Public finances, financing and taxation in Brussels

Synopsis, CFB No. 16

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The authors thank E. de Callataÿ, J. Solé, M. Hubert, N. Bernard, and G. Hubert most warmly for their comments and suggestions. The authors bear sole responsibility for the analysis and proposals put forward in this article and the opinions that they express are strictly their own.
I. Observations

1. Revenue, expenditures, balances, and indebtedness

a. Steadily rising regional expenditures

Janssens et al. (2008) studied the trend of the Brussels-Capital Region’s (BCR’s) expenditures since 2001. It appears that the rate of growth of its expenditures was very high. The mean annual rate of growth for the period 2001-2008 is 4.4% in real terms. The growth of primary expenditures was even more marked: +4.8% per year, on average, in real terms. The fastest rates of growth were seen for public works and transport (+5.6%), transfers to the local authorities (+6.1%), and cabinets (+17%).

The rapid rise of spending followed that of income, so that the balances to finance remained close to the break-even line.

b. More independent regional revenues

The Lambermont Reform led to a change in the Special Financing Law (SFL) that was important for the BCR: regional tax autonomy was increased, especially in the area of inheritance taxes, duties on gifts, the road tax on automobiles and vehicle registration fees, and registration fees on property transfers. The Region’s own income from tax revenues now accounts for 50% of its revenue [Van der Stichele and Verdonck, 2001].

Over the period 2002-2009, registration fees on property transfers account for about 20.5% (56.4% of the revenues from taxes on real estate) of the Region’s revenues and inheritance taxes 12.6% (respectively 35.3%) [Zimmer 2007]. The bulk of the BCR’s revenues from taxes on real estate is thus based on real estate transactions or inheritance, that is to say, flows, rather than on already registered property (a stock). These percentages are markedly lower in the other Regions.
c. Local expenditures financed by grants

The local (municipalities’) operating expenses and transfer expenditures to the welfare offices (CPAS/OCMW), police zones, and hospitals are increasing noticeably in the long term. Moreover, revenues from the income tax is limp within the Region’s borders, and this weighs much more heavily on the local finances than on those of the Region (where the fiscal equalization mechanism kicks in).

The result is a basic characteristic of the municipalities’ financing, namely, the steady growth of grants, especially the regional ones, from which they benefit. The various funds and subsidies increased at the rate of 4.6% per annum over the previous legislative term (2000-2006; figures do not include the City of Brussels)\(^1\), with a spurt at the end of the period. The recent improvement in the local financial situation can be explained by the injection of close to 40 million euros of regional money (Cabinet Picqué, 2008).

d. Federal grants in favour of the Region or its municipalities open to criticism

The purpose of the federal-regional cooperation agreement “BELIRIS” is to provide federal budgetary intervention in infrastructure initiatives that promote Brussels’ international role and functions as a capital. The expected commitments appropriations are of about 125 million euros per annum for 2009 and 2010, to be complemented by at least €65 million a year\(^2\) starting in 2009. When it comes to the details, we see that the commitment rate related to BELIRIS is extremely low. This agreement is managed by a Co-operation Committee that includes no fewer than eight ministers. The administration in charge of the work is a federal rather than a regional one. Moreover, the scope of the agreement is becoming more and more broad and fuzzy.

The SFL provides for federal grants to the municipalities to compensate for the buildings benefiting from an exemption for real estate tax. In the Brussels-Capital Region, this compensation is paid directly into the regional budget. The compensation covers only 72% of the theoretical shortfall and a series of other shortfalls to be made up are not compensated [Van der Stichele, 2003].

The Brussels’ municipalities benefit from a variety of mechanisms, such as the Large Cities Policy (“politique des grandes villes”), grants for the City of Brussels, etc. The result is a multiplicity of financial transfers, less consistency between policies, and risks of pandering to political clienteles.

e. Cultural Community Commissions with diverging budgetary positions

The COCOF and VGC have opposite budgetary situations. The COCOF’s budget is in dire straits, due to the budgetary difficulties with which the French-speaking Community had to grapple. The transfers from the COCOF to the French-speaking Community continued to increased even after the Lambermont agreements pro-

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2See Belgium’s official gazette (Le Moniteur belge/Het Belgisch Staatsblad), pp. 31313-31319. The amount foreseen for 2008 is €359.7 million (including money carried over from 2007); for 2009 and 2010 it is €125 million per year, plus an additional at least €65 million annually.

vided for an increase in the financing of the latter. The VGC’s position, on the contrary, is flourishing. It has relatively large amounts of financial means, thanks to the support of the Flemish Community, but also thanks to the financial transfers that are organised by the BCR.

2. Fiscal policies and other market instruments
   a. An active regional tax policy but of limited magnitude

Verdonck (2009) shows that the three Regions have made an intensive use of their fiscal autonomy to achieve their regional policy objectives. The BCR, for its part, has a host of measures aimed at encouraging home ownership and fighting against urban exodus (e.g., reduced registration fees). It has reduced the real estate tax to support social housing and to encourage economic activity. In the environmental field, it has used market instruments (water prices, elimination of rubbish collection taxes, for example) quite actively. In contrast, the Region has taken no special measures in the areas of taxes on automobile and urban tolls.

Some Flemish tax measures triggered a response from Brussels aimed at preventing movements of the tax base (inheritance taxes and registration fees on property). It therefore appears that the risks of a race-to-the-bottom in tax rates exist, despite safeguards in the financing law, especially for measures concerning businesses and mobile tax bases.

b. A multitude of uncoordinated municipal tax policies

There are major differences in the tax structures between municipalities. Moreover, the evolutions in taxes are clearly differentiated, with a marked rise in real estate tax revenue that contrasts with income tax revenue that has declined over the years in both absolute and relative terms.

The municipalities’ reliance on taxation, which includes various taxes on business as well, is increasing quickly, with municipal taxes currently accounting for about 9% of their revenue (compared with 7% in 2000).

3. Intra- and extra-regional solidarity
   a. Chronic under-financing of the Brussels-Capital Region and its constituent municipalities

The financial burden borne by the BCR as a metropolis, capital of the European Union, and capital of Belgium and the Flemish and French-speaking Communities is to a large extent borne by the inhabitants of the nineteen municipalities making up the Region, whereas the benefits of these multiple functions are felt well beyond the Region’s borders [Cattoir et al., 1999a]. In addition, BCR being a small Region, it bears higher per capita incompressible political and administrative structural costs than the other Belgian Regions. Brussels also suffers from various major budgetary shortfalls. The personal income tax is Regions collected at the place of residence, not at the place of work. This political choice is detrimental to Brussels, whereas it is advantageous for the two other regions.

The additional costs that Brussels bears plus the shortfalls with which it must cope were estimated at €490.5 million in 2003 [Van der Stichele, 2003]. Today, this figure is even higher, given various factors such as the increased road traffic in the BCR.
This figure is an unadjusted estimate that does not take account of possible existing partial compensation schemes.

b. Brussels’s solidarity with Wallonia and Flanders

There are many forms of inter-regional solidarity. The commission set up by the Flemish regional government to study the methodology used to analyse inter-regional transfers handed in its report at the end of 2006 [Cattoir et al., 2006]. According to its findings, using the workplace criterion instead of the place of residence to distribute tax revenue from personal income tax would lead to major changes: the BCR would give €1.3 billion instead of receiving €1.4 billion [de Callataÿ and Cattoir, 2007].

A recent study presenting a new estimate of inter-regional transfers in Belgium calculated that the BCR transferred a total of €212 million (€211 per inhabitant) to the other Regions in 2005 [Dury et al., 2008].

c. Limited intra-Brussels financial solidarity within a narrow regional framework

Initially a centralised Municipalities Fund had been set up to allow the redistribution of finances between rich and poor municipalities. Since the decentralization of this Fund, redistribution now takes place within each Region. Vaesen (2006) suggests that, mutatis mutandis, the redistribution in favour of the Flemish and Walloon Regions’ urban centres, especially Antwerp and Liège, respectively, that is achieved by the Regions’ grants to the municipalities, results in markedly higher transfers to these cities, per resident, than those that are effected through the general grants to the municipalities of Brussels.

4. Governance and quality of public spending

a. A fragmented political landscape that generates governance problems

Some important historical and cultural community-related developments have marked political structures, practices, and policies in Brussels [Vaesen, 2008]. The result is a complex and fragmented political and institutional system that thwarts the emergence of a consistent vision and set of actions for the Region’s territory. Shifting regional means to new priorities is a real problem for broad coalition governments such as those that have governed Brussels. Moreover, the risks of duplicating efforts or having local authorities step in for regional authorities are heightened. For example, there are some forty-one ministers or deputy mayors in charge of culture in the BCR and four public transport companies operate within Brussels’s borders. A general increase in efficiency in these areas thus seems possible.

One additional problem of governance that is linked to the foregoing concerns the politicisation and “communitarisation” of the Region’s administration, which have been exacerbated by the existence of language quotas. The regional administration ends up promoting civil servants on the basis of political or language criteria, which is no guarantee of efficiency. The complex problem of language quotas, representation, and linguistic parity is linked to the broader matter of language use in Brussels’ institutions (city halls, hospitals, and so on). It adds an additional layer to the problem of the transfer of powers.
II. Questions-issues

1. Revenue, expenditures, balances, and indebtedness

a. Regional spending linked to revenue?

The Region’s revenues have risen over the past few years, but the parallel rise in expenditures has been such that no financial reserve could be constituted to cope with a possible backward swing of the financial pendulum.

b. More vulnerable and volatile regional revenue?

Whilst the increase in fiscal autonomy was favourable to the Region in a period marked by a property boom, the Regions now have to cope with the risks that are linked to today’s greater volatility of revenue. The relative position of taxes on real property in Brussels’ total revenue, along with their nature, induces risks of revenue instability. In particular, registration fees on property transfer for payment are highly sensitive to short-term economic developments.

c. Municipal finances permanently on an IV drip?

Unable to find enough revenues of their own to cover their rising expenditures, the municipalities of Brussels are bit by bit losing their autonomy, for the increasing regional financial transfers to the municipal governments give the regional authorities a form of indirect control or influence over the local authorities. This situation is not that cut and dry, however, given the great differences that exist between municipalities in this regard. The special purpose grants scheme helps primarily the poorest municipalities, whereas wealthy municipalities, such as Auderghem/Oudergem, can rely more on their own tax revenues, which they are free to assign as they see fit.

In practice, the financial efforts are thus more often made by another level of power, the Region. Systematic reliance on ad hoc increases in regional transfers to the Region’s municipalities makes them less responsible and is not conducive to strict budget management. We see, however, that when they call upon the regional refinancing fund, more direct regional monitoring of municipalities’ finances is carried out by the authority to which they are accountable.

d. Do the federal mechanisms in favour of Brussels and its municipalities need revising?

The federal financial assistance that is received is opaque when it comes to objectives and inefficient when it comes to implementation. This increases some critics’ feelings that the BCR and its nineteen local governments waste this aid and it would be better to reduce it. For others, on the contrary, this bolsters the case for a complete and definitive transfer of this aid’s management to the BCR (example: BE-LIRIS).

e. Does the COCOF need refinancing?

In the absence of refinancing, it will be difficult to keep the services that the sectors financed by the COCOF provide at a satisfactory level in relation to their needs. This is a problem that the VGC does not have. The goal is not for these institutions, which have different powers, to reach similar sizes, but to enable them to provide the same quality of service, mutatis mutandis.
2. **Fiscal policies and other market instruments**

   a. **Is the regional tax policy in a straitjacket?**

   The BCR’s room for manoeuvre when it comes to taxation is limited because of the Region’s size and geographical location, as well as its difficult financial position.

   There are problems of fairness and effectiveness in the area of the real estate tax. It should be recalled that two identical properties can be taxed in totally different ways in Brussels, since no (federal) real estate reassessment has been conducted since 1980 (based on 1975 property values). The result is a growing gap between the taxes that are paid and real properties’ true values.

   b. **Municipal tax policies that lack a consistent and common vision?**

   The aim of taxation, besides collecting financial means, is to support policy measures through its carrot-and-stick effect. The diversity and absence of co-ordination of municipal taxes in the BCR also reflect a certain lack of a consistent political vision across the length and breadth of Brussels although such a vision is necessary, for amongst other things the Region needs to attract or simply to keep residents and businesses on its territory.

3. **Intra- and extra-regional solidarity**

   a. **Insufficient or unsatisfactory solidarity mechanisms?**

   Despite large implicit financial transfers between Brussels and Belgium’s other constituent Regions, the financial conditions that accompanied the Regions’ creation are skewed, to the detriment of the BCR and its municipalities. To balance their budgets, the latter had to resort to heavier taxation or offer fewer public services. This triggered a vicious circle: by contributing to the affluent taxpayers’ exodus to the city’s outskirts, this situation has worsened the financial situations of Brussels’ municipalities even more.

4. **Governance and the quality of public spending**

   a. **Political and institutional fragmentation that spawns malfunctioning?**

   Although this has been only partially quantified, we can surmise that the complexity of Brussels’ institutional landscape, which is the result in part of various historical compromises, is the source of various forms of inefficiency that only worsen the BCR’s already poor finances. Problems arise because of the multiplicity of public authorities in Brussels and a fuzzy division of tasks and responsibilities. This can lead to duplication of effort or too low a level of provision of certain public services. The problem of the distribution of powers amongst Brussels’ public entities is also linked to the matter of the number of municipalities that the Region contains and how their boundaries were drawn. Smaller municipalities (or districts) would clearly have to manage things differently than the larger municipalities that have been created through mergers of towns and villages.
III. Policy options

1. Revenue, expenditures, balances, and indebtedness

   a. Ensuring more stable and predictable regional revenues

   To cope with revenue’s sensitivity to short-term economic developments, we recommend increasing the proportion that is less sensitive to such conditions (e.g., income linked to consumption, to the environment, etc.) and reducing the proportion that concerns flows (registration fees on property transfer) to concentrate on income linked to a stock (such as the real estate tax).

   Linking revenue to the Region’s economic wealth, which is rising steadily, rather to the relative prosperity of its inhabitants, which has been declining steadily for the past decade, should also be sought. Seen from this angle, assigning part of the personal income tax at the source would be an interesting avenue to explore.

   b. Ensuring the municipalities’ autonomy and financial accountability

   Increasing municipal financing via regional grants can ensure a minimum of consistency between the two levels of governments’ policies, at least in theory. On the other hand, a system that relies heavily and increasingly on grants reduces the municipalities’ autonomy and responsibility.

   Various developments could ensure the autonomy, responsibility, and solidarity of the BCR’s municipalities. These include an increase in the proportion of their own income in their total revenues, which could be achieved either by reducing the grants that they receive and increasing their fiscal room for manoeuvre or by transferring municipal spending powers to the Region without linking this to financial compensation. This could be accompanied by increasing the municipalities’ financial responsibility by limiting the ad hoc regional grants on an annual basis.

   c. Financing the Communities’ Commissions in line with their needs

   To the extent that additional and increasing room for manoeuvre is given to the French-speaking Community, some of these means could very usefully benefit the COCOF in the form of a reduction in transfers to the French-speaking Community.

   In addition, a re-appraisal of the apportionment formula between the COCOF and VGC could be considered without challenging the legitimate support that is given to the Region’s Dutch-speaking residents and taking account of the sources of financing that these institutions have, on the one hand, and the services that are provided to the population, on the other hand. The development of co-operation between the two commissions would also make it possible to pool certain means, make certain savings, and/or provide new services to the residents of Brussels.

2. Tax policy and market instruments

   a. Rethinking regional and municipal tax policies

   Given the growing negative externalities related to road transport and traffic in Brussels, increasing the tax and non-tax burdens on this sector appears to be appropriate. At the very least, the federal tax scheme should be neutral with regard to the choice of transport mode, that is, it appears to be less and less justifiable to provide...
tax breaks for company cars. Concluding a co-operation agreement with the other Regions on taxes on automobile is a priority. A road toll system linked to congestion should be put to political debate based on the technical information that is now available.

The Region should have the power to oversee, co-ordinate, and even harmonise the various corporate taxes that exist at the municipal level [Aujean et al., 2005]. Failing this, we should suggest transferring the power to levy taxes in this area to the regional level. The Region is effectively in a better position to take account of the externalities that are linked to corporate taxes. In contrast, regionalising the federal corporate tax totally or in part does not appear to be justified, given the risks of fiscal competition and higher administrative and compliance costs.

To restore fairness when it comes to real estate taxes, a total or partial reassessment of real property values in the Region, or at last systematic re-appraisal of real estate’s value in the case of a transfer or succession, is a must.

Reducing the share of registration fees on property transfer in the revenue pie is advisable. This could be done by extending the targeted reductions in tax base and by guaranteeing the portability of rights. A transfer of the fiscal burden to the real estate tax may be justified in theory, but we stress the fact that this raises problems of transition.

b. Setting up a framework for action and co-ordination in the area of taxation

To ensure maximal co-ordination, consistency, and efficiency in the area of taxation, the regional authorities must be legally empowered to limit unilaterally the municipalities’ powers to levy taxes.

Increased fiscal co-ordination between the BCR and its constituent municipalities could also be facilitated by setting up an observatory on taxation and a co-ordinating body that brings together the minister and deputy mayors in charge of finance.

3. Intra- and extra-regional solidarity

a. Ensuring a fair, effective, and transparent financing of the BCR and its municipalities

In theory, several mechanisms would make it possible to better finance the Brussels-Capital Region and its municipalities. We recommend assigning part of the personal income tax to the Regions in line with the source of income. This would give the BCR a strong incentive to boost employment on its territory.

The quality of the transfer mechanisms could also be improved. By virtue of the subsidiarity principle, it does not appear to be justified to assign federal transfers to the municipalities. The Region is best able to organise the internal redistribution of monies across its territory. For the same reason, all the federal transfers should be concentrated on the regional level, including those of the Large Cities Policy.

The way BELIRIS is implemented must be completely revamped in order notably to increase the transparency and democratic legitimacy of the decisions that are taken therein and to carry out the projects faster. One option would be to transfer the con-
tracting authority for BELIRIS to the Brussels-Capital Region. Another would be to re-examine the rules on the federal level.

b. Encouraging European financing for the capital of Europe

Finally, we may wonder about the role that the European budget could play. Financing to promote the capital of Europe could be justified on a number of grounds [Van Wynsberghe, 2006]. In the context of the preparation of the EU’s post-2013 multi-annual financial framework, care should be taken to ensure that Brussels and Belgium adopt consistent strategies. This means developing and implementing quickly a strategy to pitch Brussels’ interests to the European institutions [Hubert, 2008].

c. Examining the possibilities created by an Urban Community or co-operation agreements

A partial solution to the problem of Brussels’ under-financing could be the creation of an Urban Community extending beyond the Region’s nineteen municipalities for the purpose of organising – and financing – jointly a certain number of collective goods and services, especially public transport. Given the prospect of the inevitable loss of some of the Brussels Capital Region’s autonomy, some people propose resorting to a reversible co-operation agreement and giving each participating Region the right to veto all or part of the decisions taken under such an agreement. An alternative would be to establish one-off co-operation agreements, as needed.

4. Governance, assessment, and quality of public spending

a. Re-examining the division of powers and responsibilities between the regional and municipal governments

The need for a systematic review of the way the organisation of tasks is distributed amongst Brussels’ entities is regularly brought up [Cattoir et de Callataj, 2007]. This need not necessarily be done to the detriment of the local governments. The proposal is to examine in particular the distribution of tasks in areas where major spill-over effects can occur, for example, in the secondary schools, hospitals, museums, and so on.

In parallel, other avenues also deserve consideration. These include redrawing the municipalities, which are highly disparate in size and sometimes have surrealistic boundaries, and having the BCR manage certain areas of regional interest, such as the Heysel trade fair and convention centre complex and the Bois de la Cambre/ Kamerbos woodland park.

b. Increasing the transparency of public policies and fostering a culture of assessment

Given the financial straitjacket within which it works and the segmentation of the bodies that carry out the Region’s actions, the BCR can no longer do without setting up a public policy assessment policy. Certain swathes of its action depend lastingly – and thus without democratic alternation – on the same parties or political leaders. Corollaries are real risks of a lack of transparency, a lack of oversight, and an inability to set new priorities. The development of a culture of independent policy assessment could help to open up discussion in this regard. This culture should be
founded upon clear principles: independence of the assessors, expertise, transparency, pluralism, etc.

On another level, the readability of the public operators’ achievements and the latter’s cost are not guaranteed by any official mechanism for the recurrent generation of information. Now, this is vital for political arbitration and high-quality democratic debate. We propose that an institution should be set up quickly in Brussels to collect and process statistics, assess the Region’s public policies, and produce the necessary information for this (or else an existing institution should be reformed to carry out these tasks).
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