so increasingly more through the local level of government than through the intermediate (i.e., departmental) one.

## 10.1 A COLOMBIAN MIXED STORY

### 10.1.1 Levels and Trends

This section begins by looking at the disparities between departments in per capita GDP, a proxy indicator of a subnational jurisdiction's level of income as well as its fiscal capacity. As Dunford (2000, p. 72) notes, GDP is not only "a measure of the value of the goods and services produced in a region in a given period of time" but also a measure of the primary incomes (wages, profits, etc) generated in the production of such goods and services, "although the income that results does not necessarily accrue to a region's inhabitants." For a discussion of regional income disparities based on an indicator other than GDP, see Bonet and Meisel (2007). Figure 10.1 shows per capita GDP by department in 2005, ordered from highest to lowest. Casanare (whose relatively high per capita GDP is known to be due to the exploitation of oil), San Andrés and Providencia and Bogotá rank on top, while Chocó, Guainía and Putumayo are at the bottom of the per capita GDP scale. For 2005, ten out of thirty three jurisdictions register a GDP per capita higher than that of the country as a whole. In fourteen departments it is less than, or equal to, 75 percent of Colombia's per capita GDP, the threshold used here to identify low income, low fiscal capacity jurisdictions. The other seven departments could be described as middle income, middle fiscal capacity jurisdictions.



**Figure 10-1: GDP per capita by Colombian department, 2005**

Source: Original data on GDP per capita from DANE, *Cuentas Nacionales de Colombia*, [www.dane.gov.co](http://www.dane.gov.co).

The frequency distribution of GDP per capita across departments has not changed much since 1990, as Table 10.1 illustrates. The number of departments whose per capita GDP falls within the low income, low fiscal capacity range has averaged 15 in the period 1990-2005, that is, 45 percent of the jurisdictions of the intermediate level of government, with the number of lagging departments under such criterion reaching a minimum of 13 and a maximum of 18. As it happens, the 75 percent threshold is used by the European Union to identify lagging regions, the main beneficiaries of the EU's regional aid.

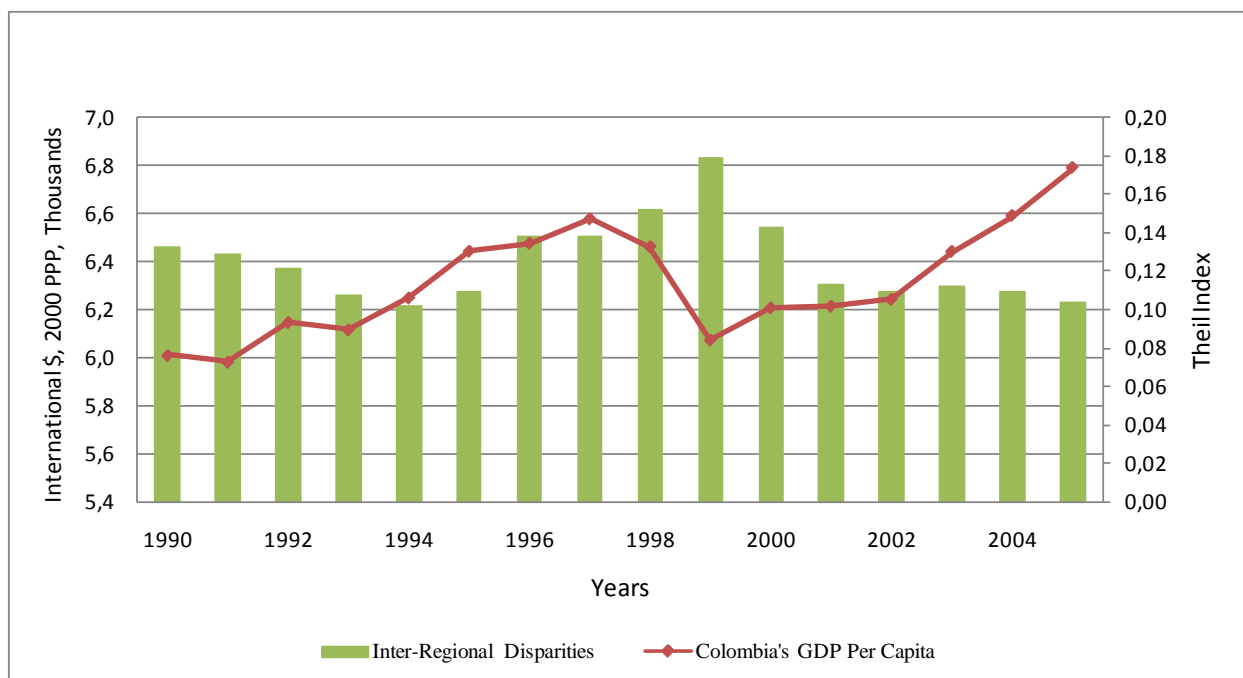
**Table 10-1: Frequency distribution of Colombian departments' GDP per capita, selected years**

| GDP Per Capita Range   | 1990                               | 1995 | 2000 | 2005 |
|--|------------------------------------|------|------|------|
|  | Number of Departments in the Range |      |      |      |
| $i \leq 75\%$ of Colombia's GDP per capita                               | 13                                 | 15   | 14   | 14   |
| $75\%$ of Colombia's GDP per capita $< i \leq$ Colombia's GDP per capita | 10                                 | 9    | 9    | 9    |
| $i >$ Colombia's GDP per capita  | 10                                 | 9    | 10   | 10   |

Source: Original data on GDP per capita from DANE, *Cuentas Nacionales Departamentales*, [www.dane.gov.co](http://www.dane.gov.co).

To give a flavor of the overall inequalities between departments in a given economic or fiscal dimension the coefficient of variation (CV) and, in some instances, the Theil index, in the version presented by Rey (2004), are employed here. The higher the scores yielded by the CV and the Theil index, the greater the degree of interregional inequality. For an explanation of the properties of these two measures of inequality, see, for instance, Cowell (1995).

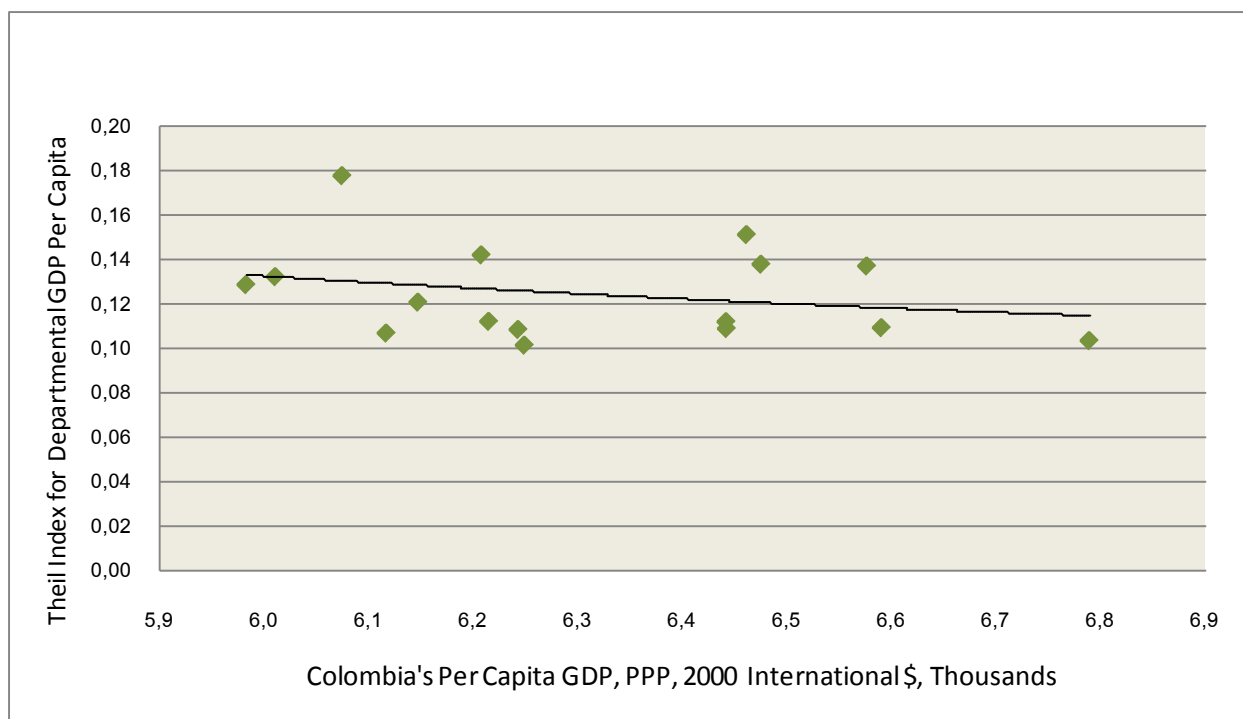
Overall per capita GDP disparities between the Colombian departments for the period 1990-2005, as measured by the Theil index, are depicted in Figure 10.2, together with the country's per capita GDP. Such disparities reveal a tendency to fall in the first half of the 1990s, a period of economic expansion. In the second half of that decade an upward trend in regional inequality of GDP per capita becomes apparent, especially as the economy fell into a deep recession. It should be noted that the core of the intergovernmental transfer system envisioned in the 1991 constitution came into nearly full effect only in 1994. The first half of the 2000s witnessed, along with an economic recovery, the reduction in overall inter-regional per capita GDP disparities, enough only to arrive at the level of inequality already observed in the mid-1990s.



**Figure 10-2: Level of income and inter-regional income disparities in Colombia, 1990-2005**

Source: Original data on departmental GDP from DANE, *Cuentas Nacionales Departamentales*, [www.dane.gov.co](http://www.dane.gov.co). Original data on Colombia's per capita GDP at PPP from The World Bank, *World Development Indicators* database, [www.worldbank.org](http://www.worldbank.org).

There is some evidence to suggest that the country's economic performance and the disparities in per capita GDP between departments are not independent of one another. As Figure 10.3 shows, over the period 1990-2005 the years of higher (lower) per capita GDP tend to be the years of lower (higher) inter-departmental per capita GDP disparities as well (correlation coefficient of -0,26). The direction of causality between the two variables could go both ways: Economic growth would favor the reduction of interregional income disparities and lesser interregional income inequalities would propel economic growth. Nevertheless, economic growth alone is unlikely to be sufficient to achieve large reductions in regional economic disparities.



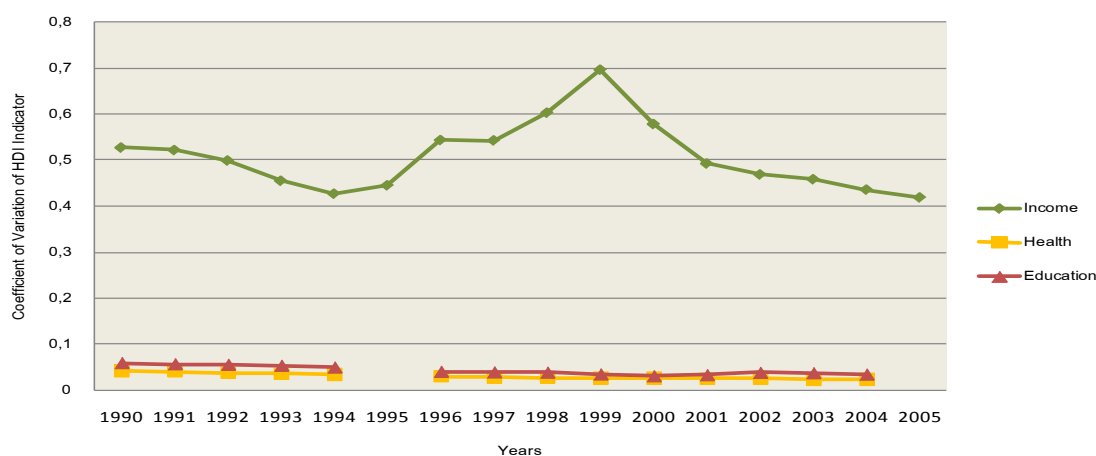
**Figure 10-3: Trend in the relationship between level of income and inter-regional income disparities in Colombia, 1990-2005**

*Source:* Original data on departmental GDP from DANE, *Cuentas Nacionales Departamentales*, [www.dane.gov.co](http://www.dane.gov.co). Original data on Colombia's per capita GDP at PPP from The World Bank, *World Development Indicators* database, [www.worldbank.org](http://www.worldbank.org).

To measure the regional outcomes in education and health, the respective components of the conventional Human Development Index (HDI) are employed here. The education indicator in the conventional HDI is a combination of the gross enrollment ratio and the adult literacy rate, whereas the health indicator is based on the life expectancy at birth (Anand and Sen 2003). For a detailed analysis of the HDI by Colombian regions, see Programa Nacional de Desarrollo Humano (2004).

For the whole 1990-2005 period, the disparities in GDP per capita between the Colombian departments have been considerably wider than the disparities in education and health outcomes, as measured by the coefficient of variation of the corresponding indicator in the

HDI (Figure 10.4).<sup>139</sup> Perhaps more important, while the disparities in GDP per capita do not show a consistent tendency to recede, the disparities in education and health outcomes have gone down more or less continually. From a policy standpoint, these results suggest that countering Colombia's regional disparities in fiscal capacity and income per capita is particularly demanding. But how have such developments in education and health been possible in the face of the observed drift in the departments' per capita GDP, considering that the disparities in fiscal capacity associated with it can translate into an uneven access to the revenues needed for financing the provision of social services?



**Figure 10-4: Inter-regional disparities in three dimensions of development in Colombia**

Source: Original data on the health and education indices, Programa Nacional de Desarrollo Humano DNP/PNUD database (available by request). Original data on GDP for the income indicator, DANE, Cuentas Nacionales Departamentales, [www.dane.gov.co](http://www.dane.gov.co).

Note: Excluding new departments.

<sup>139</sup> There may be differences in the intrinsic properties of the variables which, at least in part, may lead to divergent patterns of variability (e.g., Is income per capita intrinsically more variable than life expectancy?).

The evidence suggests that in such outcomes there may be a part played by the fiscal institutions set forth in the 1991 constitution, particularly the system of intergovernmental transfers. To see why and how, it is helpful, if not necessary, to first take a look at the division of tax revenues between levels of government, an issue which, while dealt with in the constitution only marginally, provides the background for the functioning of the constitutionally enshrined intergovernmental transfers.

Colombia's tax assignment favors the centralization of tax revenues. As Table 10.2 shows, the overall level of taxation in Colombia, expressed as the share of tax revenues in national GDP, reached 18.4 percent in 2005, compared to 10.9 in 1990. Most of the rise in tax revenues during the period accrued to the central and local levels of government. At least since 1990, the central government has consistently collected more than 80 percent of total tax revenues (e.g., 83 percent in 2005). Gaining 3 percentage points in revenue share with respect to 1990, the local level of government comes second with 9 percent of the total in 2005, followed by the departmental level with just 8 percent, losing some ground. Departmental tax revenues have hardly, if at all, exceeded 1.5 percent of GDP. From a tax revenue viewpoint, the departments emerge as the weakest level of government in Colombia.



**Table 10-2: Level of taxation by tier of government in Colombia, selected years**

| Tier of Government         | 1990                         | 1995 | 2000 | 2005 | 1990                          | 1995 | 2000 | 2005 |
|----------------------------|------------------------------|------|------|------|-------------------------------|------|------|------|
|                            | Tax revenues share in GDP, % |      |      |      | Share in total tax revenue, % |      |      |      |
| Central Government         | 8,9                          | 9,4  | 11,2 | 15,3 | 82                            | 83   | 81   | 83   |
| Departmental Governments * | 1,3                          | 1,0  | 1,3  | 1,4  | 12                            | 9    | 9    | 8    |
| Local Governments **       | 0,7                          | 0,9  | 1,4  | 1,7  | 6                             | 8    | 10   | 9    |
| Total Tax Revenue          | 10,9                         | 11,3 | 13,9 | 18,4 | 100                           | 100  | 100  | 100  |

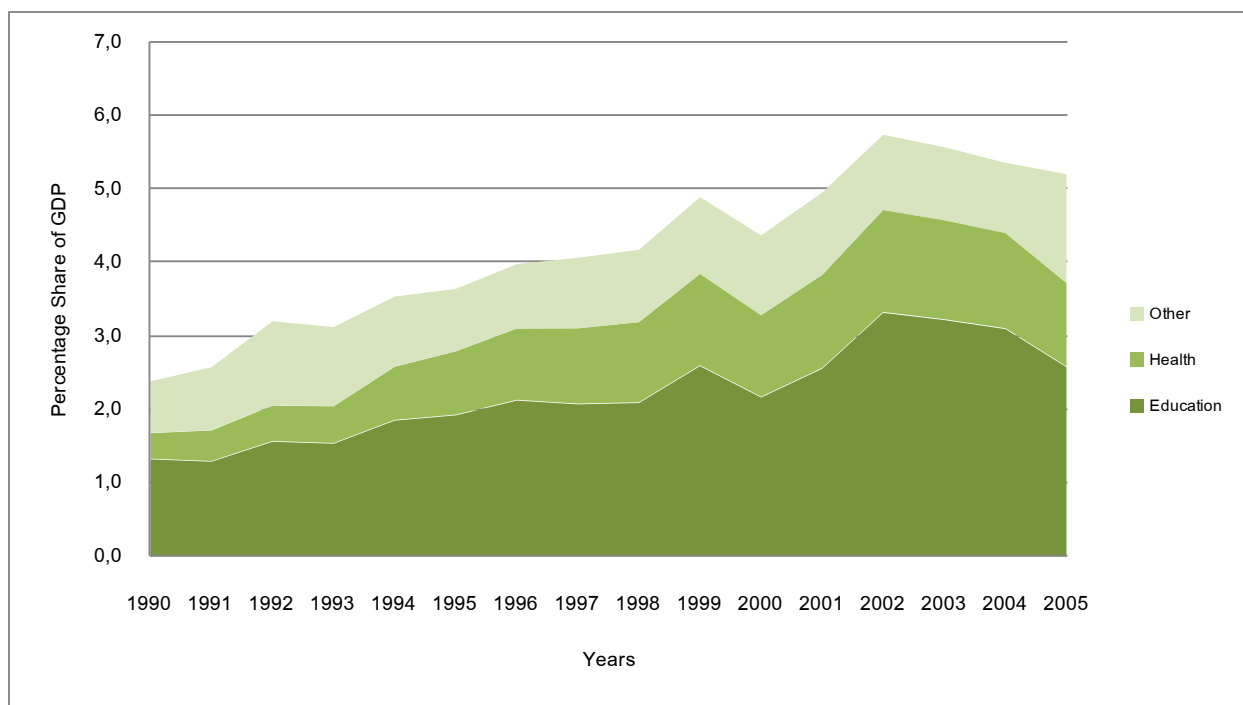
Source: Original data on tax revenues from Banco de la República, Finanzas Públicas database (available by request). Original data on GDP from DANE, Cuentas Nacionales Departamentales, [www.dane.gov.co](http://www.dane.gov.co).

\*/ Including Bogotá's departmental taxes.

\*\*/ Excluding Bogotá's departmental taxes

Since the 1991 constitution itself largely reassigned the responsibility of ensuring the provision of health and education services from the national to the subnational governments, the high concentration of tax revenues at the national level of government ends in a vertical fiscal imbalance, with the spending responsibilities of subnational governments, expressed in monetary terms, exceeding their potential revenue resources, exclusive of intergovernmental transfers.

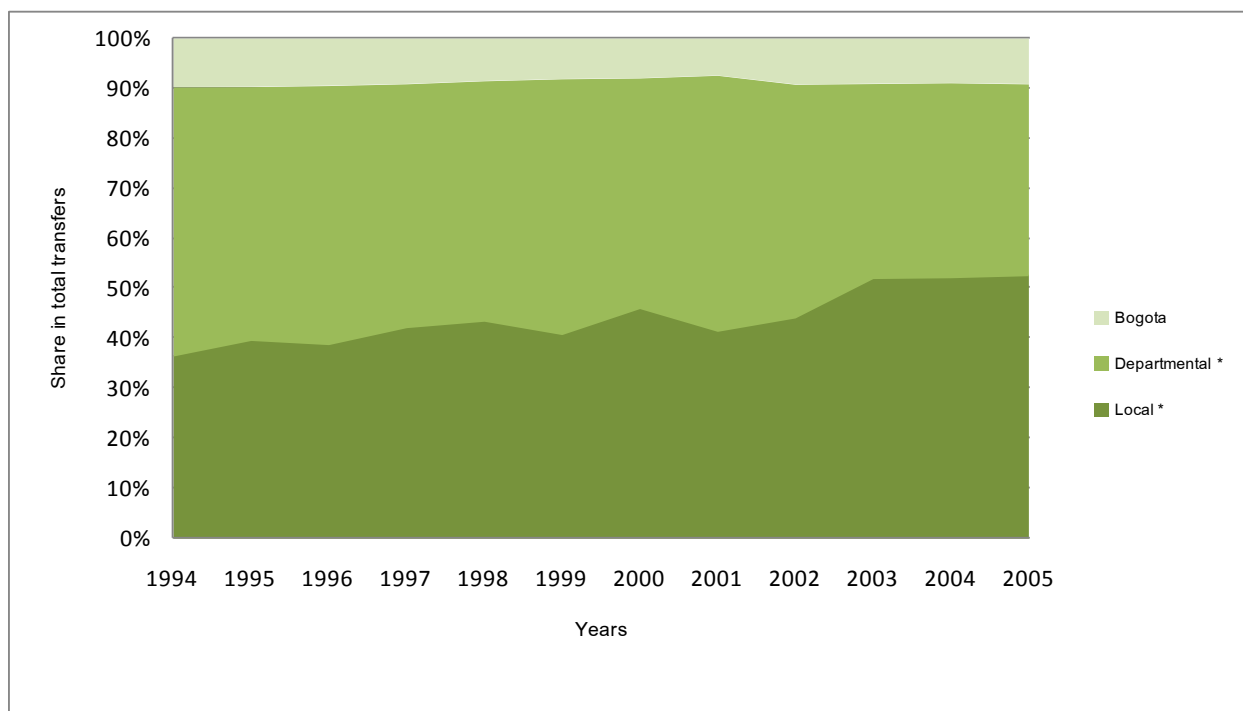
Much as a result of mandates ingrained in the original 1991 constitution and in some of its subsequent amendments, the size of transfers from the Colombian central government to the subnational governments, as a share of GDP, have indeed tended to increase, going from 2.4% in 1990 to 5.2% in 2005, after reaching their peak in 2002 with 5.7% (Figure 10.5). Both education and health care have benefited from the increase in intergovernmental transfers, but education has remained by far the most important allocation throughout the period. The constitutional mandated increases in intergovernmental transfers serve as a means for counteracting the vertical fiscal imbalance.



**Figure 10-5: Colombia's intergovernmental transfers by purpose, departmental and local aggregate**

*Source:* Original data from Departamento Nacional de Planeación, *Finanzas Públicas Territoriales* database, [www.dnp.gov.co](http://www.dnp.gov.co).

The Colombian local governments have gradually become, as Figure 10.6 illustrates, the largest recipients and executors of intergovernmental transfers under the 1991 constitution (53 percent of the total in 2005), at the expense of the departments (38 percent in the same year). Bogotá, whose transfers from the central government are hard to classify from a level of government perspective, stands alone in the figure. There has then been a trend towards the municipalization of fiscal decentralization, thereby diminishing the scope for interregional fiscal equalization policies conducted through the departments, though it does not, by itself, lead to, or precludes the possibility of, less unequal interregional health and education outcomes.

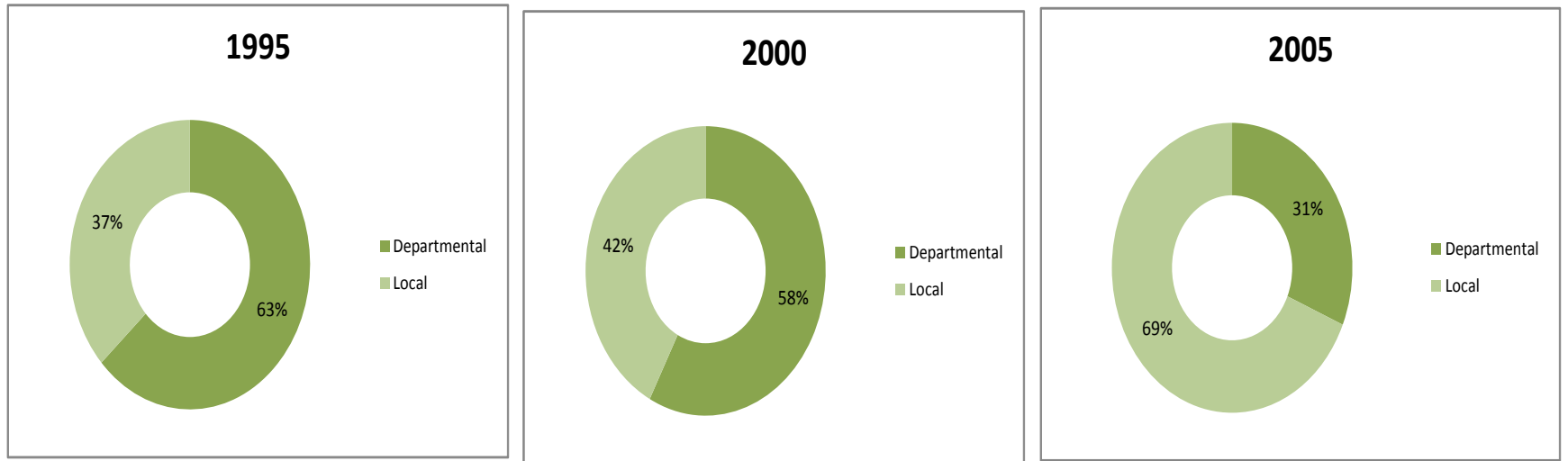


**Figure 10-6: Colombia's intergovernmental transfers by level of government**

*Source:* Original data from Departamento Nacional de Planeación, Finanzas Públicas Territoriales database, [www.dnp.gov.co](http://www.dnp.gov.co).

\*/ Excluding Bogotá.

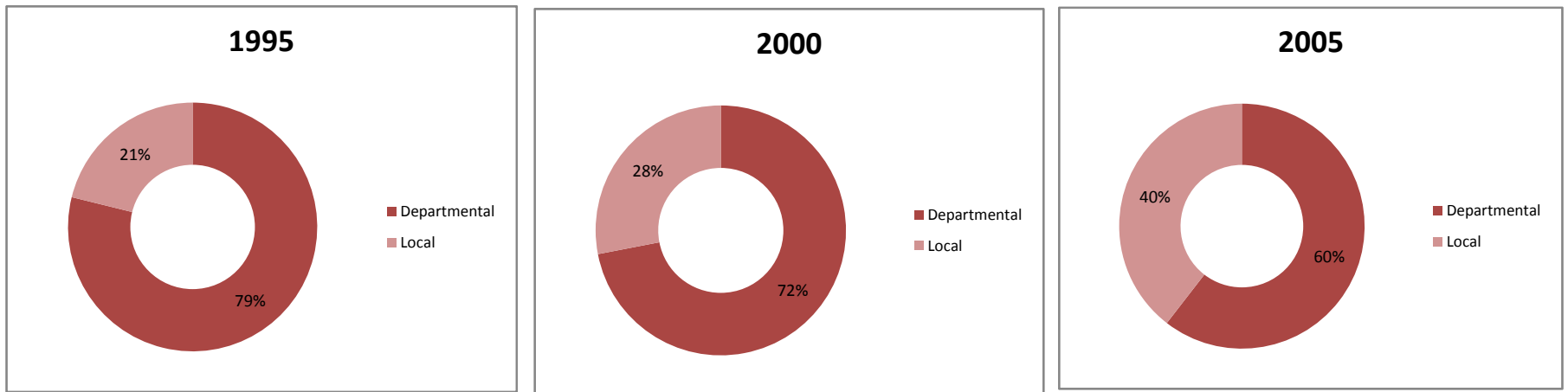
The shift in the allocation of transfers by level of government has been particularly drastic in the health sector, where the local governments came to account for nearly 70 percent of the sector's transfers in 2005, somewhat less than doubling their 1995 share (Figure 10.7). Notwithstanding that the intermediate level of government has remained the main recipient of education transfers, its role has tended to diminish considerably since the mid-1990s (Figure 10.8), and is set to go on diminishing by legal mandate.



**Figure 10-7: Colombia's intergovernmental health transfers by level of government, percentage share of the total in selected years**

*Source:* Original data from Departamento Nacional de Planeación, *Finanzas Públicas Territoriales* database, [www.dnp.gov.co](http://www.dnp.gov.co).

*Note:* Excluding Bogotá.



**Figure 10-8: Colombia's intergovernmental education transfers by level of government, percentage share of the total in selected years**

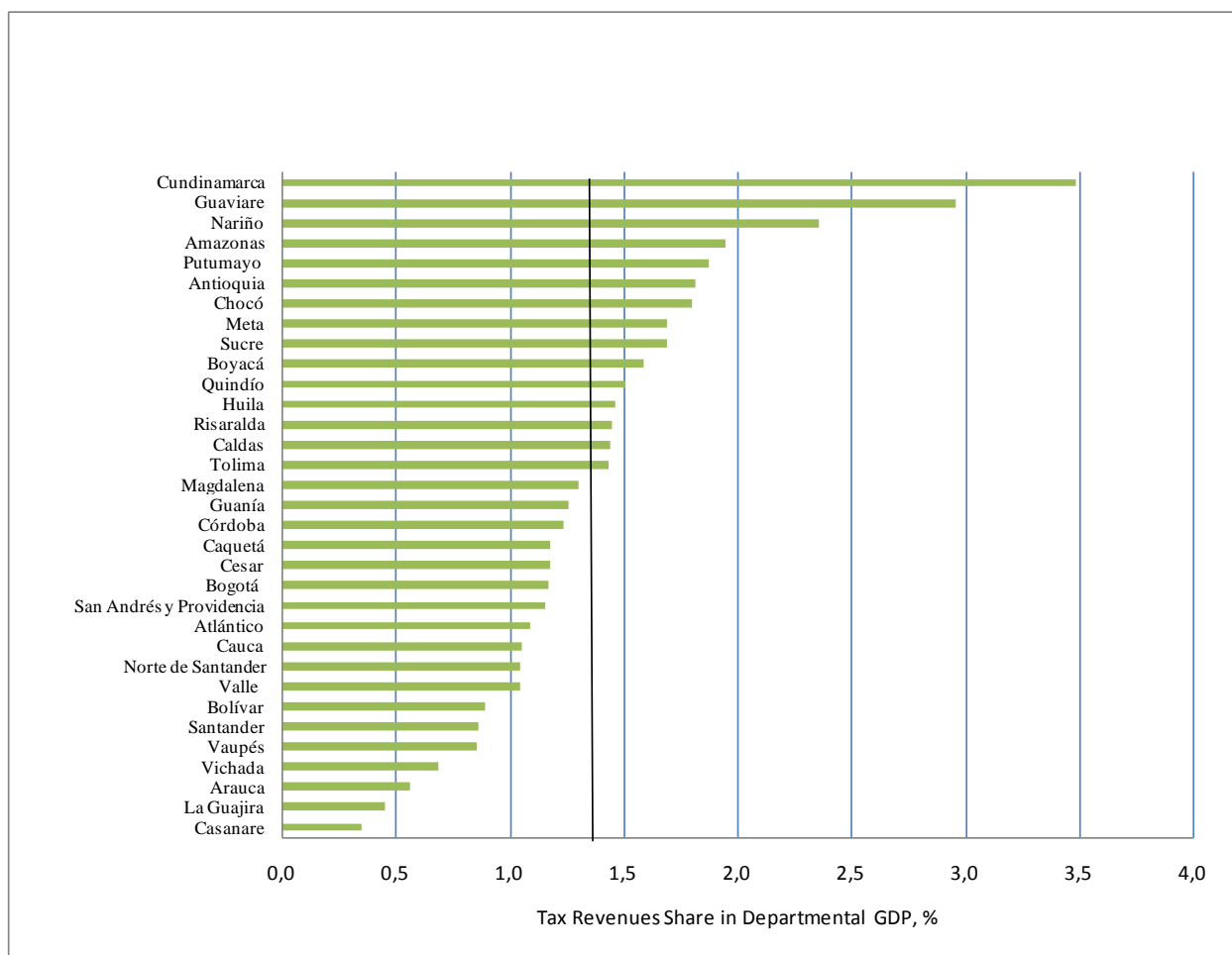
*Source:* Original data from Departamento Nacional de Planeación, *Finanzas Públicas Territoriales* database, [www.dnp.gov.co](http://www.dnp.gov.co).

*Note:* Excluding Bogotá.

On the other hand, the disparities in levels of taxation between departmental governments look relatively sharp. For example, in 2005, as Figure 10.9 shows, the governments of seven departments, from Bolivar to Casanare, collected less than 1 percent of their corresponding GDP in taxes, well below Cundinamarca, the leading department in this regard, with 3.5 percent.<sup>140</sup> Strikingly, the three lowest taxing jurisdictions, Casanare, La Guajira and Arauca, are all rich in natural resources and are entitled to royalties for their exploitation. Even excluding these oil and coal rich departments, the differences in levels of taxation remain notable. Since in Colombia the departmental tax bases and rates are as a rule uniform countrywide, such disparities in levels of taxation essentially arise from departmental differences in fiscal capacities and tax enforcement.

---

<sup>140</sup> / Note, however, that the departmental tax powers of Cundinamarca, its capital, Bogotá, and San Andrés differ from those of most other departments. This peculiarity affects somewhat the comparability of the levels of taxation.

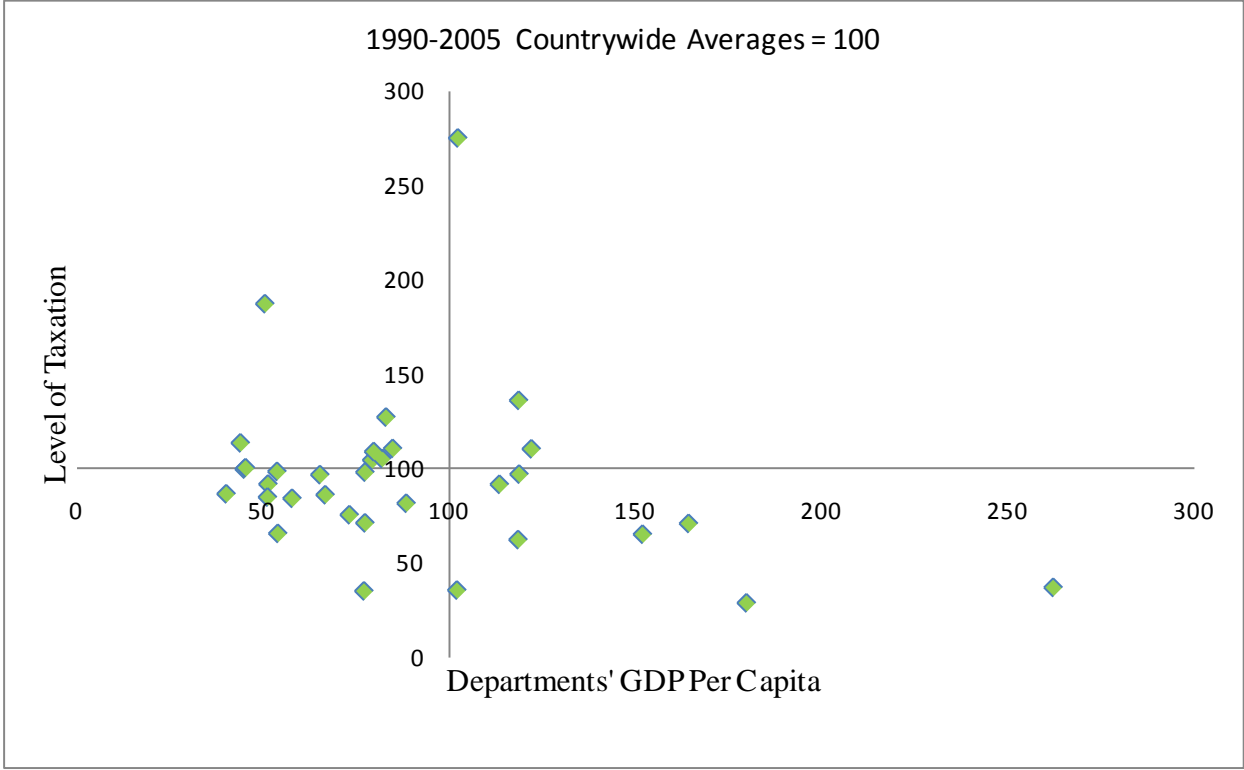


**Figure 10-9: Level of taxation by departmental government in Colombia, 2005**

Source: Original data on tax revenues from Banco de la República, *Finanzas Públicas* database, [www.banrep.gov.co](http://www.banrep.gov.co). Original data on GDP from DANE, *Cuentas Nacionales Departamentales*, [www.dane.gov.co](http://www.dane.gov.co). Note: Bogotá's and San Andrés' figures refer only to the typically departmental taxes they collect.

Figure 10.10 illustrates the relationship between fiscal capacity, measured here by per capita GDP, and level of taxation (for departmental taxes only) across departments. Relative to the corresponding countrywide average for the period 1990-2005, the largest number of departments turns out to be low fiscal capacity, low taxing jurisdictions (bottom left quadrant). Some low fiscal capacity departments manage to make a higher than average tax effort (top left quadrant). Among the high fiscal capacity departments, the majority are low taxing jurisdictions

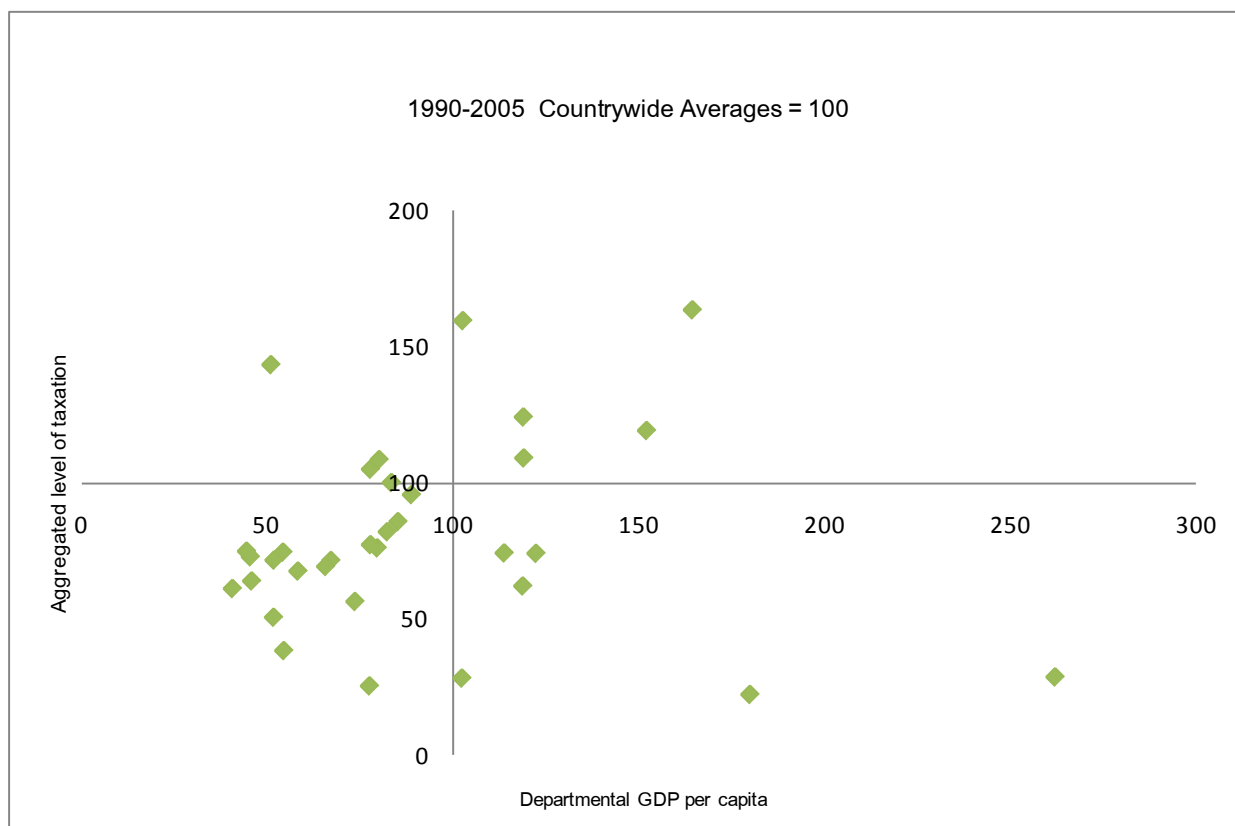
(bottom right quadrant). A similar pattern emerges when the departmental and local tax revenues are consolidated into the subnational tax revenues of the respective jurisdictions (Figure 10.11).



**Figure 10-10: Departmental level of taxation and fiscal capacity by jurisdiction in Colombia**

Source: Original data on tax revenues from Banco de la República, *Finanzas Públicas* database (available by request). Original data on GDP from DANE, *Cuentas Nacionales Departamentales*, [www.dane.gov.co](http://www.dane.gov.co).





**Figure 10-11: Subnational level of taxation and fiscal capacity by jurisdiction in Colombia**

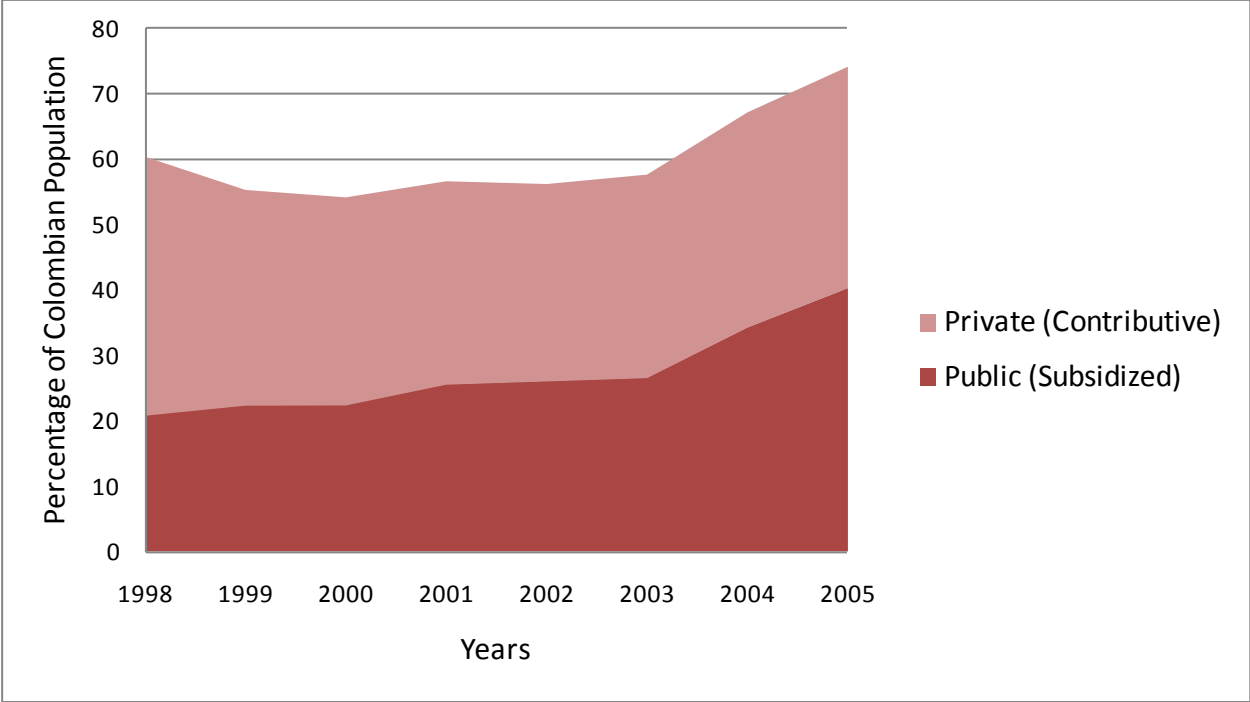
*Source:* Original data on tax revenues from Banco de la República, *Finanzas Públicas* database (available by request). Original data on GDP from DANE, *Cuentas Nacionales Departamentales*, [www.dane.gov.co](http://www.dane.gov.co).

*Note:* The level of taxation is calculated for the aggregate of departmental and local revenues by department.

Intergovernmental transfers appear to have contributed somewhat to the trending decrease in regional disparities in education and health outcomes mainly by partly financing a generally wider coverage of basic services in those areas, whatever their quantity and quality may be (recall that the coverage of services is an important criterion for the distribution of intergovernmental transfers among subnational governments).

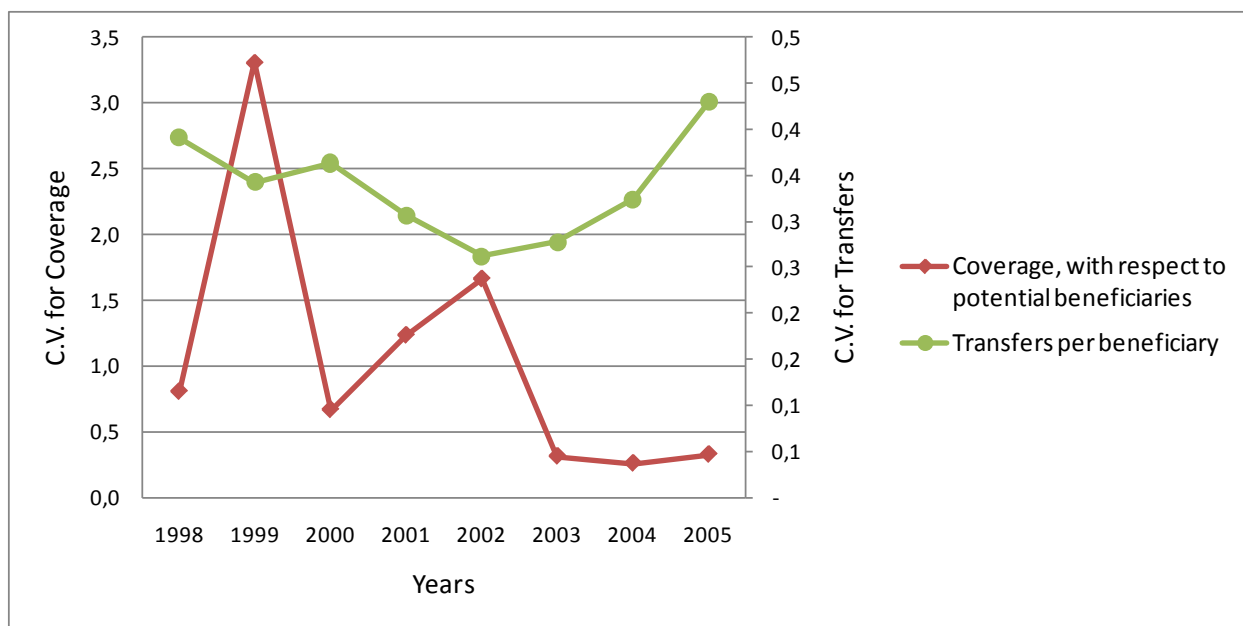
As Figure 10.12 shows, countrywide health insurance coverage climbed from 60 percent of the total Colombian population in 1998 to 74 percent in 2005 driven by the expansion of the subsidized regime, largely financed out of intergovernmental transfers. Meanwhile, interregional

disparities in the coverage of publicly funded health insurance have tended to recede since the late 1990s. Note, however, that the reduction in the regional disparities in access to insurance was not always accompanied by a fall in the regional disparities in the amount transferred per beneficiary of the subsidized regime (Figure 10.13). Between 2002 and 2005, for instance, such disparities moved in opposite directions. What is then behind the drop in the regional differences in life expectancy in Colombia? It appears that access to health insurance has been a more important factor than the amount allocated to subnational governments to cover the insurance fees. Because at relatively high levels life expectancy tends to increase at a diminishing rate, access to health services, as opposed to no access at all, may have helped the lagging departments to catch up with the leading ones.



**Figure 10-12: Health insurance coverage by type of financing in Colombia**

Source: Original data from Ministerio de Protección Social, database at [www.minproteccionsocial.gov.co](http://www.minproteccionsocial.gov.co).

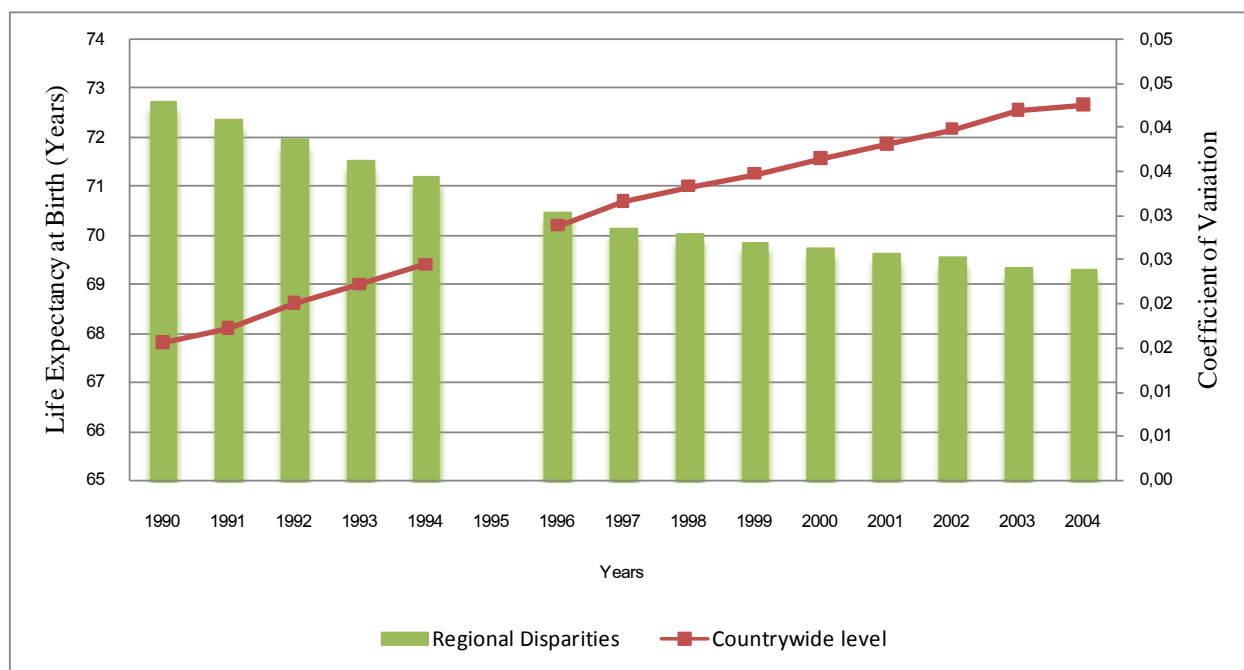


**Figure 10-13: Colombia’s publicly funded health insurance: Regional disparities in coverage and in intergovernmental transfers**

*Source:* Original data from Ministerio de Protección Social, database at [www.minproteccionsocial.gov.co](http://www.minproteccionsocial.gov.co).

There are signs that the provision of health care to Colombians has experienced non-negligible improvements since the early 1990s. Life expectancy at birth reached 72.7 years in 2004, almost 5 years longer than in 1990, while showing a sustained increase in the intervening years (Figure 10.14). According to a study by the Programa Nacional de Desarrollo Humano (2004, p. 15) , “The path of life expectancy [in Colombia] reflects important demographic and epidemiologic changes. The advances in controlling contagious diseases, due to improvements in environmental sanitation, in health education and in prenatal and child care, have superseded the increase in mortality caused by violence.” Yet, as the study emphasizes, the health conditions are rather uneven across departments. In 2004 a person born in Chocó, the department at the bottom of the life expectancy scale, was expected to live 67.6 years, compared to 74 years in

Bogotá, the jurisdiction with the highest life expectancy.<sup>141</sup> Even so, as we have seen, overall interregional disparities in life expectancy have been decreasing more or less consistently over the same period.



**Figure 10-14: Countrywide level and regional disparities in life expectancy in Colombia**

*Source:* Original data on life expectancy from *Programa Nacional de Desarrollo Humano* DNP/PNUD database (available by request).

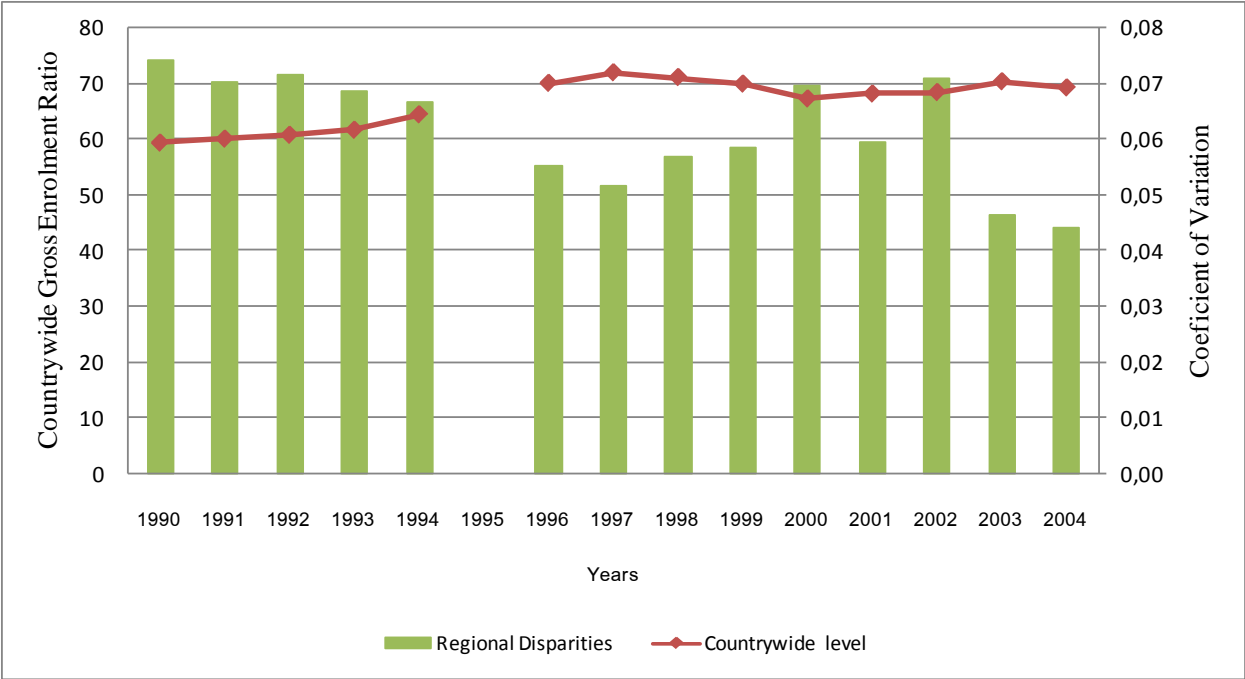
*Note:* Excluding new departments.

In the field of education there are similar signs. The 1980s and 1990s have been characterized as decades of achievements in terms of coverage. As a result, according to Vélez (2003, p. 537), today Colombians of school age and over are expected to get, on average, “a formal education of about 7 years, a substantial improvement of 2.4 years with respect to the situation in the 1970s.” While remaining a public policy challenge of great magnitude (especially concerning the situation of children in rural areas), the inequalities in access to basic education

---

<sup>141</sup> / As far as life expectancy is concerned, the so-called new departments are not included due to data availability limitations.

between departments, as measured by the coefficient of variation of the gross enrollment ratio, have tended to go down, as illustrated in Figure 10.15. The fact that during the economic recession of 1999-2001, the lessening of such interregional inequalities suffered a setback, accompanied by a descent in overall access to education, is a reminder of the influence of factors other than the fiscal institutions.



**Figure 10-15: Access to education in Colombia: Countrywide level and regional Disparities**

*Source:* Original data on gross enrollment from Programa Nacional de Desarrollo Humano DNP/PNUD database (available by request).

*Note:* Excluding new departments.

**10.1.2 Formal Models for Adaptation and Robustness**

Panel models exemplifying a strategy to evaluate the degree of regional equalization, if any, embedded in the Colombian system of intergovernmental transfers are presented below. The

basic idea of the evaluation strategy is to see whether, or to what extent, the actual distribution of transfers is consistent with some equalizing distributive yardstick (For a description of the underlying logic of the strategy, see Box 10.1).

- Education transfer (departmental *and* local, consolidated per jurisdiction)

- $T^{E,I}_{i,t} = \beta_1 + \beta_2 ER_{i,t-1} + \beta_3 LT_{i,t-1} + \beta_4 GDP_{PC\ i,t-1} + \varepsilon_{it}$

- $T^{E,GDP}_{i,t} = \beta_1 + \beta_2 ER_{i,t-1} + \beta_3 LT_{i,t-1} + \beta_4 GDP_{PC\ i,t-1} + \varepsilon_{it}$

Where  $T^{E,I}_{i,t}$  is the education transfer to departmental and local governments of department  $i$  in period  $t$  per student enrolled in basic public education;  $T^{E,GDP}_{i,t}$  is the total education transfer to jurisdiction  $i$  expressed as a share of its GDP in period  $t$ ; with the same meaning for  $i$  and  $t$ , ER is the gross enrollment ratio, LT is the subnational level of taxation (departmental plus local level), and  $GDP_{PC}$  is per capita GDP, adjusted for inflation. All variables, except for  $T^{E,GDP}_{i,t}$ , are standardized with respect to the national mean. The lags in the independent variables account for the fact that the actual distribution of transfers in a given year is generally done using data from the preceding period.

- Health transfer (departmental *and* local, consolidated per jurisdiction)

- $T^{H,I}_{i,t} = \beta_1 + \beta_2 CO_{i,t-1} + \beta_3 LT_{i,t} + \beta_4 GDP_{PC\ i,t-1} + \varepsilon_{it}$

- $T^{H,GDP}_{i,t} = \beta_1 + \beta_2 CO_{i,t-1} + \beta_3 LT_{i,t} + \beta_4 GDP_{PC\ i,t-1} + \varepsilon_{it}$

- $T^{H,GDP}_{i,t} = \beta_1 + \beta_2 HI_{i,t-1} + \beta_3 LT_{i,t} + \beta_4 GDP_{PC\ i,t-1} + \varepsilon_{it}$

Where  $T^{H,I}_{i,t}$  is the health transfer to departmental and local governments of department  $i$  in period  $t$  per person affiliated to the subsidized regime;  $T^{H,GDP}_{i,t}$  is the total health transfer to jurisdiction  $i$  expressed as a share of its GDP;  $CO_{i,t-1}$  is the coverage of the subsidized regime with respect to its eligible or potential beneficiaries; and  $HI_{i,t-1}$  is the health index in the Human

Development Index.  $T^{H, I}_{i,t}$ ,  $CO_{i,t-1}$  and  $HI_{i,t-1}$  are standardized with respect to the national mean. The other variables are defined as in the education models above.

Tables 10.3 and 10.4 summarize the results of the panel models. As for education, neither the gross enrollment ratio (an indicator of expenditure needs) nor the level of taxation (an indicator of fiscal capacity utilization) significantly affect intergovernmental transfers per student ( $T^{E, I}$ ), per jurisdiction. For the size of the education transfers ( $T^{E, GDP}$ ) per jurisdiction, however, the higher the gross enrollment ratio or the higher the level of taxation, the higher the size of the transfer, as expected for equalization purposes. Yet, GDP per capita yields a non-significant coefficient, regardless of how the education transfers per jurisdiction are defined, so that fiscal capacity would not be an influential distributive factor. The explanatory power of this model is low ( $R^2=0.15$ ). Note that the time spans of the two models intersect but, due to data availability, are not the same.

**Table 10-3: Panel models for Colombia's education transfers**

| <b>Period</b>             | <b>1996-2005<sup>a</sup></b>  | <b>1994-2005<sup>a</sup></b>       |
|---------------------------|-------------------------------|------------------------------------|
| <b>Dependent variable</b> | $T^{E, I}_{i,t}$              | $T^{E, GDP}_{i,t}$                 |
| $ER_{i,t-1}$              | 0,01<br>(0,07)<br>[0,149]     | 0,0601556***<br>(3,38)<br>[0,0178] |
| $LT_{i,t-1}$              | -0,03<br>(-0,66)<br>[0,046]   | 0,022915***<br>(3,68)<br>[0,0062]  |
| $GDP_{PC\ i,t-1}$         | 0,06<br>(0,84)<br>[0,073]     | 0,0070623<br>(0,46)<br>[0,0158]    |
| <b>Constant</b>           | 97,63***<br>(6,17)<br>[15,81] | -4,376452**<br>(-2,05)<br>[2,1359] |
| <b>R squared</b>          | 0,005                         | 0,15                               |

Notes: <sup>a</sup> Panel regression with fixed effects, t statistics in brackets and standard errors in squared parenthesis.

\*significant at the 10 per cent level

\*\*significant at the 5 per cent level

\*\*\*significant at the 1 per cent level

**Table 10-4: Panel models for Colombia's health transfers**

| Period             | 1998-2005 <sup>a</sup>         | 1998-2005 <sup>b</sup>          | 1994-2005 <sup>a</sup>                            |
|--------------------|--------------------------------|---------------------------------|---|
| Dependent variable | $T^{H,I}_{i,t}$                | $T^{H,GDP}_{i,t}$               | $T^{H,GDP}_{i,t}$                                 |
| $CO_{i,t-1}$       | -0,06<br>(-1,26)<br>[0,052]    | 0,003<br>(2,80)<br>[0,001]      | $HI_{i,t-1}$<br>0,101***<br>(-4,05)<br>[0,025]    |
| $LT_{i,t-1}$       | 0,08<br>(0,79)<br>[0,104]      | 0,002<br>(1,16)<br>[0,002]      | $LT_{i,t-1}$<br>0,006**<br>(2,45)<br>[0,002]      |
| $GDP_{PC\ i,t-1}$  | -0,79***<br>(-3,00)<br>[0,265] | -0,031***<br>(-8,73)<br>[0,003] | $GDP_{PC\ i,t-1}$<br>-0,004<br>(-0,79)<br>[0,006] |
| Constant           | 172,16***<br>(6,64)<br>[25,91] | 3,974***<br>(10,45)<br>[0,380]  | Constant<br>11,761***<br>(4,38)<br>[2,685]        |
| R squared          | 0,01                           | 0,69                            | R squared<br>0,168                                |

Notes: <sup>a</sup> Panel regression with fixed effects, t statistics in brackets and standard errors in squared parenthesis; <sup>b</sup> panel regression with random effects, z statistics in brackets.

\*significant at the 10 per cent level

\*\*significant at the 5 per cent level

\*\*\*significant at the 1 per cent level

With the exception of the role ascribed to fiscal capacity (not explicitly instituted in the distribution formula), the actual distribution of health transfers in Colombia does not appear to follow a between-jurisdiction equalizing pattern, the results indicate. When defined in terms of coverage of the subsidized regime, expenditure needs are not significant, regardless of the model specification. For the total size of the health transfers ( $T^{H,GDP}_{i,t}$ ) per jurisdiction, expenditure needs, if defined in terms of the health index of the HDI, turn out to be significant, but in the wrong direction (the higher the life expectancy in a jurisdiction, the higher the health transfer). Only in this same model, the level of taxation is significant and with the right sign (the higher the tax effort, the higher the transfer). In contrast to the case of education, in the three models fiscal capacity, as measured by GDP per capita, is significant, with the right equalization sign (the higher per capita GDP, the lower the health transfers).



### **Box 10.1: Degree of equalization of intergovernmental transfers**

The degree of equalization arising from an intergovernmental transfer – an indicator of adaptation – can be assessed by determining the extent to which the distribution of the actual transfer between subnational jurisdictions conforms to some equalizing distributive criteria suggested by theory or instituted by legislation. When applied, the theoretical distributive criteria would yield an ‘ideal’ equalizing transfer ( ${}^E T_i$ ).

The benchmark design of an equalizing transfer varies depending on whether the objective of the transfer is to equalize revenue capacity, spending capacity or a combination of the two (e.g., spending capacity at similar levels of taxation). The formulas and procedures may be adjusted to account for design features of the transfers system and the specifics of the expenditure and tax assignments between government tiers. Here I draw on Ahmad and Thomas (1997).

#### ***Revenue capacity equalization***

A transfer that would equalize revenue capacities across subnational jurisdictions of the same level of government could be written as:

$${}^E T_i = P_i [R^* - R_i]$$

Where  ${}^E T_i$  is the transfer for jurisdiction  $i$ ,  $P_i$  is the population of jurisdiction  $i$ ,  $R^*$  is the standardized revenue capacity (per capita) of the fiscal tier to which  $i$  belongs, and  $R_i$  is the revenue capacity (per capita) of jurisdiction  $i$ , given the tax assignment.

One way to estimate total revenue capacity, when the assignment of tax sources is the same across jurisdictions, is by using a macroeconomic indicator of the aggregate tax base as follows:

$$R_i^* P_i = \text{GDP}_i t^*$$

Where  $\text{GDP}_i$  is the gross domestic product of jurisdiction  $i$ , and  $t^*$  is a notional or standardized tax rate. The country GDP can be used to estimate  $R_i^* P_i$ .

Revenue capacity equalization thus defined requires the same level of taxation across jurisdictions:

$$t^* = (R_i^* P_i) / \text{GDP}_i$$

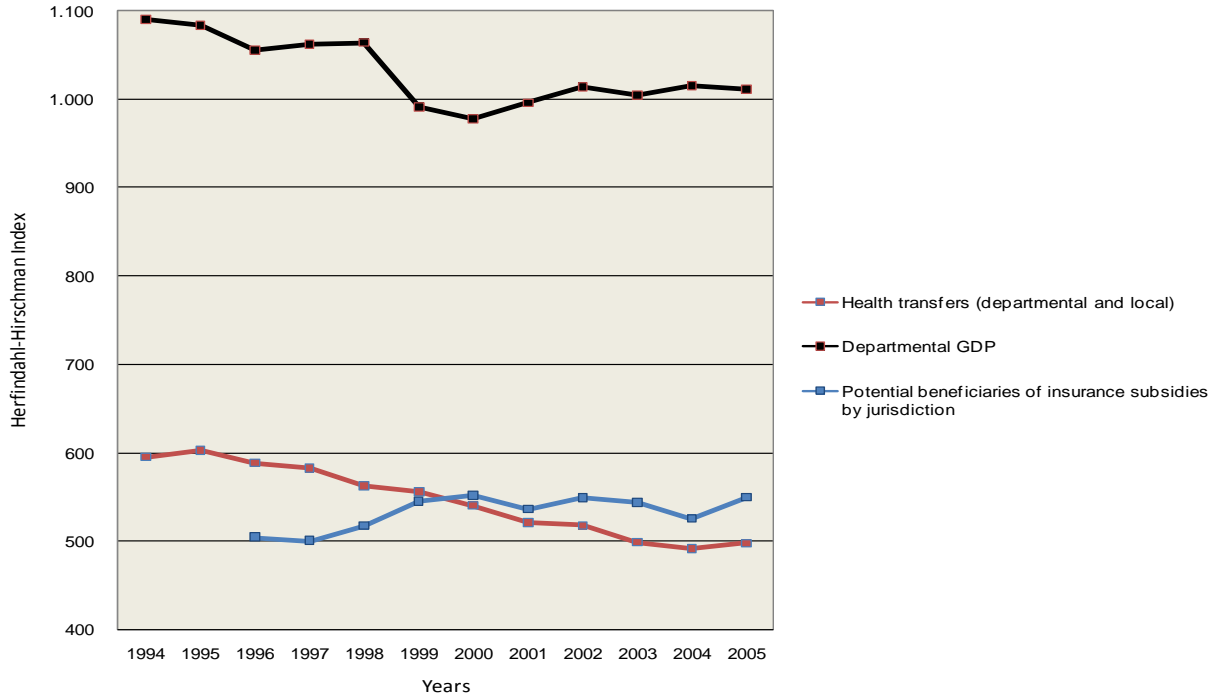
#### ***Expenditure equalization for similar levels of taxation***

A transfer that would ensure a similar level of (potential) access to public services at similar levels of tax effort can be written as a function of the (per capita) standardized expenditure needs ( $E_i$ ) and revenue capacity ( $R_i$ ) of each jurisdiction  $i$ :

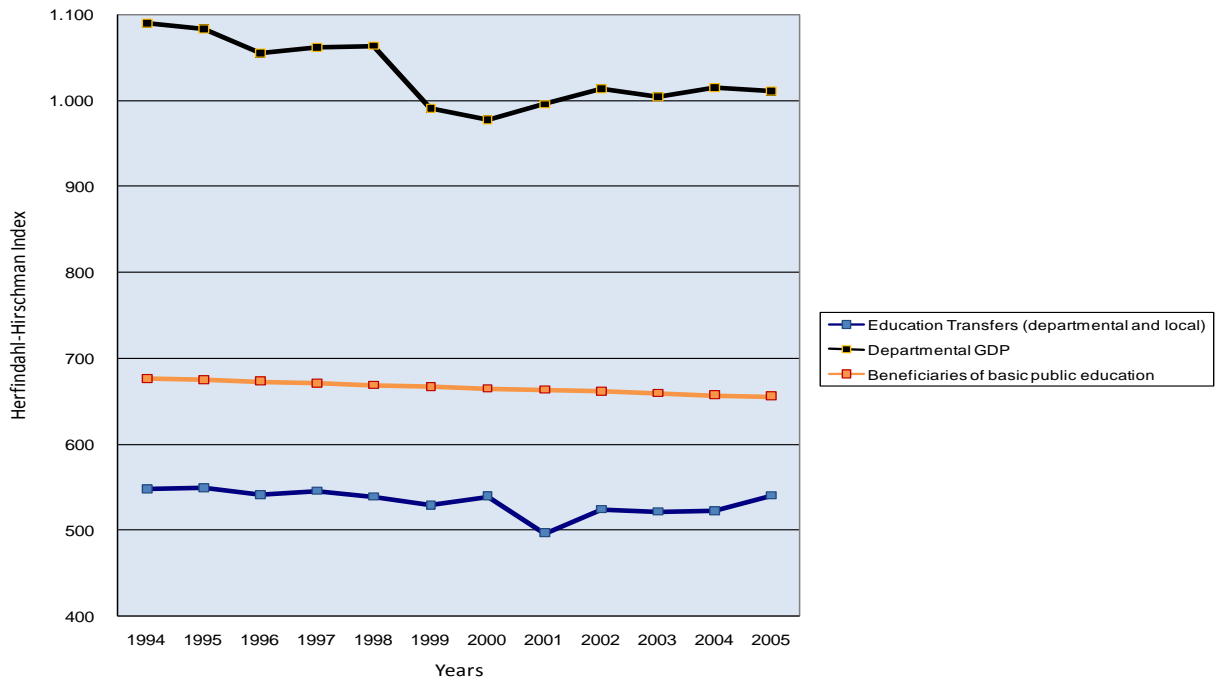
$${}^E T_i = P_i (E_i - R_i)$$

Standardized expenditure could be estimated by adjusting the desired level of per-capita consumption for each expenditure category (e.g., health care, education).

To give a sense of how robust the Colombian system of intergovernmental transfers is to changes in the geographic distribution of economic activity and population, a measure of concentration, known as the *Herfindahl-Hirschman* index (HHI), can be used as explained in Box 10.2. Since the number of jurisdictions studied (i.e., 33) has remained constant under the 1991 constitution, the changes in the HHI come from changes in the geographic concentration of transfers, economic activity or population, depending on the case. One finding is that the geographic concentration of both the health and education transfers, each one consolidated for departmental and local governments, has been substantially lower than that of GDP (Figures 10.16 and 10.17). Meanwhile, health transfers and the population of eligible beneficiaries of publicly funded health insurance exhibit a similar degree of geographic concentration, but with tendencies moving in opposite directions (Figure 10.16). In fact, for the period 1996-2005, there is a negative correlation ( $-0.7$ ) between the two HHI, suggesting that health transfers do not easily adjust to migratory movements of eligible beneficiaries. Since the early 2000s, the concentration of health transfers became lower than the concentration of eligible beneficiaries, a reversal of position with respect to the situation in the second half of the 1990s. On the other hand, the degree of geographic concentration of education transfers (departmental *plus* local) is persistently lower than that of the potential beneficiaries of basic public education (Figure 10.17). For the period 1994-2005, the correlation between the HHI of these two variables is positive ( $0.57$ ), suggesting that the response of education transfers to changes in the spatial concentration of potential beneficiaries is, at the margin, more robust than in the case of health transfers.



**Figure 10-16: Robustness of Colombia’s health transfers in selected contingencies**

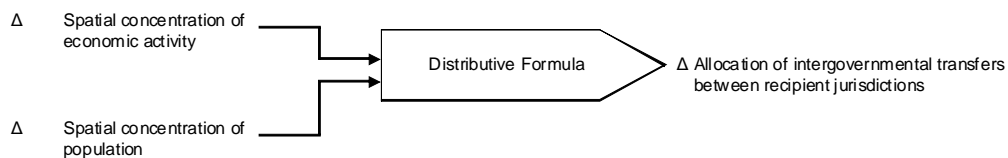


**Figure 10-17: Robustness of Colombia’s education transfers in selected contingencies**

Source: Original data from *Departamento Nacional de Planeación* (transfers), *Ministerio de Protección Social* and *Ministerio de Educación* (beneficiaries) and DANE (GDP).

### Box 10.2: A way to assess the robustness of intergovernmental transfers

The following relationships can serve as a point of departure in assessing the robustness of intergovernmental transfers over contingencies associated with changes in the spatial distribution of both economic activity and population:



Using the *Herfindahl-Hirschman Index* (HHI) as a concentration indicator, such relationships would take the following form:

$$HHI^{IT} \leftarrow (HHI^{GDP}; HHI^{POP} / \text{Distributive Formula})$$

The *Herfindahl-Hirschman Index* for intergovernmental transfers ( $HHI^{IT}$ ) can be written in turn as follows:

$$HHI^{IT} = S_1^2 + S_2^2 + S_3^2 + \dots + S_n^2$$

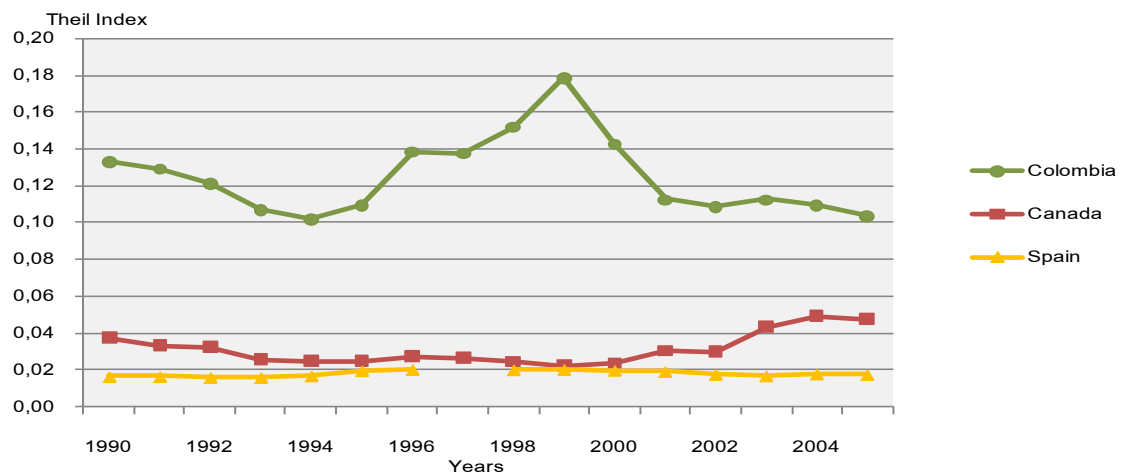
where  $S_n$  is the transfers' share of the  $i^{th}$  department. The higher the HHI, the greater the degree of spatial concentration.

The *Herfindahl-Hirschman Index* for economic activity ( $HHI^{GDP}$  and for population ( $HHI^{POP}$ ) can be calculated in a similar fashion, taking into account that in the former case  $S_n$  would represent the GDP share of the  $i^{th}$  department, while in the latter it would stand for the population share of the  $i^{th}$  department. Depending on the task at hand, population could be taken to mean beneficiaries of a given service (e.g., health care, education) or total population.

## 10.2 INTERNATIONAL COMPARISON

This section quantitatively illustrates how Colombia compares to Canada and Spain in terms of interregional economic disparities in the three dimensions of development under consideration, as well as in fiscal terms. Comparisons are undertaken for part or the whole 1990-2005 period. A detailed analysis of the Spanish case is offered by Herrero, Soler et. al. (2004).

Regional disparities in GDP per capita, as measured by the Theil index, are much more marked in Colombia than in either Canada or Spain (Figure 10.18). In fact, Canada and Spain appear fairly egalitarian as regards regional GDP per capita, which makes their institutional experience in dealing with such disparities of particular interest to Colombia.



**Figure 10-18: Per capita GDP disparities between regions by country**

*Source:* Original data on GDP per capita for Colombia, DANE, *Cuentas Nacionales Departamentales*, [www.dane.gov.co](http://www.dane.gov.co); for Canada, Statistics Canada, *Provincial Economic Accounts*, CANSIM; for Spain, Instituto Nacional de Estadística, *Contabilidad Regional de España*, hard copies and [www.ine.es](http://www.ine.es).

Among the three countries, Colombia exhibits the lowest overall level of taxation (Table 10.5), a situation that conforms to international trends, in the sense that richer countries tend to have higher levels of taxation both through time and across countries. Strikingly enough, the Colombian central and intermediate levels of government collect, respectively, the largest and smallest shares of total tax revenues by country in the group. Thus, for example, in 2005 while the Colombian central government collected almost 82.9 percent of the country's total tax revenues, its Canadian and Spanish counterparts collected, in that order, 49.7 and 55.7 percent. Only 7.6 percent of Colombia's total tax revenues accrued to the intermediate level in the same year, compared to 41.3 percent in Canada and 37.4 in Spain,<sup>142</sup> rendering the Colombian regional governments the weakest in the sample in relative terms. As a result of the higher degree of tax revenue centralization, the central government of Colombia has the largest relative potential for intergovernmental transfers. Over time, the distribution of the overall tax burden among levels of government has been unfavorable for the intermediate level in Colombia, losing more than 2 percent in revenue share between 1990 and 2005, whereas in Canada and especially in Spain it has gained ground. It could be shown that the impressive leap in the tax revenue share of the autonomous communities of the common regime in Spain (it went from 9.9 to 37.4 percent of the overall tax revenue in the period) is largely due to the reassignment of tax sources from the central to the intermediate level in the early 2000s, a demonstration of the reach of fiscal reform.

---

<sup>142</sup> . The figure for Spain refers to the *Régimen Común* only.

**Table 10-5: International comparison of levels of taxation by tiers of government, selected years**

| Level of Government | Share of GDP          |             |                      |                       |             |                    |
|---------------------|-----------------------|-------------|----------------------|-----------------------|-------------|--------------------|
|                     | 1990                  |             |                      | 2005                  |             |                    |
|                     | Colombia <sup>a</sup> | Canada      | Spain <sup>b,c</sup> | Colombia <sup>a</sup> | Canada      | Spain <sup>b</sup> |
| Central             | 8,9                   | 13,7        | 18,1                 | 15,3                  | 13,2        | 12,8               |
| Intermediate        | 1,3                   | 12,2        | 2,1                  | 1,4                   | 11,4        | 8,6                |
| Local               | 0,7                   | 3,7         | 1,1                  | 1,7                   | 3,0         | 1,6                |
| <b>Total</b>        | <b>10,9</b>           | <b>29,6</b> | <b>21,3</b>          | <b>18,4</b>           | <b>27,7</b> | <b>23,0</b>        |

| Level of Government | Share of Total Tax Revenues |              |                      |                       |              |                    |
|---------------------|-----------------------------|--------------|----------------------|-----------------------|--------------|--------------------|
|                     | 1990                        |              |                      | 2005                  |              |                    |
|                     | Colombia <sup>a</sup>       | Canada       | Spain <sup>b,c</sup> | Colombia <sup>a</sup> | Canada       | Spain <sup>b</sup> |
| Central             | 81,7                        | 46,3         | 85,0                 | 82,9                  | 47,9         | 55,7               |
| Intermediate        | 12,2                        | 41,2         | 9,9                  | 7,6                   | 41,3         | 37,4               |
| Local               | 6,1                         | 12,5         | 5,2                  | 9,5                   | 10,8         | 7,0                |
| <b>Total</b>        | <b>100,0</b>                | <b>100,0</b> | <b>100,0</b>         | <b>100,0</b>          | <b>100,0</b> | <b>100,0</b>       |

Source: Original data on tax revenues for Colombia, Banco de la República, *Finanzas públicas database* (available by request); for Canada, Statistics Canada, *CANSIM*, [www.statcan.ca](http://www.statcan.ca), and Department of Finance, *Fiscal Reference Tables*, [www.fin.gc.ca](http://www.fin.gc.ca); for Spain, Instituto de Estudios Fiscales, BADESPE, [www.estadief.meh.es](http://www.estadief.meh.es).

<sup>a</sup> The figure for the intermediate level includes Bogotá's typically departmental tax revenues.

<sup>b</sup> The figure for the intermediate level refers to the common regime only, relative to the corresponding GDP; for the local level, municipalities (*Ayuntamientos*) only.

<sup>c</sup> The figure for the local level refers to 1992.

Table 10.6 helps to understand the foundations of the reverse intergovernmental transfer arrangement, from the Basque Country and Navarre (i.e., the special or *foral* regime) to Spain's central government. The level of taxation in these two autonomous communities is substantially higher than the one observed in the remaining 15 autonomous communities (i.e., the common regime), in essence because the Basque Country and Navarre are entitled to taxes that elsewhere in Spain have been assigned to the central government. Consequently, as far as

intergovernmental transfers are concerned, the central government plays there the role of transferor within the common regimen and of transferee within the special regime. One consequence of the early 2000s reassignment of taxes within the common regimen is that the gap between the levels of taxation of the common and the special regimens has narrowed significantly.

**Table 10-6: Level of taxation of the intermediate tier of government by tax regime in Spain**

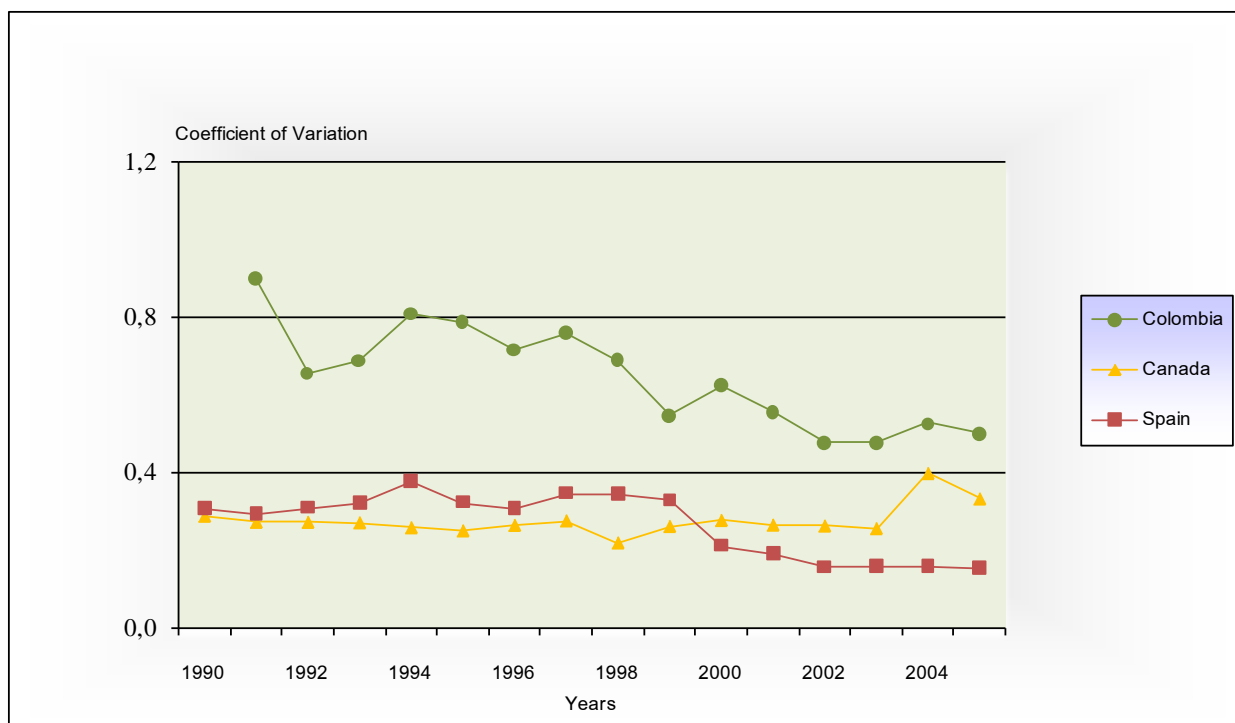
Share of corresponding GDP

| Level of Government | 1990   |                 | 2005   |                 |
|---------------------|--------|-----------------|--------|-----------------|
|                     | Common | Special (Foral) | Common | Special (Foral) |
| Intermediate        | 1,4    | 10,1            | 8,3    | 12,8            |

Source: Original data from Instituto de Estudios Fiscales, *BADESPE*, [www.estadief.meh.es](http://www.estadief.meh.es).

Perhaps not surprisingly given the patterns of per capita GDP disparities between regions, the disparities in levels of taxation between the units of government of the intermediate level have been higher in Colombia than in Canada and Spain (common regime only), albeit a downward trend is noticeable in the former case (Figure 10.19). This result suggests that the need for a system of intergovernmental transfers tailored to ameliorate the horizontal fiscal disparities is stronger in the South American country.



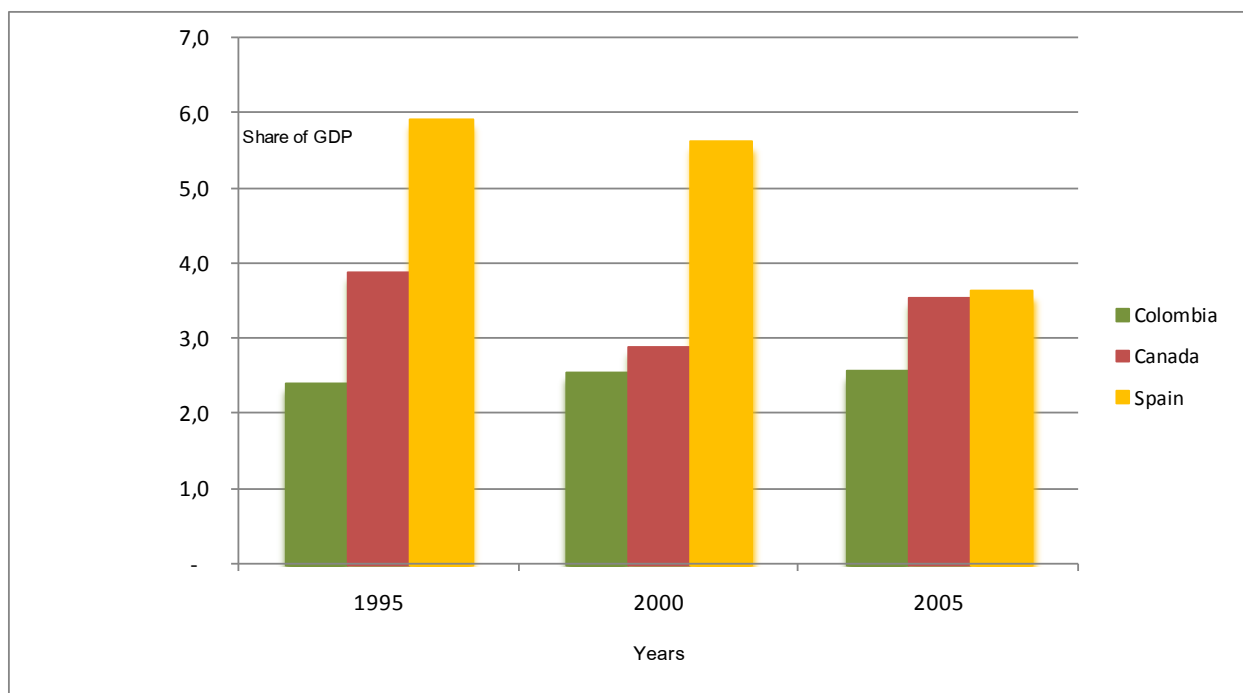


**Figure 10-19: Level of taxation disparities between regions by country**

*Source:* Original data on tax revenues, for Colombia, Banco de la República, *Finanzas Públicas* database (available by request); for Canada, Statistics Canada, *CANSIM*, [www.statcan.ca](http://www.statcan.ca); for Spain, Instituto de Estudios Fiscales, *BADESPE*, [www.meh.es](http://www.meh.es).

*Notes:* Level of taxation: Percentage share of tax revenues in GDP. For Spain, Autonomous Communities of the *Régimen Común* only.

Now, the relative size of intergovernmental transfers channeled through the intermediate level of government in Colombia has been, in recent periods, smaller than in Spain, and, since the late 1990s, is quite similar to that of Canada, as Figure 10.20 shows. As a share of the respective country's GDP, such transfers have been curtailed in Colombia and Spain over the early 2000s, while a longer downward trend, with a recent rebound, is noticeable in the case of Canada. In Colombia this cut is partly due to the constitution makers' decision to have the local rather than the departmental governments as the axes of fiscal decentralization.



**Figure 10-20: Central government total transfers to the intermediate level of government by country**

*Source:* Original data on transfers for Colombia, Departamento Nacional de Planeación, *Finanzas Territoriales*, [www.dnp.gov.co](http://www.dnp.gov.co); for Canada, Statistics Canada, *CANSIM*, [www.statcan.ca](http://www.statcan.ca); for Spain, Instituto de Estudios Fiscales, *BADESPE*, [www.estadief.meh.es](http://www.estadief.meh.es).

*Notes:* For Colombia, excluding Bogotá's transfers and GDP; for Spain, transfers and GDP of the *Régimen Común* only.

There is also an important difference between Colombia and the other two countries in the type of transfers in use. As far as the intermediate level of government is concerned, Colombia has devoted most, and at times the totality of its constitutionally mandated intergovernmental transfers to education and health. In contrast to Canada and Spain, Colombia does not have in place any transfer from the central to the intermediate level of government to address interregional fiscal or, more generally, economic disparities, other than those associated

with education and health (Table 10.7).<sup>143</sup> To be sure, the commitment to education and health care in Canada and Spain is in evidence in their central government transfers to, respectively, the provinces and territories, and to the autonomous communities. In both cases, the largest share of the referred transfers goes to such or similar purposes. Nonetheless, Canada and Spain have in place intergovernmental transfers which specifically seek to promote interregional fiscal or economic equalization. In Canada, the Equalization program, which tackles fiscal disparities among provinces, and the Territorial Formula Financing, which, though having broader objectives, copes with fiscal disparities too, account, taken together, for not less than 30 percent of total federal transfers to the intermediate level of government over the last decade and a half, or so. In Spain, the *Fondo de Compensación Interterritorial*, which addresses income disparities between autonomous communities, has absorbed around 3 percent of the corresponding total transfers.

---

<sup>143</sup> . Although intergovernmental transfers to the local governments in Colombia incorporate a general purpose component, not only it is quantitatively marginal but also is not designed to counteract interregional fiscal disparities.

**Table 10-7: Type of central government transfers to the intermediate level of government by country**

Selected years, corresponding total = 100

| Country               | Type of transfers                    | 1995  | 2000  | 2005  |
|-----------------------|--------------------------------------|-------|-------|-------|
| Colombia <sup>a</sup> | Health and education                 | 100,0 | 100,0 | 100,0 |
|                       | Equalization                         | 0,0   | 0,0   | 0,0   |
| Canada <sup>b</sup>   | Health, education and other services | 66,3  | 53,9  | 69,3  |
|                       | Equalization <sup>d</sup>            | 33,7  | 46,1  | 30,7  |
| Spain <sup>c</sup>    | Health, education and other services | 96,7  | 97,3  | 96,5  |
|                       | Equalization <sup>e</sup>            | 3,3   | 2,7   | 3,5   |

Source: Colombia's original data, Departamento Nacional de Planeación, *Finanzas Públicas Territoriales*, www.dnp.gov.co; Canada's original data, Department of Finance, *Fiscal Reference Tables*, www.fin.gc.ca; Spain's original data, Instituto de Estudios Fiscales, *BADESPE*, www.estadief.meh.es.

<sup>a</sup> Transfers to departments; Bogotá's transfers excluded.

<sup>b</sup> Transfers to Provinces and Territories. Fiscal year.

<sup>c</sup> Transfers to the autonomous communities of the Régimen Común.

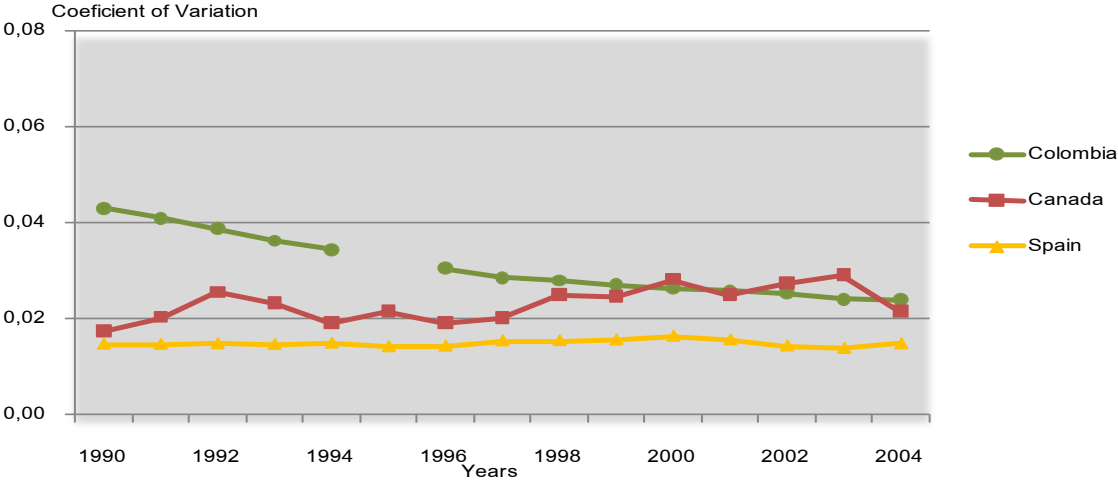
<sup>d</sup> Equalization and Territorial Formula Financing.

<sup>e</sup> Fondo de Compensación Interterritorial.

It could be stated then that the constitutional end of achieving an harmonic development of the Colombian regions lacks at least a couple of means used in Canada and Spain for similar purposes, namely, an intermediate level of government with a greater power to tax, and a system of intergovernmental transfers which, in addition to helping to finance the provision of a standardized level of health and education services, addresses other economic or fiscal disparities between regions. At some point a trade-off between the taxing and transferring options appears to arise, though. A high decentralization of tax powers, which is likely to favor the richer jurisdictions, could eventually drain the central government coffers, ending up being detrimental to intergovernmental transfers, at least in a top-down direction. Such an outcome would hamper in turn the prospects of adopting policies to address interregional fiscal disparities, even more so

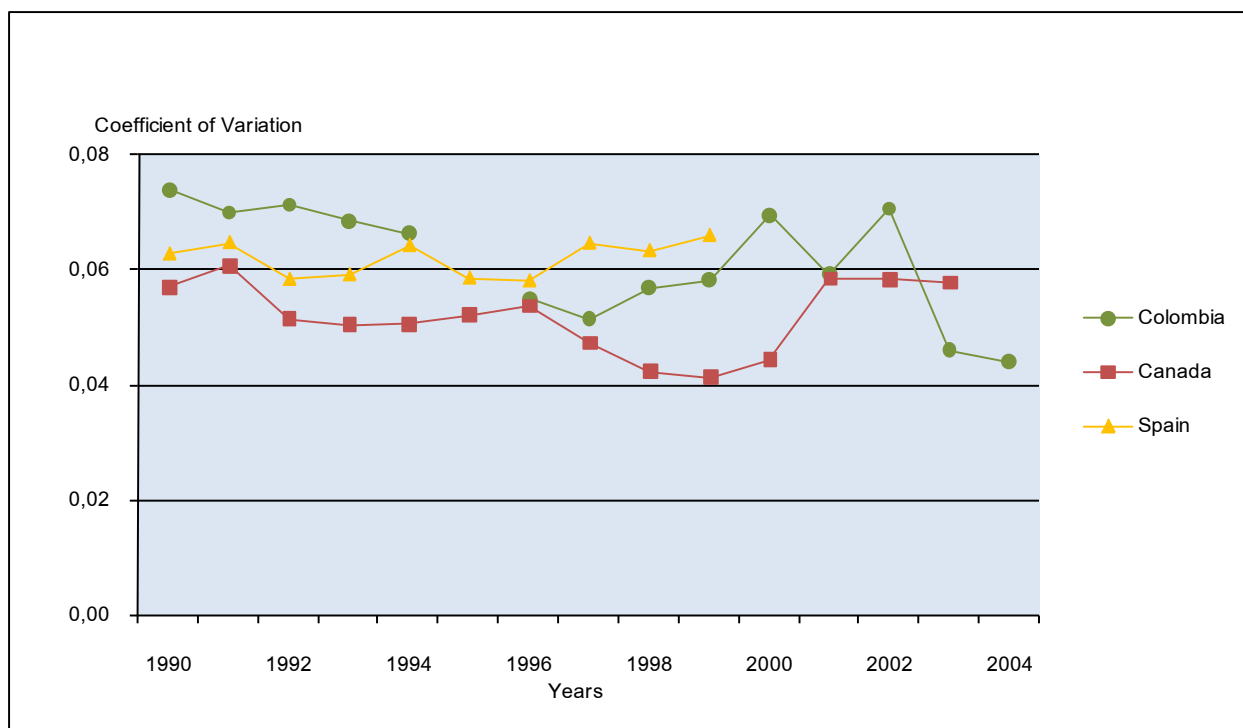
considering that a system of reverse intergovernmental transfers appears to fuel fiscal conflict beyond its usual levels.

In the early 1990s, life expectancy was substantially more unequal across the Colombian departments than across the Canadian provinces and territories or the Spanish autonomous communities (Figure 10.21). But since then interregional disparities in life expectancy have tended to fall in Colombia, to the point that in the mid-2000s they became similar to the disparities found in Canada. A broadly analogous pattern emerges in the field of basic education (Figure 10.22). Needless to say, life expectancy does not provide a comprehensive account of a population’s health conditions, but it tells something about them (likewise for gross enrollment and education).



**Figure 10-21: Life expectancy at birth disparities between regions by country**

Source: Original data on life expectancy at birth, for Colombia, *Programa Nacional de Desarrollo Humano* DNP/PNUD database (available by request); for Canada, Statistics Canada, *Canadian vital statistics*, from 1991 to 2004, [www.statcan.ca](http://www.statcan.ca), and Centre for the Study of Living Standards, 1990, [www.csls.ca](http://www.csls.ca), and for Spain, Instituto Nacional de Estadística, from 1992 to 2004, [www.ine.es](http://www.ine.es), and Herrero C., Soler A., Villar A. (2004), from 1990 to 1991.



**Figure 10-22: Gross enrollment ratio disparities between regions by country**

*Source:* Original data on the gross enrollment ratio, for Colombia, *Programa Nacional de Desarrollo Humano* DNP/PNUD database (available by request); for Spain, Herrero C., Soler A., Villar A. (2004); and for Canada, author's estimation based on enrollment and school-age population data from Statistics Canada, CANSIM, [www.statcan.ca](http://www.statcan.ca).

So, what is particularly notable about Colombia in our three-country comparison in the realm of regional economic development is the scale of the disparities in fiscal capacity rather than in the health and education outcomes, a finding that roughly conforms to the expected pattern effects of the Colombian system of intergovernmental transfers, given its design features.

## 11.0 INTERVIEWS WITH COLOMBIAN POLICYMAKERS

This chapter is devoted to analyzing the interview material obtained from a sample of Colombian policy makers, along with other complementary sources of information. The interviewees were selected on the basis of a random stratified sampling design, where the units of analysis are public sector organizations of the national, departmental, and local levels of government involved in policy decision-making in areas relevant for the study. At the national level, the organizations were stratified by branch of government (i.e., executive, congress and judiciary). At the subnational level, the departments and a selection of municipalities (i.e., the departments' capitals) were stratified by the level of per capita income relative to the national average (i.e., high, medium, and low per capita GDP).<sup>144</sup> Figure 11.1 lists the selected units of analysis.

All the interviewees are current or former heads of the selected public sector organizations who have served their terms of office at some point under the 1991 constitution (e.g., a Minister of Finance, a Governor of Magdalena, a Mayor of Pasto, and so on and so forth). In compliance with university regulations, confidentiality is protected by referring to the interviewees by their position title rather than by their names (for information *not* coming from the interviews, the sources are named where appropriate).

---

<sup>144</sup> . A department's per capita income is imputed to its capital.

| Type of Authority  | Units of Analysis  |
|--|--|
| <p><b>1. National</b></p> <p>Executive</p> <p>Congress</p> <p>Judiciary</p>  | <p>Ministry of Finance<br/>Ministry of Health (aka Ministry of Social Protection)</p> <p>Senate</p> <p>Supreme Court</p>   |
| <p><b>2. Departmental</b></p> <p>Level of per capita income <sup>a</sup></p> <p>High</p> <p>Medium</p> <p>Low</p>                | <p>Cundinamarca<br/>Guajira</p> <p>Caldas<br/>Tolima</p> <p>Cauca<br/>Magdalena<br/>Putumayo<br/>Quindío</p>   |
| <p><b>3. Local (Department Capitals)</b></p> <p>Level of per capita income <sup>a</sup></p> <p>High</p> <p>Medium</p> <p>Low</p> | <p>Bucaramanga (Santander)<br/>Yopal (Casanare)</p> <p>Cartagena (Bolívar)<br/>Neiva (Huila)</p> <p>Armenia (Quindío)<br/>Pasto (Nariño)<br/>Puerto Inírida (Guanía)<br/>Santa Marta (Magdalena)</p> |

**Figure 11-1: Interviews of Colombian policymakers: Selected sample**

<sup>a</sup> As proxied by per capita GDP. A Department’s per capita GDP is imputed to its capital.



The interviewees, as public sector authorities, have experience in policy making, or in the law and politics of policy making, under the rules of the game set by the 1991 constitution. Because the sample consist of affiliates to the three different levels of government existing in Colombia, the interviews offer a multi-perspective panorama of the role of the department within the public sector, its scope and limitations, as well as of the working of the fiscal institutions and policies and their impact on regional economic development. Their positions of authority have allowed the interviewees to be actors of varying importance in the reforms of the health system, intergovernmental transfers and territorial taxation, among other areas, and, as such, are insiders with a degree of familiarity with the political economy of the reforms, the circumstances of the policy changes and the design features of the fiscal tools involved. The views and insights of the ministers, governors and mayors, to name the most frequent positions in the sample, could thus further our understanding of how the Colombian fiscal constitution relates to regional economic disparities.

Particular attention is paid to how and to what extent, if at all, the legal framework in general, and the constitution specifically, conciliate the stated “harmonic development of the regions” goal with the declared unitary, decentralized nature of the state. The interviews call into question the assumption that in Colombia there are regional units to be the object of harmonic development not because of the absence of candidates to be recognized as regions but because no specific units appears to have been selected for regional development policy purposes. At any rate, the department, a more or less obvious candidate for such endeavor, has tended to be sidestepped or overlooked, the interviews suggest, as the vehicle for the amelioration of interregional economic inequalities.

Insights provided by the interviews suggest that the fiscal institutions and policies associated with the 1991 constitution embrace a varying regard, across the dimensions of economic development of interest for this study, for interregional disparities, while uneasily gravitating towards different points in the centralization-decentralization axis. If any equalization effort has been made, it has centered on education and health care, rather than on fiscal capacity, and it has been mainly conducted via the municipality instead of the department. When asked about the responsibilities for the institutional and policy flaws which may have obstructed the achievement of regional development goals, the interviewees tend to point more to the statutory and ordinary law, in conjunction with its implementation, than to the written constitution. In some instances, a distinction arises from the interviews between the *de jure* and *de facto* role of the departments in the functioning of Colombian multilevel system of government and in the promotion of economic development.

### **11.1 ON THE ROLE OF THE DEPARTMENTS IN DECENTRALIZATION**

Whereas the 1991 constitution calls for the harmonic development of the regions, the departments –the jurisdictions that make up the Colombian intermediate level of government– have not been transformed into the axes of regional development, in the eyes of several interviewees. The view that the constitution privileges the local over the departmental governments appears fairly generalized. A Chief Justice of the Constitutional Court describes the

1991 constitution as “primarily municipal,” just like a governor of Putumayo does.<sup>145</sup> According to the president of the National Federation of Departments, a governor himself, “the decentralization efforts [made] by the 1991 Constituent Assembly... mostly benefitted the municipal level.” (Rodado 2004, p. 23) Such local orientation would impinge upon the subnational political and fiscal life. In Bucaramanga, the capital of the department of Santander, “the political weight of the local is felt more than that of the departmental,” its mayor says. According to Cartagena’s mayor, in the capital of the department of Bolivar “it is more important to be the city’s mayor than the department’s governor.” The mayor of Yopal, Casanare’s capital, regards the department as “a sum of municipalities,” suggesting that in this case the whole is no more than its parts.

In some quarters it is believed that the constitution does not house an irrevocable imbalance of fiscal powers in favor of the municipalities and against the departments. While still agreeing with those who maintain that, at the subnational level, the constitution privileged the local governments, in such quarters it is adduced that the constitution itself kept the options open for the allocation of competences and functions between the levels of government, as well as for the assignment of revenue sources, to be the subject of revision through a statutory law called the law of territorial ordering. The slips and difficulties of decentralization and territorial autonomy would be due to the fact that the “issuing of the law of territorial ordering has been deferred by more than a decade,”<sup>146</sup> the speaker of the national Congress states, echoing the aforementioned

---

<sup>145</sup> . A strikingly similar diagnostic has been put forward by President Alvaro Uribe, in an appraisal of his experience as governor of Antioquia: “The Colombian path to decentralization,” he asserts, “has basically favored the municipalities. The departments have been abandoned in the last few years.” See Uribe, A., “El Departamento desde mi perspectiva como gobernador”, *Departamentos al Día*, Federación Nacional de Departamentos y Fondo Cuenta, No. 3, Bogotá, Dic. 2003, p. 7.

<sup>146</sup> . More than a dozen law proposals have been sent to congress with that aim, but thus far none of them has been approved.

view. In other words, the fault would reside in the lack of appropriate legal development of the 1991 constitution.

In an illustrative metaphor, a former member of the Constituent Assembly, dubs the law of territorial ordering “the mother of decentralization” and regards it as a paradox that, albeit the mother law had not, and still has not, been passed, several laws that supposedly were to be its offspring had been already approved, such as the laws of the departmental and municipal regimes and the laws that regulate intergovernmental transfers (Lleras de la Fuente 1996, p. 63). Put another way, it is as if the offspring laws were born before the mother law. This course of action is sanctioned by the constitution, pointing to the existence of a constitutional design flaw.

The fiscal links between the national and local governments are portrayed in the interviews as more numerous and stronger than those with the departmental governments. For the Constitutional Court’s chief justice, “the department’s coordination function tends to be blurred in the constitution.” Likewise, mayors tend to attribute a secondary, marginal importance to the relationship of their municipalities with the respective departmental government. Thus, Inírida’s mayor reports that “my relationship, as a mayor, with the national government is closer than with the departmental government.” Armenia’s mayor maintains something similar: “We keep a very close fiscal relationship with the national government; with the department, it is almost non-existent.” “Subnational power rests with the mayor,” the same mayor adds. According to the mayor of Santa Marta, “as far as education is concerned, the district of Santa Marta interacts directly with the national government.” This type of judgment is made by the authorities of other local governments in the sample, pertaining to departments of varying degrees of development and located in different parts of the country.

In the governors' accounts, the relationship of the departmental governments with the municipalities of their respective jurisdiction, though often valued positively, emerges as little institutionalized, even fortuitous, not so much because of the participants' lack of will as because of the absence of formal authority, or the weakness thereof, of the departments over the municipalities in many subjects of public interest.<sup>147</sup> Caldas' governor points out that, in other than a small number of fields, including that of planning, in which the departments are entitled to exercise some authority over their municipalities, the relationship between governors and mayors is for most practical purposes one of equals.

Although a certain convergence of opinions concerning the situation faced by the departments in recent periods is apparent, large divergences surface on the role the departments ought to play, and even on whether they should continue to exist. For some interviewees, the departments (and their governments) should be strengthened, should become the pivotal jurisdictions for political and fiscal decentralization, as well as for materializing the harmonic development of the regions. A point of view along this vein is that of president Uribe (2003, p. 7): "It is necessary," he says, "to strengthen the intermediate level of government represented by the departments...; otherwise, decentralization runs the risk of becoming a go-nowhere dialogue between the central government and more than a thousand municipalities..." Meanwhile, the Constitutional Court chief justice is not ready, in his words, "to declare the death of the departments"; on the contrary, he ponders, the departments seem to have experienced a sort of revival. Caldas' governor regards the strengthening of the intermediate level of government as a

---

147 . The governor of Cundinamarca used to assemble the 116 mayors of the department to do the follow-up of the development plans and set up a number of administrative centers to bring the departmental government closer to the municipalities, but many of those efforts, he says, "unfortunately were interrupted after my mandate came to an end."

necessary condition for the development of the country and warns on the potential dangers for democracy of not moving in that direction: “Colombia, run from Bogotá directly through the municipalities, would resemble Francoist Spain, where the central and local governments existed, but there were no autonomous communities or a true intermediate level of government whatsoever.”

Instead of making the departmental governments stronger, others reckon, it would be better to focus their activities on a narrow set of tasks. Thus, for example, for the Minister of Health (also known as Minister of Social Protection), “as regards the provision of health care, the departments should concentrate on offering technical assistance to their municipalities. The pillar of decentralization and development should be the local level of government; the municipality is the unit of government that should be strengthened, the unit that should assume the main responsibility in the delivery of health and other services such as education and potable water.” Still others, including the Congress speaker, hold the view that a new subnational level of government should be created, the component units of which would be officially called “regions”, formed in turn by two or more departments, without necessarily replacing them and without changing the unitary character of the Colombian state. It is adduced, correctly, that the constitution already contains a procedure to create such level of government. A variant of this view is held, among others, by Inirida’s mayor, who agrees with the creation of the regions as formal political entities but “in the form of states within a federal system.” Those who are against these proposals typically argue that the fact that the constitution authorizes the creation of a new level of government does not necessarily imply that it is a good thing to go ahead. “What to do then?,” a Colombian finance minister asks, “Close down the 32 departments, as some are proposing, to turn them into administrative monsters as would be the 12 regions organized like

political entities? The odds are that that would not be the sensible thing to do.” (Restrepo 2006, p. 18)

A number of mayors consider it desirable to grant greater legal powers to departmental governments in fiscal and regional development affairs, but, as the mayor of Armenia puts it, “only as long as municipal autonomy is respected.” If this prescription were to be followed, the departments would have to be strengthened by reallocating to them functions and revenue sources currently in the hands of the central government, or by allocating to them new functions and revenue sources, while fundamentally preserving the municipal status quo, especially in matters of taxation and transfers, which, as we have seen, in Colombia are constitutionally protected. Anyway, it is far from clear how the departments could be made stronger without substantially furthering their powers over the municipalities.

Decentralization tends to be regarded as necessary for Colombia, even as several interviewees think that it has not advanced but backed down, not least in the fiscal sphere. “I see a tendency towards the concentration of resources and policy making powers at the central level of government, not a tendency towards decentralization and the strengthening of the regions as pillars of regional planning and development,” the mayor of Cartagena asserts.

Notwithstanding the more or less generalized agreement over the need to deepen decentralization, disagreement prevails over the subnational level of government towards which the additional decentralized powers should be assigned, either the local or a higher level of government. The 1991 constitution gives the departments “the role of a hinge” between the national and local levels, according to the mayor of Neiva, but “a law clarifying the scope and application of both the complementarity and subsidiarity principles in the exercise and financing of the functions of the three levels of government is missing.” By complementarity the mayor

was alluding to the principle that the policies and actions of the national and subnational governments should complement rather than replace each other, while by subsidiarity he was alluding to the principle that state functions should be assigned to the lowest government level at which such functions can be effectively carried out. Both principles are found in the Colombian constitution.

## **11.2 FISCAL DISPARITIES AND ECONOMIC DEVELOPMENT**

The existence of acute interregional economic and fiscal disparities is generally recognized by the interviewees. Among the national authorities, for example, the minister of finance points out that “the differences in wealth and development between the country’s regions are evident.” The minister of health tells us that “we continue having a lot of inequity... Health care in Bogotá is like that available in an average European city, whereas in Chocó and other lagging departments it resembles that of some African countries.” According to the Supreme Court chief justice, the 1991 constitution seeks to reduce such “geographic asymmetries.” The principle of equality contained in the constitution, the chief justice asserts, applies as much to people and social groups as to regions, without going into details as to the nature and scope of such equality (e.g., equality before the law?; economic equality?) or as to how the three types of equality could be reconciled with one another in case of conflict. For the minister of finance, the depth of such disparities “is a sufficient argument to pursue horizontal fiscal equity, that is, fiscal equity across subnational governments, through a suitable system of intergovernmental transfers and subventions.”



The idea that the Colombian constitution and law seek the equalization of health and education basic services throughout the country is confirmed by the interviewees of the three levels of government. According to the minister of health, the status of rights conferred to the access to such services in 1991 entails their universalization. No such legal commitment existed prior to the new constitution. “In the centennial 1886 constitution the word health was nowhere to be found,” the minister points out, symbolizing “an approach to health care as a gift rather than as a right.” While claiming that the country has moved closer to it, the minister acknowledges that universal basic health care and education has not been reached so far, and that the coverage of services by subnational jurisdictions differs more than would be desirable. Among the factors which would explain the interregional disparities in health care the minister highlights the distribution of intergovernmental transfers between the municipalities, particularly concerning the subsidized regime: “The most populated municipalities, which are generally the richest, tend to take a proportionally bigger slice of the intergovernmental transfers designated for the subsidized regime.” In Colombia’s legislation, according to the minister, “there are no means for the rich municipalities to compensate the poorest ones.” Note that the compensation is thought of by the minister in inter-municipal, rather than in interregional, terms.

In the eyes of the Constitutional Court chief justice, guaranteeing rights like the rights to health care and education in the context of decentralization involves difficulties derived from the allocation of competences between levels of government and to “the limited availability of funds.” The scope of rights enforcement has been one of the most highly contested issues of the 1991 constitution. There are those who believe that the rights enshrined in the constitution are an imperative, more or less regardless of the budget constraint, which is seen as a highly flexible fiscal tool, adjustable whenever necessary to ensure their fulfillment, whereas others believe that

the enforcement of rights is conditional to the budget constraint, typically seen here as hard to change (Alesina 2001; Moncayo 2002).

When asked about how the legal framework has affected the disparities across departments in the provision of basic health care, Cundinamarca's governor pointed more to the law than to the constitution. The governor notes, for example, how under Law 100 of 1993 "the equalization of the mandatory health plan of the subsidized regime with that of the contributory regime has not been achieved." We have already explained how the differences between these two types of plans translate into disparities in the access to basic health care services between persons and, eventually, between regions. Despite its deficiencies, Law 100 of 1993 "has allowed the expansion of health services coverage; it has made it possible for many people, who were previously excluded, to have access to such services now," the governor contends. Other governors agree with this view on the evolution of coverage, without necessarily endorsing the overall philosophy of Law 100.

To the question of whether the fiscal institutions or policies associated with the 1991 constitution tend to favor the less or the more developed departments or regions, the minister of finance replies that "the constitution is relatively neutral on this point". In his opinion, "if some deficiency is found" in the rules regulating the distribution of national transfers among subnational governments, "it is attributable more to the laws that develop the constitution, such as Law 60 and Law 715, than to the constitution itself." The minister of finance believes that the law could distribute intergovernmental transfers between rich and poor regions in a more equitable fashion within the existing constitution despite the design flaws it may have.

For the mayor of Pasto, "one of the great social achievements of the 1991 constitution, perhaps the most tangible, is that under its wing the subsidized regime was adopted..., a clear

step forward compared with the previous charity model.” Recall that national legislation seeks to achieve universal health coverage by means of subsidies to health insurance purchases, channeled in turn via the subsidized regime. Inirida’s mayor reports that the coverage of health insurance in the municipality’s jurisdiction has increased substantially in recent years, so as to benefit more than 90% of the population nowadays, but believes that, as a result of Law 100, health insurance carriers “keep most of the subsidized regime’s money for themselves, hindering the fulfillment of its objective.” In the same vein, the governor of Tolima believes that health insurance subsidies (commonly described as demand subsidies) “have served mainly to enrich the private health insurance carriers.”<sup>148</sup> In contrast, the minister of health holds an overall positive view of health insurance, whether private or public, describing it as “the appropriate tool, sanctioned by the constitution and the law, to reach universal health coverage.” The fact that the participation of the private sector in the provision of health care, particularly of private hospitals and health insurance carriers, has been sanctioned by legislation “does not mean that health care has been privatized in Colombia,” assures the minister. Such private participation would have the character of a simple delegation of functions on the part of the state, which would keep its power to regulate the health sector.

For the governor of La Guajira, Law 100 of 1993 has contributed to the increase in health insurance coverage in his jurisdiction over the last decade. In his view, however, intergovernmental transfers should be allowed to finance not only the demand of health services, as typically occurs, but also their supply, via hospital facilities, something that the law has sought to discourage. The rationale for this view would be that the department is short of hospital facilities: “Let us suppose that we continue spending on health insurance coverage as the law

---

<sup>148</sup> . In the view of Tolima’s governor, “greater coverage has meant more students in the classroom but with lesser resources per student.”

expects us to do; so, where are the sick going to be attended?” According to Santa Marta’s mayor, “in our city we endured a serious situation as a result of the central hospital closing. The local government does not own a hospital and private hospitals are in short supply... Many ill people are referred to Barranquilla’s hospitals.” These views clash with those of the minister of health, for whom “the demand-driven allocation of subsidies has proved to be more efficient than its supply-driven counterpart.”

The minister of finance is in favor of accelerating the transfer of functions for the delivery of health services from the national to the subnational governments, a process known as certification, since “thus far, slightly over half of all departments and well under half of all municipalities have been certified, with no new department certification approved in the last year or so.” Inirida’s mayor regrets that “the previous mayors did not go ahead with the certification process,” adding that “currently, health care delivery in our municipality is a responsibility of the department’s government.” In the field of education, things would be different for Inirida, according to the mayor: “I began the certification process in education, but soon realized that by completing it our municipality would get less money per student than what we are used to receive.” The blame is laid on the formula employed for distributing intergovernmental transfers.

Education, health and other transfers are generally seen by the interviewees as key fiscal tools for reducing the distances in economic development separating the Colombian subnational jurisdictions. According to Putumayo’s governor, “we have always said that central government’s revenues should be spent across subnational jurisdictions using fairer criteria.” For the mayor of Nariño’s capital, “in Pasto a discourse of grievance against the marginalization in which the Colombian state holds the peripheral regions has long been on the move.”

None of the interviewees attributed to the departmental governments (or the municipal ones for that matter) the main responsibility as regards the levels of employment and income in their corresponding jurisdictions. “We need to be conscious,” Pasto’s mayor stresses, “that employment creation to a large extent depends on national economic policies.” The national government does not have at its disposal, he suggests, public expenditure tools that automatically favor those departments experiencing idiosyncratic recessions, with rates of unemployment higher than the national average. Partly owing to this, Pasto’s local government set up a local development agency, which according to the mayor is “a pioneering policy tool in the country”, one of whose objectives is to make the jurisdiction more attractive to income generating economic activities. The mayor believes that there is enough room for the promotion of development at the subnational level. Other jurisdictions, like Bucaramanga, have taken similar steps.

In the view of some interviewees, key constitutional provisions favorable to a less imbalanced regional development have not been implemented by legislation. “Against the constitution makers’ desires,” Tolima’s governor argues, “we have a centralist, presidentialist republic, where the winners have been the great urban centers of Bogotá, Cali, Medellín and Barranquilla, whereas the losers have been the rural areas, the peasants.” “The country has not explicitly developed the 1991 constitution as regards the territorial ordering of the state,” the same governor states. This judgment is shared by the Supreme Court chief justice, who rejects the idea that the constitutional rules concerning such territorial ordering are flawed. Several interviewees point to the need of issuing the law of territorial ordering envisioned in the constitution.

Inadequate or the lack of implementation of the constitution's regional development provisions is also ascribed to inaction of the national government, as opposed to Congress' inaction. Government inaction is in turn usually attributed to the lack of political will. "The department of Cauca has been abandoned by the national government," says its governor, in a typical expression of such a view.

Governors and mayors alike report little or no formal participation of the subnational authorities in the processes that have led to the approval of the constitutional amendments related to intergovernmental transfers and the several national laws dealing with, or having an impact on, the subnational public finances, a practice that appears to be common in unitary states, where the national government and congress are principal actors in the production of legislation. Subnational governments in good part voice their views and concerns through the National Federation of Departments and the Colombian Federation of Municipalities. In addition to their lobbying activities, these organizations hold periodic assemblies and meetings in which members of the national government usually play a prominent role.

As far as the constitutional amendments of the intergovernmental transfer system are concerned, governors and mayors appear to have paid more attention to the total size of the transfers than to the rules for their distribution among subnational governments. After all, the interviewees indicate, the core of such amendments has been the transfers' share in the central government's current revenues, which determines the size of the transfer pie. According to the governor of Cundinamarca, the governors, thanks to their political action, prevented intergovernmental transfers from being cut in 2001. The formula ultimately adopted, which in essence links the transfers' total size to the country's economic growth, is seen favorably by this governor.

In a joint statement on the latest amendment proposal of the intergovernmental transfers system, in course as of 2007, the governors spell out their position on the issue of interregional disparities in economic development (Gobernadores 2006, pp. 10-15). What should be achieved, they suggest, is interregional equality in terms of “a standardized level of basic services”. Because “our subnational jurisdictions differ in economic strength,” they argue, “deep inequalities and asymmetries in fiscal capacity” arise, which they referred to as “horizontal imbalances,” an expression found in the theoretical fiscal literature. Considering, in addition, that “in Colombia the central level of government has kept for itself the taxes of greater revenue potential (VAT, income tax, financial transaction tax)” and that “the subnational governments have had to bear a set of poorly designed, hard to collect, nuisance taxes on smoking, drinking and other vices,” the governors have come to the conclusion that “those subnational governments of lower fiscal capacity are not in the position of providing even a standardized level of basic services.” In such circumstances, they go on to argue, “horizontal imbalances can only be dealt with through a strong and fair system of territorial compensation.” On the whole, there is the suggestion that the intergovernmental transfer system (i.e., *Sistema General de Participaciones*) should deal with “both the vertical and horizontal fiscal imbalances that characterize the national reality.”

While being generally thoughtful, the Colombian governors’ joint statement is misleading in asserting that, owing to the inequalities in fiscal capacity, “the same level of tax effort cannot be required from all the subnational governments.” This assertion appears to be based on a definition of tax effort in terms of the absolute level of revenue collections in each subnational jurisdiction. Seen in this light, the concept of tax effort would not have much sense. An equal or similar tax effort, also known as level of taxation, can be delivered by subnational governments

(and could therefore be required) when it is measured, as is conventionally done, by the ratio between the tax revenues of a jurisdiction and its fiscal capacity (e.g., GDP; potential tax base).

The minister of finance favors the distribution of health and education intergovernmental transfers “on a capitation basis, in other words, on the basis of a subnational jurisdiction’s demand for [the corresponding] basic services.” In practice, this distributive criterion would lead to the provision of a standardized level of basic services throughout the country, regardless of tax effort, a proposal similar to that put forward by the governors. The aforementioned minister points out that, to date, the main distributive criteria for intergovernmental transfers has been the actual, as opposed to the standardized, provision costs of health and education services in each jurisdiction, criteria which, he rightly emphasizes, can reproduce the inequalities of the past.

It is worth noting that more than a few interviewees mentioned the experience of foreign countries in using intergovernmental transfers with the objective of reducing inter-regional disparities in economic development. The governor of Caldas, for example, maintains that “for a unitary decentralized state such as Colombia’s to achieve subnational economic development,” it is necessary to incorporate “a solidarity fund and a compensation fund” similar to those “existing in Spain.”

Taking into account that the 1991 constitution turned the royalties from the exploitation of nonrenewable natural resources into an entirely subnational revenue source, the interviewees generally indicate that the legal rules for allocating such royalties between subnational governments tend to accentuate, rather than moderate, interregional fiscal disparities. For Tolima’s governor, the presence or absence of nonrenewable natural resources in a given jurisdiction is a sort of lottery. Precisely because of such an accidental element, Armenia’s mayor believes that “allocating the greater proportion of royalties to the producing jurisdictions



amounts to a great injustice.” But even in those jurisdictions rich in nonrenewable natural resources there is dissatisfaction with the rules for the intergovernmental allocation of royalties. In La Guajira, according to the governor, 6 of the 15 municipalities receive coal and gas royalties. Although the departmental government receives royalties too, the governor maintains that there is an excessive municipal bias in the allocation of royalties. “Riohacha, the department’s capital, does not get any royalties at all. If a greater proportion of La Guajira’s royalties were departmental, I could have solved many deficiencies of the water and sewage system”, he contends.

Similar to the intergovernmental transfer system, in the case of royalties the tendency would be towards municipalization, with a secondary role for the department. Even with the municipalities as main beneficiaries, there could be some equalization element in the royalties’ distributive rules, but, as the interviewees readily point out, it does not happen that way.

Complaints about the way in which royalties are earmarked by national legislation are not uncommon. “The law requires us to spend the royalties’ proceeds on basic education and health care,” Yopal’s mayor says, “but the department of Casanare has already reached full coverage in those areas.” Putumayo’s governor points in the same direction: “... we have got a very narrow margin for investing the royalties that our department receives in areas other than those established by national law. For instance, 11 out of the 13 municipalities of Putumayo do not have a slaughter house that meets minimum salubrity standards, but the law does not allow us to invest in slaughter houses.” A similar remark is made by La Guajira’s governor.

A recurring concern of the governors and mayors interviewed has to do with the representation of their jurisdictions in the national congress, particularly in the Senate, whose members are chosen in a nationwide electoral district. “Regrettably, owing to the nationwide

electoral district, the department of Quindío has had no senators in most of the congressional terms since the adoption of the 1991 constitution... We want Quindío to be represented in the Senate,” says the governor of that traditionally coffee growing department. Yopal’s mayor points out that the departments located in the Amazonia and the Orinoquia “cover 52 percent of the Colombian territory and agglutinate 6% of the population,” but, according to him, both the territory and the population are underrepresented in the Senate: “Of a total of more than 100 senators, we [the Orinoquia] only have two,” the governor stresses. This complaint finds echo in other jurisdictions, such as Putumayo and La Guajira. “We do not have a senator representing Putumayo,” the governor says, “We would be interested in having a senator for our department.” “A great weakness of ours is that La Guajira did not have a senator in the previous congressional term”, observes the governor, “Today at least it has one.”

Among other things, the nationwide electoral district for the Senate is criticized because it affects the quality of representation and harms the scarcely populated subnational jurisdictions. As Tolima’s governor remarks, “a senator elected nationwide can hardly fulfill her representation functions ... Senate seats are disproportionally won by the most populated jurisdictions and as a result we only have a few senators from the Amazonian and Orinoquian departments, not to mention the department of Chocó.” Those departments with no senators are deprived of an instrument to ventilate their problems and concerns at the national level of government, where the main policy decisions are made, given the unitary character of the country. They do not have a say, for instance, in Senate decisions regarding the subnational distribution of intergovernmental transfers.

The governors themselves suggest a variety of formulas to correct such a situation. For example, the governor of Cundinamarca proposes that “20% of the Senate could be elected

nationwide, with the remaining 80% elected in regional electoral districts. In such a way the Senate could work for each of the country's regions... I believe that the nationwide electoral district has been very harmful for democracy." Some find inspiration in the rules for apportioning congressional seats used in other countries. Tolima's governor looks at the American case: "in the U.S. each state is entitled to two senators, regardless of population size. They manage to equalize the states: the smallest one is worth as much as the largest one."

In contrast, the Colombian House of Representatives, the lower chamber of congress, is generally praised for incorporating an element of territorial representation, even as its operating rules, as some interviewees claim, are unhelpful to the open expression of the needs and preferences of the departmental jurisdictions. Thus, according to Putumayo's governor, "our department has two representatives in the House of Representatives, but the rules regulating the members of congress's participation in decisions concerning the regional allocation of national public spending are too restrictive. Taking a stance in favor of one's region is almost illegal. There is a double standard in this regard." The spatial composition of congress is increasingly seen as a critical constitutional factor in the definition of public policies affecting subnational governments, including those policies concerned with interregional economic disparities.

Regarding the territorial composition of the Constitutional Court, the chief justice holds the view that the "regional balance" in policy making, particularly as much as "the major public policies" are concerned, is guaranteed more by the regional balance of power in the chambers of congress than by the regional balance in the composition of the constitutional court, where other factors should be given priority. But, between the executive, on the one hand, and congress, on the other, who has more influence on the regional composition of national public expenditure? The finance minister maintains that, under the 1991 constitution, "the executive has more

prerogatives and powers to direct public expenditure.” Comparatively, the powers of congress would be limited.

### **11.3 POLITICAL AND FISCAL AUTONOMY**

The popular election of governors, which joined the popular election of mayors implemented since 1986, is usually considered the most important 1991 constitutional change with respect to the departments. Under the previous constitution, the governor of Quindío tells us, “a governor was chosen by the country’s president and interior minister on the basis of the political recommendations coming from the department... The situation is different under the 1991 constitution: you are popularly elected, so that the central level of government does not have as much direct influence on your departmental government as it used to have.” The new method of selecting the heads of the departmental and local governments seems to have shaken subnational political life. “Formerly, the governor depended on the will of the country’s president and the mayor on the will of the governor,” says Armenia’s mayor. “Elected governors and mayors acquire more obligations towards a jurisdiction’s political class and citizens than their appointed counterparts,” the mayor believes. It is not unusual to find favorable opinions of the popular election of governors and mayors, such as that of the governor of Putumayo, who describes it as “very positive.”

Among the governors prevails the idea that there is a gap between the political power derived from their popular election and the departments’ fiscal powers derived from national legislation. A number of testimonies point in that direction. “The room for action that national legislation confers to the departments in matters of taxation is very limited,” says

Cundinamarca's governor. A similar view is held by the governor of Putumayo: "The departments' legal obligations and responsibilities towards their communities have multiplied under the 1991 constitution, but the resources have not increased in tandem." For the governor of La Guajira, "a big problem is that our departmental government is short of meaningful own revenues." According to Tolima's governor, "since their budgets are meager, the departments are led to beg for national government money."

The nearly null autonomy to determine the use or destiny of intergovernmental transfers is another source of concern for subnational authorities. For the governor of Caldas, education and health care, which happen to be the transfers' uses originally authorized by the 1991 constitution, are indeed high-priority areas, but the role for departmental governments envisioned in national legislation is little more than that of mere payers of the teachers' payroll and hospital operating expenses. Departmental executives and assemblies, the governor critically points out, are left with little or no room to determine the uses given to intergovernmental transfers. Voicing the joint governors' stand on the issue, the head of the National Federation of Departments declares that "we are aware of the institutional weakness and limited fiscal capacity of the intermediate level of government." (Rodado 2004, p. 23)

The perception that the departmental governments are fiscally weak and that such weakness has negative repercussions on their possibilities of becoming important actors in the promotion of regional development is also found among local authorities. Due to "the lack of revenues, Santander's departmental government goes practically unnoticed in the department's capital," says Bucaramanga's mayor. For the mayor of Armenia, "departmental government spending in Quindío's municipalities is meager; in the case of Armenia, it is meager."

To what factors is the fiscal weakness of the departments attributed? The role of national legislation in the departments' fate is beyond doubt for the governors' spokesperson: "The fiscal weakness of the departments is, to a great extent, the result of the constitution and the law." In the eyes of the interviewees, the individual contribution of the constitution and the law often appears unclear or vague, however, especially when it comes to the technical details and the small print of fiscal legislation. In their joint statement, the governors complain about the current assignment of taxes between levels of government, assignment made by ordinary law but that, once adopted, the constitution tends to freeze: "Of every one hundred pesos that the [Colombian] state collects from tax sources, [the national level] gets 81, the municipalities 12, and departments 7," the statement reads (Gobernadores 2006, p. 10).

By reason of their dependence on beer, liquor and cigarette excise taxes, the departments are described by different interviewees as "bartender governments" (i.e., *gobiernos cantineros*). The bulk of the departments' economic activity falls outside the orbit of departmental taxes. Consider the case of Cundinamarca, a department located at the geographic heart of the country. Even though Cundinamarca registers one of the highest levels of per capita income in Colombia, the departmental government benefits little from it in tax revenue terms. "Cundinamarca," the governor tells us to illustrate the situation, "is the largest exporter of flowers in the country, but it does not translate into tax revenue for the department." National and local governments are considered better equipped by the tax legislation than their departmental counterparts to tax the economic activity of their respective jurisdictions. In addition, departmental taxes, especially excise taxes, are seen as nuisance taxes. "The departments," the governors say in their joint statement, "have borne the burden of a series of ill-designed, hard to collect, low-yielding taxes on vices."

Consumption goods taxed by the departments, such as alcoholic beverages and cigarettes, facilitate tax evasion and smuggling. In some departments such illegal practices have become the norm rather than the exception, to the point of being deemed part of their community culture. In La Guajira, a department which shares a long border with Venezuela, “the historical fact of smuggling,” as the governor calls it, erodes the department’s tax bases. It has not been possible to enforce, or there has not been the willingness to enforce, the state’s tax sovereignty that the constitution proclaims. “Most foreign beer imported to Colombia through La Guajira does not pay taxes of any kind...; attempts to collect the department excise taxes have led to social unrest and public safety problems.” Smuggling and informality affect taxes other than excises as well: “The vehicle stock of La Guajira is mostly Venezuelan and lacks the required registration... which would allow the determination of its legality.” This results in tax evasion and a low revenue collection of the motor vehicle tax.

But the governors themselves call attention to the fact that the departments’ fiscal weakness should not be ascribed to national legislation only, or the lack thereof. The scant development of economic activity in some jurisdictions, which restricts fiscal capacity, is another critical factor frequently pointed to. It is implied that even if new sources of tax revenue were assigned to the departments, the governments of the lagging jurisdictions would not benefit much in terms of revenue yielding. Notwithstanding that it is a coastal department, “there is no road connecting the department of Cauca to the Pacific Ocean,” the governor says. For the governor, while Cauca has huge potential for mining and agriculture, among other activities (ethnic diversity is singled out as an important cultural and economic asset), so far such potential wealth has not been materialized. The low level of geographic integration, associated with the lack of

roads and intra-departmental transportation, would have hindered the expansion of economic activity.

Geographic isolation is accompanied in some departments by a small population size. “Guainía,” located in the border between Colombia, Venezuela and Brazil, “is the only department that has a single municipality, Inírida,” says Inírida’s mayor. “The department has around 43,000 inhabitants and 75,288 km<sup>2</sup>. Population density is very low and the distances between some communities are enormous. The highways of our department are the rivers. Transportation is largely fluvial. All this makes such communities hard to reach for the departmental government. The department’s economy is mainly based on gold extraction and fishing,” the mayor goes on to explain. Sometimes it is not so much the scant development of economic activity which contributes to the departments’ fiscal weakness but the presence of economic activity of the wrong kind. Putumayo, a department located in the country’s south, “has historically been an economy of enclaves: rubber and oil, for example. Recently, illicit crops have gained ground,” the governor points out. Because of their illicit character, such crops do not constitute a reliable and stable source of revenue, even though it does not situate all the income arising from illicit activities beyond the reach of formal taxation, the interviewee suggests.

Guainía, turned into a department by the 1991 constitution, is an example of a jurisdiction with relatively low fiscal capacity. Peculiarly, its jurisdiction entirely overlaps with the jurisdiction of Inírida, the capital and only municipality of the department. The dependence of Guainía’s economy on government activities is very high, according to Inírida’s mayor. Transfers from the central level of government play a crucial role there. With the budget constraint as an Achilles’ heel, Guainía’s political leaders have gone as far as to propose, the mayor reports, “the



establishment of a single subnational government there with a view to preventing the duality of functions, even more so given that there is hardly any tuning between the departmental and local governments.”

The interviews provide a glimpse of the episodes of subnational governments’ fiscal stress and the policy responses to them. Among the subnational jurisdictions in the interviewing sample, departments such as Magdalena and La Guajira, as well as the local governments of Santa Marta and Inírida, have been bailed out by the national government over the last decade or so, according to their governors and mayors. The mayor of Santa Marta describes his experience as follows: “I took over a broken, highly indebted local government, with a large bureaucracy and quite a few teachers hired with no budget backing... I had to downsize the department’s public sector. All our resources were channeled towards fiscal adjustment. Other than that, I could do very little.”

The fiscal performance programs have come with the monetary and human costs associated with downsizing, but the interviewees tend to see them as necessary under the circumstances. By virtue of such policy responses, “Putumayo is currently,” according to its governor, “a fiscally healthy department.” An overall assessment is provided by a former head of the National Federation of Departments and Huila’s governor: “With the fiscal performance programs... enforced under the umbrella of Laws 358 of 1997, 550 of 1999 and 617 of the 2000, the departments... have recovered their fiscal and institutional viability...” (Villalba 2005, p. 13) In the opinion of the finance minister, the 1991 constitution was right in mandating the regulation of the subnational governments’ access to loans for the sake of fiscal responsibility and macroeconomic stability, and congress has done a good job in crafting such a mandate into a series of laws. Some excesses appear to have been committed, though. Law 617 of 2000, for

example, sets ceilings on the subnational governments operating expenditures (*funcionamiento*), a move criticized by some interviewees for encroaching on subnational governments' autonomy.

Factors causing subnational fiscal stress can be classified as factors beyond and within the subnational authorities' control. Departmental public finances are vulnerable to fluctuations in economic activity (mostly a non-controllable factor for the subnational authorities), especially to severe slowdowns, as the 1999 recession made apparent. Yet, as the recession also showed, the departmental governments' policy options are heavily constrained by national legislation, another non-controllable factor from a subnational standpoint for many practical purposes. The departments, for instance, are not authorized by national legislation to vary independently the tax rates applied to most of their taxes. National legislation also set certain requirements as to the size of the departments' bureaucracy.

Decisions by the departmental or municipal authorities –a controllable factor- may nevertheless contribute their part to subnational fiscal crises, like the decision to hire personnel without having the necessary budgetary backing, which the governor of Magdalena and the mayor of Santa Marta singled out as a problem in their jurisdictions, while attributing it to previous administrations.

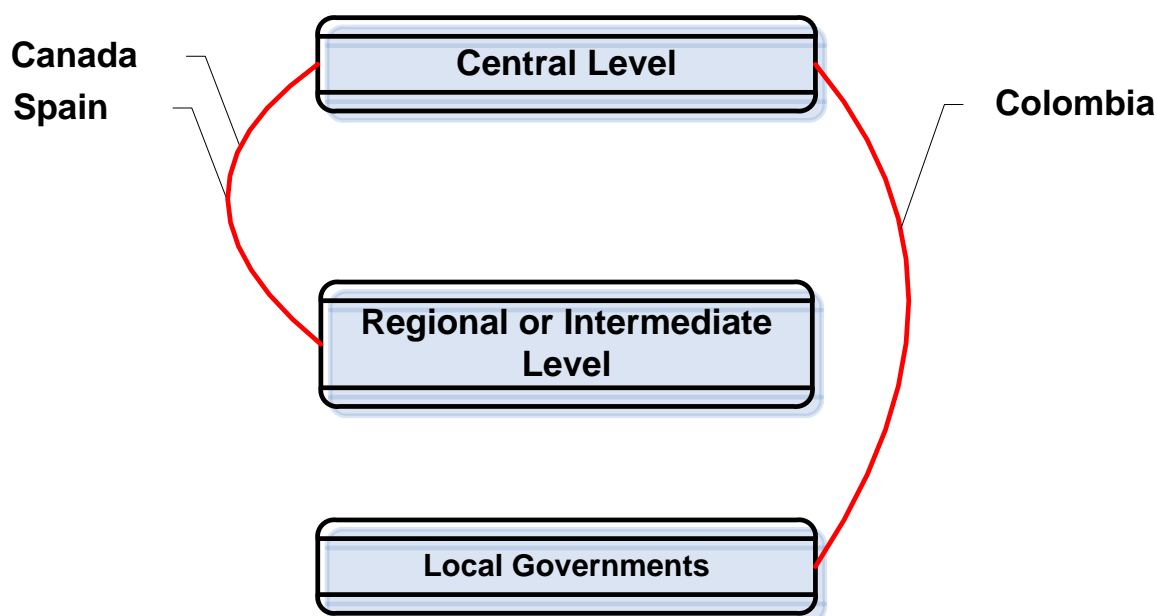
Valle del Cauca's governor, Angelino Garzón, portrays the terms of the centralization-decentralization debate as follows: “[In Colombia] two totally different political conceptions prevail. The national government's conception, which holds that the country must be centralized even in fiscal affairs, and the departmental governments' conception, which, albeit sheltering a variety of opinions, holds that the country must have more [decentralization] and regional autonomy.” Yet many of the interviewees seem to agree with Yopal's mayor when he states that “in general terms, since the 1991 constitution the country has become more decentralized.”

Oftentimes it goes unnoticed, however, that decentralization does not necessarily go hand in hand with the harmonic development of the regions, which arguably requires the institutionalization of fiscal mechanisms aimed at tempering interregional fiscal disparities.

## 12.0 CONCLUDING REMARKS

The mandate for state intervention to “promote the harmonic development of the regions,” enshrined in the Colombian 1991 constitution, offers an anchor for policies directed towards the moderation of regional economic disparities. A similar type of anchor is provided by the Canadian and Spanish constitutions. Yet the international comparison carried out here indicates that the importance accorded to interregional equalization as an end in itself varies across the dimensions of development. Thus, as far as education and health care are concerned, the public policy goals can be best described as interpersonal equalization of basic services, which implies but is not the same as interregional equalization. But because government responsibilities for the provision of such services largely rest on sub-central levels of government, whose component jurisdictions generally differ in terms of wealth and fiscal capacity, some sort of fiscal equalization across the relevant sub-central jurisdictions becomes a necessary condition for the achievement of the interpersonal goals. The reduction of overall regional economic disparities, which may include but goes beyond education and health care, is a public policy goal in its own right in Canada and Spain. Programmatic fiscal tools to counteract such regional disparities are built-in in their systems of multi-level government finance. In what can be taken as a sign that the “harmonic development of the regions” constitutional mandate has yet to gain ground in the policy making arena, fiscal tools of that kind are by and large absent from the Colombian fiscal institutions. Perhaps this is not that surprising given that in Colombia the dominant

intergovernmental linkages are those between the central and the local (*not* the regional) levels of governments, unlike Canada and Spain, where the strongest connections involve the central and regional or intermediate levels (Figure 12.1).



**Figure 12-1: Dominant linkages between levels of government by country**

To the question of what the current Colombian fiscal constitution seeks in matters of education and health care, the short answer would be universal coverage of basic services and decentralization. This is the framework for policy in the two areas provided by the written constitution. As it happens, so too can be characterized the situation in Canada and Spain, although with caveats. For a given basket of services, universal coverage is a more far-reaching goal than equalization *between* regions because it also implies equalization *within* regions. In a conventional means and ends policy framework, universal coverage would be the collective goal, while decentralization would be the means to achieve it. This framework for policy poses serious challenges in terms of coordination within a multi-level system of government. One reason such coordination is hard to achieve is that the institutional architecture of multilevel government and

universal coverage is not always crafted in the legal system as interrelated means and ends; instead, sometimes their legal design runs in parallel or in loosely coupled loops. But this problem is hardly exclusive to Colombia. Even at the constitutional stage the span of choice may be limited for historical and other reasons. Besides, the spatial distribution of political and fiscal power associated with decentralization can be a valid end in itself.

Although the legal form taken by the aspiration to universal education and health care, which varies across countries (e.g., different types of rights and commitments, public service status), is not irrelevant, the international comparison undertaken here suggests that still more important is the existence and enforcement of such collective aspiration. The wording of the constitution leaves little doubt about the existence in Colombia of a universal coverage goal, but, notwithstanding the progress towards it, the outputs of the strategy of enforcement appear to have been less than satisfying. A rights-based approach to universalization may undermine the credibility of the legal system in the event that it is not accompanied by a corresponding willingness to tax and when enforcement is lax, the Colombian experience suggests. These failures do not invalidate, however, the goal of universal coverage.

In Canada, the main enforcement mechanism of the commitment to reducing disparities in opportunities and in access to essential public services between regions, and even within the regions, seems to be the operation of the system of democratic federalism, where the balance of powers between levels of government occupies in turn a prominent place. Thus, on the word of Baier (2002, p. 34), “Canadians appear to side with the Supreme Court as an interpreter of rights, but the judicial review of federalism is somehow seen as inferior to governmental negotiation and compromise.” Indications are that in Colombia, in part by constitutional design, the balance of powers, the vertical one in particular, plays a secondary role in enforcing the education and

health goals, not to mention the harmonic development of the regions aspiration, in any case much lower than in Canada and, probably, than in Spain. Judicial enforcement, especially via the writ of protection (*acción de tutela*), has tended to be given precedence. Ingrained in the Colombian constitution, the writ of protection is conceived as an enforcement resource of last resort, and usually has only case by case effects. If left alone, these features make it an unlikely avenue for the universalization of services. Judicial enforcement, so applied, may complement but not substitute for the structure of government and the balance of power as enforcement mechanisms.

Taking into account that Colombia divides the government responsibilities associated with the provision of basic health and education services between the local and intermediate levels of government (with the local expected to gain more and more weight), while maintaining the regulation and financing responsibilities essentially at the national level, universal coverage requires at least the following: *i*) mutually complementary mechanisms of fiscal equalization between local jurisdictions and between departmental jurisdictions, particularly as regards standardized expenditure needs, which is the variable selected in the Colombian institutional arrangement as the basis for equalization in the referred areas; *ii*) national regulation aimed at coordinating the functions and resources of the local and departmental governments within each and between all subnational jurisdictions; and *iii*) institutional and financial mechanisms to convert, in each and all subnational jurisdictions, basic education and health care into public goods, that is, into goods that, among other things, are non-excludable (i.e., goods available to everyone), which implies the jurisdictional match or near match between supply and demand for such basic services. A large part of the rationale for these requirements arises from the fact that in Colombia both the departments and the municipalities are creatures hierarchically

subordinated to the national level (the authority of the departmental governments over the local governments in their respective jurisdiction is marginal), as well as from the fact that subnational jurisdictions differ sharply in their wealth and levels of income and, therefore, in their tax revenue potential.

There are reasons to believe that the Colombian multilevel government approach to universal coverage of basic health and education services is particularly prone to system-wide coordination failures induced by legislation. The Canadian and Spanish approaches are not immune to such type of coordination failures, which could arise in one or more of the chain links mentioned above, but their scope is likely to be more limited or localized. Whereas in Colombia countrywide legislation needs to coordinate three levels of government, in Canada and Spain countrywide coordination involves only two levels (this is probably truer for Canada). The potential for coordination failures are likely to grow with the number of levels of government, and with the number of units of government within each level to be covered by the legislation. Unlike Colombia, in Canada and Spain coordinating the functions and resources of the regional and local governments by countrywide legislation is not an institutional design imperative for converting basic education and health care into public services within each regional jurisdiction. This may help to curb the spread to the system as a whole of what otherwise would be local failures in the provision of services.

One route that Colombia could follow would be to choose the intermediate level of government as the standard-bearer for the provision of basic health and education services, and its component units, the departments, as the subjects of the fiscal equalization required for universal coverage purposes. In addition to reducing the risks of coordination failures caused by central level legislation, this option would allow a greater exploitation of the economies of scale



compared to an alternative centered on the local level, but would probably face opposition from local governments, whose increasing role would be curtailed. While in principle closer to the possible beneficiaries of services, municipalization, the route followed by Colombia in recent years, is likely to carry costs in terms of underused economies of scale and can be more demanding from a coordination standpoint, since by construction the number of municipalities is larger than the number of departments or regions. To the extent that municipalization is more decentralized than departmentalization (or regionalization), the Colombian route for the provision of education and health services may be a case in which more decentralization is not necessarily a good thing.

It should not be overlooked that universal coverage of basic education and health care can in principle be achieved through different institutional combinations along the centralization-decentralization axis. Whatever the level of government in charge of the provision responsibilities, access to the referred social services should not be conditioned upon the beneficiaries' ability to pay, if universal coverage is to be attained. Should the intermediate level of government be chosen as the standard-bearer of the provision of services, legislation to ensure the non-exclusion of potential beneficiaries, whatever their place of residence happens to be, would be essential for a successful reform. As the interviews with Colombian policy makers indicate, fear that a system of intergovernmental transfers with the departments as sole transfer recipients and managers would end up enhancing the opportunities for the diversion of resources by regional politicians, or benefiting only a few municipalities with high political clout, is one of the main barriers to a reform aimed at making the departments the axes of the provision of social services. Of course, the non-exclusion condition remains valid if the responsibilities for such

provision are divided, as currently occurs in Colombia, between the intermediate and local levels of government.

Fiscal equalization between sub-central jurisdictions, regional or other, for basic education and health care purposes, provided through the intergovernmental transfer system, becomes a condition, an intermediate policy target if you like, for making access to such services independent from the beneficiaries' ability to pay. It in effect would ensure that subnational governments have the potential to finance universal coverage within their respective jurisdictions.

As regards health care, Canada separates access to basic services from the patients' ability to pay by requiring each province to make the same health insurance plan available to everyone. Colombia offers two types of health insurance, depending on the sufficiency or insufficiency of the beneficiary's ability to pay. In light of our comparative exercise, the Colombian approach to universal coverage suffers from two major flaws. The first is that the beneficiaries of publicly subsidized health insurance are selected by a means testing program, which by design has the potential for exclusion, just what should be avoided in a universal coverage environment. The second flaw is that the publicly subsidized health insurance plan is at a disadvantage in terms of quality and quantity of services. From the perspective of the regional disparities in basic health care, the design of this scheme is likely to take a higher toll on the jurisdictions with greater incidence of poverty. After all, relatively more people there have the potential of being excluded from health insurance, whereas the number of people with health insurance that receive inferior health services can be expected to be relatively higher than in the national average.

A particularly favorable opportunity for the Colombian central level of government to harness intergovernmental transfers to accomplish universal coverage of basic services arises from the unitary nature of the country and the high reliance of subnational government finance on such transfers. The constitutional grounds for the health and education transfers are solid, in contrast to what happens in Canada, where their constitutionality is in some respects questioned. The Colombian central level of government has not made much of the opportunity, though. While the significant increase in the volume of intergovernmental transfers induced by the 1991 constitution has helped to reduce regional disparities in coverage, the formulas for allocating the transfers to the subnational jurisdictions still tend to favor the reproduction of past inequalities, assessed on a per eligible beneficiary standardized basis. This creates the conditions for basic education and health services to differ markedly between jurisdictions. In what can be seen as a reminder of the importance of path dependence in institutional change, this distributive pattern in important respects resembles the one in place in the pre 1991 constitution years.

Under the Colombian 1991 constitution, the notion of education and health expenditure needs that has prevailed for distributing intergovernmental transfers among subnational governments refers mainly to the expenditure needs derived from the population already covered with the corresponding services, giving the population not yet covered a marginal weight. This is somewhat at odds with the universal coverage goal embodied in the constitution.

Moving towards a situation where expenditure needs are standardized on a per capita basis, with all the potential or eligible beneficiaries of the services in each jurisdiction counted for distributive purposes (not only the already covered), be the school-age population for education, or total population for health care, seems more consistent with a universal coverage goal. To avoid or limit the free rider problem, transfers could be designed in a way that allows

regional governments to provide a similar level of services at similar levels of taxation, to paraphrase the Canadian constitution. The wording of the 1991 constitution, as amended, appears sufficiently open to allow the transition to the new situation.

A source of concern in Colombia is the presumed inconsistency between the private delivery of basic health and education services, on the one hand, and universal coverage, on the other. The exploration advanced here suggests that hospitals, clinics and even the medical services themselves can be public, private or other (e.g., third sector organizations), as indeed occurs in all three countries, but if universal coverage of basic services is to be achieved, access ought not to be conditioned by the patients' ability to pay. A similar reasoning applies in the case of education.

Considering that for government functions other than education and health care, intergovernmental transfers to the intermediate level of government are practically non-existent in Colombia, it seems desirable to introduce a general-purpose transfer. The general rather than specific purpose of this transfer would let departmental governments adapt the use of the transfer to their changing needs, a positive development given that the current system of transfers as a rule does not favor regional adaptability. Along with the tax revenue weakness of the Colombian departments, the absence of a general purpose transfer helps explain the inadequate provision of regional infrastructure and regional public goods in the country. There is, our exploration of the fiscal constitution suggests, a near vacuum of economic government at the intermediate level of government in Colombia.

Spain's Interterritorial Compensation Fund and Canada's equalization payments, which address regional income-related disparities by means of restricted fiscal equalization, are, especially the latter, rich sources of ideas for the design of a general-purpose equalization

transfer tailored to Colombian conditions. Canada's equalization payments are truly general purpose, and their allocation among the provincial governments seeks to reduce disparities in potential tax revenue, adjusted by provincial tax effort. One advantage of their design is that it encourages cooperation among countrywide taxpayers (federal or national) and regional taxpayers, creating a kind of partnership for regional development, while discouraging, at least at the margin, free-riding on the part of regional governments. A similar tax effort requirement exemplifies a way of harnessing the potential of the intermediate level of government, more through incentives and less through fine print legislation attempting to control the behavior of people and to anticipate all relevant circumstances. A fiscal tool like the Interterritorial Compensation Fund, designated for public investment (therefore, not truly general purpose), can help remove infrastructure bottlenecks at the regional level. The nature of the problem that a general purpose equalization transfer is suited to deal with (e.g., regional income disparities or their immediate consequences) transcends the boundaries of systems of government and legal traditions.

In the event that the role of departmental governments in the Colombian political and fiscal decentralization is expanded, an important step would be to strengthen departmental taxation. A good deal can be learned from Canada and Spain on how to do it. Both countries rely extensively on tax sharing between the central and intermediate levels of government, in contrast to the Colombian approach that is based on the allocation of exclusive tax revenue sources to each level of government. Proposals that seek to strengthen departmental taxation at the expense of national taxation are not uncommon. Tax sharing, however, does not need to erode national taxation.

Spain offers an example of large, if not dramatic, fiscal change harnessed by means of the legal system. In 1990 the Spanish intermediate level of government of the common regime (that is, excluding the Basque Country and Navarre) was, in terms of its overall level of taxation, almost as weak as that of Colombia (Table 12.1). Largely as a result of a major tax reassignment from the central to the intermediate level, whose effects came to be realized starting in 2002, the autonomous communities of the common regime gained substantial tax revenue leverage, an illustration of the malleability of fiscal relations between levels of government. Intergovernmental transfers experienced a more or less concomitant reduction. Crossing the borders of legal traditions and systems of government, Spain is getting closer to Canada and away from Colombia in terms of the fiscal strength of the intermediate level. The case may be that a fiscally strong intermediate level works in and is appropriate for different institutional contexts.

**Table 12-1: Changes in the tax burden of the intermediate level of government by country**

| Country               | Level of Taxation (Share of GDP) |                              |
|-----------------------|----------------------------------|------------------------------|
|                       | Initial Level, 1990              | Change between 1990 and 2005 |
| Colombia <sup>a</sup> | 1,3                              | 0,1                          |
| Canada                | 12,2                             | -0,8                         |
| Spain <sup>b</sup>    | 2,1                              | 6,5                          |

| Country               | Share of Corresponding Total Tax Revenue |                              |
|-----------------------|--|------------------------------|
|                       | Initial Share, 1990                      | Change between 1990 and 2005 |
| Colombia <sup>a</sup> | 12,2                                     | -4,6                         |
| Canada                | 41,2                                     | 0,1                          |
| Spain <sup>c</sup>    | 9,9                                      | 27,5                         |

Source: Table 10.5

<sup>a</sup> The figure includes Bogotá's typically departmental tax revenues.

<sup>b</sup> The figure refers to the Common Regime only, relative to the corresponding GDP.

<sup>c</sup> The figure refers to the Common Regime only.

As the Canadian and Spanish examples show, tax sharing, particularly of the major taxes (e.g., income taxes and VAT), goes a long way towards ensuring the relative fiscal and political autonomy of both the central and regional governments. But tax sharing makes the need for tax coordination between and within levels of government particularly compelling. One objective of tax coordination would be to prevent the country's overall level of taxation to go beyond a threshold deemed desirable. Another objective would be to assign a share of the overall tax room to each level of government, taking into account their respective functions and expenditure responsibilities. Tax coordination, in the form, for instance, of tax rate bands or tax rate floors, would also be required to avoid destructive tax competition between regional governments, if, as would be desirable, they are given some freedom to set their own tax rate schedules. Since in Colombia the original power to tax rests with the central level of government, both vertical and horizontal tax coordination would probably require national legislation.

A likely consequence of giving the intermediate level of government access to the income tax or VAT bases is the deepening, rather than the moderation, of horizontal fiscal disparities (i.e., disparities between departments). For tax decentralization and the balanced development of the regions not to become incompatible objectives, it is necessary to build institutions for mobilizing tax revenue from the advanced regions to the lagging ones. A key piece of such institutions is the intergovernmental transfer system.

Probably for the majority of policy makers interviewed for this study the decentralization of fiscal powers is not inconsistent with a deeper policy involvement by the national level for reducing regional economic inequalities. This view is upheld by the direction of the flow of transfers in Colombia, which goes from the national to the subnational level.

Intergovernmental transfers are not the only programmatic tool to counteract regional fiscal or economic disparities. The income tax is another such kind of tool. For it to work as an automatic stabilizer of the regional business cycles, the tax rate schedule and the other elements of the tax need to be designed following a progressive pattern. In Colombia, the potential countercyclical effectiveness of income taxation is undermined by its relatively low coverage, as a result, among other things, of tax exemptions. In recent decades, income taxation has been losing ground as a source of national tax revenue. A policy to moderate regional economic disparities would have in the income tax one proven tool for the task, with the advantage that its automatic stabilizing effect would render the fiscal constitution more robust.

Automatic fiscal stabilizers built into the legislation, such as regional equalization payments and progressive income taxation, offer a promising avenue for counteracting regional economic disparities in Colombia.

In none of the fiscal constitutions examined here is public indebtedness used as a programmatic tool to deal with regional economic disparities. Access to credit by sub-central governments is regulated by the central level of government in Colombia and Spain, mainly for macroeconomic stabilization and debt sustainability purposes. Canada, where provincial indebtedness is not federally regulated, can be an example of fiscal discipline or prudence, culturally and politically self-enforced. Meant to finance public investment, as mandated by law in Colombia and Spain, indebtedness by sub-central governments can help overcome barriers hindering regional development. However, indebtedness is no permanent solution to the horizontal fiscal disparities conundrum, given its generally sporadic nature and the linkage between a sub-central government's credit worthiness and ability to pay, ability that in turn ultimately depends on the fiscal capacity of the corresponding jurisdiction.



Colombia's constitution authorizes the differential legal treatment of departmental governments in terms of degrees of autonomy and fiscal powers. The use given up to now to such constitutional authorization is far from having the extent that *de jure* fiscal asymmetry exhibits in Spain (Basque Country and Navarre) and Canada (Quebec) for historical and other reasons. It is not clear how *de jure* fiscal asymmetry may further the reduction of regional economic disparities when the asymmetry favors the richest regions (bear in mind, however, that *de jure* fiscal asymmetries do not necessarily exist for counteracting regional economic disparities). For example, if as a result of differential legal treatment in the fiscal realm, the contribution of the rich regions to the central public treasury is limited, at best, to be directly proportional to the size of their economies, interregional progressive taxation (another thing might occur from an interpersonal perspective) would be precluded as far as such type of regions is concerned. In this situation equalization transfers are still feasible, however.

If the differentiation of legal treatment consists of fiscal agreements between the central government and each regional government, the least politically powerful regions would be likely to get relatively unfavorable deals. Moreover, the complexity of each and all the fiscal agreements can make it difficult to distinguish the regional fiscal disparities that may eventually arise from legislation from those arising from other factors, such as "the play of the forces in the market," which according to Myrdal (1957, p. 26), "normally tends to increase, rather than to decrease, the inequalities between regions," as a result of the operation of what is known as the principle of circular and cumulative causation. This is not to say that such agreements cannot be coordinated to prevent unwanted effects, only that the challenge may indeed be huge.

A fiscal treatment favorable to the economically lagging regions can be introduced in the legislation without granting permanent entitlements to particular regions. For example, taking

into account the budget constraint of the national government, equalization payments in Colombia could be limited only to the lagging regions. In order to avoid the entrenchment of region-specific entitlements in the fiscal constitution, the criteria for selecting the beneficiary regions should be general or jurisdiction-blind, as exemplified by the requirement that their GDP per capita should not be higher than a certain threshold (e.g., 75% or 80% of national per capita GDP). Permanent jurisdiction-specific entitlements are pervasive in the legislation that governs the allocation of royalties for the exploitation of natural resources, for instance. Generality in the form of jurisdiction blindness would contribute to enhancing the fiscal constitution's robustness. A case can be made as well for fiscal benefits for sparsely populated regions or regions with extreme weather. The Canadian territories are examples of regions with such features.

Particularly with regard to the intergovernmental transfer system, the Colombian 1991 constitution has tended to be less a framework for policy and more the setting for the formulation of the policies themselves. Unlike the Canadian and Spanish cases, Colombia has shown an inclination to entrench the design details of the intergovernmental transfer system in the constitution. This proneness to details in the constitution may be an attempt to tackle the time inconsistency of governments, but it renders the constitution less robust to changes in the economic and fiscal conditions, as has been the case of the rules for determining the volume of intergovernmental transfers. Some design shortcomings of the original education and health transfers associated with the sequence in the allocation rules have been remedied (now the designated uses are set before the criteria for distribution among beneficiary jurisdictions), but there are signs that other design shortcomings have been maintained in, or added to, the fiscal constitution.

As the Spanish and Canadian constitutions exemplify, a system of intergovernmental transfers can be harnessed to address regional economic disparities with a general mandate and some guidelines to that effect included in the written constitution. It may be necessary or useful to entrench programmatic policy tools in the constitution, but their specifics do not naturally belong there. One step to bring some stability to the Colombian written constitution, while guarding against the time inconsistency of governments, would be to move the details of the transfers' design to hierarchically lower legislation of a kind requiring qualified majority voting for its approval and amendment.

A dose of territorial representation in the Senate, combined with popular representation in the House of Representatives, is likely to be a better guarantee of regionally balanced development policies than the entrenchment of the policies in the written constitution, even more so when the constitution can be easily amended, as occurs in Colombia. Such dose of territorial representation would help to level the political playing field for decisions related to regional development policies, which in the unitary system of government that prevails in Colombia are in essence a prerogative of the central level of government. In Spain and Canada, a reform of the upper chamber of congress in such direction has at times been in the political spotlight. Territorial representation, as a way of gearing the policy making process, may well be the constitutional guarantee of last resort for the fiscal state to contribute to the harmonic development of the regions.

To sum up, the findings of this study indicate that the Colombian departments, the jurisdictions of the intermediate tier of government, have been largely neglected, often sidestepped, as potential axes of decentralization and standard-bearers of fiscal equalization, contributing to the creation of what could be described as a near vacuum of economic

government at the regional level. No current regional substitutes for the departments exist. The reduction of fiscal disparities at the subnational level (not necessarily their elimination) is considered possible and desirable, in the latter case insofar as it is a condition for achieving a less imbalanced economic development within and between jurisdictions. Colombia has made progress in reducing the geographic disparities in basic health and education coverage mainly via the local governments, but a locally based provision of such services under the existing unitary system of government appears particularly susceptible to system-wide coordination failures caused by legislation. For a similar basket of basic services, universal provision of education and health care, an interpersonal equalization policy goal shielded by the Colombian 1991 constitution, can hardly be accomplished, the findings show, as long as access is dependent on the beneficiaries' ability to pay and as long as intergovernmental transfers are allocated on the basis of non-standardized expenditure needs, two conditions that are likely to be markedly harmful to the most impoverished jurisdictions.

In contrast with the Canadian and Spanish cases, the Colombian system of intergovernmental relations does not have a programmatic fiscal tool both to counter the impact of geographic disparities in fiscal capacity on the public finances of regional governments and to fund regional public spending in areas other than education and health, in spite of the fact that in Colombia the regional disparities in fiscal capacity, as measured by per capita income, are exceptionally acute. There is arguably a need for income-related regional equalization by way of a general purpose intergovernmental transfer. Given the budget constraints faced by the Colombian central government, the recipients of the transfer could in principle be only jurisdictions that lag well behind in terms of per capita fiscal capacity, with no permanent entitlements for specific jurisdictions. This scheme would probably work at its best when

accompanied by tax sharing between the national and intermediate levels of government, alongside progressive income taxation.

## APPENDIX A. SCORING OF INTERGOVERNMENTAL RELATIONS

| Criteria  | Colombia | Canada | Spain |
|---|----------|--------|-------|
| Federal (+); Unitary (-)                            | -3       | 3      | 0     |
| Centralization (+); Decentralization (-)            | 0,8      | -1,3   | -0,5  |
| Formal representation of the regions                | -1       | -1     | -1    |
| Rules for selecting regional chief executives       | -4       | -3     | -4    |
| Constitutional assignment of residual power         | 4        | 2      | 3     |
| Allocation of fiscal powers to regional governments | 4        | -3     | 0     |

NOTE: Criteria on the centralization/decentralization dimension were given equal weights.

### Scoring

- +/-4 Very High
- +/-3 High
- +/-2 Medium
- +/-1 Low
- 0 In between

## **APPENDIX B. DISTRIBUTION OF COLOMBIA'S GENERAL PURPOSE TRANSFER**

Measures of relative poverty (*RP*), the degree of urbanization (*U*), fiscal efficiency (*FE*) and administrative efficiency (*AE*) are the prescribed distributive criteria of Colombia's General Purpose Transfer. The distribution formula can be written as follows:

$$GP_{i,t} = [0.4 (RP_{i,t}) + 0.4 (U_{i,t}) + 0.1 (FE_{i,t}) + 0.1 (AE_{i,t})] GP_t$$

Where  $GP_t$  and  $GP_{i,t}$  represent the total amount of the general transfer and the amount allotted to municipality  $i$  in period  $t$ , respectively. Between 2002 and 2005 there was, however, a transition period in the application of this formula, whereby a growing proportion of the total transfer was allocated in line with the formula.

## APPENDIX C. TRANSFERS FROM THE BASQUE COUNTRY AND NAVARRE TO SPAIN'S CENTRAL GOVERNMENT

In determining the size of the block transfer of each autonomous community, the heart of the calculation is to price the functions of Spain's central government, net of the value of those central government functions taken on by the autonomous governments, and to apportion the resulting amount according to the Basque Country's and Navarre's shares in Spain's total income.\* Formally,

$$Tri = [(CGF - CGFi) Yi/YT] - Ci$$

Where

$Tri$  : Amount of transfer of autonomous community  $i$  to Spain's central government;

CGF : Value of central government functions;

$CGFi$  : Value of central government functions carried out by autonomous community  $i$ ;

$Yi$  : Total income of autonomous community  $i$ , as measured, for instance, by GDP;

$YT$  : Spain's total income, as measured, for instance, by GDP;

$Ci$  : Compensations to autonomous community  $i$ .

It is worthwhile noting that, via the block transfer to the central government, the Basque Country and Navarre help financing the *Interterritorial Compensation Fund* (Fondo de Compensación Interterritorial), as it classifies as part of the central government functions not taken on by the autonomous communities of the *foral* regime.

---

\* . SPA. *Ley Quinquenal del Cupo del País Vasco 2002-2006 and Ley 25/2003, modificación del Convenido Económico de Navarra.*



## BIBLIOGRAPHY

- Acemoglu, D., S. Johnson, et al. (2001). "The Colonial Origins of Comparative Development: An Empirical Investigation." The American Economic Review **91**(5): 1369-1401.
- Agranoff, R. and J. A. Ramos (1997). "Toward Federal Democracy in Spain: An Examination of Intergovernmental Relations." Publius **27**(4): 1-38.
- Ahmad, E., Ed. (1997). Financing decentralized expenditures: an international comparison of grants. Studies in fiscal federalism and state-local finance. Cheltenham, UK ; Brookfield, Vt., US, Edward Elgar.
- Ahmad, E., M. Albino-War, et al. (2006). Subnational Public Financial Management: Institutions and Macroeconomic Considerations. Handbook of fiscal federalism. E. Ahmad and G. Brosio. Northampton, MA Edward Elgar Publishing.
- Ahmad, E. and R. Thomas (1997). Types of transfers - A general formulation. Financing Decentralized Expenditures. E. Ahmad. Cheltenham, UK, Edward Elgar: 361-381.
- Alesina, A. (2001). Reformas institucionales en Colombia. Bogotá, Fedesarrollo: Alfaomega.
- Alesina, A. and R. Perotti (1999). Budget deficits and budget institutions. Fiscal institutions and fiscal performance. J. M. Poterba and J. Hagen. Chicago, The University of Chicago Press: 13-36.
- Alviar, O. and F. Rojas (1985). Elementos de finanzas públicas en Colombia. Bogotá, TEMIS.
- Anand, S. and A. Sen (2000). "The income component of the human development index." Journal of Human Development **1**(1): 83-106.
- Anand, S. and A. Sen (2003). Human Development Index: Methodology and Measurement. Readings in Human Development. S. Fukuda-Parr and A. K. Shiva Kumar. New Delhi, Oxford University Press.
- Anderson, J. E., Ed. (1994). Fiscal equalization for state and local government finance. Westport, Conn., Praeger.
- Arrow, K. J. (1963). "Uncertainty and the Welfare Economics of Medical Care." The American Economic Review **53**(5): 941-973.
- Axelrod, R. M. and M. D. Cohen (1999). Harnessing complexity: organizational implications of a scientific frontier. New York, Free Press.
- Ayala, L. (2003). El sistema de garantías de rentas: Un balance a los 25 años de la Constitución. Gasto Público en la Democracia. J. Salinas and S. Alvarez. Madrid, Instituto de Estudios Fiscales.
- Bahl, R. W. and J. F. Linn (1992). Urban public finance in developing countries. Oxford [England]; New York, N.Y., Published for the World Bank by Oxford University Press.

- Baier, G. (2002). Judicial review and Canadian federalism. Canadian federalism: Performance, effectiveness and legitimacy. H. Bakvis and G. D. Skogstad. Oxford; New York, Oxford University Press.
- Bell, G. (1998). The Decentralised State: An Administrative or Political Challenge? Colombia : The Politics of Reforming the State. E. Posada-Carbó. New York St. Martin's Press.
- Beramendi, P. and R. Máiz (2004). Spain: Unfulfilled Federalism (1978-1996). Federalism and Territorial Cleavages. U. Amoretti and N. Bermeo. Baltimore and London, The Johns Hopkins University Press: 123-154.
- Bird, R. and P.-P. Gendron (2001). VATs in Federal States: International Experience and Emerging Possibilities. Working Paper Series, Andrew Young School of Policy Studies, International Studies Program. Georgia State University. **4**.
- Bird, R. M. (1999). Fiscal federalism. The encyclopedia of taxation and tax policy. J. J. Cordes, R. D. Ebel and J. G. Gravelle, Urban Institute Press.
- Bird, R. M. and A. Tassonyi (2003). Constraining Subnational Fiscal Behavior in Canada: Different Approaches, Similar Results? Fiscal decentralization and the challenge of hard budget constraints. J. Rodden, G. S. Eskeland and J. I. Litvack, MIT Press.
- Bird, R. M. and F. Vaillancourt (2006). Changing with the times: Success, failure, and inertia in Canadian federal arrangements, 1945-2002. Federalism and Economic Reform: International Perspectives. J. S. Wallack and T. N. Srinivasan, Cambridge University Press.
- Boadway, R. (2005). The vertical fiscal gap: Conceptions and misconceptions. Canadian fiscal arrangements: What works, what might work better. H. Lazar. Montreal & Kingston, McGill-Queen's University Press.
- Boadway, R. W. and H. M. Kitchen (1999). Canadian Tax Policy. Toronto Canadian Tax Foundation.
- Bonet, J. and A. Meisel (1999). La convergencia regional en Colombia: una visión de largo plazo, 1926–1995. Coyuntura Económica. Bogotá, Fedesarrollo. **29**.
- Bonet, J. and A. Meisel (2007). Polarización del ingreso per cápita departamental en Colombia. Ensayos sobre política económica. Bogotá, Banco de la República. **25**.
- Braën, A. (2002). Health and the Distribution of Powers in Canada. Discussion Paper No. 2, Commission on the Future of Health Care in Canada.
- Brennan, G. and J. M. Buchanan (1980). The power to tax: analytical foundations of a fiscal constitution. Cambridge, Cambridge University Press.
- Brennan, G. and J. M. Buchanan (1985). The reason of rules: constitutional political economy. Cambridge; New York, Cambridge University Press.
- Breton, A. (1996). Competitive governments: an economic theory of politics and public finance. Cambridge; New York, Cambridge University Press.
- Brooks, S. (2004). Canadian democracy: an introduction. Don Mills, Ont. ; New York, Oxford University Press.
- Brown, D. M. (2002). Fiscal federalism: the new equilibrium between equity and efficiency. Canadian federalism: performance, effectiveness, and legitimacy. H. Bakvis and G. Skogstad. New York, Oxford University Press: 59-84.
- Buchanan, J. M. (1950). "Fiscal Federalism and Fiscal Equity." The American Economic Review **40**(4): 583-599.
- Buenahora, J. (1997). La democracia en Colombia: un proyecto en construcción. Bogotá, Tercer Mundo Editores.

- Cárdenas, M. (1993). Crecimiento y convergencia en Colombia: 1950 – 1990. Planeación y Desarrollo. Bogotá, Departamento Nacional de Planeación.
- Castro, J. (1998). Descentralizar para pacificar. Santafé de Bogotá, D.C., Colombia, Editorial Ariel : Planeta Colombiana Editorial.
- Cifuentes, E. (2003). Reflexiones sobre la influencia de la Constitución española de 1978 en la Constitución colombiana de 1991 La Constitución de 1978 y el constitucionalismo iberoamericano. F. Fernández. Madrid, Centro de Estudios Políticos y Constitucionales 281-310.
- Clark, D. (1997). The Fiscal Transfer System in Canada. Financing Decentralized Expenditures: An International Comparison of Grants. E. Ahmad. Cheltenham, UK, Edward Elgar: 70-102.
- Comisión Racionalización de las Finanzas Públicas (1997). El saneamiento fiscal, un compromiso de la sociedad. Bogotá, D.C., Colombia, Ministerio de Hacienda y Crédito Público.
- Commission on Fiscal Imbalance (2002). A New Division of Canada's Financial Resources. Québec.
- Commons, J. R. (1925). "Law and Economics." The Yale Law Journal **34**(4): 371-382.
- Commons, J. R. (1931). "Institutional Economics." American Economic Review **21**: 648-657.
- Cooter, R. (2000). The strategic constitution. Princeton, N.J., Princeton University Press.
- Cowell, F. A. (1995). Measuring Inequality. New York, Prentice Hall/Harvester Wheatsheaf.
- Christaller, W. (1966). Central places in southern Germany. Englewood Cliffs, N.J., Prentice-Hall.
- de la Fuente, A. (2005). Los mecanismos de cohesión territorial en España: un análisis y algunas propuestas. Laboratorio de Alternativas. Madrid, Fundación Alternativas. **2005**.
- de la Fuente, A. and X. Vives (2003). Políticas públicas y equilibrio territorial en el Estado Autonómico. Bilbao, Fundación BBVA.
- Deber, R. B. (2002). Delivering Health Care Services: Public, Not-For-Profit, or Private? Discussion Paper No. 17, Commission on the Future of Health Care in Canada.
- Dickerson, M. and T. Flanagan (1982). An Introduction to Government & Politics. Toronto, Methuen.
- Dillinger, W. and S. B. Webb (1999). Decentralization and Fiscal Management in Colombia. Policy Research Working Paper. Washington, The World Bank. **2122**.
- Dirección de Desarrollo, T. (2004). Evaluación del Sistema General de Participaciones 2003. Bogotá, Departamento Nacional de Planeación.
- Dixit, A. and J. Londregan (1996). "The determinants of success of special interests in redistributive politics." The Journal of Politics **58**(4): 1132-1155
- Dixit, A. and J. Londregan (1998). "Fiscal Federalism and Redistributive Politics." Journal of Public Economics(68): 153-180.
- Dunford, M. (2000). Regional disparities in the EU through the lens of official statistics. Integration and transition in Europe. G. Petrakos, G. Maier and G. Gorzelak. New York, Routledge
- Echavarría, J. J., C. Rentería, et al. (2002). Decentralization and bailouts in Colombia. Washington, D.C., Inter-American Development Bank, Research Dept., Latin American Research Network.

- Elster, J. (2000). Ulysses unbound: studies in rationality, precommitment, and constraints. Cambridge ; New York, Cambridge University Press.
- Escobar, M.-L. and P. Panapoulou (2003). Salud. Colombia: Fundamentos Económicos de la Paz. M. Giugale, O. Lafourcade and C. Luff. Bogotá, Banco Mundial y Alfaomega.
- Fals-Borda, O. (1996). Región e historia: Elementos sobre ordenamiento y equilibrio regional en Colombia. Bogotá, IEPRI : TM Editores.
- Frankel, J. A. and D. Romer (1999). "Does Trade Cause Growth?" The American Economic Review **89**(3): 379-399.
- Fukuda-Parr, S. and A. K. Shiva Kumar, Eds. (2003). Readings in human development: concepts, measures, and policies for a development paradigm. New Delhi ; New York, Oxford University Press.
- Gallup, J. L., J. D. Sachs, et al. (1999). "Geography and economic development." International Regional Science Review **22**(2): 179-232.
- García, M. (2005). El debate a la financiación autonómica con los resultados del nuevo sistema. Documentos. Madrid, Instituto de Estudios Fiscales. **2006**.
- Gaviria, A., C. Medina, et al. (2006). Evaluating the Impact of Health Care Reform in Colombia: From Theory to Practice. Documentos CEDE Bogotá, Universidad de los Andes. **6**.
- Gavison, R. (2002). "What belongs in a constitution?" Constitutional Political Economy **13**(1): 89-105.
- Glendon, M. A., M. W. Gordon, et al. (1999). Comparative legal traditions in a nutshell. St. Paul, Minn., West Group.
- Glenn, H. P. (2004). Legal traditions of the world: sustainable diversity in law. Oxford ; New York, Oxford University Press.
- Gobernadores, F. N. d. (2006). Posición de los departamentos frente al proyecto de Acto legislativo que modifica el SGP. Departamentos al Día. Bogotá, Federación Nacional de Departamentos y Fondo Cuenta.
- Gómez-Pomar, J. (2002). El sistema de financiación de las Comunidades Autónomas de Régimen Común. Presupuesto y Gasto Público. Madrid, Ministerio de Economía y Hacienda, España. **28**.
- González, F. and V. Calderón (n.a.). Las reformas tributarias en Colombia durante el siglo XX. Documentos. Bogotá, Departamento Nacional de Planeación.
- Goodin, R. E., Ed. (1996). The theory of institutional design. Theories of institutional design, Cambridge University Press.
- Groenewegen, P. (1990). Taxation and decentralization: a reconsideration of the cost and benefits of a decentralized tax system. Decentralization, local governments, and markets. R. Bennett. New York, Oxford University Press: pp. 87-115.
- Gunther, R., J. R. Montero, et al. (2004). Democracy in modern Spain. New Haven, Yale University Press.
- Gutiérrez, C. and P. N. Ospina (1996). Desempeño financiero de las entidades municipales. Coyuntura Económica. Bogotá, Fedesarrollo. **26**.
- Hall, R. E. and C. I. Jones (1999). "Why Do Some Countries Produce So Much Output Per Worker Than Others?" The Quarterly Journal of Economics **114**(1): 83-116.
- Haq, M. u. (1995). Reflections on human development. New York, Oxford University Press.
- Harris, C. (1998). Regionalism and the Canadian archipelago. Heartland hinterland: a regional geography of Canada. L. McCann and A. Gunn, Prentice Hall Southeast Asia Pte Ltd

- Harrison, M. I. and A. Shirom (1999). Organizational diagnosis and assessment: bridging theory and practice. Thousand Oaks, Calif., Sage Publications.
- Hernández, G., C. Soto, et al. (2000). Exenciones tributarias: Costo fiscal y análisis de incidencia. Archivos de Macroeconomía. Bogotá, Departamento Nacional de Planeación.
- Herrero, C., A. Soler, et al. (2004). Capital Humano y Desarrollo Humano en España, sus Comunidades Autónomas y Provincias. 1980-2000. Valencia, Instituto Valenciano de Investigaciones Económicas.
- Hooghe, L. and G. Marks (2001). "Types of Multi-Level Governance." European Integration Online Papers 5(11).
- Horowitz, D. (2002). Constitutional design: proposals versus processes. The architecture of democracy. A. Reynolds. Oxford, New York, Oxford University Press.
- Junguito, R., L. Melo, et al. (1995). La descentralización fiscal y la política macroeconómica. Borradores Semanales de Economía. Bogotá, D. C., Banco de la República.
- Kalmanovitz, S. (2002). Constitución y modelo económico El debate a la constitución. V. M. Moncayo. Bogotá, Universidad Nacional e ILSA.
- Kanth, R., Ed. (1994). Paradigms in Economic Development. Armonk, New York; London, M. E. Sharpe.
- Katz, A. N. (1986). Canada, Australia, and New Zealand. Legal traditions and systems: an international handbook. A. N. Katz. New York, Greenwood Press: 51-64.
- Kesselman, J. and R. Cheung (2004). "Tax Incidence, Progressivity, and Inequality in Canada." Canadian Tax Journal 52(3).
- Krugman, P. R. (1995). Development, geography, and economic theory. Cambridge, Mass., MIT Press.
- Lawlor, T. and M. Rigby, Eds. (1998). Contemporary Spain: essays and texts on politics, economics, education and employment and society. London ; New York, Longman.
- Lazar, H. (2000). In Search of a New Mission Statement for Canadian Fiscal Federalism. Toward a New Mission Statement for Canadian Fiscal Federalism. H. Lazar. Kingston, ON McGill Queens Univ Press.
- Leeson, H. (2002). Constitutional Jurisdiction over Health and Health Care Services in Canada. Discussion Paper Commission on the Future of Health Care in Canada.
- Lempert, R. J., S. W. Popper, et al. (2003). Shaping the next one hundred years: new methods for quantitative, long-term policy analysis. Santa Monica, CA, RAND.
- Lewis, W. A. (1988). The roots of development theory. Handbook of development economics. H. B. Chenery and T. N. Srinivasan. Amsterdam, Elsevier. **Vol. I**.
- Litvack, J. I., J. Ahmad, et al. (1998). Rethinking decentralization in developing countries. Washington, D.C., World Bank.
- Lopez-Casasnovas, G., J. Costa-Font, et al. (2004). "Diversity and regional inequalities: Assessing the outcomes of the Spanish 'system of health care services'." Health Care and Fiscal Decentralisation in Spain Retrieved September 11, 2006, from <http://www.econ.upf.edu>.
- Lleras de la Fuente, C. (1996). Contexto general de la constitución económica. Constitución económica de Colombia. FINDETER. Bogotá, El Navegante Editores.
- MacNevin, A. S. (2004). The Canadian federal-provincial equalization regime : an assessment. Toronto, Canadian Tax Foundation.
- Magone, J. M. (2004). Contemporary Spanish politics. New York, Routledge.
- Martineau, P. (2005) "Federal Personal Income Tax: Slicing the Pie." Analysis in Brief.

- Martinussen, J. (1997). Society, state and market: a guide to competing theories of development. London Zed Books: Fernwood Pub. .
- McMillan, M. L. (2004). "Financial Relationships between Regional and Municipal Authorities: Insights from the Examination of Five OECD Countries." Working Papers Retrieved August 29, 2006.
- Merryman, J. H. (1985). The civil law tradition: an introduction to the legal systems of Western Europe and Latin America. Stanford, Calif., Stanford University Press.
- Mill, J. S. (1991). Considerations on Representative Government. New York, Prometheus Books.
- Millar, J. (1997). The Effects of Budget Rules on Fiscal Performance and Macroeconomic Stabilization, Bank of Canada.
- Ministerio de Economía y Hacienda de España (2006a). Los presupuestos de las comunidades y ciudades autónomas: Descripción general. Badespe. Madrid.
- Ministerio de Economía y Hacienda de España (2006b). Los presupuestos generales del Estado: Descripción general. Badespe. Madrid.
- Misión de Finanzas Intergubernamentales (1984). Intergovernmental finance in Colombia : final report of the Mission on Intergovernmental Finance. Cambridge [Mass.], International Tax Program, the Law School of Harvard University.
- Monasterio, C. (2002). El Sistema de Financiación Autonómica 2002. El Nuevo Modelo de Financiación Autonómica (2002). J. Salinas. Madrid, Instituto de Estudios Fiscales.
- Moncayo, V. M., Ed. (2002). El debate a la constitución. Bogotá, Universidad Nacional de Colombia : Instituto Latinoamericano de Servicios Legales Alternativos.
- Montenegro, A. (1995). "Constitutional design and economic performance." Constitutional Political Economy 6(2): 161-169.
- Musgrave, R. A. (1959). The theory of public finance: a study in public economy. New York,, McGraw-Hill.
- Musgrave, R. A. (1983). Who should tax, where, and what? Tax assignments in federal countries. C. E. McLure Jr. Canberra,, The Australian National University Press: p. 2-19.
- Myrdal, G. (1957). Economic Theory and Underdeveloped Regions. London, Me thuen & Co Ltd.
- Newton, M. T. and P. J. Donaghy (1997). Institutions of modern Spain: a political and economic guide. Cambridge ; New York, Cambridge University Press.
- North, D. C. (1990). Institutions, institutional change, and economic performance, Cambridge University Press.
- Oates, W. E. (1972). Fiscal federalism. New York, Harcourt Brace Jovanovich.
- Oates, W. E. (1999). "An essay on fiscal federalism." Journal of Economic Literature 37(3): 1120-1149.
- Ocampo, J. A. (1984). Centralismo, descentralización y federalismo en la historia de Colombia. Crisis mundial, protección e industrialización. J. A. Ocampo and S. Montenegro. Bogotá, Cerec.
- Okun, A. (1962). "Potential GNP: Its measurement and significance." Proceedings of the Business and Economics Section.
- Olson, M. J. (1969). "The Principle of Fiscal Equivalence: The Division of Responsibilities among Different Levels of Government." The American Economic Review 59(2): 479-487.

- Parra, G., I. León, et al. (2005). Los beneficios tributarios en el impuesto sobre la renta en Colombia. Cuadernos de Trabajo. Bogotá, Dirección de Impuestos y Aduanas Nacionales.
- Parra, N. H. (1992). El nuevo ordenamiento territorial y sus finanzas. Los cambios constitucionales 1991. N. H. Parra. Bogotá, Sociedad Económica de Amigos del País.
- Perry, D. B. (2001) "Cold but Hospitable." Canadian Tax Highlights.
- Perry, G. (1996). Estado y sector privado en la Constitución de 1991. Constitución económica colombiana. FINDETER. Bogotá, El Navegante Editores.
- Perry, G. and M. Huertas (1997). Historia de una crisis anunciada: regulando el endeudamiento de las municipalidades y departamentos en Colombia. Descentralización fiscal en América Latina. Nuevos desafíos y Agenda de Trabajo. G. Aghón and H. Edling. Santiago de Chile, CEPAL/GTZ.
- Persson, T. and G. E. Tabellini (2003). The economic effects of constitutions. Cambridge, Mass., MIT Press.
- Popper, K. R. (1961). The poverty of historicism. New York, Harper & Row.
- Posada-Carbó, E. (1996). The Colombian Caribbean: a regional history. Oxford, Oxford University Press.
- Programa Nacional de Desarrollo Humano (2004). Las regiones colombianas frente a los objetivos del milenio. Bogotá, DNP y otros.
- Ramsay, C. (2002). A Framework for Determining the Extent of Public Financing of Programs and Services. Discussion Paper No. 16, Commission on the Future of Health Care in Canada.
- Rawls, J. (1987). "The Idea of an Overlapping Consensus." Oxford Journal of Legal Studies 7(1): 1-25.
- Rayner, J. and S. McLarnon (2001). Fiscal Relations Between the Federal and Territorial Governments in Canada: A Comprehensive Overview, Consortium for Economic Policy Research and Advice (CEPRA).
- Restrepo, J. C. (1999 and 2000). Memorias de Hacienda, 1998-2000. Bogotá, Ministerio de Hacienda y Crédito Público.
- Restrepo, J. C. (2006). Algunas reflexiones sobre la nueva fórmula de transferencias. Departamentos al Día. Bogotá, Federación Nacional de Departamentos y Fondo Cuenta.
- Restrepo, J. H. (1996). Economía y constitución en Colombia. Lecturas de Economía. Medellín, Universidad de Antioquia.
- Restrepo Piedrahita, C. (1995). Constituciones políticas nacionales de Colombia. Bogotá, Universidad Externado de Colombia, Instituto de Estudios Constitucionales.
- Rey, S. J. (2004). Spatial Analysis of Regional Income Inequality. Spatially Integrated Social Science. M. Goodchild and D. Janelle. New York, Oxford University Press.
- Reynolds, A., Ed. (2002). The architecture of democracy: constitutional design, conflict management, and democracy. Oxford studies in democratization;. Oxford, UK, New York.
- Rivera, R. (2001). Hacia un nuevo federalismo para Colombia. Bogotá, Colombia, Editorial La Oveja Negra.
- Rodado, C. (2004). Propuestas concretas para afrontar los problemas de los departamentos y la nación. Departamentos al Día. Bogotá, Federación Nacional de Departamentos y Fondo Cuenta.

- Rodríguez, J. A. (1999). Crisis fiscal departamental: Razones y proporciones. Coyuntura Social. Bogotá, Fedesarrollo.
- Rodríguez, J. A. (2001). El Estado unitario descentralizado: Una crítica del enfoque constitucional colombiano. Cuadernos de Economía. Bogotá, Universidad Nacional de Colombia. **XX**.
- Rodrik, D., A. Subramanian, et al. (2004). "Institutions Rule: The Primacy of Institutions Over and Integration in Economic Development." Journal of Economic Growth **9**(2).
- Ross, C. J. (2002). Contemporary Spain: A handbook. London; New York  
Arnold
- Russell, P. H. (2004). Constitutional odyssey: Can Canadians become a sovereign people? Toronto ; Buffalo, University of Toronto Press.
- Safford, F. and M. Palacios (2002). Colombia: fragmented land, divided society. New York, Oxford University Press.
- Salinas, J., Ed. (2002). El nuevo modelo de financiación autonómica. Estudios de Hacienda Pública. Madrid, Instituto de Estudios Fiscales.
- Salinas, J. and S. Alvarez, Eds. (2003). El gasto público en la democracia. Estudios de Hacienda Pública. Madrid, Instituto de Estudios Fiscales.
- Sánchez, F. (2006). Descentralización y progreso en el acceso a los servicios sociales de educación, salud y agua y alcantarillado  
Documentos CEDE. Bogotá, CEDE, Universidad de los Andes.
- Sartori, G. (1997). Comparative constitutional engineering: an inquiry into structures, incentives, and outcomes. Washington Square, N.Y., New York University Press.
- Schultz (1961). "Investment in human capital." The American Economic Review **51**(1): 1-17.
- Seers, D. (1972). "What are we trying to measure?" Journal of Development Studies **8**(3): 21-36.
- Sen, A. (1988). The concept of development. Handbook of development economics. H. B. Chenery and T. N. Srinivasan. Amsterdam, Elsevier. **Vol. I**: 9-26.
- Sen, A. (1999). Development as freedom. New York, Alfred A. Knopf.
- Sheikh, M. and M. Carreau (2002). A Federal Perspective on the Role and Operation of the Tax Collection Agreements. Annex 1. Federal Administration of Provincial Taxes. New Directions, Department of Finance, Canada.
- Simon, H. A. (1996). The sciences of the artificial. Cambridge, Mass., MIT Press.
- Slack, E. (2005). Territorial Formula Financing. Ottawa, Expert Panel on Equalization and Territorial Formula Financing.
- Smart, M. and R. Bird (1996). Federal fiscal arrangements in Canada: An analysis of incentives. Proceedings of the National Tax Association Annual Conference on Taxation. Boston, International Centre for Tax Studies
- Solow, R. (1957). "Technical change and the aggregate production function." The Review of Economics and Statistics **39**(3): 312-320.
- Stevenson, G. (2004). Unfulfilled union: Canadian federalism and national unity. Montreal, McGill-Queen's University Press.
- Stiglitz, J. E. (1988). Economics of the public sector. New York, W.W. Norton.
- Ter-Minassian, T. and J. Craig (1997). Control of Subnational Government Borrowing. Fiscal Federalism in Theory and Practice. T. Ter-Minassian, International Monetary Fund.
- Thirsk, W. R. (1983). Tax assignment and revenue sharing in Canada. Tax assignment in federal countries. C. E. McLure Jr. Canberra, The Australian National University Press.



- Tiebout, C. M. (1956). "A pure theory of local expenditures." Journal of Political Economy **64**: 416-424.
- Tirado, A. (1992). Derechos humanos y sus mecanismos de protección constitucional. Los cambios constitucionales. N. Parra. Bogotá, SEAP: 45-80.
- Tobin, J. (1964). "Economic Growth as an Objective of Government Policy." The American Economic Review **54**(3).
- Treff, K. and D. B. Perry (2004). *Finances of the Nation 2004*. Toronto, Canadian Tax Foundation.
- United Nations Development Programme. (1990). *Human development report*. New York, Oxford University Press: v.
- Uprimny, R. (2006). Should Courts enforce social rights? The Experience of the Colombian Constitutional Court. Bogotá, DeJusticia.
- Uprimny, R. and C. Rodríguez (2005). Constitución y modelo económico en Colombia: Hacia una discusión productiva entre economía y derecho. Debates de Coyuntura Económica, Bogotá, Fedesarrollo.
- Uribe, A. (2003). El Departamento desde mi perspectiva como gobernador. Departamentos al Día. Bogotá, Federación Nacional de Departamentos y Fondo Cuenta.
- Vallés, J. (2002). Implicaciones de la normativa de estabilidad presupuestaria en el ámbito autonómico. El modelo de financiación autonómica. J. Salinas. Madrid, Instituto de Estudios Fiscales.
- Vélez, E. (2003). La educación. Colombia: Fundamentos Económicos de la Paz. M. Giugale, O. Lafourcade and C. Luff. Bogotá, Banco Mundial and Alfaomega.
- Villalba, R. (2005). "Autonomía fiscal y administrativa de los departamentos." Departamentos al Día (7).
- Watts, R. L. (1987). "The American Constitution in Comparative Perspective: A Comparison of Federalism in the United States and Canada " Journal of American History **74**(3): 769-792.
- Watts, R. L., Queen's University (Kingston Ont.). Institute of Intergovernmental Relations., et al. (1999). Comparing federal systems. Montreal ; Ithaca, Published for the School of Policy Studies Queen's University by McGill-Queen's University Press.
- Weber, A. (1969). Theory of the location of industries. New York, University of Chicago press.
- Wiesner, E. (1992). Colombia, descentralización y federalismo fiscal: informe final de la misión para la descentralización. Santafé de Bogotá, Presidencia de la República, Departamento Nacional de Planeación.
- Yebra, P. (2004). Constitución Financiera Española. Veinticinco Años. Madrid, Instituto de Estudios Fiscales.
- Yifu Lin, J. and J. B. Nugent (1995). Institutions and economic development. Handbook of development economics. J. R. Behrman and T. N. Srinivasan, Elsevier Science B. V. **III**: 2301-2370.