The Reform of German Federalism: Part I

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Constitutional reform in Germany – Modernization of the German federal system is only a first step – Why reforming German Federalism was necessary – Steps and factors in the constitutional reform process – Substance – Issues and agenda for future reform on financial relations.

In the summer of 2006, after years of very intense and controversial debate on how to modernize the German federal system, both the Bundestag and Bundesrat decided to accept certain reforms with the necessary two-thirds majority. This very comprehensive constitutional reform, which entered into force on 1 September 2006, affected 25 articles of the Basic Law. However, all political actors involved and all observers agree that this reform package, focusing primarily on the distribution of competency, is only a first step. A second step, dealing with the financial relations in the German federal system, will have to follow. Preparations began before the end of 2006, but there are widespread doubts whether the second step will succeed before 2009 under the present Grand Coalition government.

This article[1] will start by explaining the main arguments for reforming German federalism, and will identify the major goals of the actors, the *Länder* and the federal government, who are involved in this process. It will then give an overview on the reform debate and the efforts made to achieve a solution which would be supported by the necessary majorities. In the next section, this article will list, analyze and evaluate what has been achieved in the first part of the reform by the summer of 2006. Finally, the article will conclude with perspectives for the second part of the constitutional reform, the realization of which is far from certain. It concerns the issues on the agenda, interests and positions of the stakeholders and the difficulties pertaining to agreeing on a solution which would be accepted and recognized as fair and balanced.

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[1] This article draws on another article of the author: 'Ein neuer Anlauf zur Föderalismus-Reform: Das Kompromisspaket der Großen Koalition', in Europäisches Zentrum für Föderalismus-Forschung Tübingen (ed.), *Jahrbuch des Föderalismus 2006. Föderalismus, Subsidiarität und Regionen in Europa* (Nomos, Baden-Baden 2006) p. 139-157.

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On the need to reform German Federalism

German Federalism, protected against abolition by a special constitutional provision (Article 79(3) Basic Law), also known as the 'eternity clause', has undergone a very dynamic development and has been the subject of a series of reforms.[2] From its inception in 1949, the two levels of government – Federation and *Länder* – were not separated in the sense of a 'dual federalism' pattern, but became interconnected and interdependent in different respects. German Federalism represented a form of 'co-operative federalism', and, as early as 1960, an observer coined the label 'unitarian federal system',[3] which drew attention to the fact that politics in the Federal Republic of Germany often resulted in uniform policy solutions.

A constitutional reform in 1969 strengthened and intensified the interconnectedness of Federation and *Länder*, especially once the so-called 'Joint Tasks' were introduced. With the introduction of these 'Joint Tasks', both levels of government were compelled to agree on policy solutions and to share financial responsibilities. Sometimes such an agreement can only be reached after a long bargaining process.[4]

This new pattern of German Federalism was heavily criticized[5] and, in the 90's, under the Christian Democrat/Liberal coalition, efforts were started to 'loosen' the interconnectedness by reducing 'Joint Tasks' and by offering the *Länder* a higher level of autonomy. Their understandable demand for financial compensation – greater autonomy requires a larger portion of financial resources – could not be met. The overall economic situation and development did not allow the Federation to be that financially generous. Secondly, German reunification stopped all efforts to reduce 'Joint Tasks', since the disparities within Germany grew considerably and made the five new *Länder* (which were considerably weaker in comparison to the eleven old *Länder*) dependent on the Federation.

It was not until the mid 90s that criticism of the German federal system grew stronger and resulted in a large-scale debate on whether or not there should be

[2] *See* the special issue on 'Federalism and Intergovernmental Relations in West Germany: A fortieth year appraisal', 19 *Publius. The Journal of Federalism* (1989), No. 4; *also* Ch. Jeffery (ed.), *Recasting German Federalism. The Legacies of Unification* (Pinter, London and New York 1999). *See also* two overviews in German: H. Laufer and U. Münch, *Das föderative System der Bundesrepublik Deutschland* (Leske & Budrich, Opladen 1998); and R. Sturm, *Föderalismus in Deutschland* (Bayerische Landeszentrale für Politische Bildungsarbeit, München 2003).

[3] K. Hesse, *Der unitarische Bundesstaat* (Müller, Karlsruhe 1962).

[4] F.W. Scharpf who has written widely on different aspects of German federalism has coined the term 'Politikverflechtung' to characterise the pattern of German federalism after the introduction of the so-called Joint Tasks; *see* F.W. Scharpf et al., *Politikverflechtung: Theorie und Empirie des kooperativen Föderalismus in der Bundesrepublik* (Kronberg, 1976).

[5] F.W. Scharpf has spoken of the so-called 'Politikverflechtungsfalle' (The 'Joint Decisions trap'); *see* his article 'Die Politikverflechtungsfalle. Europäische Integration und deutscher Föderalismus im Vergleich', 26 *Politische Vierteljahresschrift* (1985) p. 323-356.

comprehensive reforms.[6] The overall intention was to replace the pattern of interlocking relationships between the federal and *Länder* governments by a structure with greater autonomy and less mutual dependency of both sides on one another. The reform debate focused on those features of the German federal system, which were regarded as weaknesses and deficits. The first subject under discussion was the distribution of legislative powers.

The Basic Law defines the division of legislative powers between the Federation and the *Länder*. Certain matters belong to the exclusive jurisdiction of the Federation (listed in Article 73 Basic Law), and only a few matters fall under the exclusive competence of the *Länder*. These issues include those relating to the local level of government, the organization of the administration, matters pertaining to law enforcement and public order, and also culture, education and the media. Furthermore, there are certain matters that fall under concurrent jurisdiction (listed in Article 74 Basic Law), and matters for which the Federation has the right to create framework legislation (listed in Article 75 Basic Law).

The major reason for what observers have labeled as the 'unitarian' character of the German system is that the Federation has widely exploited the provisions for concurrent (and framework) legislative powers. Article 72 Basic Law sets out the conditions under which the Federation may create legislation in matters which fall under concurrent jurisdiction. This is permitted 'if and to the extent that the establishment of equal living conditions throughout the federal territory or the maintenance of legal or economic unity renders federal regulation necessary in the national interest'. Until 1994, the Basic Law spoke of 'the uniformity of living conditions'; but the new term ('equal living conditions', in the sense of 'equivalent')[7] did not and could not prevent the Federation from acting. The *Länder* were compensated for this loss of autonomous legislative power with a significant increase in their right to participate in federal legislation via the Bundesrat. The term 'participatory federalism' (*Beteiligungs-Föderalismus*) refers to this pattern. Politically, the *Länder* participation has resulted in increased participation by the

[6] *See* for example U. Männle (ed.), *Föderalismus zwischen Konsens und Konkurrenz. Tagungs- und Materialienband zur Fortentwicklung des deutschen Föderalismus* (Nomos, Baden-Baden 1998); U. Münch, 'Konkurrenzföderalismus für die Bundesrepublik: eine Reformdebatte zwischen Wunschdenken und politischer Machbarkeit', in Europäisches Zentrum für Föderalismus-Forschung Tübingen (ed.), *Jahrbuch des Föderalismus 2001. Föderalismus, Subsidiarität und Regionen in Europa* (Nomos, Baden-Baden 2001) p. 115-127; Th. Fischer and M. Große Hüttmann, 'Aktuelle Diskussionsbeiträge zur Reform des deutschen Föderalismus. Modelle, Leitbilder und die Chancen ihrer Übertragbarkeit', in Europäisches Zentrum für Föderalismus-Forschung Tübingen (ed.), *Jahrbuch des Föderalismus 2001. Föderalismus, Subsidiarität und Regionen in Europa* (Nomos, Baden-Baden 2001) p. 128-142.

[7] M. Nettesheim, my Tübingen colleague from the Law Faculty, has rightly argued that the correct translation of the German term *Gleichwertigkeit der Lebensbedingungen* would be 'equivalent' and not 'equal', as in an official translation of the Constitution.

Prime Ministers, which has led to further political decline and marginalization for the *Länder* parliaments.

As far as the framework legislation of the Federation is concerned, this type of law should only give broad guidelines and leave to the *Länder* the responsibility of deciding on details and inserting substantive provisions into the framework. In practice, however, the *Länder* have complained that the provisions set by the Federation have included too much detail.

The second subject under discussion was the Bundesrat. This is the institution for *Länder* participation in federal legislation. It is composed of members of the Land governments (3 to 6 votes according to the size of the population, which have to be cast uniformly and must not be split). There are two categories of bills. The first category of bills are referred to as objection bills (*Einspruchsgesetze*). These can be opposed by a Bundesrat majority, but will enter into force if the Bundestag overrides the Bundesrat objection with an absolute majority, or a two-thirds majority if two-thirds of the Bundesrat votes have been cast against the bill. The second category of bills are the so-called consent bills (*Zustimmungsgesetze*). The main criteria for this second type of bill are that they either affect administrative powers of the *Länder* (they must implement federal legislation) or create financial implications for the *Länder*.

Since more than half of all federal legislation has fallen into the category of consent bills, the federal government (with its parliamentary majority in the Bundestag) is often dependent on the consent of the Bundesrat. When *Länder* governments are formed by parties who are also opposition parties at the federal level, and when they represent the majority in the Bundesrat, they may try to make use of their numerical strength. In order to avoid a Bundesrat veto, the federal government has to make concessions. Bargaining processes, which are often not transparent, can result in compromising solutions. These solutions have been criticized as being suboptimal in terms of substance and limited in their ability to solve problems, and lacking democratic legitimacy, since the accountability remains unclear.

The third feature of the federal system, which was criticized, was the so-called 'Joint Tasks' (*Gemeinschaftsaufgaben*), defined in Articles 91a and 91b Basic Law. They were criticized because they have promoted and strengthened the interlocking relationship pattern between the two levels of government – Federation and *Länder* – and because the executive powers (especially the bureaucracies) on both sides dominate at the expense of the parliaments on the federal and *Länder* levels. Responsibility has been blurred, and the rule of co-financing has reduced the freedom to manoeuvre from a Land which is tempted by the prospect of receiving federal resources.

The fourth subject under discussion was financial affairs and financial relations between the different levels, very sensitive issues in all federations. They can affect the nature and structure of the respective federal system, and this certainly applies to Germany as well. Since these provisions determine the volume of available financial resources, they are closely related to and interdependent on provisions concerning the allocation of power to the Federation and the *Länder*.

In Article 106, the Basic Law provides that the most important tax revenues (in terms of volume) are joint taxes, which are shared between the Federation and the *Länder*. The income and corporation tax revenues are shared between both parties equally, and the turnover tax (VAT) is divided by a ratio which has to be determined (and adjusted regularly) by a federal law which requires the consent of the Bundesrat. Other tax revenues are apportioned either to the Federation or the *Länder*. Provisions which allow the Federation to grant the *Länder* (and municipalities) financial assistance are particularly important. They are utilized 'for particular important investments (…) provided that such investments are necessary to avert a disturbance of the overall economic equilibrium, to equalise differing economic capacities within the federal territory, or to promote economic growth' (Article 104a(4) Basic Law). Last but not least, there is a mechanism for horizontal equalization amongst the *Länder*. This mechanism divides the *Länder* into a (smaller) group of net-payers and a group of net-receivers. As a result of these different arrangements and mechanisms, no Land has less than 99,5% of the average financial strength. This levelling has been criticized primarily by the net-payers among the *Länder* and by those who are in favour of a greater level of competition between the *Länder* and increased efforts of weaker (net-receiver) *Länder* to improve their financial situations. This assumes that the otherwise weaker *Länder* would prefer to rely on transfers, which would guarantee a fairly strong financial basis.

An issue of particular interest on the agenda for reforming German federalism was the participation of the *Länder* in the decision-making process on European Union matters at the national and Union levels.[8] A new Article 23 Basic Law (the former Article 23 had become obsolete with German reunification) was formulated and included in the Basic Law in connection with the ratification of the Treaty of Maastricht in 1992. This so-called 'Europe-Article' (supplemented by the 'Law on the co-operation of Federation and *Länder* in affairs of the European Union' and the subsequently concluded Agreement between the federal and *Länder* governments) strengthens the position and role of the *Länder* in dealing with European Union matters.

[8] *See* on this issue R. Hrbek, 'The effects of EU integration on German federalism', in Ch. Jeffery (ed.), *Recasting German federalism. The legacies of unification* (Pinter, London 1999) p. 217-233.

At the domestic level, the *Länder* have the right via the Bundesrat – after having been informed 'comprehensively and at the earliest possible time' by the federal government – to give opinions. These detailed and complex provisions set out a graded obligation on the part of the federal government to observe Bundesrat opinions. If the European Union measure concerned falls within *Länder* competence, the federal government is obliged to take the Bundesrat opinion 'decisively' into account.

At the European Union level, the *Länder* have the right to participate in negotiations in European Union bodies. *Länder* representatives (nominated by the Bundesrat) form part of the German delegation. If the issue concerned 'centrally affects exclusive legislative competences of the *Länder*', the *Länder* claim that their concerns must be taken into account in a proper manner.

The federal government argued[9] that this involvement and participation of the *Länder* would have a negative effect on the ability to successfully pursue German interests and concerns. The government, therefore, demanded that Germany's representation in Brussels had to be the sole responsibility of the federal government which would mean that only members of the federal government would be authorized to negotiate in European Union bodies. Co-ordination with the *Länder* would have to take place and be managed internally (at the domestic level) in advance. Procedural provisions in Article 23 Basic Law should, therefore, be removed. The *Länder* argued that they have the right to legislate in the areas of their exclusive competence and that they have the right to participate in passing Federal legislation. Moreover, if these functions have been transferred to the European Union, the *Länder* argued that they must have the right to participate respectively. Concerning the experiences with the participation of the *Länder* on the basis of Article 23 Basic Law, they insisted that their participation has never been the reason that Germany has experienced disadvantages. The *Länder*, therefore, argued in favour of maintaining Article 23 and strengthening their position, particularly in areas of their exclusive competence. Both sides, Federation and *Länder*, agreed that a solution must be found for sharing costs created by a violation of international or European commitments between the Federation and the *Länder*.

In conclusion, the reform debate concentrated on the following major points: the interlocking relationship and interdependence between the Federation and the *Länder* (relating to the distribution of competences, with a unitarian trend in the large field of concurrent powers), and the introduction of Joint Tasks. Interdependence relates to the financial resources, and is especially related to equalization

[9] On this debate *see* R. Hrbek, 'Der deutsche Bundesstaat in der EU. Die Mitwirkung der deutschen Länder in EU-Angelegenheiten als Gegenstand der Föderalismus-Reform', in Ch. Gaitanides et al. (eds.), *Europa und seine Verfassung* (Europe and its constitution) *Festschrift für Manfred Zuleeg* (Nomos, Baden-Baden 2005) p. 256-273.

mechanisms in the vertical and the horizontal dimension as well. There was concern about unitarian solutions in many policy fields and about the powerful role of the Bundesrat in federal legislation, especially relating to consent-bills requiring approval by the majority in the Bundesrat. And finally, the role of the *Länder* in dealing with EU matters at the domestic and particularly at the EU level was an additional point on the reform agenda.

Steps towards reform of federalism: institutions, actors, procedures

Against the background of the diagnosis that the German federal system was suffering from weaknesses and deficits, a debate on the appropriate therapy started in the mid 90s. A series of reform demands and proposals were submitted.[10] The participants were academics, political actors (especially from the stronger *Länder*, the so-called 'net-payers') and there were even several representatives from the business world. The latter argued that the structures of the German federal system created a barrier against launching successful reforms in the economic and social system *(Reformstau)*.

Two *Länder* (Bavaria and Baden-Württemberg), as net-payers, called upon the Federal Constitutional Court to annul the current (horizontal) equalization system. They anticipated an incentive for comprehensive reforms from the Karlsruhe Court, but the Court only ruled that criteria for the equalization system should be defined in a federal law *(Maßstäbegesetz)*.[11]

Finally, the two major stakeholders – the *Länder* and the federal government – declared their willingness and determination to launch concrete reform measures. They agreed to elaborate on their respective positions for further negotiations in a joint working group by the spring of 2003. In March of 2003, the *Länder* Prime Ministers formulated their 'guidelines for negotiations with the federal government' on the modernization of the federal system. In April 2003, the federal government formulated its position. Both sides agreed in principle on loosening their interlocking relationship and competences as well as financial responsibilities, but their positions differed on what this would and should amount to, concerning certain details.

[10] *See* R. Hrbek and A. Eppler (eds.), *Deutschland vor der Föderalismus-Reform. Eine Dokumentation*, Occasional Papers Nr. 28 (Europäisches Zentrum für Föderalismus-Forschung Tübingen, 2003).

[11] F. Kirchhof, 'Die Erfüllung finanzverfassungsrechtlicher Vorgaben durch das Maßstäbe-Gesetz vom September 2001', in Europäisches Zentrum für Föderalismus-Forschung Tübingen (ed.), *Jahrbuch des Föderalismus 2002. Föderalismus, Subsidiariät und Regionen in Europa* (Nomos, Baden-Baden 2002) p. 224-231.

In November 2003, the Bundestag and the Bundesrat established a joint Commission. The goal was for this Commission to elaborate on proposals for the modernization of German federalism.[12] The mandate for the Commission, however, did explicitly exclude two aspects of the federal system which have always been part of the discussion: the financial relations and a new delimitation of the *Länder (Neugliederung*). One could, therefore, expect only partial reforms, or a first step, focusing on the allocation of competences. The Commission was composed of sixteen members of the Bundestag and Bundesrat respectively. The four members from the federal government, six members from *Länder* parliaments and three members chosen to be representatives of the local entities, had only advisory functions. Twelve experts (academics, nominated by the Commission via proposals made by the Bundestag party groups) participated in the considerations.

The establishment of the Commission after a long period of discussion was taken as an indication that a decision on the reform would be probable. Both sides had put themselves under pressure. There were, on the other hand, severe doubts that a solution which would receive the necessary two-thirds majority support in both the Bundestag and Bundesrat could be achieved. The basic positions and guidelines of both sides remained too far removed from each other, and, secondly, controversial debates were to be expected once details were discussed.

During the Commission's work, an approximation on a number of issues had been reached, and partial results had already been agreed upon. There were, however, still dissenting opinions concerning substantial questions. After one year of intense debates and considerations, the two co-chairpersons, Bavarian Prime Minister Stoiber (CSU), representing the *Länder*, and the chairman of the SPD party group in the Bundestag, Müntefering, announced in December 2004 that the Commission was unable to submit a proposal that both parties could agree on. It became clear that there were a series of major issues where it had been impossible to overcome dissent. These issues pertained to competences in the fields of environmental law, internal security and, in particular, education. In addition, the extent of *Länder* participation in dealing with European Union matters was also a problem.

The failure of the Commission was a disappointment, since there had been high expectations from the moment of its establishment. Attempts to explain the failure referred to disparities and differences between the interests of the *Länder*, to party-political differences, to institutional self interests of *Länder* Prime Ministers (who have always used the Bundesrat as a framework and a basis for playing a strong role at the federal level) and the federal government (which pushed to curb *Länder* participation in European Union matters). Also, the need to have a solu-

[12] Bundesrat-Drucksache 750/03 (17 Oct. 2003) and Bundestag-Drucksache 15/1685 (16 Oct. 2003).

tion (as a package deal) as the only outcome acceptable to all (or at least to the overwhelming majority of stakeholders involved) was an issue. Last but not least, a lack of a jointly agreed upon concept and understanding of the basics of the federal system existed, particularly concerning the extent of the differences which would be recognized as acceptable in a federal entity.[13] There were, however, many voices demanding new efforts for bringing about reform.

We can identify the following steps and factors which, finally, resulted in the constitutional reform decided upon during the summer of 2006. In the context of the so-called 'Job-Summit' in the spring of 2005, top politicians from the federal government and the parliamentary opposition agreed to re-launch the federalism reform project. The procedural approach differed from the Joint Commission: there were now non-public talks and negotiations among a very small group of people, who enjoyed the full support of the Chancellor (Gerhard Schröder) and the opposition leader (Angela Merkel). The attempts to reach a compromise seemed to have been successful: a special meeting of all *Länder* Prime Ministers scheduled for the end of May was expected to confirm and 'ratify' the solution. The outcome of the Nordrhein-Westfalia Land elections on 22 May 2005, disastrous for Chancellor Schröder's party, made him prepare for federal elections in the early fall. This stopped any further move towards federalism reform for the moment. But insiders and observers concluded that the efforts produced progress.

Two judgments given by the Federal Constitutional Court on the conditions under which the Federation would be authorized to legislate in areas of concurrent or framework legislation (according to Article 72(2) Basic Law, quoted above) were of considerable importance.[14] A group of *Länder* governments had brought two federal bills in the field of higher education and the university system before the Court, which ruled in favour of the *Länder* and gave a very restrictive interpre-

[13] *See* the contributions of W. Renzsch, Th. Fischer, I. Kemmler, M. Chardon, U. Münch, M. Große Hüttmann and H.-J. Dietsche and S. Hinterseh, in Europäisches Zentrum für Föderalismus-Forschung Tübingen (ed.), *Jahrbuch des Föderalismus 2005. Föderalismus, Subsidiariät und Regionen in Europa* (Nomos, Baden-Baden 2005); furthermore the contributions in R. Hrbek and A. Eppler (eds.), *Die unvollendete Föderalismus-Reform. Eine Zwischenbilanz nach dem Scheitern der Kommission zur Modernisierung der bundesstaatlichen Ordnung im Dezember 2004.* (Occasional Papers Nr. 31, Europäisches Zentrum für Föderalismus-Forschung Tübingen, 2004); further articles include R. Sturm, 'Föderalismus-Reform: kein Erkenntnisproblem, warum aber ein Gestaltungs- und Entscheidungsproblem?', *Politische Vierteljahresschrift* (2005) p. 195-203; A. Benz, 'Kein Ausweg aus der Politikverflechtung? Warum die Bundesstaats-Kommission scheiterte, aber nicht scheitern musste', *Politische Vierteljahresschrifte* (2005) p. 204-214; F.W. Scharpf, 'Nicht genützte Chancen der Föderalismus-Reform', Max Planck Institute for the Study of Societies Working Paper 06/2 (April 2006).

[14] *See* St. Schmahl, 'Bundesverfassungsgerichtliche Neujustierung des Bund/Länder-Verhältnisses im Bereich der Gesetzgebung' in Europäisches Zentrum für Föderalismus-Forschung Tübingen (ed.), *Jahrbuch des Föderalismus 2006. Föderalismus, Subsidiariät und Regionen in Europa* (Nomos, Baden-Baden 2006) p. 220-236.

tation of these conditions. The federal government, therefore, was confronted with a situation in which it was not able to decide on norms in areas in which it had hoped (and demanded) to dominate the *Länder*. The political response to these two judgments by the Federal government now seemed to show a willingness to agree to *Länder* demands in the field of education.

A salient and controversial issue in the considerations of the Commission to prepare reforms within German federalism was the participation of the *Länder* in European Union matters. It was evident that a solution would have to take into account provisions in the EU Constitutional Treaty, as far as they would relate to the *Länder*. When the EU Constitutional Treaty came before Parliament in May 2005, the *Länder* gave their approval via the Bundesrat,[15] but, as in previous cases (e.g., the Treaty of Maastricht in 1992), this was only possible on the basis of an agreement between the *Länder* and the federal government, in which the latter made some concessions to the *Länder* which could strengthen their role and position.

One concession was that whenever national parliaments would become involved directly in European Union decision-making, the Bundesrat would have the right to exploit all new legal and procedural opportunities. This would relate particularly to the application of the principles of subsidiarity and proportionality ('early warning system'). It extends to the right to appeal to the European Court of Justice.

Another agreement concerned the application of Article IV-444 of the EU Constitutional Treaty containing a clause allowing the governments to make particular issues subject to qualified majority decisions and no longer to unanimity ('Passerelle-Clause'). The *Länder* were concerned with having a provision in which the federal government would be obliged to observe a Bundesrat veto in such cases. This was also agreed to in the framework of the ratification. Furthermore, it was agreed that the *Länder* via the Bundesrat could participate in the appointment of the German members to the European Court of Justice. Until this new provision, the federal government was free to nominate candidates for these offices. Finally, it was agreed that the Bundesrat would not only participate with respect to the legislative acts of the European Union but to recommendations as well.

On the whole, the *Länder* could strengthen their position and this could be taken as an indication that both sides were ready and willing to reach consensus.

The last and decisive step towards a constitutional reform on German federalism was made in connection with the formation of a Grand Coalition, following the national elections in the fall of 2005. The party leaders of CDU, CSU and

[15] Bundesrat-Drucksache 340/05 and Bundesrat-Drucksache 339/05 (Beschluss).

SPD (Merkel, Stoiber, and Müntefering) agreed to make the reform a priority for their governmental programme. They submitted a mandate to a newly established working group to promote the project within the framework of negotiations forming the coalition. The document, which was produced by this working group, was included in the coalition agreement of 11 November 2005 as an annex. The *Länder* Prime Ministers approved this compromise package on 14 December 2005 and established a *Länder* working group, which would deal with details and co-ordinate them with the federal government. All these steps were taken without the participation of the Bundestag, which resulted in dissatisfaction by groups of the Bundestag members in March 2006 when the draft of the very comprehensive bill was introduced formally in the legislative process.[16] They protested and insisted on the Bundestag's right to get involved in the decision-making process. However, very few details were actually modified.

The reform of German Federalism: Part I

With 25 articles of the Basic Law reviewed, the reform package was a very comprehensive one. In addition to and as a consequence of these amendments to the Constitution, new legal provisions at a lower level were created. However, this reform was only the first step of the ambitious project to modernize German federalism. It focused on the competence of the Federation and the *Länder* with the primary goal to make them more independent from each other in their legislative activities. In addition, the reform package contained few (and rather marginal) provisions in financial affairs, a clause on the capital (Berlin) and its functions, and more precise rules for the participation of the *Länder* in European Union matters. One section of the reform package was designed in order to continue reform efforts and immediately start with preparations toward the second step, which would have to deal with financial relations.

The clause on the capital (Berlin)

There is a new paragraph in Article 22 Basic Law, which states that Berlin is the capital of the Federal Republic of Germany. The representation of the state as a whole is a function given to the Federation; details shall be arranged via federal legislation. The intention of this clause has been to discharge the Land (city state) of Berlin financially when expenses for representational functions are due.

[16] Bundestag-Drucksache 16/813 and 17/814 (7 March 2006).

The participation of the Länder in EU matters

According to Article 23 (6) Basic Law,[17] *Länder* representatives participate in deliberations of European Union bodies (Council and formations of the Council). The Federal government was in favour of deleting this paragraph, since it argued that transferring the leading role in such Council negotiations to *Länder* representatives would raise problems. The solution specifies that such a delegation to *Länder* representatives shall be restricted to three policy fields: school education, culture and broadcasting. The *Länder* had argued that their designation as states requires that, in cases where European Union matters centrally affect exclusive legislative competences of the *Länder*, they must take on the role of representing Germany in the respective European Union body.

Legislative competences

The reform package concentrates on the allocation of legislative competences.

Federal Framework Legislation as listed in Article 75 Basic Law will be abolished; Article 75 Basic Law will become obsolete. Competency previously under Federal Framework Legislation shall be re-distributed as follows: certain responsibilities will fall under the exclusive competence of the Federation (e.g., measures to prevent expatriation of German cultural assets) and others under concurrent legislation. Concerning the controversial field of higher education, the Federation shall only be responsible (as concurrent legislative powers) for two issues: admission to university and university degrees.

One innovation is the new provision in Article 72(3) Basic Law on the reversed concurrent legislative powers of the *Länder* (*Abweichungsgetzgebung der Länder*). Once a federal law dealing with a specific area (which falls into the concurrent legislative power of the Federation) has been decreed, individual *Länder* are authorized to decree a law which deviates from the federal law. This, however, does not prevent the Federation from reacting by enacting a federal law which also differs from that deviation. Observers warn against this scenario, which they have labeled the 'ping-pong-effect'. Its occurrence, however, is unlikely, since a Land government eager to deviate, must have very good, strong and convincing arguments to back up their position, since it is accountable to its electorate. The same applies to the Federation. This innovative provision opens the way towards differing solutions and seems to be in line with the concept of 'best practice'. One cannot exclude the emergence of an 'asymmetrical federalism' pattern. Reversed

[17] Art. 23(6) Basic Law reads: 'When legislative powers exclusive to the Länder are primarily affected, the exercise of the rights belonging to the Federal Republic of Germany as a member state of the European Union shall be delegated to a representative of the Länder designated by the Bundesrat. These rights shall be exercised with the participation and concurrence of the federal government; their exercise shall be consistent with the responsibility of the Federation for the nation as a whole'.

concurrent powers relate to aspects of environmental law and to the issues concerning university degrees and admission to university. Deviations, however, shall not be possible before August 2008 and January 2010 (environmental issues) respectively.

The *Länder* will have the exclusive competence in the field of remuneration, pensions and related benefits and careers of members of the *Länder* public service, municipalities and judges. This was a highly disputed issue: weaker *Länder* first objected since they feared that qualified civil servants might be tempted to go to the *Länder* with higher salaries. But the danger of greater asymmetry seems, again, to be unlikely, since the budgetary situation of the *Länder* does not allow them to be generous. And with respect to the differences in the cost of living within Germany, one can argue (and it certainly has been argued!) that uniform salaries are problematic and unjust as well.

There are further fields which go from federal concurrent legislation into the exclusive competence of the *Länder*. Among them are highly controversial fields such as legal aspects for specific care facilities (e.g., for children, for physically or mentally handicapped people) and less salient fields such as closing times of shops, or regulations relating to bars, restaurants, gambling facilities, fairs, exhibitions and markets.

On the other hand, there will be an increase in the exclusive competences of the Federation; such as the law relating to weapons and explosives (which was previously under concurrent powers), and the production and utilization of nuclear energy for peaceful purposes (including the construction of respective plants and installations). A new field in this context is the defense against the threat of international terrorism in situations where the Land authorities are no longer capable of dealing with its consequences. Such a federal law would need the consent of the Bundesrat.

A major goal of the reform project was to reduce the number of consent-bills, which amounted to approximately 60% of all federal bills. This was primarily due to the provision of Article 84(1) Basic Law, which reads: 'Where the *Länder* execute federal laws in their own right, they shall regulate the establishment of the authorities and their administrative procedure in so far as federal laws enacted with the consent of the Bundesrat do not otherwise provide'. This article was amended as follows: In the future, the Federation can – without the consent of the Bundesrat – by means of its federal laws, intervene with and regulate the establishment of the authorities and the administrative procedure of the *Länder*. However, the *Länder* are allowed to deviate. If the Federation wants to avoid a deviation by the *Länder* from its administrative rules contained in a bill due to a special need for a uniform federal administrative procedure, such a bill will still require the consent of the Bundesrat.

It was expected that the share of consent-bills would, as a consequence of the new provisions, amount to approximately 35%. A study conducted by the administrative service of the Bundestag[18] confirms and supports these expectations. The study analyzed the effect of the new provision as if it had been applied in the past: consent-bills would have been reduced in the period 1998-2002 from 55,2% to 25,8%, and in the period 2002-2005 from 51% to 24%. But this quantitative picture is not convincing (as has been underlined in the reactions to the figures). One must take a closer look to see the saliency of each individual bill. In the past, several consent-bills were rejected because they were regarded as political key projects.

In response to a practice which was heavily criticized, an amendment to Article 85(1) Basic Law was issued. It decrees that federal laws must not pass down special tasks to municipalities. Joint Tasks (Article 91a and Article 91b Basic Law), another target of wide spread criticism, were not abolished. Two of these tasks ('improvement of regional economic structure' and 'improvement of the agrarian structure and of coastal preservation') were maintained. Only Joint Task 1 ('extension and construction of institutions of higher learning, including university clinics') was eliminated. In the future, this task will belong to the *Länder*. However, the *Länder* will be given a financial compensation from the Federation.

Article 91b Basic Law (which until now regulated the co-operation of the Federation and the *Länder* in the fields of educational planning, and the promotion of research institutions and research projects of supra-regional importance) was reformulated and now relates to the following two fields: the co-operation in the promotion of extra-university research institutions and projects, of university research projects (where the approval of all *Länder* is required) and of university buildings for research (including large-scale equipment), and also the assessment and evaluation of the efficiency of the educational system (as it compares internationally) and to produce reports and give recommendations.

Provisions concerning some aspects and details of financial relations

Only certain aspects of the reform package fall into the field of financial relations between the Federation and the *Länder*.

The provision in the Basic Law (old Article 104a(4) Basic Law), which permitted the Federation to grant the *Länder* financial assistance for particularly important investments by the *Länder* or by municipalities under specified conditions (namely 'provided that such investments are necessary to avert a disturbance of

[18] H. Georgii and S. Borhanian, 'Zustimmungsgesetze nach der Föderalismus-Reform. Wie hätte sich der Anteil der Zustimmungsgesetze verändert, wenn die vorgeschlagene Reform bereits 1998 in Kraft gewesen wäre?', Ausarbeitung. Deutscher Bundestag, Wissenschaftliche Dienste, WD 3-37/06 and 123/06 (Berlin 2006).

the overall economic equilibrium, to equalize differing economic capacities within the federal territory, or to promote economic growth'), was subject of concern amongst those who complained about the interlocking relationship between the two levels. The reform package maintains this possibility and only adds certain new provisions designed to reduce the preponderance of the Federation. The financial assistance can be granted only for a limited period of time, and its use has to be examined regularly. The volume of the annual transfers must show a declining tendency over time.

A new Article 143c Basic Law provides for the financial compensation of the *Länder* by the Federation. The *Länder* are entitled to receive particular amounts of the budget from the Federation, if these amounts are no longer used for the previous Joint Task concerning 'extension and construction of institutions of higher learning'. There are criteria on how to distribute the finances among the *Länder*. The five new *Länder* successfully pushed for the inclusion of a sentence in this new article which says that the (political) agreements on financial transfers from the 11 old to the 5 new *Länder* (*Solidarpakt II*) shall remain untouched until 2019.

There is also a new paragraph (6) in Article 104a Basic Law dealing with the internal cost sharing in case of violations of international or European commitments between the Federation and the *Länder*. The Federation has to bear 15% of the burden, the *Länder* 85%. Concerning the costs incurred by the *Länder*: all *Länder* together are responsible for 35% and the Länder directly responsible for the costs must provide 50%.

Another case of cost sharing is dealt with in a new paragraph (5) of Article 109 Basic Law. It relates to the obligation for fiscal and budgetary discipline in the framework of the European Union (Monetary Union). The new clause declares that the Federation and *Länder* are jointly responsible for adhering to these convergence criteria and that, in case of sanctions from the European Union, 65% of the burden is for the Federation and 35% for the *Länder.* All *Länder* together contribute 35% of the burden for the *Länder* and 65% has to be paid by those *Länder* which are directly responsible for the violation of the European rule.

In conclusion, the reform package can achieve certain goals formulated at the beginning of the formal reform efforts. The interconnectedness between the Federation and the *Länder* became weaker and was reduced (through, for example, the elimination of framework legislation, and the creation of exclusive competences for the Federation or the *Länder*) but it was only a very modest step. It did not, for example, eliminate Joint Tasks. The number of consent-bills can be expected to become smaller, but major issues will continue to fall into this category. This might be taken as an indicator that some form and degree of interconnection does belong necessarily to a federal structure. The *Länder* have been strengthened. This

can be seen, for example, through the fact that they have been given additional new competences and the provisions on reversed concurrent legislative powers offer further possibilities for autonomous policy decisions. However, we must wait to see how these reforms will function and in what way the *Länder* will make use of them. The new rules on cost sharing are seen as positive. They emphasize that the two levels of government – Federation and *Länder* – are connected. The reform package is an attempt to find a new balance between both levels. Through this new pattern, German federalism may become increasingly dynamic.

Most political actors, especially those from the two big parties forming a Grand Coalition, welcomed the reform as a fair package deal. Apart from new provisions, they underlined how important it was to have produced an outcome at all; a failure would have affected very negatively the image of 'the political class'. Academics were less enthusiastic in evaluating the first step of the reform. For them, it was a very small step only and they criticized the fact that there had not been a discussion, let alone an agreement on what German federalism should look like. In the broader public, there were no expectations that much would change. And until spring 2007, new provisions in the field of competency did not yet produce an effect. This is primarily due to the Grand Coalition with consensual decisions. Both – political actors and academic observers – agree that what has been achieved in this first step of the reform must be complemented by reforming the financial relations.

Outlook and perspectives: Towards reform of German Federalism, Part II

The mandate given to the Reform Commission of the Bundestag and the Bundesrat in 2003 demanded concentration on the distribution of competency between the Federation and the *Länder*. The goal was to loosen the interconnectedness and strengthen the autonomy of both sides. Financial relations – although a key issue for all states with a federal structure – had been excluded, because all those involved were convinced that a solution for this issue could not be expected for the moment. But all agreed at the same time that modernization of German federalism would require dealing with this issue of financial relations as well. Parallel to the decision of the first part of the reform in the early summer of 2006, an announcement was made to start with the second part immediately. In March 2007, the Bundestag and the Bundesrat established a joint Commission, which shall deal with the financial relations and try to prepare a second reform package.

There are, however, widespread doubts that the Federation and the *Länder* will succeed and make the reform of German federalism into a comprehensive whole. One major reason for this pessimistic evaluation is the diverging interests among

the *Länder*. The weaker *Länder* have accommodated to the existing pattern of financial relations and argue against what they perceive to be greater changes. They object to the idea of competition in financial matters and insist on the principle of solidarity (in financial affairs as well) as a cornerstone of the German federal system. They blame the net-payers, when demanding thorough changes, for trying to escape this obligation.

The discussion on a reform of the financial relations focuses on four points.[19] The first and most urgent point deals with the question of how to reduce and prevent creating further debts. The reason behind the concern is the high level of public debts of the Federation and the *Länder* (including the municipalities), with huge differences between the *Länder*. To totally prohibit debt would not only be a very radical, but also an unrealistic and inappropriate rule. Another approach would be to set an upper limit for debts, perhaps combined with the obligation to reduce the existing amount of debts. Should such rules be decreed in the Basic Law? Some argue that this would not be in line with the federal structure, and they underline that each Land has the right to make their own decisions concerning this point and include respective rules in the constitution of the Land. There is, on the other hand, the need to allocate debt limits, enacted by the European Union, to the Federation and the *Länder*. Furthermore, one would have to include social welfare/security systems. It seems to be difficult to find a solution which conforms to the idea of a federal system and yet finds general support. An integral part of such new provisions would be to have an institution (most probably a new one, composed of independent personalities with a high reputation) with powers, which provide that all territorial entities adhere to the new rules and also have the ability to impose sanctions.

The second question deals with the issue of how to finance public affairs and tasks. It has been a special feature of the German federal system that legislation/rule-making is the primary responsibility of the Federation, whereas the *Länder*'s responsibility is to execute and implement the laws. The Federation has the legislative power on taxes and the *Länder* are beneficiaries (this means that certain parts of the revenues are reserved for them). There are three major ways in how this problem can be solved. The first is to allocate revenues to either the Federation or the *Länder*. This would enable the *Länder* to act autonomously and prevent the Federation from unduly and problematically influencing the *Länder*.

[19] The following is based on the contribution of I. Kemmler presented to a conference on the reform of German federalism, organized by Konrad-Adenauer-Stiftung, Bertelsmann-Stiftung and Europäisches Zentrum für Föderalismus-Forschung and held in Cadenabbia 21-23 Sept. 2006 (will appear in a publication on this conference); and the oral presentation of F. Kirchhof in a panel-discussion on the occasion of the 2006 Theodor Eschenburg-Lecture at the University of Tübingen, 11 Nov. 2006 (the summary of the panel discussion will be published together with the Lecture, given by A. Benz on 'Föderalismus-Reform in der Entflechtungsfalle').

A second option would be that the Federation would have to refund and provide restitution to the *Länder* for their function of implementing federal laws. A third way would be for the Federation to grant the *Länder* annual financial aids, the so-called 'golden leash' (*goldener Zügel*).

Since the last option would make the *Länder* dependent on the benevolence of the Federation and subject to the 'golden leash' of the Federation, the other two options – with a preference for the first and, perhaps, a combination of the first and the second – would better meet the goal to increase the autonomy of the *Länder*.

The third question is on the autonomy of the *Länder* to decide on taxes (e.g., to decide on a top-up system for income and corporation tax). Such a reform step would really mean autonomy for the *Länder*. One must however, consider that the Internal Market of the European Union has abolished borders. To establish new borders, domestically, would not fit into this pattern. Furthermore: excise duties are being harmonized in the European Union. Also, one cannot exclude the possibility of the formation of a cartel by the *Länder*, rather than their competing with each other. Those who defend these arguments against *Länder* autonomy in the area of taxation, therefore, prefer to allocate particular taxes fully to the *Länder*.

The fourth question relates to the equalization, especially horizontal equalization, amongst the *Länder*. This is, no doubt, the most sensitive issue on the agenda. There are advocates for eliminating horizontal equalization completely. Others argue in favour of reducing the volume of these transfers, excluding the levelling effect of the present system. One cannot expect consensus amongst the *Länder*. The Federal Constitutional Court in its answer to the case (which net-payers had submitted) only demanded that criteria must be given – and one has to expect that the *Länder* will not agree on such new criteria. As far as vertical equalization is concerned, the same set of questions will arise: shall such transfers from the Federation be reduced to secure a minimum basic standard (and how much should such a basic standard be)? Secondly, what are the criteria for such transfers (e.g., number of inhabitants, geographical size, or other abstract factors), in order to prevent the Federation from using the 'golden leash' once again?

In conclusion, the agenda on reforming financial relations is full of highly controversial issues, and the interests of the *Länder* differ greatly. This explains why the financial relations were not dealt with systematically in the first round of reform efforts. It is understandable that actors and observers doubt that the second part of the German Federalism's reform attempts will succeed.

The main reason for the ambiguous (and not at all convincing) result of the first part of the reform seems to be – and political actors and academic observers agree on this – that there is no consensus on what federalism and the federal

structure mean. The spectrum extends from those who advocate a high degree of centralist and unitarian solutions on the one hand, and those who are in favour of a high degree of autonomy of the *Länder* as constituent parts of the federal state on the other. The contrast between these two schools of thinking is not new; it created the discussion on which type of federal system should be implemented in the new West German state during the founding period of 1948-49. The solution at the time was a compromise. Afterwards, German federalism developed in a very dynamic way, with the pendulum swinging in the direction of a unitarian pattern. This was brought about by intense co-operation and interconnectedness. At present, there are efforts under way to make the pendulum swing back. The first part of the reform package can be characterized as a step in this direction, but a very modest one only. It remains for us to see whether or not the second step will follow and, in the event that it is implemented, whether or not it will change the format of German federalism.