Press release - BAK Taxation Index: Fiscal sustainability 2016

Sustainable cantonal finances generate fiscal leeway

Basel, 20 Dec. 2016 – Current studies on the sustainability of financial policies conclude that, in contrast to the majority of the EU countries, fiscal policies in the Swiss cantons under review are sustainable. The Swiss cantons thus have the leeway necessary to offer internationally attractive tax levels.

The fiscal policies of both the Swiss cantons and Switzerland as a whole are sustainable. All of the cantons under review easily meet the EU sustainability criteria for the period to 2030 (fiscal gap below zero with assumed target debt of 60% of GDP). Top of the field is the Canton of Glarus, but even the Canton of Appenzell-Ausserhoden at the bottom of the league is well within the range. Matters are different in the EU, where few countries can keep up with the Swiss cantons. In the majority of the EU states, fiscal policies are not sustainable. Among Switzerland's neighbouring countries, only Germany has achieved fiscal sustainability.

The two main factors responsible for the success of the Swiss cantons are low public debt and comparably favourable government budgets (primary balance ratios). However, similar to most European countries, demographic change will raise costs in all of the Swiss cantons, for instance in the form of rising health and pension expenditure. Nevertheless, the current fiscal status of the cantons is sufficiently sound to absorb such additional costs. It should be noted that the calculations are based on the legal framework conditions of the year 2014 and the cantonal finances in the period 2010 to 2014.

Locations with fiscal sustainability are in a position to retain their tax rates over the long-term and may even have the leeway to lower tax rates, while non-sustainable locations face tax increases. For a number of years now, the BAK Taxation Index has shown that the Swiss cantons offer highly attractive tax rates in international comparison, both to corporations and to highly-qualified individuals. According to Chief Economist Martin Eichler, "thanks to their fiscal sustainability, the Swiss cantons are in an excellent position to maintain the attractiveness of their tax regimes in international competition."

Contact

Martin Eichler
MD, Chief Economist
T + 41 61 279 97 14
martin.eichler@bakbasel.com

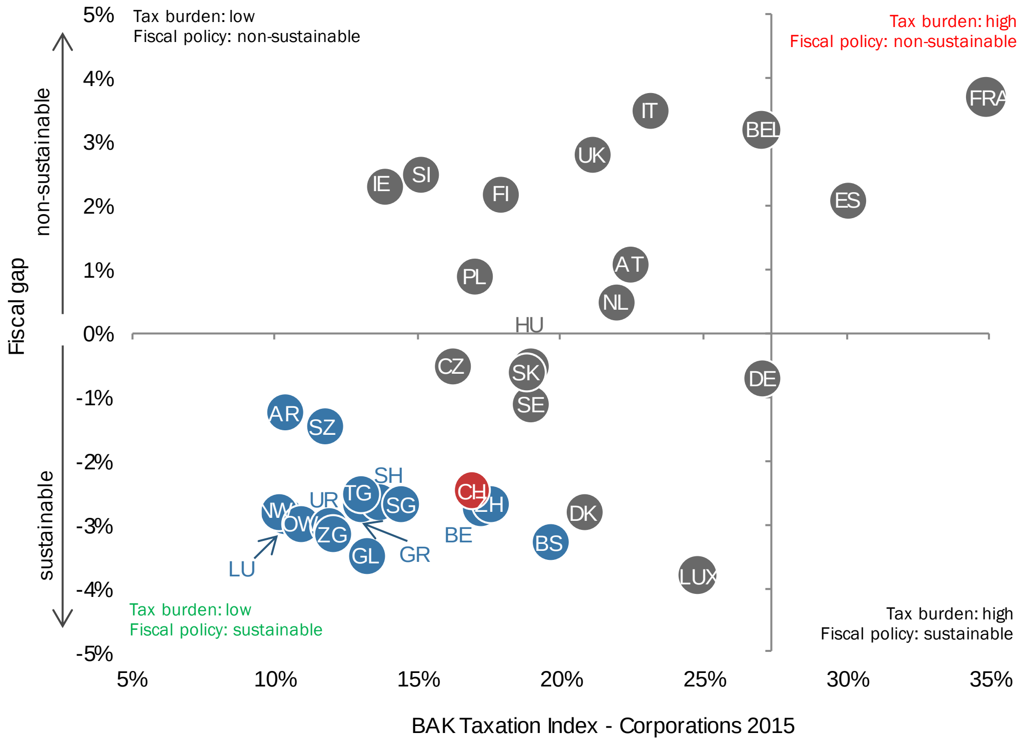
Mark Emmenegger
Research Associate
T + 41 61 279 97 29
mark.emmenegger@bakbasel.com

Combined view of tax burden on highly qualified individuals and sustainability

X axis: Effective average tax burden for highly qualified individuals (single, no children, income EUR 100,000) in the main locations (exception: Italy: Lombardy); X axis cuts the Y axis at the average tax rate of the BAK Taxation Index. Y axis: Fiscal gap = Extent by which the primary ratio in the base year (2017) would have to be adjusted in order to achieve a gross debt ratio of 60% by 2030; positive values: achievement of target entails improvement of primary balance ratio; negative values: achievement of target ensured even if primary balance ratio deteriorates. Swiss cantons including communes and assigned federal share (including social insurance).

Source: BAKBASEL / ZEW

Combined view of corporate tax burden and sustainability



X axis: Effective average tax burden for corporations in the main locations (exception: Italy: Lombardy); X axis cuts the Y axis at the average tax rate of the BAK Taxation Index. Y axis: Fiscal gap = Extent by which the primary ratio in the base year (2017) would have to be adjusted in order to achieve a gross debt ratio of 60% by 2030;
positive values: achievement of target entails improvement of primary balance ratio; negative values: achievement of target ensured even if primary balance ratio deteriorates. Swiss cantons including communes and assigned federal share (including social insurance).

Source: BAKBASEL / ZEW

Code	Country/canton	Fiscal gap	Tax burden - Highly qualified individuals	Tax burden – Corporations
LUX	Luxembourg	-3.8%	40.2%	24.8%
GL	Glarus	-3.5%	29.0%	13.2%
BS	Basel-Stadt	-3.3%	32.6%	19.6%
ZG	Zug	-3.1%	23.6%	12.0%
UR	Uri	-3.0%	26.0%	11.9%
OW	Obwalden	-3.0%	24.9%	10.9%
LU	Luzern	-2.9%	27.4%	10.3%
DK	Danmark	-2.8%	48.0%	20.8%
NW	Nidwalden	-2.8%	26.4%	10.1%
BE	Bern	-2.7%	35.3%	17.2%
SG	St. Gallen	-2.7%	33.4%	14.4%
ZH	Zürich	-2.7%	29.8%	17.5%
GR	Graubünden	-2.7%	30.5%	13.0%
SH	Schaffhausen	-2.6%	31.6%	13.6%
TG	Thurgau	-2.5%	30.0%	13.0%
CH	Schweiz	-2.5%	32.4%	16.9%
SZ	Schwyz	-1.5%	25.9%	11.7%
AR	Appenzell Ausserrhoden	-1.2%	30.5%	10.3%
SE	Sverige	-1.1%	56.0%	18.9%
DE	Deutschland	-0.7%	41.0%	27.0%
SK	Slovenská Republika	-0.6%	32.4%	18.8%
CZ	Česká Republika	-0.5%	26.0%	16.2%
HU	Magyarország	-0.5%	38.3%	18.9%
NL	Nederland	0.5%	46.8%	21.9%
PL	Polska	0.9%	32.0%	17.0%
AT	Österreich	1.1%	41.0%	22.4%
ES	España	2.1%	44.4%	30.0%
FI	Suomi	2.2%	53.3%	17.9%
IE	Ireland	2.3%	49.2%	13.8%
SI	Slovenija	2.5%	47.9%	15.1%
UK	United Kingdom	2.8%	48.6%	21.1%
BEL	Belgique/België	3.2%	57.7%	27.0%
IT	Italia	3.5%	52.9%	23.1%
FRA	France	3.7%	47.4%	34.9%

Fiscal gap = Extent by which the primary balance ratio in the base year (2017) would have to be adjusted in order to achieve a gross debt ratio of 60% by 2030; positive values: achievement of target entails improvement of primary balance ratio; negative values: achievement of target ensured even if primary balance ratio deteriorates. Swiss cantons including communes and assigned federal share (including social insurance). Tax burdens according to BAK Taxation Index 2015 (cp. annotations to diagrams above).

Source: BAKBASEL / ZEW

Sustainability of fiscal policy

The evaluation of fiscal sustainability in the context of the BAK Taxation Index is based on an EU indicator used to monitor the financial sustainability of the member states (latest publication: 'Fiscal Sustainability Report 2015'). In specific, this is the 'fiscal gap indicator S1' which has been designed to evaluate fiscal sustainability in the (medium-term) period 2017 (base year) to 2030.

The fiscal gap indicator depends on a country's intertemporal budget constraint, which requires that the present value of the target debt plus all future revenue must cover the present value of the initial debt plus all future expenditure. The target debt is assumed to be a debt ratio (government debt as a percentage of GDP) of 60% for all locations. This figure is in line with the Maastricht criteria and ensures comparability of the results of different regional administrative bodies. The impact of demographic change is included in the future expenditure.

The fiscal gap indicator that is derived from the intertemporal budget constrain is defined as the difference between the sustainable primary balance ratio and the primary balance ratio in the base year (the primary balance ratio is consistent with the primary balance – i.e. the difference between primary income and primary expenses – as a percentage of GDP). The sustainable primary balance ratio is the primary balance ratio that would have to be achieved every year starting from the base year (2017) in order to achieve a gross debt ratio of 60% at the end of the reference period (2030). Hence the fiscal gap indicates the extent by which the primary balance ratio in the base year would have to be adjusted to achieve the gross debt ratio of 60%. It should be noted that, according to the interpretation of the fiscal gap, negative values indicate sustainable fiscal policy and positive values non-sustainable fiscal policy.

The following two examples illustrate the interpretation of the fiscal gap: In the BAK Taxation Sustainability Module 2016, France's fiscal gap amounts to 3.7% and the country's primary balance ratio in the base year (2017) to -0.5%. This means that, every year in the period 2018 to 2030, France requires a primary balance ratio that exceeds the primary balance ratio in the base year by 3.7 percentage points, i.e. a primary surplus ratio of 3.2% (= sustainable primary balance ratio), in order to achieve a gross debt ratio of 60% in 2030. Conversely, the fiscal gap in the Canton of Zug amounts to -3.1% and the primary balance ratio in the base year (2017) to 0.4%. In theory, in the period 2018 to 2030, the Canton of Zug can therefore afford an annual primary balance ratio that is -3.1 percentage points lower than that in the base year, i.e. a primary deficit ratio of -2.7% (=sustainable primary balance ratio), and still achieve the target debt ratio of 60% in 2030.

The cantonal data are processed such that the individual cantons include both their communes and a federal share (including social insurance) that is commensurate with their economic performance. Hence, the total of all cantons represents the country as a whole.

A separate methodology paper relating to this study provides a detailed overview of the approach and sources used. The methodology paper and further information and studies pertaining to the BAK Taxation Index project are available at www.baktaxation.ch → Sustainability of Fiscal Policy.