5 Switzerland

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Introduction and Overview

An 1825 map of Switzerland, depicting customs and border controls within the country, shows a panoply of diverging jurisdictions and thus, a multitude of customs offices and stations (Zellweger and Keller, 1825). Crossing Switzerland, at the time, from north to south, from Basel to Chiasso, or vice-versa, implied passing through no fewer than some 25 customs offices by which goods en route had to be cleared and dues paid to each of the seven cantons located on this route, and of course each in their own currency. Apart from additional costs, the imposition of tariffs by all the sovereign cantons of what at the time was a loose Confederation also implied extra time so that the burdens of time and cost actually diverted trade around Swiss territories. Dense tariff barriers and the consequential loss of business to more competitive and direct routes in Austria, Germany, and France were prime motivations in founding the federation under a new constitution in 1848. The removal of these and additional barriers continued to be an important part of the liberal agenda in the nineteenth century under the constitution of 1874. It became an important concern again toward the end of the twentieth century, shaping the current rules under the 1999 federal constitution.

Situated in the heart of Western Europe, Switzerland emerged in the thirteenth century as a loose security alliance of independent rural and urban polities, many of which were situated on the main European trade routes across the Alps. The control of these routes, in particular those between Germany and Northern Italy, laid the foundations of formal independence from the German Empire. The foundations of modern Switzerland were subsequently laid during the reign of Napoleon Bonaparte. The polities were organized in cantons during the Helvetic Republic and were joined by formerly dependent territories. The country was deeply divided between

liberals and conservatives and fell into a brief civil war in 1847. The victors then established a new Confederation in 1848, which was federal in form and built upon the principles of democracy, liberty, and solidarity. It adopted policies of common defense, foreign policy, and neutrality. It was able to stay out of European struggles during the nineteenth century, and World Wars I and II.

Today, modern Switzerland consists of twenty-six cantons (six of which are considered "half-cantons," namely Obwalden and Nidwalden, Basle-City and Basle-Land, Outer Appenzell and Inner Appenzell). Five cantons are unilingual or predominantly French speaking, amounting to some 20 percent of the population of some 7.8 million inhabitants. Nineteen cantons are unilingual or predominantly Swiss German speaking, and one Italian speaking. The Roman language of Rhaeto-Romanian is spoken in parts of two of the cantons. Radio and television are broadcast in these four languages, and print media show a considerable variety in all but Rhaeto-Romanian. People speak local dialects as their main language. Local identity is important and precedes national identity. Attitudes to public affairs very greatly across the country, with substantial differences between the East and West (Geneva is quite different from Appenzell). While the French-speaking part is strongly influenced by French traditions of statehood, traditions of local autonomy prevail in the German-speaking areas. Cultural and geographical diversity is key to understanding historical and contemporary Switzerland.

The country was industrialized in the nineteenth and twentieth centuries, with machine tools, watches, chemicals, and pharmaceuticals as the strongest sectors. Agriculture and tourism remain mainstays in rural and alpine areas. The economy is both extraverted and introverted. On the one hand, the country strongly depends upon exports. Services amount to 70 percent of GDP, with financial services amounting to 10 percent thereof. Export industries were exposed to international competition due to GATT and WTO membership of Switzerland, in 1966 (de facto as of 1955), and 1995, respectively. On the other hand, much internal Swiss trade continued to benefit from protection, shaping what has been called a dual economy. As a result, Swiss annual growth between 1980 and 2003 averaged only 1.5 percent, substantially lagging behind the Eurozone (2.25 percent) and the United States (3 percent) in that period. Moreover, domestic prices in 2004 were estimated to be 40 percent above the average of EU prices (Giorno, 2004). This weak

growth and high costs partly reflected continued protection against foreign trade in agriculture and services and persistent barriers to internal trade within the country. As well, the country's high production costs and wage levels were important in motivating renewed efforts to overcome the dual nature of the Swiss economy in the 1990s.

Of course, Switzerland has come a long way since the customs map was drawn up in 1825. Customs stations were reduced to two when entering and leaving the country, along the north-south or east-west routes. It essentially emerged as a single and integrated economy in which tariff and most non-tariff barriers on industrial goods were gradually removed. While some non-tariff barriers still may exist today, they play a minor role, hardly affecting economic growth and GDP. Yet, other internal barriers emerged as of paramount importance. Regulation of services has remained the province of the cantons to a considerable degree. Until recently, and partly still today, the cantons have operated monopolies in utilities, in particular water, electricity, and local transportation. Each of them has its own rules on regulated professions (except medicine), education, and health care. While federal legislation partly harmonized these areas, substantial obstacles in the field of non-tariff barriers and restrictions in services prevailed over decades among the 26 cantons of Switzerland.

After years of relative neglect, the issue of internal barriers was again taken up in Switzerland at the end of twentieth century, largely because of the influence and impact of the law of the European Union (EU). While Switzerland is not a member of the EU, it is closely linked to European integration by some 130 bilateral agreements, which are based upon the initial 1972 free-trade agreement and a policy of unilateral compliance with EU rules and standards (Cottier and Oesch, 2005; Breuss, Cottier, and Müller-Graff, 2008). The EUs movement to create and complete a single market within the "EC Treaty" triggered policies of aligning Swiss law to European developments. The country adopted a policy of rendering its laws and regulations largely compatible with EU law (*autonomer Nachvollzug*) in order to avoid unnecessary obstacles to its export industries. This policy is essentially driven by the intention of preserving and improving Swiss competitiveness. It comes at the cost of the country losing the possibility of setting its own standards and regulations. In this vein, Switzerland aligned its technical standards to those of the EU in its legislation on technical barriers to trade. Subsequently, it

unilaterally introduced recognition of product standards of the EU and its member states (principle of *Cassis de Dijon*). Stringent disciplines were adopted with respect to public procurement, based upon the WTO Agreement on Government Procurement. These policies were adopted following the rejection by a narrow majority of voters and a large majority of the cantons of Switzerland's joining the European Economic Area (EEA), mainly on the grounds that it would strongly impinge upon national sovereignty without offering adequate means to participate in the process of EU legislation.

Of particular interest in the present context, these external policies had important spin-offs for Swiss inter-cantonal commerce regulation. The *Internal Market Act* adopted the principle of *Cassis de Dijon* on mutual recognition of product standards (goods and services) for the purpose of commerce between cantons (and communes). Government procurement among cantons was liberalized. More stringent disciplines in anti-trust regulation were introduced, modeled on the basis of EU law, reducing inter-cantonal barriers such as geographical allocation of markets.

The recent influence of EU law in completing the Swiss internal market has been profound. At the same time, the law has failed to remove all barriers and distortions. *Inter alia*, remaining barriers are due to the lack of transparency and of disciplines on cantonal subsidies. In the field of health care, cantons still are largely segmented. The same holds true for taxation the regulation of which lies, to a considerable extent, in the competence of the cantons. The lack of harmonization in education results in limited labour mobility. Cultural barriers translate into continued segmentation of media markets. Unlike in the EU, courts have not played a strong role in removing such barriers. The prerogatives of federalism have generally prevailed. Legal analysis failed to assess the economic costs of regulations in a systematic and sufficiently developed manner. Switzerland remains a polity built bottom up and on the basis of regulatory competition and multi-layered governance. Concern for local jurisdictions, including communes based on the "sovereignty" of the cantons, formally recognized by the 1999 constitution, inevitably renders the removal of all modern non-tariff barriers difficult to achieve even today. We continue to face the challenge of finding an appropriate balance between federalism, diversity, and market integration. It is unlikely to be ever settled as it reflects competing constitutional interests.

Constitutional and Legal Provisions

The historical process briefly described above is paralleled in constitutional law. Foundations to overcome inter-cantonal barriers were laid in 1848, further refined in 1874, but largely ignored up to the end of the twentieth century until the 1999 constitution was framed during the completion of the EC internal-market program of 1992. In substance, the constitution of 1999 is largely an updating and clarification of the constitutions of 1848 and 1874, and the minor alterations made in the meantime, upon which it builds. Still, it introduced some relevant amendments and clarifications with respect to the removal of remaining intercantonal barriers.

The Swiss System of Governance

The federal constitution of 1848 was largely influenced by the US constitution of 1787 (Anderson, 2008; Church, 2004; Haller, 2009; Linder, 1998). A system of two chambers of Parliament, comparable to the US Senate and House of Representatives, was introduced. The Council of States (Conseil aux Etats, Ständerat) consists of 46 members—two seats for each canton and one seat for each half-canton. The National Council (Conseil national, Nationalrat) consists of 200 members, elected on the basis of proportional representation. Large cantons, such as Berne and Zurich, are entitled to some 30 members of the National Council while small cantons are guaranteed at least one seat. The balance of power is established by granting equal rights and obligations to the two chambers, resulting in a relatively strong position of smaller rural cantons vis-à-vis the metropolitan urban cents. In both chambers, members are organized along party lines; the cantons are not empowered to instruct elected representatives in the Council of States. The executive branch, the Federal Council (Conseil fédéral, Bundesrat), consists of seven members elected for four years by both chambers of Parliament, reflecting both geographical distribution and the parties' seat shares in Parliament. They must resign their parliamentary seats and once elected, the Federal Council is not responsible to the legislature, as in presidential systems.

In the early days of the Confederation, Switzerland was shaped by a liberal majority, which gradually gave way to a coalition government of the main political parties. This evolution was essentially

due to the introduction of instruments of direct democracy in the late nineteenth century, in particular the popular right to seek and hold referenda on legislation, and to bring initiatives with a view to amending the constitution. These instruments eventually led to the inclusion of all relevant political parties in the composition of the executive branch so as to minimize the risk of successful challenges from the populace. Since 1959, the Federal Council has been, in essence, a broad coalition. It is composed of members representing conservative, moderate, and centre-left parties, with, at the same time, a balance between the German-speaking and French-speaking regions of the country. However, there are no fixed numbers of seats for these two regions. The Italian-speaking part of Switzerland has been intermittently represented in the Federal Council.

Overall, the Swiss system of governance evolved on the basis of vertical and horizontal separations of powers. Vertically, the cantons enjoyed high levels of autonomy from the early foundation of the Confederation, including the power to tax and to control the implementation of federal law. Horizontally, powers are carefully shared among the chambers of Parliament and the Federal Council. The judiciary in Switzerland is essentially based upon the courts of the cantons. Genuine jurisdiction of federal courts is limited to matters of federal administrative law and selected areas of penal law. The Federal Supreme Court (Tribunal fédéral, Bundesgericht) essentially operates as a court of appeal, and its role includes constitutional review of cantonal legislation and compliance with international agreements by cantons and the federal government. Unlike in the United States or Germany, constitutional review does not extend to federal legislation except in case of violations of international law (in particular the European Convention on Human Rights), so the check on federal encroachments on cantonal powers is essentially through the popular right to force a referendum.

Foreign-policy powers of the federal government are comprehensive and almost exclusive (Thürer and MacLaren, 2009). Except for local and minor issues of trans-boundary co-operation, the treaty-making power is vested in the Confederation. It includes areas pertaining to the prerogatives of the cantons in a domestic context, such as education and health care. The cantons, however, are entitled to be heard in the process of shaping foreign policy, and extensive consultations are held when prerogatives of the cantons are affected under the constitution (cf. article 55 of the constitution). This has become of particular

importance in the process of European integration. Bilateral agreements increasingly affect prerogatives of the cantons. Consultation with the cantons essentially takes place within the Conference of Cantonal Governments (Conférence des gouvernements cantonaux, Konferenz der Kantonsregierungen), including its meetings with the federal government. Practical arrangements can include the participation of members of this conference in diplomatic delegations, which facilitates information flows and ongoing consultations in the negotiating process.

Creating a Single Market in Constitutional Law

Resulting from a liberal revolution (the only one successful on the European continent at the time), the federal constitution of 1848 laid the foundations for largely removing obstacles to a single internal market and for creating an appropriate framework for it in Switzerland (Kölz, 1992; Cottier and Merkt, 1996; Schott, 2010). Exclusive powers to regulate international commerce were given to the federal government. Freedom of establishment for individuals and legal entities and the introduction of a common currency, the Swiss Franc, were major steps in 1848 (though the National Reserve Bank was introduced only in 1907). In 1874, freedom of commerce was added (Auer, Malinverni, and Hottelier, 2006; Grisel, 2006; Winzeler, 1994). For several decades, the power to adjudicate cases turning on freedom of commerce rested with the Federal Council, and only in 1912 was jurisdiction transferred to the Federal Supreme Court. The Confederation was given powers to regulate civil law, which includes both commercial and civil legislation. Company law was harmonized on this basis at the beginning of the twentieth century, as were much of civil and penal law in 1912 and 1949, respectively. In the twentieth century, the evolution of the welfare state mainly emerged by further centralization, in particular the establishment of nation-wide pension and social insurance schemes. The creation of a dense, modern rail network during industrialization and of national highways under federal jurisdiction in the twentieth century was a major contribution to shaping a single market.

Particular Provisions

The federal constitution of 1999 essentially reproduces the power-sharing arrangements laid down in the constitutions of 1848 and

1874. The relationship of the cantons and the federal government are characterized by long and stable traditions. Subsidiarity continues to constitute the guiding principle for the allocation of competences and powers between the different layers of government (Federation, cantons, and communes), explicitly provided for in article 5a of the constitution (Byrne and Fleiner, 2005). Moreover, the new constitution brought about some amendments and clarifications which are of particular importance in the present context. The following provisions are essential for bringing about a single market in the country:

- Article 24 reiterates freedom of establishment which all citizens of the country enjoy. No restrictions to mobility, as were still predominant in the nineteenth century, exist any longer. Today, any such restrictions are limited to foreigners whose rights and obligations are essentially defined by legislation and international agreements (article 121).
- Freedom of commerce, established as a fundamental or constitutional right in 1874, amounts to the most important foundation for addressing internal barriers to trade and economic relations. Stipulated today in article 27, it subjects restrictions imposed by the cantons or the executive branch of the federal government to constitutional review by the courts, in particular the Federal Supreme Court. However, judicial review does not extend to acts of the Federal Parliament except for rights protected by the European Convention on Human Rights.
- While there was controversy over the extent to which freedom of commerce might also entail horizontal guarantees comparable to the US interstate commerce clause, article 95 of the new constitution explicitly requires the Confederation to "seek to create a unified Swiss economic area" and thus to remove unjustifiable obstacles to trade and commerce among the cantons (Aubert and Mahon, 2003). The provision clearly was inspired by the frustrating experience in negotiating the 1995 *Internal Market Act*.[1] At the time, cantons argued that the act was unconstitutional and impinged upon their sovereign right to autonomously regulate businesses and professional activities (Auer and Martenet, 2004). The 1999 constitutional provision offers an ex-post foundation for powers which heretofore were controversial. At the same time, it remains of limited effect as it does not entail a constitutional power to centrally regulate government procurement. We shall return to this point.

Of great importance are further provisions in the 1999 constitution which fully or partly centralize formerly decentralized tasks, or which bring about harmonization of laws among the cantons. Of relevance to inter-cantonal commerce are in particular the following:

- The Confederation is empowered to legislate on-road transport, which ensures the construction of a network of motorways. It controls roads of national importance and decides which transit roads must remain open to traffic. Similarly, the Confederation has the authority to legislate on rail transport, shipping, and aviation (articles 82, 83, and 87).
- The Confederation has the authority to establish principles on the use of energy sources and on the economic and sufficient use of energy. It is responsible for legislation on the transport and supply of electrical energy (articles 89-91).
- The Confederation is responsible for postal and telecommunication services and for legislation on radio and television as well as on other forms of public broadcasting of features and information (articles 92 and 93).
- The Confederation is empowered to legislate on various economic matters. It legislates against the damaging effects in economic or social terms of cartels and other restraints on competition. Moreover, it takes measures to protect consumers. It legislates on the banking and stock-exchange system and is responsible for money and currency. The Confederation supports regions of the country that are under economic threat and promotes specific economic sectors and professions, if reasonable self-help measures are insufficient to ensure their existence. Equally, it ensures that the agricultural sector, by means of a sustainable and market-oriented production policy, makes an essential contribution toward the reliable provision of the population with foodstuffs, the conservation of natural resources, and the upkeep of the countryside and decentralized population settlement (articles 94–104).
- The Confederation is responsible for legislation on external economic relations. It safeguards the interests of the Swiss economy abroad by taking, in special cases, measures to protect the domestic economy (article 101).
- The Confederation legislates on employee protection, relations between employers and employees, recruitment services, and the

declaration of collective employment agreements to be generally applicable. It also takes measures with respect to social security (articles 110–120).

- The constitution entails provisions on federal taxes and principles of taxation binding upon cantons, while leaving them ample regulatory powers (articles 127–134).

All these provisions are accompanied by acts and regulations implementing constitutional policies. They establish the core of shared rules that apply uniformly to the entire country.

Areas left to the cantons by the constitution essentially entail education, police, health care, cultural policies, and professional qualifications (unless they have been centralized, based on article 95, such as medical professions). Importantly, direct taxes essentially remain the autonomous domain of both cantons and communes. Article 129 empowers the Confederation only to harmonize certain aspects, including tax liability, the object of the tax and the tax period, procedural law, and the law relating to tax offences. Explicitly excluded from harmonization are, *inter alia*, tax scales, tax rates, and tax allowances.

In many fields, the federal government and the cantons have concurrent authority under the constitution. Comparable to EU law, federal law, to the extent it exists in a field, prevails in cases of concurrency while the cantons are entitled to enact supplementary or implementing legislation so long as it does not conflict with federal law. The implementation and enforcement of law are essentially the responsibility of the cantons, even within the province of federal law. The system of courts of first instance is almost entirely based upon courts of the cantons, with federal courts only at the level of appeal and final adjudication. The one exception is that federal courts have exclusive jurisdiction in selected areas of penal law. In all other fields, they are merely entitled to review decisions of cantonal courts or federal authorities and agencies. As a result, implementation of federal law in different cantons often shows differences in interpretation, thus adding a layer of regulatory competition even in areas essentially harmonized by federal law.

Switzerland's Internal Market: Its Functioning and Barriers

Within the federal system, there have been ongoing efforts to remove tariff and most non-tariff barriers among the cantons since

the foundation of the Confederation in 1848. These efforts have been markedly successful over time. However, there are still major internal barriers. Some of these barriers concern traditional market-access restrictions and governmental measures, which result in uneven playing fields. Current legislation, partly based on necessary revisions, would arguably allow removing them.

Other barriers do not directly concern market freedoms as such, but otherwise hamper efforts to bring about a truly common market, in particular with respect to labour mobility. Some of these barriers may be partly inherent to Swiss federalism, to some extent reflecting a variety of different cultural backgrounds and linguistic differences, and the price to pay for decentralized governance and local autonomy in cantons and communes. They hardly can be successfully addressed on the basis of the current constitutional framework and existing legislation.

Market Access Restrictions and Uneven Playing Fields

Most of the remaining traditional non-tariff barriers restricting inter-cantonal market access are located in the field of services, particularly professional qualifications. Cases submitted to the Federal Supreme Court have essentially dealt with prohibitions on the exercise of cross-border services or on establishment by professionals whose qualifications were obtained in a different canton (Diebold, 2010). The following two examples are typical cases from the rich jurisprudence of the Federal Supreme Court on the interpretation and application of the *Internal Market Act*. They address free movement of qualified lawyers and of professionals in the paramedical field such as physiotherapists:

- In 2008, the Federal Supreme Court decided that the requirement for an attorney-at-law to have more than five years of work experience in the canton of Vaud in order to be granted the right to employ trainees was inconsistent with the *Internal Market Act*. Such a five-year requirement was not necessary in order to achieve the goal of ensuring appropriate training (BGE 134 II 329, *Blanc et Iynedjian v. Canton of Vaud*).
- In 2008, the Federal Supreme Court was called upon to examine a decision rendered by the authorities of the canton of Zurich,

which had not granted a psychotherapist admitted in the canton of Grisons the right to offer her services, self-employed, in the canton of Zurich. The Federal Supreme Court held that such a refusal was not based on legitimate reasons, thus violating the principle of proportionality (BGE 135 II 12, *X. v. Canton of Zurich*).

The admission of restaurant and bar operators from other cantons and communes has also been at issue in some cantons. Other areas, such as taxi and sanitary services, have hardly been addressed. Most of these remaining barriers are likely to be removed on the basis of current legislation, which empowers affected persons and the Competition Authority to challenge them.

In the field of government procurement, the divergence of forms and procedures renders applications cumbersome and more difficult for non-local bidders. Although market access between cantons is provided for by an inter-cantonal concordat and supported by the *Internal Market Act*, explicitly providing for non-discrimination at cantonal and local levels, market segmentation continues to exist (Oesch, 2010).[2] Finally, it is difficult to challenge government procurement decisions without damaging business relations with the authority concerned. It is difficult to assess the implications of these barriers in real terms, but we expect them to be significant in practice.

Distortions in markets continue to exist due to subsidies and state aid at the level of cantons and communes. Unlike in EU law, Swiss constitutional law does not offer disciplines on recourse and use of subsidies by the cantons. Federal legislation on subsidies only applies to federal agencies and can be easily removed by more specialized legislation. Cantons, in particular in the field of economic promotion and attracting foreign direct investment, engage in unilateral tax practices and rebates of substantially distorting effect. There is no transparency in this regard, and levels of subsidization on the level of the cantons amount to one of the best-guarded secrets in the country.

In the field of health care, cantons still are largely segmented, and mandatory insurance, despite relying upon federal law, is calculated on the basis of expenses and costs of each of the cantons. Without additional insurance, patients cannot easily seek treatment in a canton other than that of their residence. Free-market access for

insurance companies and inter-cantonal consumption of services by patients are restricted. As a consequence, there is no or little competition among medical centres. So far, cantons have not even agreed as to where expensive investments on high technology medical treatment, such as heart surgery, should be made. Overall structures are not suitable to bring about cost efficiency. Soaring health costs—second worldwide per capita after the United States—range among the unsettled challenges of modern Switzerland.

Lastly, inter-cantonal and inter-communal barriers, which are traditionally considered inherent to existing Swiss federalism, relate to taxation. Direct taxes remain, to a considerable extent at least, the autonomous domain of both cantons and communes. They have the authority to determine tax scales, tax rates, and tax allowances (article 129 of the constitution). Unlike other federations in Europe, in particular Germany and Austria, Switzerland's tax system is very competitive and shows considerable differences among the various entities at the sub-federal level (Hinny, 2010; Kirchgässner and Guptara, 2006). Tax competition is a sensitive matter, in Switzerland as in any other country (Anderson, 2010). On the one hand, it is commonly held that it results in lower overall tax burdens for individuals and enterprises, thus stimulating (labour) mobility and economic activity (Feld, 2009). On the other hand, it is argued that excessive forms of tax competition lead to uneven playing fields for competitors located in different cantons, potentially resulting in market distortions and potentially to "a race to the bottom," with the hollowing out of a tax base. Legislation contains instruments on the equalization of financial resources and burdens between the Confederation and the cantons as well as among the different cantons (cf. article 135 of the constitution) and the Swiss model of equalization is relatively generous to poorer cantons; however, this does not directly address the issue of tax competition. In 2011, the Swiss people will be called upon to vote on the popular initiative "For fair taxes. Stop the abuse of tax competition," which has been submitted by the Socialist Party. The initiative seeks to limit considerably tax competition between cantons and communes. It provides, *inter alia*, that salaries of individuals exceeding SFR 200,000 per annum shall be subject to a tax of 22 percent at minimum. The Federal Council recommends rejecting the initiative (Message du Conseil Fédéral, 2009).

Other Barriers

Some important barriers to internal trade and mobility within Switzerland are to be found outside traditional market-access limitations. For example, key barriers to labour mobility include social barriers as well as remaining legal barriers associated with the highly decentralized school system. Each canton—even different communes within a canton—have quite different curriculums for students of a given age, which makes mobility and coordination among different systems difficult. There have been efforts to bring about harmonization, based on articles 61a and 62 of the constitution, but they mainly operate on the basis of an inter-cantonal agreement. The Accord intercantonal sur l'harmonisation de la scolarité obligatoire (HarmoS project) was approved of by 15 cantons and came into force in August 2009. However, in seven cantons the voters rejected accession. Other cantons are yet to decide, either by Parliament or by a referendum.[3] One reason why Switzerland has one of the most advanced rail systems in Europe is that families face so much difficulty in moving because schooling is badly coordinated. It is easier to commute daily within the relatively small expanses of the country, crossing tunnels, bridges, and valleys, than to move a family. In addition, moving into a different region with a different language presents cultural hurdles that should not be underestimated. Again, commuting seems to be the answer.

In the same vein, language barriers remain an important challenge in daily life, in particular in education. Today, even educated people no longer master German or French as a second language easily, let alone Italian or Rhaeto-Romanic. English is often referred to as a common denominator. While this presents few problems to business and academia, it adds to existing problems in the school system that are further amplified by a multitude of immigrants with different backgrounds. Adherence to a language group and language skills tend to favour local applicants for jobs. Language also has a disintegrating effect in terms of the media. Newspapers are essentially limited to particular regions and none of them enjoys extensive circulation throughout the entire country. Likewise, radio and television programs are segregated along language barriers and do not truly compete for quality. Content is often limited to one or the other part of the country. Except for bilingual music radio programs during the night, there are no common programs, lagging behind what

can be found on the European level with Arte as a bilingual public channel or with synchronized Euro News.

Processes and Means for Addressing Barriers and Enhancing the Market

Statutory Law and Inter-cantonal Agreements

Market integration has been primarily addressed by way of gradually harmonizing and centralizing pertinent pieces of legislation, in particular commercial, civil, and penal law. The development of common policies and federal responsibilities was seen to be key in creating the common and integrated market. The emergence of a regulatory framework under GATT and subsequently the WTO has also been of great importance in shifting traditional patterns within the country, and it exerted considerable influence on shaping domestic legislation. Government procurement perhaps is the most important example. The process of European integration has played a significant role in the late-twentieth century as the formation and completion of its common market placed Switzerland under pressure to address its role as a high-priced market. Models developed in the EU were adopted and used to bring down still existing barriers among the cantons. Harmonization and unilateral adjustment to EU law often had the side effect of removing diverging standards among cantons. Remaining obstacles, mainly in the field of professional qualifications and market access of regulated professions, were only taken up by legislation under the influence of European integration and pressure to lower overall price and cost levels at the end of the twentieth century. Competition policy was reinforced as a main tool to achieve these goals and to reduce privately induced market segmentation. Harmonization of technical norms and standards and the introduction of government procurement disciplines were equally instrumental in reinforcing the domestic economy.

Specific remedies to address distortions are typically being sought on the basis of framework legislation instead of detailed harmonization. Cantons are left with considerable policy space to implement these frameworks. They operate under weak judicial supervision and see little incentive to leave privileges granted to local constituencies behind. The lack of federal courts of first instance renders effective judicial protection more difficult, and the slow progress in removing trade barriers

in the twentieth century is largely due to this weakness and a lack of general awareness of the economic and social costs of protectionism.

In part, cantons seek to bring about harmonization among themselves, finding recourse in binding inter-cantonal agreements (concordats). Prominent efforts relate to co-operation in internal security, education, and government procurement.[4] The strategy seeks to avoid granting additional powers to the federal government. However, as concordats are not necessarily signed and implemented by all cantons, coordination may remain piecemeal, thus leaving barriers to trade in place and market access impaired. Major efforts mentioned above to fully harmonize primary school education are likely to fail due to resistance in a number of cantons (HarmoS project).[5] Eventually, the federal government may have to intervene and enact legislation to harmonize primary and secondary education curricula, such as entry age, duration, and objectives, across the country. Interestingly, article 62 of the constitution explicitly grants the Confederation the authority to achieve harmonization by federal legislation if such harmonization is not achieved by means of coordination among the cantons themselves, resulting in a new type of a "conditional competence" of the Confederation (Biaggini, 2007).

Main Statutory Instruments

The formation of a single economic area within Switzerland strongly relies upon the implementation of a great number of statues, many of which implement international treaty obligations and constitutional tasks mentioned above. Specifically, three acts are of particular importance as they relate directly to the completion of the internal market: the *Internal Market Act*, the *Act on Technical Barriers to Trade* and the *Act on Cartels and Other Restraints of Competition* (*Cartel or Competition Act*). All three were enacted in 1996, following the rejection by voters of Switzerland's joining the European Economic Area (EEA Agreement) in 1992. They have been partly amended in the meantime, based upon experiences in a process of trial and error. All efforts essentially aim to reduce costs and increase competitiveness. The same holds true for a fourth element on government procurement.

1. The *Internal Market Act*: In the aftermath of the Swiss decision not to join the EEA Agreement, the dichotomy of a competitive

export economy and of protected domestic industries gave rise to fears that Swiss products would no longer be competitive on European and world markets. Costs needed to be reduced and it was found that high costs were partly due to market segmentation based upon divergent regulations of cantons in remaining regulatory areas. For example, heating equipment needed to comply with certain standards provided for by one canton, thus barring installation of equipment admitted in another canton under different standards. It often resulted in de facto monopolies of local suppliers. The *Internal Market Act*, inspired by the jurisprudence of the European Court of Justice relating to mutual recognition and equivalence, introduced the so-called principle of origin: products and services lawfully put on the market in conformity with local regulations are entitled to be sold and used throughout the country (Cottier and Merkt, 1996; Martenet and Rapin, 1999; Zwald, 2007). The act, in other words, is built upon the so-called *Cassis-de-Dijon* principle as developed by the European Court of Justice.[6] It is only with recourse to compelling public interests, such as public security and morality, health and life of humans, animals, or plants and the protection of the environment, that the cantons remain entitled to enforce their own regulations in relation to goods and services originating in other cantons. Importantly, the act applies across the board, including services and professional qualifications. Unlike in the EU, it is not limited to trade in goods. Moreover, the act entails provisions relating to government procurement, introducing non-discrimination at cantonal and local levels and securing minimum publication requirements.

Enforcement of the implementation of the act was essentially left to the courts. The Federal Supreme Court was reluctant to forcefully implement the act and to follow the parallel jurisprudence of the European Court of Justice. While the principle of origin was admitted in some cases, concerns for sovereignty and regulatory autonomy of the cantons prevailed in others. Moreover, the court narrowly construed the act. It declined to apply its provisions in cases in which economic operators were not granted the right to establishment and limited its scope to classical inter-cantonal barriers to trade in goods and services. It was eventually found that the act is not sufficiently effective, and Parliament revised and amended it in 2004. The revision

essentially entails the extension to controversial cases of establishment. It tightens exceptions that can be invoked and allocates a more active role to the Competition Authority in prosecuting cases.[7] The act still fails to apply to core public functions, such as free movement of government officials, leaving employees in the public sectors potentially excluded.

2. The *Act on Technical Barriers to Trade*: Market segmentation in Switzerland as a whole was essentially due to the operation of national or even cantonal production standards, for example relating to construction and admission of automobiles. These standards often deviated from European norms and standards or those of EU member states. They tended to increase prices. With a view to remove international non-tariff barriers, the *Act on Technical Barriers to Trade* obliges federal regulators to align Swiss standards to those of the main trading partners, in particular the EU (Tercier and Bovet, 2002; Merkt-Matthey and Bridy, 2007). Domestic standards therefore were aligned, thus allowing importation of products from EU and EFTA states more freely. Harmonization of Swiss with EU standards by federal law binds the cantons, of course.[8] Thus, the alignment also has the side effect of removing differences among cantonal standards where they still exist. Overall, the policy has been successful and has contributed to decreasing prices, in particular in the automotive sector and construction. The act, however, does not apply to standards enacted by cantons. These are subject to the *Internal Market Act* and thus to mutual recognition rules in line with the principle of origin.

A recent revision of the act was aimed at unilaterally introducing the *Cassis-de-Dijon* principle with respect to imports from the EU and its member states (Message du Conseil Fédéral, 2008; Oesch, 2009). Whatever the Swiss standards, products complying with Community standards (in cases of harmonized product standards) or with standards of a EU/EEA member state (in cases of non-harmonized product standards) are essentially entitled to be marketed in Switzerland without any further state control. A list of exemptions, defined by the federal government, marks sensitive products for which compliance with domestic standards remains mandatory. The policy does not require reciprocity on the part of the EU. It is a measure of unilateral

liberalization, seeking to reinforce competitiveness of Swiss products. Introducing the principle unilaterally was controversial but defended on the grounds that Swiss export industries produce on the basis of European standards anyway and little would be gained by waiting for a reciprocal agreement. The revision entered into force in mid-2010. Opponents had failed to collect sufficient signatures required to hold a statutory referendum on the draft legislation.

3. The *Competition Act*: The third pillar crucial in completing the Swiss internal market is the *Competition Act* of 1995 (Tercier and Bovet, 2002; Ducrey, 2007). Essentially modelled after EU law, the act substantially improved protection from cartels and the abuse of a dominant position. It also introduced merger controls. However, while the act strongly reinforced protection as compared to the previous act of 1965, first experience showed significant weaknesses in enforcing anti-trust disciplines in Switzerland. In particular, the Competition Authority was not entitled to sanction first-time violations and was limited to expressing warnings. In 2004, the act was amended, introducing incentives and defenses for "whistleblowers" (leniency program) as well as the right of the Competition Commission to sanction violations in the first place.

Interestingly, and unlike EU law, the creation of a single market is not an explicit goal stated by the act. Yet, like any other competition act, it contributes to overcoming private barriers to trade, which traditionally were formed often along borders and territories of cantons or regions (e.g., in defining exclusive dealership or other limitations to advertise and do business outside a defined geographical area). Moreover, when liberalization of electricity supplies failed in a referendum in 2002, markets were partly opened on the basis of the *Competition Act* shortly thereafter (Ducrey, 2007; Jagmetti, 2005; Weber and Kratz, 2005). The Competition Authority determined that a cantonal electric power enterprise abused its dominant position by not granting other enterprises access to its grid infrastructure for the transport and supply of electricity. It based its conclusion on the fact that the electric power enterprise did not possess a legal monopoly, awarded by the cantonal government, but only a de facto monopoly due to its market share. As the enterprise could not

present legitimate business reasons to the contrary, it was obliged to make its grid infrastructure available to other electricity suppliers. Upon appeal, the Federal Supreme Court confirmed the ruling of the Competition Authority. The Court noted that the decision of the people not to accept a new law, which would have brought about the partial removal of internal barriers to trade in electricity, did not automatically mean that the *Competition Act* would not be applicable. In 2008, a new *Act on the Supply of Electricity* came into force.

The 2004 revision of the act reinforced the procedural powers of the Competition Authority. Experience shows that local cartels are being prosecuted more successfully than before. The act, however, does not respond to problems of judicial assistance and co-operation with the EU. While the act is largely framed on the basis of EU law, Switzerland is not part of the European Competition Network (ECN), and is therefore excluded from actively and formally co-operating with the EU Commission and with the competition authorities of the member states. Efforts to bring about enhanced co-operation by means of a bilateral agreement on legal assistance are only beginning and have remained politically controversial. The EU Commission does not depend upon such an agreement as it often takes action against Swiss companies operating in the EU that in turn depend upon parent companies located in Switzerland. It is unclear to what extent the attempt to address market segmentation within the country, through prosecutions by the EU, contributes to maintaining internal barriers between cantons because of the difficulty in prosecuting effectively from outside the country.

In early 2009, a special group issued an evaluation report on the efficiency of the *Competition Act*. It suggested that the main reform prospects should focus on independency of the Competition Authority, the conclusion of co-operation agreements with the EU, the harmonization of the merger control regime with that of the EU, and the review of restrictions on vertical agreements.[9] On this basis, the Federal Council presented, in mid-2010, recommendations to the Parliament for revisions and amendments to remedy the identified weaknesses and to render the *Competition Act* more effective.[10]

4. Government Procurement Regulations: Prior to the adoption of the WTO Agreement on Government Procurement (GPA), disciplines on government procurement in Switzerland were loose and

scattered, often to the benefit of local suppliers (Oesch, 2010). The GPA was implemented both on the federal level (*Government Procurement Act* of 1994, as accompanied by an ordinance) and on the level of cantons (cantonal laws on government procurement) (Fetz, 2007). Furthermore, cantons joined efforts by concluding an inter-cantonal concordat (Accord inter-cantonal sur les marchés publics of 1994, substantially revised in 2001). As of 2009, all cantons had become signatories to the revised concordat. The Agreement on Government Procurement of 1999 between the EC and Switzerland further extended the scope of application for government procurement under the GPA, based upon relatively low thresholds. In addition, market access between cantons is supported by the *Internal Market Act*, explicitly providing for non-discrimination at cantonal and local levels, though the federal government does not have full powers to regulate government procurement by cantons and communes. Despite partial harmonization, substantial differences in form and procedures remain, which tends to favour local suppliers familiar with existing substantive and procedural rules.

By 2010, the procurement regime at the federal level was partly reviewed. At the same time, efforts to further harmonize the federal and cantonal legislation failed to materialize.[11]

The Role of Courts and of the Federal Competition Authority

The main internal barriers in Switzerland were overcome by the liberal revolution in 1848 and subsequent constitutions. These provided the basis for gradual shifts of powers to the federal level and for harmonization of laws and infrastructure, both of which are crucial to forming a common market. It is interesting that the removal of trade barriers to inter-cantonal commerce was most effective when the power to apply and implement freedom of commerce was with the executive branch until 1912. Once adjudicatory powers shifted to the courts—in particular the Federal Supreme Court—the horizontal dimension of creating a common Swiss market gave way to protecting federalism and the prerogatives of the cantons. As judges traditionally served in cantonal courts before being elected by Parliament to the Federal Supreme Court, most of them were more

sensitive to cantonal sovereignty than to the costs of restrictive market regulations and their potentially negative effects on welfare and social and economic development. With the advent of the welfare state, attention shifted to limiting vertical governmental intervention and to safeguarding that restrictions of constitutional freedom of commerce comply with the rule of law.

Since 1912, the courts have not played a leading part in bringing about a common market in Switzerland by removing inter-cantonal trade barriers. Legal analysis failed to assess the economic costs of regulations in a systematic and sufficiently developed manner. The economic analysis of law has not played a significant role in litigation. The costs and inefficiencies of decentralized regulation were rarely assessed and taken into account in balancing pros and cons of mutual recognition. Disguised protectionist motives often were not exposed. In the same vein, the Federal Supreme Court denied giving direct effect to GATT and the Free Trade Agreement with the EC, unlike other international agreements, including the EFTA Convention. In contrast to the European Court of Justice, Swiss courts operate under long traditions of favouring federalism. The lack of judicial support in implementing the *Internal Market Act* induced further legislative reforms, reinforcing the role of competition authorities in monitoring and prosecution. The judiciary did not take the lead in the process.

It is only since the revision of the *Internal Market Act* that the courts have become more assertive in applying the revised act as consistent with the constitutional clause of freedom of inter-cantonal commerce. Most of the efforts and achievements are due to the political process and legislation, with the executive branch of the federal administration taking the lead in preparing legislation. While the cantons often expressed opposition through their lobbies in defense of their own prerogatives, the relevant acts were supported, at the time when they were put in force, by a vast majority in the national Parliament. All major parties were in favour of their enactment. No referendum was requested by 50,000 voters. The same holds true for the various revisions since then. Thus, (slightly) changing majorities in the national Parliament as well as the (slightly) varying composition of the Federal Council have not played a significant role in driving the agenda.

In order to further strengthen the efforts to remove remaining inter-cantonal barriers, the Federal Competition Authority has been called upon to play an active role in this context. The *Internal Market*

Act of 1995 mandated the Competition Authority to monitor the enforcement of the act. In so doing, the Competition Authority has established a special "Competence Centre for the Internal Market,"[12] While the Competition Authority first did not have standing in judicial proceedings on allegedly unnecessary market access restrictions, the revision of the *Internal Market Act* in 2006 introduced the right for the Competition Authority to file law suits with courts. It was considered necessary to have a public prosecutor as private parties normally refrain from bringing complaints under the act due to the political and financial costs and the difficulties linked to litigating against authorities upon which they depend for obtaining marketing approvals. This revision proved to enhance the effectiveness of the act. In fact, the Federal Competition Authority has actively challenged inter-cantonal trade barriers on various occasions, either as complainant or as intervener assisting a private party. In the future, it may be necessary to grant the Competition Authority an even more active role in prosecution.

Conclusions and Possible Lessons

The process of reducing trade barriers within Switzerland allows for a number of observations and lessons.

Effective removal of trade barriers required a liberal majority government in the nineteenth century. Little further progress was achieved after the large rainbow coalitions were installed upon the introduction of the referendum in 1874. Since 1912, when jurisdiction to adjudicate cases on freedom of commerce was transferred to the Federal Supreme Court, efforts declined as the courts preferred to protect federalism, and political parties had their main base, loyalty, and affiliation on the level of cantons, rather than the Confederation. Effective removal of trade barriers requires that the courts carefully balance prerogatives of federalism and market integration. It requires that the courts take into account the respective costs. History shows a lack of proper economic analysis and cost awareness. It shows that a proper theory addressing federalism, market integration, political and economic costs needs to be introduced in constitutional doctrine and theory and balanced with the benefits of decentralized governance. Thus, legal reasoning should seek to assess the financial costs of regulations to taxpayers, producers and consumers alike, and balance those with the advantages and

prerogatives of decentralized regulation. More profoundly, the question arises as to the proper role of the judicial branch in relation to the legislature. Swiss experience shows that legislation has been required to bring about liberalization and that the courts have followed suit.

Legislation has been very much a process of trial and error. Efforts to reduce barriers were initially met by resistance on the part of affected industries, be it in the case of the *Internal Market Act* or the field of competition policy. Once a first step was made, further revisions of the acts corrected past omissions that had come to light. Attitudes and perceptions changed. Removal of trade barriers therefore has very much been a process of gradual steps. The agenda cannot be set too widely at one point in time. Swiss experience shows that legislation can benefit with successive revisions, learning from past experience and changes of attitudes, in particular on the part of the cantons, industry associations and consumers.

Competition policy emerged as an important and interesting tool to liberalize inter-cantonal commerce in Switzerland. The Competition Authority was mandated to monitor the enforcement of the *Internal Market Act*. While it first did not have the right to file law suits with the Supreme Court, giving the Competition Authority standing has proved to enhance the effectiveness of the act. It is necessary to have a public prosecutor as private parties normally refrain from running the risk of litigation in the field. The *Competition Act*, finally, was instrumental in dismantling excessive monopoly rights in electricity that limited inter-cantonal commerce by private actors. It successfully substituted for legislation on the liberalization of electricity which, at the time, failed to pass by referendum.

External influences, through GATT/WTO law as well as the process of European integration, were critical in bringing about major progress in removing remaining barriers within Switzerland at the end of the twentieth century. Internal-market integration no longer can be separated from regional and global developments. Both call for efficiency and lower prices. Thus, progress has been made due to impacts from without, more often than from internal forces alone. This phenomenon is not limited to trade regulation. The constitutional framework and structures are subject to inherent and implied changes induced by changing patterns of international relations and interdependence. The distinctively Swiss patterns of direct democracy and federalism, which have often been brakes on integration,

may erode over time as matters are increasingly addressed in international agreements, be they multilateral or bilateral in nature (Cottier, 2007).

Today, the main challenge to be faced domestically is in the field of cantonal subsidies. There is a lack of transparency and of constitutional constraints by which distortions caused by subsidies could be properly assessed. Recent experience in disputes with the EU relating to tax rebates shows the cost of such shortcomings in external relations as well. Major obstacles also remain in the field of health services where federal legislation needs to liberalize the rights of patients to use health-care services in cantons other than those where they reside.

Some major barriers to mobility within the country reflect cultural differences and factors that cannot be properly addressed through traditional market-access tools. These factors are difficult to address by means of economic legislation and may decline due to structural and cultural changes in society. They result in reduced labour mobility, even though formal barriers may have been removed. This is particularly true in education, health care, and the media sector. Again, lessons may be learned from without: enhanced student exchange programs on all levels of education among different regions of the country can learn from European integration and its international programs (Erasmus and Socrates). Such programs could replace the experience Swiss formerly gained from joint training in the army, which encouraged mutual understanding and cohesion among the different regions.

The economic importance of contemporary inter-cantonal trade barriers in goods and services should not be overstated. Overall, Switzerland was able to prosper even with regulatory competition in many fields and despite the existence of inter-cantonal trade restrictions. Overall, in international comparisons, it is regularly considered to be one of the most competitive countries and economies. The philosophy of decentralization has proved to work well, leaving people and groups to address their own destiny in a local context. It resulted in a culture of respect for the law, based upon self-determination. The economic price is felt worth paying, as long as the country is prospering. With the emphasis on international trade and exchanges, the removal of remaining barriers no longer seems to be of vital importance compared to the days when extensive and frequent tariffs induced foreign commerce to avoid the country in the first place. It would seem to amount to an effort of diminishing returns.

While initial steps in the nineteenth century were of crucial importance, and most of the twentieth century amounts to an opportunity missed, welfare gains from liberalization in the twenty-first century will mainly stem from international liberalization of market access and appropriate regulation of trade in goods and services, both in Europe and worldwide.

Some enduring barriers may be partly inherent to Swiss federalism and the price to pay for decentralized governance and local autonomy in cantons and communes. They cannot be successfully addressed on the basis of the current constitutional framework and existing legislation or by inter-cantonal co-operation. Curbing costs of remaining market barriers would entail, in our view, significant harmonization and coordination by the federal government. Partly, it would entail new constitutional powers, which a majority of the people and the cantons may be willing to grant only in times of economic crisis and penury. Further harmonization of taxation, enhanced disciplines on subsidies, or common and uniform rules on government procurement throughout the country challenge the traditional fabric of Swiss society and its constitutional traditions. It shows the need to develop a set of factors both relating to economic efficiency and to self-determination within federal structures based upon which an objective assessment can be made.

It is more likely that these barriers will be removed by efforts and forces from outside, in particular from the process of European integration, but also by new disciplines emerging in WTO law. As much as traditional barriers to services were addressed only upon the impulse to keep pace with evolution in the EU and the WTO, the same may happen in the future once these modern barriers are effectively addressed in international and European law. Just as Switzerland has been unable to liberalize agricultural trade in recent decades for reasons closely related to its structures and traditions, so is it unlikely that addressing these modern internal barriers can be resolved without external pressure.

Notes

1. See the *Internal Market Act*, Chapter D.
2. See Government Procurement Regulations, Chapter D.
3. See the accord and the ratification process in the cantons http://www.edk.ch/dyn/11737.php and Chapter D.

4. See the inter-cantonal concordat on government procurement, Chapter D.
5. See the *HarmoS* project, Chapter C.
6. The *Cassis-de-Dijon* principle was first introduced by the ECJ, based on Articles 28 and 30 of the "EC Treaty" ("Prohibition of Quantitative Restrictions between Member States"), in its groundbreaking judgement on the prohibition by the German authorities to import *Cassis de Dijon* liquor into Germany of February 20, 1979 (C-120/78, *REWE Zentral AG vs. Bundesmonopolverwaltung für Branntwein*, ECR 1979 649).
7. See the role of the Competition Authority in prosecuting cases, Chapter D.
8. This holds equally true with respect to harmonization which has been achieved bilaterally with the EU (mutual recognition of conformity tests), as the federal power to conclude international treaties prevails over existing Cantonal competences in a domestic context, see Chapter B.
9. See http://www.weko.admin.ch and the link to the evaluation of the *Cartel Act*.
10. See http://www.news.admin.ch/message/index.html?lang=de&msg-id=34047 and the link to the proposed legislative changes, including an explanatory text.
11. See http://www.bbl.admin.ch and the link to the revision of public procurement laws.
12. See http://www.weko.admin.ch and the link to the secretariat. The duties of the Competence Centre for the Internal Market include i) conduct of investigations; ii) preparation of the Competition Authority's opinions and recommendations; iii) representation of the Competition Authority on the Federal Procurement Commission; and iv) responding to questions on the *Internal Market Act* from the public sector (in particular cantons and communes) and the private sector.

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