

**The Taxing Powers of Subnational Governments:
and the Role of Own Taxes in Italy:
Issues and Perspective**

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**BUNDESMINISTERIUM FÜR FINANZEN-OECD MEETING ON
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1 Introduction

The aim of this paper is to discuss main issues of fiscal federalism and tax decentralization in Italy; in particular, the allocation of taxing powers to subnational level of governments, the use in last ten years of these powers, the current structure of own taxes, and whether some changes might be desirable in the next future to increase the accountability, visibility and efficiency of the activities of the subcentral level of governments.

First of all, we briefly review the traditional model of tax assignment in standard public economics. We start from the traditional Musgravian distinction of the three functions of government and the accordingly allocation of possible taxes to the various levels of governments, to end with the caution we have to use when we try to carry out the traditional theory of fiscal federalism in most of OECD countries – in particular, the traditional approach should be broadened by dealing with new issues in fiscal federalism, such as the distribution of risk, the political economy and the equity effects of different architectures. In the third paragraph we address the main trends and forces acting in the Italian experience of decentralization. We briefly discuss the institutional background and then we analyse the allocation of spending, functions and financing in the framework of the Italian fiscal federalism. In the fourth paragraph, we concentrate on the main characteristics of the taxing power of SCGs in Italy. We describe the main regional and municipal own taxes, their quantitative and economic weight, and we make a tentative balance of the degree of tax autonomy of the Italian sub-national governments. In paragraph five, we ask whether Italian sub-central governments do really make use of taxing power assigned to them: we show that, on the whole, SCGs largely use their power and in many cases set the rates of own taxes at higher allowable level. In the sixth paragraph, we deal with the existing main obstacles for sub-central governments to make additional use of their taxing power, and we briefly address how could them be removed. Finally, in the last paragraph, we overview the main issues and possible future challenges to the Italian fiscal federalism.

2 Models of Tax Assignment

2.1 The tax assignment issue

In the traditional model of tax assignment, the most productive taxes in terms of ability to supply high revenue are normally attributed to central government. This model was quite understandable and justified in the world of the last fifties years,

where fiscal decentralisation was not on the top of the agenda. In this phase, state intervention in the economy was essentially motivated by ideological and market failures motives. Most traditional public goods and services were supplied by central governments that therefore felt entitled to get the larger part of total tax revenue.

The development of the theory of fiscal federalism¹ has made clear the positive effects on efficiency and accountability that a multilevel system of government can engender on the different tiers of government. The spread of democracy, the end of the Cold War and global conflicts, among other factors, have tended to rise ethnic ambitions and local demand of populations. Regional and local communities have increased their ambition to develop autonomously different sets of policies, and in fact the increasing in preferences' heterogeneity have tend to augment the list of functions assigned to sub-national governments. But this development has occurred with a clear bias in the financing structure of decentralized governments: in a word, 'too much expenditure, too little revenue'. Taxes assigned to lower levels of government have proved to be largely inadequate in many OECD countries. This situation has led to give much relevance to fiscal transfers and mechanisms of resource equalisation across regions, which have tended to produce perverse incentive for sub-national governments in the management of public finances. The greater the role of fiscal transfers, the lesser the incentives to politicians to be responsible and accountable for the electors. Many subnational governments have therefore developed fiscal irresponsibility and budget imbalances, given that the central governments have ended to offset any financial excess. But if local politicians are not accountable for their decision, then the incentive to efficiency that should come from a decentralized form of government might not occur.

It is therefore clear that we need a new rationale in assigning the functions of government to lower level of governments, not only in terms of spending responsibilities but also in the distribution of taxing powers.

2.2 The traditional model of tax assignment

In a multilevel system of government, the starting point of the tax assignment issue is the well-known Richard Musgrave's (1983) "who should tax, where and what". The theory of fiscal federalism suggests a very clear distinction among the three main functions of government: stabilization, redistribution and allocation. The first

¹ See, for example, the seminal works of Musgrave (1959, 1969, 1973), Oates (1968, 1972), Oates (1977a, 1977b), Musgrave (1983).

two, given the spillover effects and externalities, are normally considered as better assigned to the central level of government, while allocation can be subdivided across the different levels of governments according to the criterion of coincidence between beneficiaries and taxpayers². The distinction between pure public goods and local public goods – or club goods, by Buchanan and Oates – makes very clear this argument. What matters is the spatial incidence of benefits: people who benefits from the supply of goods from a certain level of government should be the same on which the cost of financing is levied, i.e., the burden of the financing of goods supply, managed by a certain level of government, should be levied on the same people who will benefit from it. Functions such as national defence, security and justice have to be supplied by the central government while transports and cleaning services – just to make an example – can be assigned to lower levels of government.

However, this approach appeared suitable and ready-to-use for countries with a federal structure, where a federal government and a federal budget do exist. Moreover, the theory of fiscal federalism is per se static, in the sense that it can be quite helpful when the country is already federal from a legislative and constitutional point of view. Its use for example, in some unitary OECD countries, as well as in the EU setting, is much more problematic given that this theory cannot help in deciding the dynamic of different expenditures and taxes assignments at the different stage of its evolution. In general terms, when the process of decentralization is at stake, we need a much more flexible criterion, which might be useful as a guide in deciding the different assignments in the different stages of the nation evolution. Last but not least, some political economy issues has to be added and considered in the theoretical approach.

The typical solution given to Musgrave's questions comes, for example, from the distinction of the benefit principle as compared to the ability to pay principle. According to Oates (1999)³:

- a) lower levels of government should, as much as possible, rely on benefit taxation of mobile economic units, including households and mobile factors of production;
- b) to the extent that non-benefit taxes need to be employed on mobile economic units, perhaps for redistributive purposes, this should be done at higher levels of governments;

² The MacDougall Report (1977) has been a very important step in the history of EU fiscal federalism construction.

³ See also Bird (1989, 1999) from which we took some of the following distinctions.

c) to the extent that local governments make use of non benefit taxes, they should employ them on bases that are relatively immobile across local jurisdictions.

Olson (1968) stressed instead the importance of the ‘principle of fiscal equivalence’ to strongly link expenditures to taxes in order to give rise to a greater degree of fiscal responsibility. Most of the discussion underlines the importance of having, if not earmarked taxes, source of revenue tightly linked with the benefits of expenditure.

Summarising the different position both in academia and political circles⁴, the natural candidates for the local levels of governments seem to be taxes which essentially insist on relatively immobile bases – for example property taxes – and where the base is relatively uniformly distributed – for example consumption taxes such as VAT and some forms of excises, much less taxes such as those on personal incomes and corporation.

Levies on users in form of charges and tariffs have traditionally been another good source of revenue for local governments, being inspired to the benefit principle. Other important taxes, such as the income tax and the corporate tax have usually been considered as a preferable source of revenue for central governments – see box 1 – even if many federal and unitary countries make a large use and rely on these taxes.

4 See for example, McLure (1983), Musgrave (1983), Oates (1999, 2002, 2005), McLure (1993, 2000, 2001, 2005) and Bird (1989).

Box 1
The Traditional Model of Tax Assignment

Levels of Government	Kind of Taxes
Central	Corporate income tax, Income and progressive tax, Tax on natural resources,
Intermediate (states, provinces, etc.)	Some form of sales tax, charges, but also income tax
Local	Property tax, Charges, User fees, etc.

2.3 Tax Assignment in an Era of Globalization and Decentralization: A New Look at Tax Assignment

The old model of tax assignment should be reviewed. The process of competences and expenditures decentralization towards the intermediate, regional and provincial, levels of government highlights how much the old principles appear inadequate in some sense to the new situation in various countries. For example, it is now clear that VAT or other form of levies on specific consumption can be an optimal source of revenue not only for central governments – state or federations – but also for the intermediate ones – regions, provinces, etc.⁵

The need to find new additional, stable and consistent source of tax revenue comes also from the fact that the “own revenues” of intermediate levels of governments have so far proved to be largely insufficient to finance the expenditure needs. As perfectly stated by Bird (1993, 1999, p. 6) “the resulting *vertical fiscal imbalance* is in practice almost invariably resolved by transfers. Unsurprisingly, much of the effort and ingenuity economists have devoted to intergovernmental fiscal affairs in recent decades has thus been spent on designing ever newer and better transfers”.

⁵ There is here a strange puzzle. The old federal countries have always used, in some sort, many possible forms of consumption taxes for the subcentral levels of government. The experiences of USA, Canada, Australia but also India and Brazil, show that this type of taxes can be a good and an important source of revenue for the lower tiers of government. Within the EU there is instead a bias against these type of taxes.

We should instead wonder why, *surprisingly*, economists have dedicated so much time to transfers and much, much less to find new and adequate form of revenue for the intermediate levels of governments. The new European context, the new dimension of decentralization and fiscal federalism in many unitary states, the decline of the myth of progressive taxes, all call for a new look at principles of tax assignment⁶.

⁶ See on this, Bird (1999), McLure (2001).

3. Main trends and forces acting in the Italian experience of decentralization

3.1 The institutional background and the historical records

It is useful to start by recalling the main steps of the Italian decentralization process in the last 30 years in favor of Regions and local governments.

- a) First, we have in 1972 the decrees where the initial transfer of functions from the central government to regions has been envisaged and realized;
- b) After that, we have to mention the D.P.R. 616 of 1977 where some administrative functions were devolved to regions;
- c) A crucial keystone was the 1978 Law no.833 which created the National Health Service on a regional dimension;
- d) Finally, we have the Law no. 59 of 1997 which envisaged the administrative decentralization of many competence to regions (the "Bassanini Law", that entered into force only from 2000).

By considering the total government expenditure, net of the interests expenses on the public debt and pensions expenditure, we have that in 2005 Regions manage 29.5% of total consolidated expenditure. If we consider also the 22.9% of the total expenditure managed by local governments, the degree of expenditure decentralization on the whole in Italy is currently at 52.4% – see graph 1 – of total government expenditure, a substantial percentage especially if it is compared to the 44.1% of 1996 – if we consider the spending for interests and pensions, this level reduces to 30%.

The degree of decentralization of public spending will progressively be increasing, as a consequence of the recent changes of the Constitution introduced with the Constitutional Law no.3 of 2001. Among the main innovations, especially three are worth mentioning:

- a) changes to article 117 of the Constitution which modify the allocation of legislative powers between the central government and regions: on one side, we have powers and competences under the exclusive responsibility of the central government (exclusive State competences); on the other, we have those under the legislative competition (concurrent competences) between the central government and regions; finally, all those not listed as exclusive State competencies or concurrent competences are attributed to the exclusive legislative power of regions;

- b) changes to article 118 of the Constitution which introduce the subsidiarity principle, according to which all functions are exerted by municipalities, being preserved the possibility to confer them to higher levels of governments (provinces, regions, central state), so to guarantee the uniform implementation of spending functions across the national territory;
- c) changes to article 119 of the Constitution which relate to the financing of sub-central governments and introduce the possibility for lower levels of government to establish and levy local own taxes and other own revenues in conformity with the Constitution and with the coordination of the national public finance and of the tax system. In addition, sub-national governments should have an amount of unconditional revenues such as own taxes or transfers – either in the form of a tax sharing on state revenues or of an equalization transfers – sufficient to finance the decentralized spending functions. It will be possible to introduce specific and conditional grants only in favor of certain sub-central governments and in order to achieve specific objectives, which are explicitly mentioned in the same article of the Constitution.⁷

3.2 The allocation of functions

In graph 2 we have shown the different share of public expenditure according to the different levels of government and the various economic functions.

On one hand, we have certain sectors – like defense, education, industry and social welfare – where the role of central government is still preponderant, on the other, we have some functions for which subcentral governments play a key role in the management of expenditure but also in decision making, such as health, transports, tourism and agriculture, road, territory. It has to be noted that the highest degree of decentralization is achieved in public health spending: health spending of the central government amounts to a limited 5% of total health outlays⁸.

Graphs 3 and 4 consider, respectively, the local and regional budgets and show the percentage distribution of the total expenditure by functions.

In Provinces' and Municipalities' budgets, the most important functions in terms of share of total outlays are: general administration, (mainly remunerations of public employees), territory (community amenities and environmental protection – with a

⁷ We have discussed these issues in Buglione (2006) and Buglione-Marè (2003).

⁸ In the education sector, compensations of employees are still paid by the central government with the only exception of some special regions.

high quota allocated to waste management), roads, public assistance and public transports. Public education represents also an important sector in which local governments show relatively high shares of budget spending, mainly devoted to the maintenance of schools, to new investments and to the payments of non-teaching staff.

Social and health sectors represent the main spending functions in regional balance sheets, with a share on total outlays near to 80%. Health care spending is managed at the regional level through the Local Health Authorities with the specific aim to guarantee over the national territory the essential levels of treatment (national standards), which are determined by the central government in close cooperation with regions.

3.3 Financing

During the 90s, Italy has experienced a significant process of tax decentralization towards regions and local governments. The key steps of this process are the following:

- in 1992, the tax on vehicles has been fully regionalized;
- in 1993, Central Government decided the setting up of the communal tax on dwellings, housing and real estate (ICI);
- in 1996, in the same way, a Regional business tax (IRAP) and a regional surcharge on the central government income tax (*addizionale regionale Irpef-RSIRPEF*) have been introduced;
- from 1999, the possibility to introduce a surcharge on the central government income tax (*addizionale comunale IRPEF-MSIRPEF*) has been attributed to Communes;
- in 2002, the tax sharing to the revenue of the central income tax has been provided to Communes (*compartecipazione al gettito Irpef*).

This process has given rise to a significant increase in the tax revenue of the SCGs. In 1996, the share of SCGs' tax revenue was only the 12% of the total national tax revenue (net of social security contributions), while in 2001 this share raised to 20.2% and in 2005 to 22.4% (Graph 5).

At this time, the tax revenue is approximately equal to 50% of the total current revenue of Regions and to 45% of that of Communes, which can also rely on other significant own sources of revenue different from taxation, such as charges, the sale of goods and services, fines and sanctions.

It should be emphasized that the process of tax decentralization implemented in Italy has essentially entailed the attribution of own taxes to the SCGs, own taxes in the sense that at least the tax rate can be chosen by SCGs, also if in a range fixed by CG. Hence, in this period the weight of the revenue from taxes has increased, as well as the tax autonomy of the SCGs. If we appraise the degree of tax autonomy as the ratio between the revenue from own taxes and the total current revenue, at present this is nearly equal to 40%, both for ordinary Regions and local governments. This value is much lower, around 18% for Special Regions, since for them most of the tax revenue comes not from own taxes but from tax sharing to national taxes (income tax, VAT, etc.) (Graph 6).

4 Main characteristics of the taxing power of SCGs in Italy

4.1 What are the regional and municipal main own taxes

We will concentrate on ordinary Regions and Municipalities, the most important levels of sub-national authorities, at least in terms of resources managed. We will focus on the main own taxes of regions and communes.

For the regions, the main own taxes are:

- The regional tax on productive activities (Irap) (73,8% of total tax revenue)
- The regional surcharge on the Central Government Income Tax (RSIrpéf) (14,5%)
- The regional tax on vehicles (RTV) (9,2%).

As Table 1 demonstrates, these taxes are responsible of 97.5% of the total own tax revenue of all the regions, and the situation is not significantly different between ordinary and special regions. Moreover these taxes provide 35.3% of total current revenue. This percentage rises to 42.2, if only the ordinary regions are considered (in special regions, given the importance of shared taxes, the revenue of own taxes is only 14.4% of total current revenue).

With respect to IRAP, it has to be noted that it is a tax on business – mainly, firms and companies – and on Public Administrations – in this last case, the tax is based on wages paid to employees⁹. There is therefore a private IRAP and a public one. Relating to the private component of IRAP, a few remarks can be done on its merits and drawbacks:

- Given the huge tax base – roughly, the total value added net of depreciation and some other small minor items – this tax can provide a very significant tax revenue with a relative small rate;
- the compliance of the tax is quite simple and not costly;
- it does not foster accountability, being paid at a first stage only by firms and companies, as well as by individual taxpayers running a productive activity on a permanent basis, hence by a limited number of residents and voters;
- by taxing the remuneration of the production factors (profits, as well as interests and wages), it produces a procyclical revenue, with adverse effects in downturns;

⁹ The definition of value added used in the case of IRAP is that of the income-type, not the consumption-type such that used with VAT.

- the regional distribution of revenue is highly uneven, requiring large financial transfers in favor of less developed regions to restore equity;
- it presents difficulties in the regional definition of its revenue, when it refers to firms with operating plants located in different regions of the country.

With the public component of IRAP, the main problem is that this is a central government tax on which regions have no real taxing power (the fixed tax rate is the same for all regions). Hence, it should be considered as a form of tax sharing rather than a genuine own local tax. For Southern regions – where the public component has the highest share (with peaks over 40% in some cases) – this represents a significant reduction in their taxing power.

As regards the regional surcharge on the central government income tax (RSIrpef), the main difficulty relies on the fact that the tax base is the same as that of the central government Irpef. Hence, regional revenues will vary – positively, or negatively – according to changes of the tax base as introduced by the central government. Moreover, the additional tax creates inequalities between individuals with income levels lower than the minimum taxable threshold and individuals with income levels immediately higher than the minimum: the former are exempted from the additional tax while the latter are taxed on the overall tax base. Finally, the different rates set by Regions inevitably end to interfere with the scale of progressivity of the central personal income tax, creating problems, spillovers and negative undesired effects.

For the communes, the main own taxes are:

- The municipal property tax (ICI) (61,6% of total own tax revenue)¹⁰
- The Municipal Surcharge on the Central government Income Tax (MSIrpef) (8,5%).

As Table 2 demonstrates, these taxes, for all the communes, are responsible of 70.2% of the total own taxes revenue.

The incidence on total current revenue is instead not very high (26.5%), but this is mainly due to the importance, in the communal budgets, of the revenue coming

¹⁰ In May 2008, the Italian Government has decided to abolish this tax on the owner and occupants of the ‘first house’, while leaving it unchanged on secondary house and luxury residences.

from the tax sharing to Irpef and from other own sources of revenue, as fines and sanctions (most of all on vehicles!), and tariffs on services.

Despite the fact that the property tax is recognized, also from a theoretical perspective, as being the most adequate local tax, it has to be noted that in Italy there exist other taxes on housing levied by the central government, some referring to the value of the house itself, others referred to the transfer of property. This contributes to increase the overall tax burden related to housing properties.

The municipal additional tax on IRPEF, is structured on the model of the regional additional on the central personal income tax and for which the same considerations and drawbacks apply.

Another important municipal tax relies on waste management. The amount to pay is strictly linked to the real estate ownership or house renting and for this reason it can turn out to be regressive. According to the existing laws, this tax should be transformed in a charge paid on the basis of the amount of waste produced. Until now, this transformation has not been completely implemented, but in any case, it should be considered as a tariff, given that the tax revenue cannot exceed the cost of the service, and that in many cases it is paid out directly to the firms which manage the service.

4.2 Tax autonomy of sub-national governments

The range of powers attributed to SCGs on the taxes we have mentioned is summarised in table 3, where we have considered the following elements:

- 1) The **possibility, for SCGs, not to levy the tax.** First of all, this is true for the municipal surcharge on Irpef (MSIrpef). Others SCGs optional taxes are the municipal earmarked tax for public works (introduced by CG in 2007) and the regional tax on gasoline (RTG, max. 0,025 euro/litre). Until now, the RTG has been introduced by 4 regions and the earmarked tax for public works by less of 20 communes. For this reason and also because the tax revenue is very limited they are not considered in this paper.
- 2) The possibility to choose the tax rate: it is the basic element for a tax to be considered “own” and it is always present. The choice can always be done within a range (min. and max.) fixed by CG. The only exception is for the regional tax on vehicles: indeed, a 10% raise of the tax rate could be replicated each year.

3) The possibility to vary the tax rate for specific categories of taxpayers (or tax bases, in the case of ICI and RTV). This is true for all the taxes here considered, included the MSIRPEF according to the new rules introduced by CG in 2007. For example, many regions apply Irap at the minimum tax rate (3.25%) just for some entrepreneurial activities (managed by women, by youths, or for virtuous firms).

For the purpose of evaluating the degree of taxing powers and autonomy of the SCGs, it is also important to stress that:

- with the only exception of the surcharge on Income Tax (regional and communal), SCGs can always decide on many aspects of the management of the taxes (i.e., tax compliance, collection, etc.);
- all the mentioned regional and communal own taxes are disciplined in general terms by CG laws. These laws can always be modified autonomously by the CG. For example, this has occurred in the last years for Irap and Ici. CG, at least in theory, can also abolish some of these taxes, of course providing SCGs with an equivalent amount of revenue¹¹;
- CG can oblige SCGs with budget deficits to apply the mentioned regional and municipal taxes at the maximum rate. At present, this is true for 4 regions with relevant budget deficit in the health sector.

¹¹ This is what should happen with the ICI abolition on 'first house' just decided.

5 Do Italian sub-central governments make use of taxing power assigned to them?

The answer is definitely affirmative. For the Regions – graph 7– this is true for all the taxes here considered:

- for the Irap, 95% of the Regions (100% in the North and in the Centre) use their fiscal power. That means that the tax rate is almost always different from the ordinary one and that in many cases the tax rate is differentiated for specific categories of taxpayers. For example, 85.7% of the regions apply the minimum tax rate to promote special kind of firms (i.e. firms managed by youths or by women, or which are considered virtuous according to parameters fixed in regional laws). 47.6% give total exemption to the non profit sector.
- for the RSIrpef, 62% make use of their fiscal power, with negligible differences between North-Centre and South. This means that 57% apply tax rates higher than the ordinary one (62% in the South) and that 38% differentiate the tax rate according to the taxpayer's revenue (54% in the North).
- Finally, more than 40% of regions apply the RTV using a tax rate higher than the ordinary one. Moreover, many regions are planning to introduce or have introduced special facilities for vehicles considered less pollutant.

Also the communes appear very in favour of using their fiscal power:

- for the ICI, which has been introduced by CG in 1993, almost all of them apply tax rates higher than the ordinary one and have introduced facilities for specific types of housing and properties or taxpayers (i.e., according to the revenue or the family composition). In fact, the situation it is so differentiated that is practically impossible to give general data.
- For the MSIrpef, it is important to stress the percentage of communes which levy this “optional” tax, introduced by CG in 1999. Among the 7,469 communes considered by the Ministry of Interior¹², 72% now apply the tax (almost 80% in the North-Centre) and also in 2002 the tax was very widespread (graph 8).

It is also interesting to consider the level of the tax rate chosen by communes for the MSIrpef. As graph 9 demonstrates, in 2006 less than 10% have adopted a very

¹² The total number of Communes is around 8.100.

low tax rate (less than 0.2%) and 29% the maximum tax rate possible in this year. As we have said, from 2007 it is possible to apply a tax rate of 0.8%, and some communes have already made use of this possibility (for example, the town of Trieste). From 2007, it also possible to differentiate the tax rate according to the level of taxpayers revenue and the data of the Ministry of Economy show that 678 communes have already made use of this power.

6 What are the main obstacles for sub-central governments to make more use of their taxing power and how could they be removed?

The main obstacles for sub-central governments to make more use of their taxing power are:

- According to the present Constitution, the CG has to promulgate a law for coordinating the fundamental principles of the vertical fiscal system. Given that this law has not been still promulgated, SCGs have no the possibility to introduce and discipline new SCGs taxes, as provided for in art. 119 of the Constitution;
- The too limited range of manoeuvrability according to the CG laws which rule the present SCGs taxes, perhaps with the exception of ICI;
- the CG desire to reduce the national (overall) fiscal pressure, starting from SCGs taxes, some of which are considered very unpopular.

The first obstacle seems to be very important. The experience demonstrates that if CG adopted the law for the coordination of the general fiscal system, SCGs would be prone to introduce new taxes. In fact, some of the special regions, which already have this possibility, given their special autonomy, have introduced new taxes in the last years (for example, taxes on tourism, on second houses, etc.). Anyway, we also think that this might reveal as a ‘minefield’ for the Italian fiscal federalism and the process of tax decentralization, since an excessive proliferation of new SCGs taxes could have serious negative effects on the overall efficiency of the fiscal system, be harmful for taxpayers and economic growth and perhaps be incompatible with the EU tax rules.

The second obstacle seems also very important. Of course, the present range of manoeuvrability could be extended but this would require a simultaneous reduction of CG taxes and expenditures which is very difficult to implement. Otherwise, the consequence would be a rise of the overall national fiscal pressure, already one of the highest in Europe, with the obvious undesired effects in term of incentives, growth and evasion.

Finally, the relatively high level of the fiscal pressure existing in Italy and the difficulties to reduce CG expenditures explain the last obstacle for a larger use of SCGs fiscal power. Given the political relevance of a reduction of the total tax pressure, last Central governments have indeed introduced severe limitations on

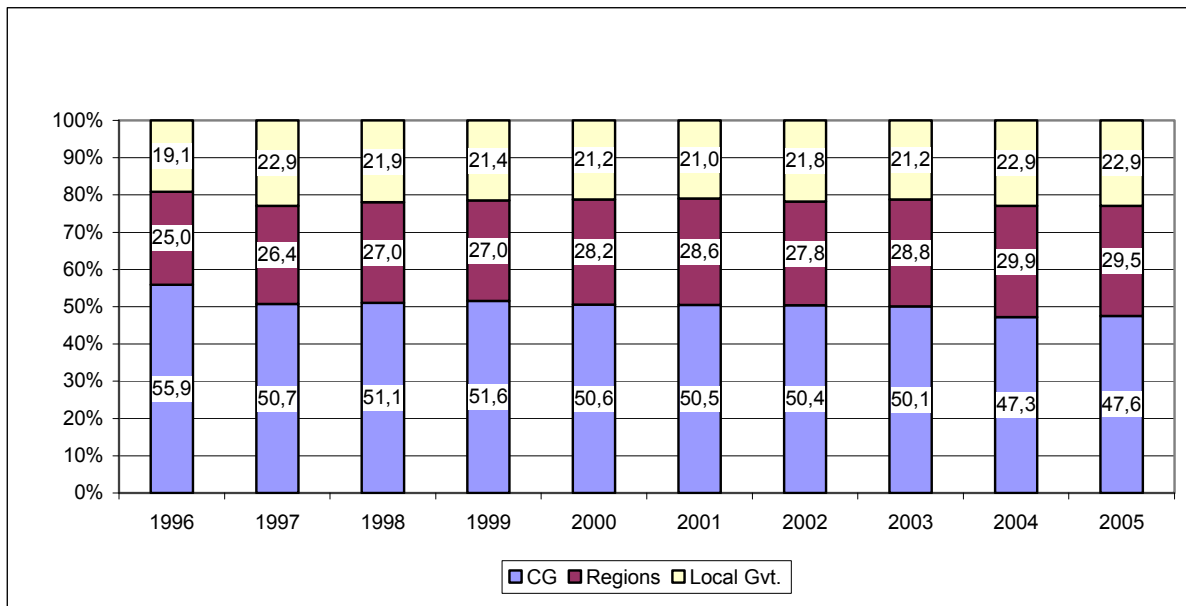
the SCGs tax powers: the more recent ones are the reduction of the Irap tax base and general rate; the reduction of the communal property tax rates for some low income taxpayers. Of course, these limitations would produce a reduction of SCGs tax revenue, reduction that must have to be compensated by larger CG transfers.

7 Main issues and conclusions

In our view, in reforming the Italian fiscal federalism the following are the most important goals:

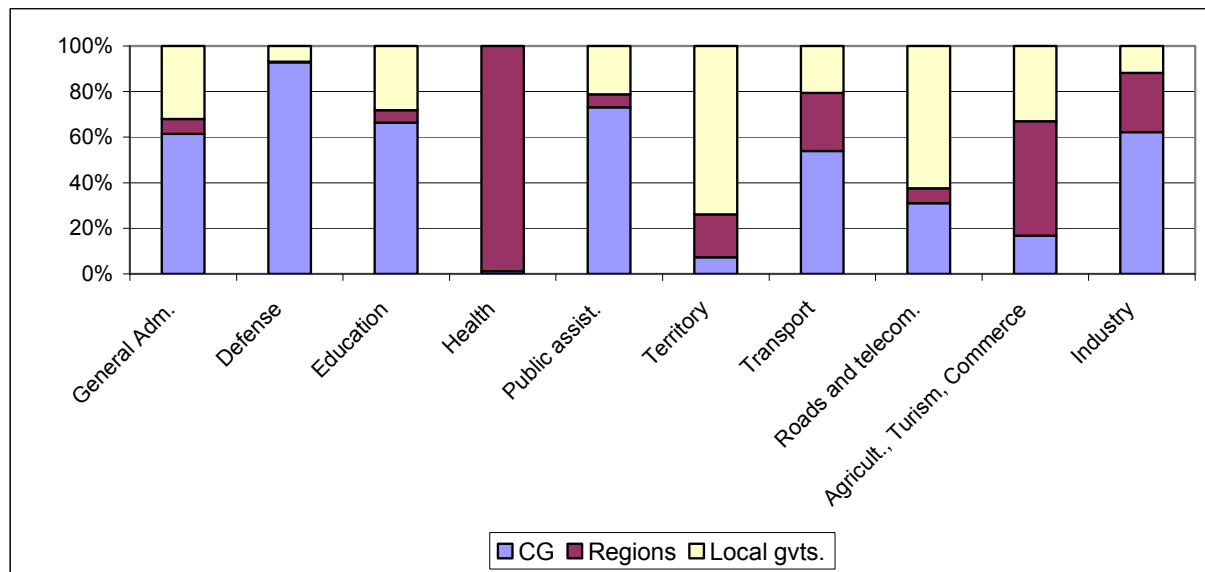
- a) if fiscal federalism has to promote efficiency and accountability, then fiscal and tax decentralization has to be strengthened;
- b) taxes with lowest per capita revenue disparities amongst the various areas of the country should be preferred, so as to reduce the scope of equalization transfers necessary to bear and finance the expenditures of SCGs with lower fiscal capacity;
- c) to improve the evaluation system of standard fiscal capacity (national and for the single SCGs) and objective costs of SCGs' specific public services provision, by adopting methodologies specifically tailored for each levels of government and previously agreed with the bodies representing such governments;
- d) on the basis of the standard self-financing capacity of each SCG, to guarantee the coverage of a uniform quota of the cost of public services provision (lower than the total cost) for all SCGs. This should occur through tax-sharing and equalization transfers for lower fiscal capacity SCGs. Such measures would encourage efficiency and adequate exploitation of taxable bases;
- e) to reward the tax effort accomplished by SCGs with lower fiscal capacity, providing for higher equalization transfers in favor of these SCGs whereby tax burden is increased above standard levels.

Graph 1 - Total final public expenditure by level of government



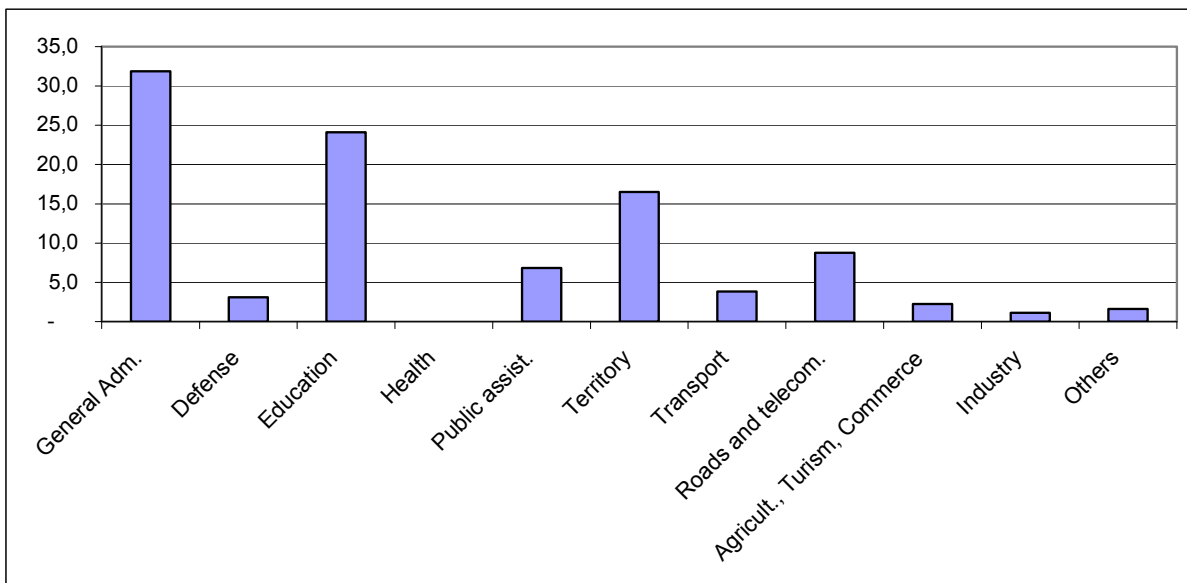
Source: based on data of Ministry of Economy - Dpt. for development policies

Graph 2 - Total final public expenditure by function and by level of gvt - Year 2005



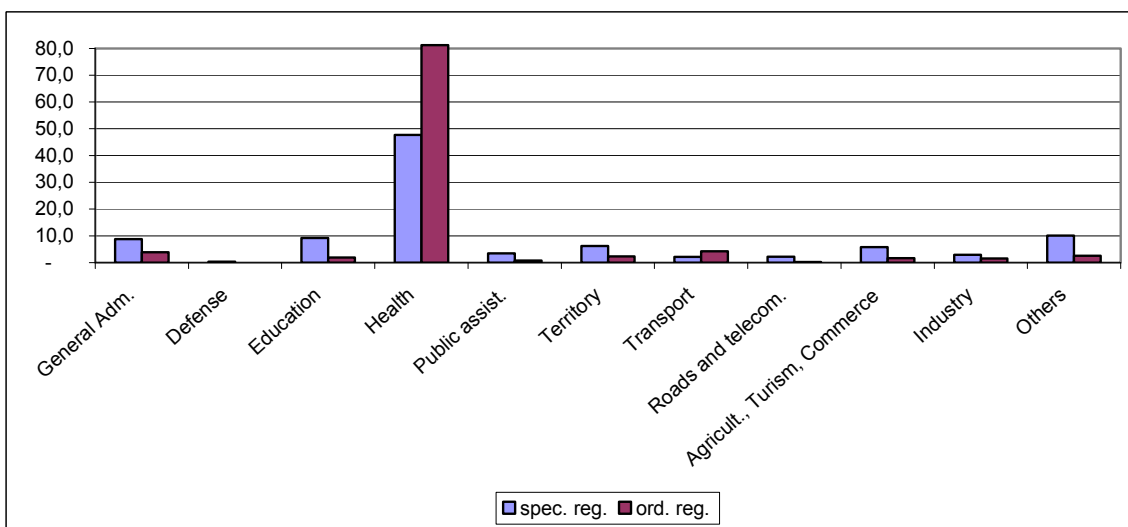
Source: based on data of Ministry of Economy - Dpt. for development policies

Graph 3 - Total expenditure of Local Govt. by function (%) - Year 2005



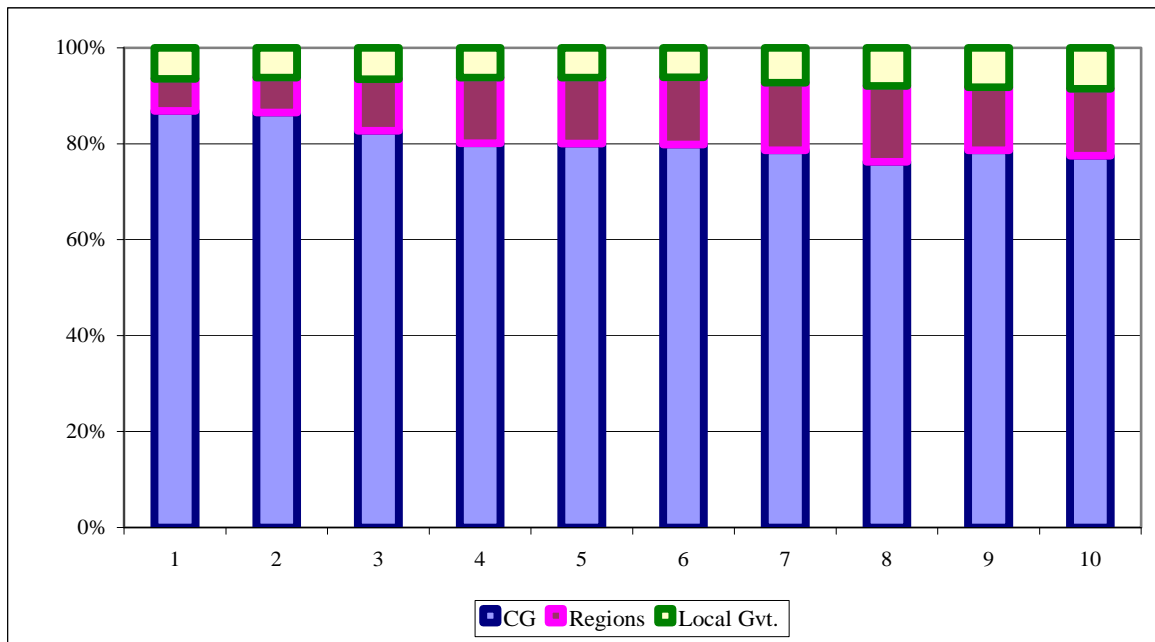
Source: based on data of Ministry of Economy - Dpt. for development policies

Graph 4 - Total expenditure of Regions by function (%) - Year 2005



Source: based on data of Ministry of Economy - Dpt. for development policies

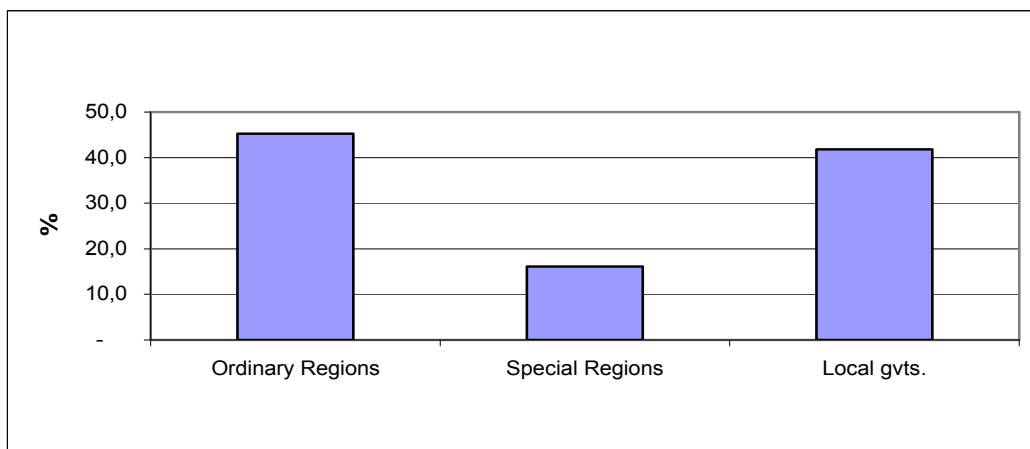
Graph 5 - Total fiscal revenue by level of government (1)



(1) Net of compulsory contributes

Source: based on data of Ministry of Economy - Dpt. for development policies

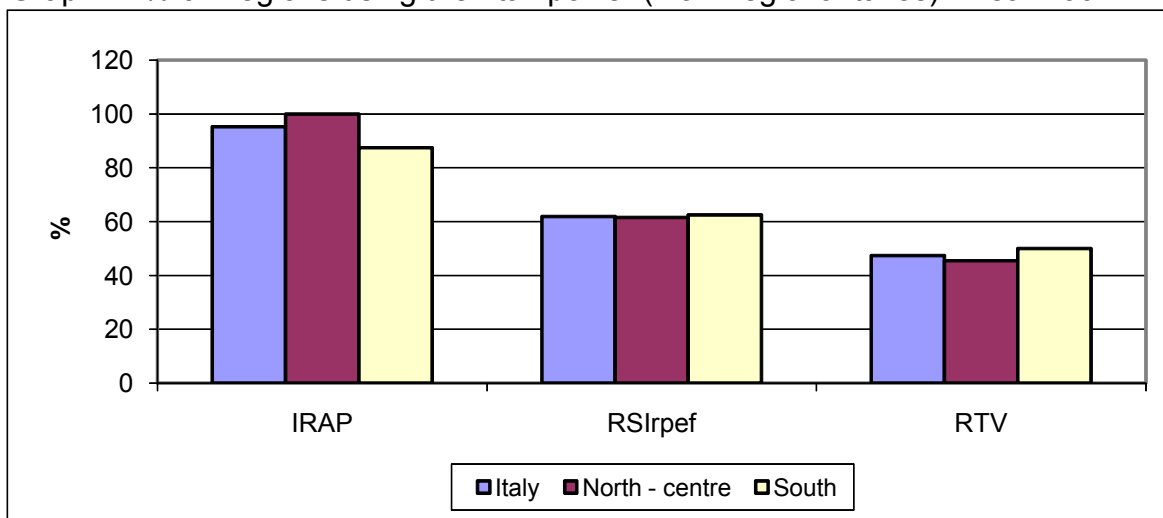
Graph - 6 Level of fiscal autonomy (1) for Ordinary Regions, Special Regions and Local Gvt. - year 2005



(1) Own tax revenue / total current revenue

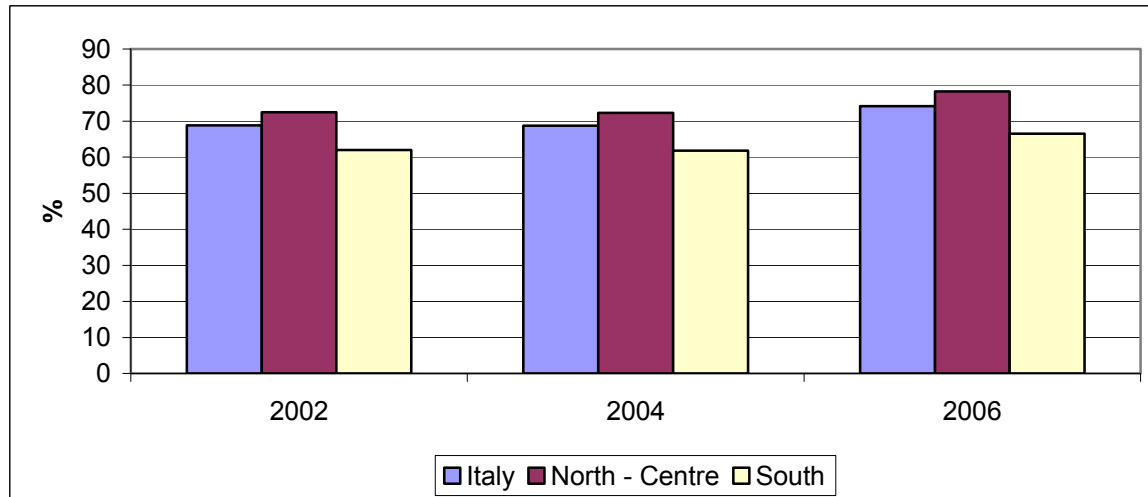
Source: based on data of Ministry of Economy - Dpt. for development policies and on data Issirfa-cnr

Graph 7- % of Regions using their tax power (main regional taxes) - Year 2007



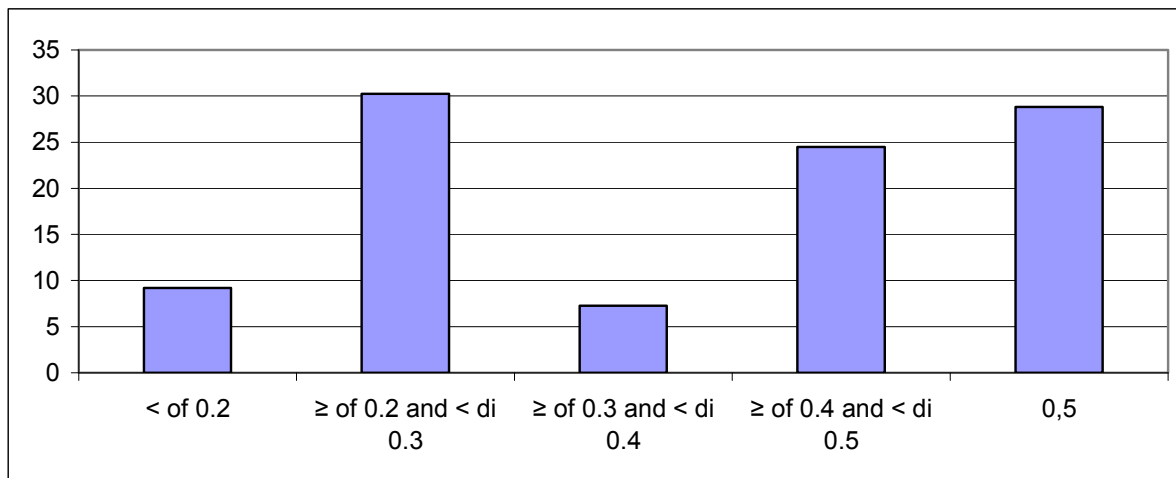
Source: based on data of Corte dei Conti, Relazione sulla gestione finanziaria delle regioni Roma 2007

Graph 8 - % of Communes which apply the MSIrpef - Years 2002, 2004, 2006



Source: Ministero dell'interno, Dipartimento per gli affari interni e territoriali, Relazione annuale sullo stato di attuazione della addizionale comunale all'Irpef

Graph 9 - Communes which apply the MSIrpef - % distribution by level of tax rate - year 2006



Source: Ministero dell'interno, Dipartimento per gli affari interni e territoriali, Relazione annuale sullo stato di attuazione della addizionale comunale all'Irpef

Table 1 - Regions' main own taxes

Own taxes	IRAP	RSIrpef	RTV	Total
All the Regions				
tax revenue 2006	35.645	6.998	4.449	47.092
% of total own tax revenue	73,8	14,5	9,2	97,5
% of total current revenue	26,7	5,2	3,3	35,3
Ordinary Regions				
tax revenue 2006	31.664	6.346	4.347	42.357
% of total own tax revenue	73,1	14,7	10,0	97,8
% of total current revenue	31,5	6,3	4,3	42,2
Special Regions				
tax revenue 2006	3.981	651	101	4.733
% of total own tax revenue	79,9	13,1	2,0	94,9
% of total current revenue	12,1	2,0	0,3	14,4

Source: based on data ISSIRFA-CNR

Table 2 - Main own taxes of Communes

Own taxes	ICI	MSIrpef	Total
All the Communes			
tax revenue 2005	11.736	1.619	13.355
% of total own tax revenue	61,6	8,5	70,2
% of total current revenue	23,3	3,2	26,5

Source: National Accounts

Table 3 - Range of taxing powers attributed to SCGs on principal own taxes

Range of powers	Regions			Communes	
	IRAP	RSIrpef	RTV	ICI	MSIrpef
Possibility not to levy the tax	no	no	no	no	Yes
Possibility to choose the tax rate (inside a range determined by CG)	yes	yes	yes	yes	yes
General tax rate at which the tax must be levied if SCGs do not choose a different one	4.25% of the value of the tax base (*)	0.9% of the value of the tax base	3 euro/Kw (**)	0.004% of the value of the tax base	-
Permitted range of tax rates	3.25% - 5.25%	up to 1.4%	up to 10% each year	up to 0.007%	up to 0.2% (of the value of the tax base) each year. Max 0.5% (***)
Possibility to vary the tax rate for specific categories of tax payers	yes	yes	yes	yes	no (****)
Possibility to decide some aspects of the tax management	yes	no	yes	yes	no
Possibility for CG to oblige SCGs with budget deficits to apply the tax at the maximum rate	yes	yes	yes	yes	Yes
Possibility for CG to change autonomously the discipline of the tax or to abolish the tax	yes	yes	yes	yes	Yes

(*) 3.90% from 2008. The range of rate variability will be +/- 1%.

(**) tax rate for cars in the pollution class euro 0, with no more than 100 kw

(***) From 2007, the upper limit is 0.8% and the 0,2% limit for the yearly increase has been abolished

(****) Yes from 2007

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