Università degli Studi di Bari
Dipartimento di Scienze Economiche e Metodi Matematici

Southern Europe Research in Economic Studies
S.E.R.I.E.S.

WORKING PAPER NO. 0038

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From transfers to tax “co-occupation”: the Italian reform of intergovernmental finance*

Ernesto Longobardi

Abstract

The paper provides some insights into the current reform of the system of intergovernmental relations in Italy. A most relevant change is the abolition of transfers from a higher level of government as an ordinary means of finance for sub-central governments, with the exception of grants having an explicit equalisation purpose. Since the room for autonomous local taxes is quite narrow, transfers are going to be substituted, to a large extent, by different forms of “co-occupation” of central taxes. Using the OECD taxonomy about tax autonomy, it is shown that the effective increase in “infra-marginal” tax autonomy of sub-central governments brought about by the reform will be quite modest. At the margin, however, where autonomy really matters, there could be enough room for the exercise of effective discretion. The main problem is that both the central and the sub-central governments fear the decentralisation of tax power. The former because it feels that, at least in the transitional period, the electorate might not properly distinguish the different fiscal responsibilities; the latter because they would prefer not to tax their electorate, notwithstanding their preferences for more stable and predictable sources of finance with respect to the current system.

Keywords: Intergovernmental finance, decentralisation, tax assignment, tax autonomy.

JEL Classification: H71, H77.

1. Introduction

Constitutionally Italy is still a unitary country, even if the amendment of 2001 has made the country resemble very closely a federal system, having granted to the intermediate level of government, the regions, some prerogatives that are typical of states in a federal contest[1]. Scholars in constitutional law (Bassanini, 2011; Fusaro, 2009) define today’s Italy as a regional or regionalised country, which is probably undergoing a process towards federalism, even if the ultimate outcome of such a process is still very difficult to predict. In 2009 an act has been approved establishing the framework of a deep reform of governmental fiscal relations and enabling the Government to implement it through a series of legislative decrees, which should be completed within the end of the year (2011). The reform is essentially characterised by two main innovations. The first one consists in the introduction of expenditure needs as the main criterion for financing sub-central governments (SCGs), in substitution of the current system, in which the actual amount of transfers depends, mainly, on the pattern inherited from the past. The second relevant change is given by the abolition of transfers from a higher level of government as an ordinary means of finance for SCGs, with the exception of grants having an explicit equalisation purpose. This modification was dictated by the constitutional reform of 2001, which has banned any form of derivative finance. The paper is mainly concerned with this latter aspect. Since the room for autonomous local taxes is quite narrow, transfers are going to be substituted, to a large extent, by different forms of “co-

* Paper presented at the OECD Seminar, *Taxonomy of Grants and Measurement of Decentralisation*, OECD, Paris, March 10-11, 2011.

[1] Bergvall et al. (2006) p. 20 include Italy among federal countries.

Università di Bari
Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

occupation" of central taxes. The term co-occupation, or cohabitation, is used here to indicate both tax-sharing arrangements and different systems of overlapping taxation (or "piggyback taxation").

This paper is organized as follows. In section 2 the current situation of intergovernmental financial relations in Italy is briefly described. The OECD taxonomy is discussed and used in order to measure effective tax autonomy at the regional, municipal and provincial level. In the following section the impact of the reform is considered. A main concern is to verify the success of the reform in decentralising effective tax power to SCGs. The third section offers some further elements for an evaluation of the new design of intergovernmental fiscal relations. The open question is whether the movement from transfers to tax co-occupation will actually enhance autonomy, accountability and responsibility of sub-central governments, which is the main declared objective of the reform.

2. The current system of intergovernmental fiscal relations

2.1 Some facts and figures

In Italy there are three tiers of government. The state at the centre, the regions at the intermediate level and two distinct entities at the local level: provinces and municipalities. The regions are 20. Immediately after the Second World War a special statute was guaranteed to five regions, conferring them a large institutional and financial autonomy. The provinces are 107, while the lowest entities, the municipalities, are 8,094, a very large number relatively to many other comparable countries. More than 70% of the municipalities have less than 5,000 habitants.

Table 1. Expenditure for levels of Government (2008)

	Millions of Euro	% of GDP
General Government		
Total	774,636	49.41%
net of interests payments	693,475	44.23%
Central Government		
total	430,484	27.46%
net of interests payments	354,249	22.59%
Local Government (1)		
total	244,615	15.60%
Net of interests payments	239,026	15.25%
Social Security		
Total	284,129	18.12%
Net of interests payments	283,800	18.10%
(1) Regions, Provinces, Municipalities		
Source: National Accounts		

Being Italy, formally, a unitary country, in national accounts regions are considered together with provinces and municipalities, their accounts being consolidated into the subsector local government. Table 1 shows the relative weight of local government in terms of

Università di Bari
Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

expenditure[2]. Given a total consolidated expenditure of general government close to half of GDP, the share of local government, which provides a measure of fiscal decentralisation (Bergvall et al. 2006), is 31.6 %. If considered net of interest payments, the share of local expenditure rises to 34.5%.

Considering the figures of the balance sheets of the three sub-central aggregates provides a closer insight into intergovernmental finance. This is done in tables from 2 to 10.

Table 2 and 3 consider separately the 15 regions with an ordinary statute (RSO) from the 5 with special statute (RSS).

Table 2 shows that in RSO the expenditure of the regions, which for more than 8/10 consists in expenditure for health care, is just twice that one of municipalities, while the role of provinces is quite modest. In RSS the role of regions relatively to local government is even stronger.

Table 2. Expenditure for levels of Local Government (2008)

	Millions of Euro	% of GDP
Regions with an ordinary statute (RSO)		
Regions	136,851	8.73%
Provinces	13,028	0.83%
Municipalities	67,765	4.32%
Regions with a special statute (RSS)		
Regions	42,872	2.73%
Provinces	1,926	0.12%
Municipalities	14,318	0.91%

Source: Balance Sheets (accrual basis)

Table 3 considers the revenue side of regions' balance sheets. It can be noticed that the percentage of tax revenue out of total revenue is very high both in ordinary (77%) and in special regions (82%). Hence, apparently, Italian regions benefit of huge tax autonomy. However, as it will be shown in the next paragraph, the effective power of ordinary regions over resources formally registered as tax revenue is much lower.

[2] All the figures presented in the paper refer to 2008.

Università di Bari
Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

Table 3. Regions: the total revenue (2008)		
	Millions of Euro	% of GDP
Regions with an ordinary statute (RSO)		
Tax revenue	97,693	76.90%
Transfers (from State and EU)	27,141	21.36%
Non-tax revenue	2,202	1.73%
Total	127,036	100.00%
Regions with a special statute (RSS)		
Tax revenue	32,005	81.63%
Transfers (from State and EU)	6,048	15.43%
Non-tax revenue	1,154	2.94%
Total	39,207	100.00%
Source: Balance Sheets (accrual basis)		

In Table 4 the tax revenue of ordinary regions is split into its main components. It can be seen that five items provide more than 96% of total revenue. The most important source of revenue is the regional share of VAT (47.45% of the regional tax revenue). However, as it will be argued below, the regional VAT sharing currently adopted in Italy is such just nominally, being, in fact, a transfer in all respects.

Table 4. Regions with an ordinary statute (RSO): the tax revenue (2008)		
	Millions of Euro	% of Total
Regional share of VAT revenue	46,359	47.45%
Regional Business Tax (IRAP)	34,185	34.99%
Regional tax rate on PIT (IRPEF) base	6,998	7.16%
Vehicle tax	5,171	5.29%
Regional share of the state excise on petrol	1,684	1.72%
Others Tax Revenue	3,296	3.37%
Source: Balance Sheets (accrual basis)		

The second source of revenue (34.99%) is a regional tax on business activity (IRAP). Introduced in 1998, the tax is levied on the value added, net of depreciation, both of market and non-market entities. The value added is calculated according to the "base form base" method, considering the balance sheet's values. In recent years the tax has been the object of a growing hostility from the taxpayers. In their view and perception, the tax is unfair and jeopardizing firms' profitability: because it must be paid independently of the existence and amount of profits, it may turn a profit in a loss and it compromises the capacity of marginal firms to stay in the market. Mainly as a consequence of public opinion's pressure, the abolition of IRAP has long been in the agenda of the government. In fact, by now, all political parties share the view that the tax should be repealed, or at least depleted through the exclusion of the labour income component from the tax base. The main obstacle to such a perspective is the importance of the tax as source of revenue and the difficulty in finding alternative tax resources for regions.

Università di Bari
Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

In a decreasing order of importance, the remaining three items of regional tax revenue are a regional surcharge levied on the personal income tax (IRPEF) base (7.16%), a tax on the possession of cars and other vehicles (5.29%), and a regional share of the State excise on petrol (1.72%).

The regional tax revenue composition will be considered again in more detail in the next paragraph, in order to evaluate the effective degree of autonomy and discretion recognised to ordinary regions by the current regime.

Tables 5, 6 and 7 refer to municipalities belonging to the ordinary regions[3]. Table 5 shows that the most important category of income at the municipal level still consist of transfers, received mainly from the State and the Region where the municipality is located, and in a smaller extent from EU and other entities. The tax revenue amounts to 28.6% of the total. A relevant share is provided by non-tax revenue (fees, user charges, profits from municipal enterprises etc.).

Table 5. Municipalities in RSO: the total revenue (2008)

	Millions of Euro	% of Total
Tax revenues	17,890	28.62%
Transfers	25,752	41.19%
Non-tax revenue	18,874	30.19%

Source: Balance Sheets (accrual basis)

Table 6 shows the importance of the two main sources of tax revenue at the municipal level. About a half of it is provided by a municipal property tax (ICI) levied on real estate. Since 2008 owner-occupied houses have been exempted. A municipal tax rate levied on the State PIT base, introduced in 1999, yields 14.14% of the total tax revenue.

Table 6. Municipalities in RSO: the tax revenue (2008)

	Millions of Euro	% of Total
Local property tax (ICI)	8,604	48.09%
Municipal tax rate on PIT (IRPEF) base	2,530	14.14%
Others Tax Revenue	6,756	37.76%

Source: Balance Sheets (accrual basis)

Table 7 gives the composition of transfers received by municipalities according to the donor (the State or the Region) and to the economic nature (current or capital account). Municipalities receive 70% of grants from the State: more than 90% of them are in current account. Instead, the 60% of grants received from the Region are in capital account.

[3] Their number is 6.704, corresponding to the 85.7% of the total.

Università di Bari
Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

Table 7. Municipalities in RSO: transfers from the State and the Region (2008)			
	Millions of Euro		
	From the State	From the Region	Total
In current account	12,861	2,429	15,290
In capital account	1,382	3,670	5,052
Total	14,243	6,099	20,342
Source: Balance Sheets (accrual basis)			

It can be mentioned here that generally transfers to local governments (municipalities and provinces) are mandatory, non-earmarked and general purpose when they are in current account; while, if in capital account, they are still mandatory but earmarked.[4]

Tables 8, 9 and 10 provide the same information as tables 5, 6 and 7 with reference to provinces belonging to RSO. In table 8 it can be seen that provinces are more dependent on transfers than municipalities (49% of total revenue against 41%).

Table 8. Provinces in RSO: the total revenue (2008)		
	Millions of Euro	% of Total
Tax revenues	4429	37.03%
Transfers	5859	48.98%
Non tax revenue	1673	13.99%
Source: Balance Sheets (accrual basis)		

Table 9 provides the composition of tax revenue. The two most important sources of tax revenue at the provincial level are two forms of vehicle taxation. The first is levied on the insurance policies covering car drivers from damages to third parties; the second is levied on the registration of the vehicle. The third provincial tax in order of yield is a surcharge on the state tax on electricity consumption.

Table 9. Provinces in RSO: the tax revenue (2008)		
	Millions of Euro	% of Total
Tax on cars' insurance	1,855	41.88%
Tax on cars' registration	1,073	24.23%
Surcharge on electricity tax	825	18.63%
Others Tax Revenue	676	15.26%
Source: Balance Sheets (accrual basis)		

Table 10 shows the composition of grants received by provinces. It can be seen that provinces, differently from municipalities, receive the far larger part of their grants from the Region and that the share of grants in capital account is much bigger than that one in current account.

[4] For the taxonomy of grants see OECD (2002), Blöchliger-King (2006), Bergvall et al. (2006).

Università di Bari
Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

Table 10. Provinces in RSO: transfers from the State and the Region (2008)			
	From the State	From the Region	Total
In current account	770	2,821	3,591
In capital account	323	1,528	1,851
Total	1,093	4,349	5,442
Source: Balance Sheets (accrual basis)			

2.2 Measuring tax autonomy at the sub-central level

OECD (1999 a), (1999 b), (2002) and Blöchliger-King (2006) have proposed an indicator for measuring the taxing power of SCGs. The indicator comprises 5 main categories of autonomy and 13 sub-categories. Categories are ranked in decreasing order in term of taxing power.

a. Category “a” represents full power over tax rate, tax allowances and tax credits: the category is split into two sub-categories according if the SCG is or is not obliged to consult a higher order of government when changing an element of the tax.
b. Category “b” represents the power to change the tax rate, without any limit (b.1) or within a range established by a higher order of government (b.2).[5]
c. Category “c” encompasses the power to modify the effective tax rate through both tax allowances and tax credits (c.1), only tax allowances (c.2), only tax credits (c.3)[6].
d. Category “d” includes 4 different arrangements of tax-sharing: d.1 when the SCGs determine the revenue split; d.2 when the revenue split can be changed only with the consent of SCGs; d.3 when the revenue split is determined in legislation and it may be changed unilaterally by a higher level government, but less frequently than once a year; d.4 when the revenue split is determined annually by a higher level government (usually as part of the annual budget process).
e. Category “e” includes all other cases in which the central government determines the all the parameters of the SCG tax.

It can be mentioned that, as far as tax-sharing arrangements are concerned (category d), the sub-category d.1 has resulted statistically not very meaningful: in OECD (1999 b) and (2002) surveys no country reported tax revenue under this item, while in Blöchliger-King (2006) just one country (Greece). More or less the same can be said for sub-category d.4.

Blöchliger-King (2006) and especially Blöchliger-Petzold (2009) have envisaged a different criterion for the scrutiny of tax-sharing arrangements, mainly directed to “draw a dividing line between tax-sharing and intergovernmental grants”.

Four test criteria have been established in order to identify tax-sharing (Blöchliger-Petzold, 2009, pp. 4-5):

1) *Risk sharing*: the amount of revenue allocated to the SCG must be strictly related to total tax revenue, so that the SCG fully bears the risk of tax revenue slack and fluctuations;

[5] Blöchliger and King (2006), p. 159 refer that category b includes essentially the “piggy-backing” type of tax. In fact, there could be cases in which SCGs are conferred an autonomous tax, but limiting their autonomy to tax rate changes, without giving the possibility of modifying the tax base or introducing tax credits. As it will be seen below this is, for example, the case of IRAP and other local taxes in Italy.

[6] The ranking of the “c” sub-categories as here been inverted respect to Blöchliger and King (2006), to stick at the criterion of a decreasing taxing power.

Università di Bari
Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

2) *Un-conditionality*: the SCG must be free in deciding how to use the revenue allocated, i.e. the revenues must be unconditional (non-earmarked);
3) *Formula stability*: the revenue share between the two levels of government involved must be predetermined in advance and not changed in the course of a fiscal year;
4) *Individual proportionality*: the revenue share of each SCG must be strictly related to what it generates on its own territory, i.e. there must be no horizontal redistribution or fiscal equalisation across SCGs.

Any arrangement classified under category "d" in the OECD tax autonomy classification and any intergovernmental grant can be put through the test and ri-classified as:

- *strict tax-sharing,* if is fulfils all four criteria;
- *tax-sharing,* if it fulfils the first three criteria but not the fourth;
- *intergovernmental grant*, if it does not fulfil one or more out of the first three criteria.

It is worth noticing that Blöchliger-Petzold (2009) (henceforth B-P) propose, in a quite innovative fashion, to consider *tax-sharing* all taxes falling in the "e" OECD category.

In Table 11 the OECD taxonomy for SCG taxes has been merged with the B-P criteria to identify tax-sharing respect to intergovernmental grants: categories a, b and c of the OECD taxonomy are considered in order to classify SCG taxes; while the B-P test is used in order to split all the revenue reported as tax-sharing or grants in the three categories of strict tax-sharing, tax-sharing and intergovernmental grants. It is also followed the B-P's proposal to consider strict tax-sharing all the taxes belonging to the "e" category.

Table 11. A taxonomy of tax autonomy

Sub-central taxes	a	a.1	The SCG sets the tax rate and any tax relief, without needing to consult a higher level government
		a.2	The SCG sets the tax rate and any tax relief, after consulting a higher level of government
	b	b.1	The SCG sets the tax rate without upper or lower limits
		b.2	The SCG sets the tax rate within a range established by a higher level government
	c	c.1	The SCG sets both tax allowances and tax credits
		c.2	The SCG sets tax allowances only
		c.3	The SCG sets tax credits only
Tax sharing	d	d.1	Strict tax-sharing (risk sharing, un-conditionality, formula stability, individual proportinality)
		d.2	Tax sharing (risk sharing, un-conditionality, formula stability)
Intergovernmental grants (G)			
Source: Blöchliger and King (2006), Blöchliger and Petzold (2009).			

The Italian SCGs' revenue from taxes and transfers will now been reconsidered in the light of the taxonomy of Table 11, in order to measure effective tax autonomy. The situation preceding the current reform is considered[7].

The regional level

- The regional VAT sharing was introduced in 2000 as a means of finance of the regional health care system, in substitution of transfers, starting from the financial year 2001. Initially the

[7] It can thus be considered the 2010 situation, because some of the novelties of the reform have already been implemented, starting form this year (2011).

Università di Bari
Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

regional share was established in 25.7% of the national VAT revenue[8]. The receipts should have been distributed among regions according to a proxy of the VAT base, which was identified in regional households consumption, as reported in regional economic accounts. However, since the beginning, the actual implementation of the arrangement has resulted very different from the design. The regional aggregate share of revenue was increased from year to year to keep up with the growth of regional expenditure in health care: it has now reached 44,7%. The distribution among regions in each year in part depends on rough indicators of expenditure needs and in part is the result of a bargaining process between the State and the regions on one side and among regions on the other side. In any case the distribution of receipts among regions includes a relevant component of horizontal equalisation. In conclusion, the VAT regional sharing in Italy does not fulfil any of the four B-P criteria and should be classified as a transfer[9].

- When the regional business tax (IRAP) was introduced the autonomy of the region was limited to the possibility of increasing the 4,25%[10] standard rate by one point (up to 5,25%). Regions could not decrease the rate, neither they could introduce tax allowances or credits. Moreover, from 2002 even the possibility to increase the rate was suspended (until the end of 2006). The financial law for 2008 has in principle substantially enhanced the discretion of the regions, establishing that, with an own law, each region can regulate the tax as a regional tax, set the rate, introduce different forms of tax relief. However this amendment has not become fully operative, because its implementation had been subordinated to a national law establishing the framework within which regions could exert their enhanced autonomy. This law has never been put forward. In conclusion IRAP was born as a tax of the b.2 category. Since 2002, for a few years, it collapsed to a disguised form of strict tax-sharing (d.1). Since 2008 it potentially belongs to the a.1 category, but for the time being it has just gone back to its original nature of b.2.
- The regional "piggy-backing" tax, applied on the base of IRPEF, the national PIT, was introduced in 1998. The regions were conferred a limited discretion in setting the rate, but no one on the side of tax relief. For the first two years the range for tax changes was settled between a minimum of 0.5% (considered the standard rate) and a maximum of 1%. Since 2000 the minimum has been increased to 0.9% and the maximum to 1.4%. As in the IRAP case, the tax rates were frozen since 2002 up to 2006. In conclusion the regional PIT surcharge belongs to b.2 category. During the years when the possibility of modifying the rate was precluded, the regional income tax degenerated in a form of strict tax-sharing (d.1).
- The regional vehicle tax is levied on cars and other vehicles, generally on the base of the possession, in some minor cases of the circulation. The regions have a limited power to vary the tariffs: each year they can increase or decrease by 10% the tariffs of the previous year. For some reasons very rarely regions make use of this faculty. In principle regions are not empowered to modify the tax base or to introduce tax relief, even if some regions have marginally done it. The tax must thus be classified in the b.2 category.
- The regional share of the excise on petrol was introduced in 1996. It belongs to the category of strict tax-sharing (d.1), because it fulfils all the four B-P criteria. Formula stability: the regional share does not change in the course of the fiscal year, and not even over the years (since its institution, the component of the tax attributed to regions has changed just once, in 2001, when it increased from 242 to 250 lire for a litre). Risk sharing: given formula stability and individual proportionality, the regions bear the risk of revenue fluctuations[11]. Un-conditionality: the regional revenue is not earmarked. Individual proportionality: the revenue is

[8] Net of the shares devolved to RSS and to the EU.
[9] As a grant it must also be considered conditional (it funds the health system), although in the "weak" sense of block-grants (Bergvall et al., 2006, p. 118)
[10] The rate was decreased to 3.9% starting from 2008.
[11] I wonder if formula stability and individual proportionality imply (and are implied by?) risk sharing.

Università di Bari
Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

allocated to the region where the station, which has sold the petrol, is sited (place of actual consumption).

The municipal level

- The local tax on real estate (ICI), introduced in 1992, is the most important municipal tax, even if in 2008 its role has been depleted by the exclusion from the tax base of owner-occupied houses. The tax base is given by the cadastre values of immobile property. Undoubtedly the tax belongs to category b.2, because municipalities can set the rate within the range 0.4%-0.7%, while they can not modify the tax base or introduce any form of tax relief.
- The municipal "piggy-backing" tax on IRPEF base was introduced in 1999. Originally municipalities were empowered to set the rate up to a maximum level of 0.5%, being enabled to reach the maximum level only in a three years period, with annual tax rate increases not larger than 0.2%; no power were instead given over tax relief. However the rates were frozen in 2003, liberalized in 2007, when the maximum rate was also increased to 0.8%, again frozen 2008. The conclusion is the same as with the regional income tax surcharge: the local tax must in principle be classified in b.2, but since 2003, with the exception of 2007, it has been *de facto* downgraded to d.1 (strict tax-sharing).

The provincial level

- The tax on cars' insurance (RCA), introduced in 1999, in all respect should be considered a form of strict tax-sharing, because provinces have no power over the rate (12.5%), which is set at the central level, let alone over the tax base. The individual proportionality criterion is met because the yield is allocated to provinces according to the registration of the vehicle and the public registers are located at the provincial level. Thus in any sense this tax must be considered a strict tax-sharing arrangement.
- The provincial tax on cars' registration (IPT) enters the b.2 category because provinces are allowed to increase the national tariffs up to the 30% and they are also entitled to introduce mild form of tax relief.
- The provincial component of the excise on electricity should again be included in b.2 category, because provinces are empowered to increase the standard rate, which is 0.0093 euro/ kWh, up to a maximum rate of 0,011362.

The results of the classification of the main items of tax revenue in Italian SCGs budget are summarised in Table 12. The 2010 situation is photographed.

Università di Bari
Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

Table 12. A classification of Italian SCGs main tax revenue items according to the OECD taxonomy

Regions	
Regional share of VAT revenue	G
Regional Business Tax (IRAP)	b.2
Regional tax rate on PIT (IRPEF) base	b.2
Vehicle tax	b.2
Regional share of the state excise on petrol	d.1
Municipalities	
Local property tax (ICI)	b.2
Municipal tax rate on PIT (IRPEF) base	d.1
Provinces	
Tax on cars' insurance	d.1
Tax on cars' registration	b.2
Surcharge on electricity excise tax	b.2

Note: The classification refers to 2010 legislation

The results confirm the finding of a number of investigations showing that the measure of tax autonomy provided by an aggregate indicator, as the ratio between tax revenue and total revenue, results strongly cut down when the OECD taxonomy is applied. In Italian ordinary regions what is registered in the budgets as tax revenue amounts to about 77% of total revenue. In fact almost a half of it is given by an entrance that is considered a tax-sharing arrangement, but is a grant in any meaningful sense (the regional VAT sharing). Two important regional taxes, IRAP and the income tax surcharge, are characterized by a limited degree of autonomy on the rate side, even if in the recent experience they have been *de facto* transformed in a tax-sharing arrangement. The municipal surcharge on PIT must still (2010) be considered a form of tax-sharing. The same can be said for the most important provincial tax (the tax on cars' insurance).

3. The on-going reform of intergovernmental finance

3.1 The premise

The premise of the current reform is given by the constitutional amendment of 2001, which established that intergovernmental grants were to be abolished as an ordinary means of financing SCGs. According to the amended art. 119 of the Constitution regions, provinces and municipalities must be put in the condition to finance their expenditure with own taxes or fees and with tax-sharing arrangements. Only two forms of transfers are still admitted: those with an explicit equalisation purpose and some earmarked grants directed to finance policies with specific objectives, enumerated in the Constitution, such as enhancing regional development, promoting social cohesion and solidarity, guaranteeing the exercise of the fundamental rights of the person.

Università di Bari
Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

Thus the goal of the 2001 reform has been the alignment of expenditure functions and fiscal responsibilities, in order to fill up any vertical fiscal imbalance, other than the component due to disparities in fiscal capacity among territories, which should be dealt with through an appropriate mechanism of equalizing transfers.

Different arguments have been used in favour of such a perspective. The point of enhancing accountability has been particularly popular. The basic idea is that the decentralisation of the power to tax would have the effect of turning the economic cost of providing public services into a political cost for the local government, to be evaluated in front of the political benefit arising on the expenditure side. Thus the local government would be induced to act as any other economic agent in a decentralised setting: taking decisions comparing marginal costs and benefits.

It has however been stressed[12] that a necessary and sufficient condition for the accountability effect is the alignment of expenditure and taxation *at the margin.* A fixed, even consistent, amount of "inframarginal" expenditure could be financed by grants, provided that any increase over that level were certainly covered with taxes under the full control and responsibility of the SCG. The essential point would not be that grants should be null or few, but that they should be totally inelastic to local expenditure decisions. The question then becomes the credibility of the higher level government commitment not to intervene to bail out the SCG.

Bird (2011), while sharing the theoretical point, argues (p. 156 note) that, as a matter of fact, "since few, if any, countries are likely to achieve such perfection, the better part of wisdom would appear to be to follow the advice that emerges from the literature": "If subnational governments are to be big spenders, they must, in the interest of fiscal responsibility and accountability, also become bigger taxers" (p. 156).

3.2 The framework

In 2009 a law was passed which was meant to implement the constitutional reform of 2001, for what concerns the finance of SCGs. The Law 42/2009 established the general framework of the new intergovernmental financial relations and enabled the Government to produce the detailed norms through own legislative decrees, within two years from the promulgation of the law13. The Government has recently completed the task, having emanated eight decrees, which have gone through the scrutiny of a parliamentary committee and are now operative. In particular, the legislative decree 23/2011 has regulated the municipal finance, while with legislative decree 68/2011 the new financial arrangements for regions and provinces have been introduced.

In this paragraph the main contents of the Law 42 are briefly described, while the next one will consider in some more detail the new financial regime of SCGs resulting from the decrees.

Two essential innovations characterize the new system of intergovernmental fiscal relations delineated by the law. The first was dictated by the constitutional reform of 2001, as we have seen: the abolition of transfers, others than those having a strict equalising nature and some special earmarked grants. The second consists in the introduction of *expenditure needs* as the main criterion for financing SCGs, in substitution of the present system, in which the actual amount of transfers mainly depends on the pattern inherited from the past, which in Italy is referred to as the "criterion of the historical expenditure" and has so far proved very difficult to be modified[14].

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[12] See, for example, Boadway and Shah (2009), p. 97 and 157; Bird (2011) p. 146 and 150-51.

[13] The dead line was May 21, 2011, but has been later postponed to November 21, 2011.

[14] Bird (2011 p. 140) argues: "Existing fiscal institutions usually reflect the results of an accretionary process of policy change over time, and the inertia inherent in such institutions must not be underestimated". OECD (2002 p. 15) includes in

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Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

In framing new regional finance, expenditure of regions is split into two categories:

1. Public services that must be provided uniformly across all the country ("essential services") at a minimum standard, named *essential levels of provision,* which must be established by the State with separate legislations and which for the time being have been identified in health, education, social protection and local transports (the latter limited to capital expenditure);
2. All other public services.

The two categories of expenditure differ with respect to the nature and the degree of equalisation. As far as essential services are concerned, equalisation refers to *expenditure needs* and is supposed to be complete (100% equalisation). Expenditure needs must be determined with respect to normative costs required for the provision of the minimum standard. With reference to the other services equalisation considers the *tax capacity* and is less than 100%.

The law enumerates the different possible sources of tax revenue for the regions:

a) *Derivative* own taxes (by which is meant the regional taxes instituted by a law of the State);
b) Own taxes (*strictu sensu,* i.e. instituted with a regional law);
c) Tax sharing arrangements, and particularly VAT sharing;
d) "Piggy-back" taxes, and particularly the IRPEF surcharge;
e) Equalising transfers[15].

The equalisation mechanism envisaged for essential services postulates that the rate of taxes and the ratios of tax-sharing are set at the level necessary to provide the richest region with sufficient revenue to cover its expenditure needs. For all the other regions the tax resources must be integrated with the access to an equalising fund, which is financed by shares of VAT and of the IRPEF regional surcharge[16].

At the local level (municipalities and provinces) the framework is very similar. Expenditure is distinguished in "fundamental" and "not fundamental", with the same implications in terms of finance and equalisation.

The expenditure of municipalities and provinces must be financed with:

a) Own taxes (instituted with a law of the State or of the Region);
b) Tax sharing arrangements (with State or regional taxes);
c) "Piggy-back" taxes;
d) Equalising transfers.

It is worth emphasising that the movement from transfers to local taxation, which is the essential feature of the reform, is supposed to be revenue neutral. This implies that state taxation must be reduced to the same extent of transfers, and both must be equal to the increase in the SCGs tax revenue.

3.3 The implementation

It was an easy prediction (Gastaldi, Longobardi and Zanardi, 2009) that, being the scope for new taxes at the sub-central level very limited, the goal of substituting grants with tax resources would have been mainly pursued enlarging the space of "co-occupation" of the same taxes among different levels of government[17].

Taxes may be co-occupied by different levels of government according to two main general formulas:

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the category of "related to objective criteria" "grants which have historically been distributed in a certain way and id the case of which legal or administrative limits or established custom are seen as preventing governments from changing the distribution of the grant very much from year to year".

[15] Beside the other transfers admitted for very special purposes by the Constitution.

[16] An equalising mechanism of the same nature was proposed by Bird (1993) p. 218, see also Bird (2011) p. 150.

[17] The term "co-occupation" is used by Boadway and Shah (2009, p. 86 and 191).

Università di Bari
Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

(1) Revenue-sharing, whereby SCGs are assigned a fraction of the revenue produced within their jurisdiction;

(2) Overlapping taxation (or piggyback taxation), which may involve two different forms of levies:

   (a) with the *tax on base system,* a surcharge is applied by a SCG on the *tax base* of the higher level government;

   (b) with the *tax on tax system,* a surcharge is applied by a SCG on the *tax liability* of the higher level government.

The Italian reform makes a widespread use of both revenue sharing and overlapping taxation; in the latter case, following a tendency started in the late '90s, the modality of the tax on base system is chosen[18].

In the following the different forms of tax co-occupation introduced or modified by the two legislative decrees will be identified, going through a brief presentation of all the legislative innovations.

Regional finance

The reform of regional finance is supposed to start being operative in 2013. The main aspects are the following.

1. The regional surcharge on IRPEF base is reformed, with the aim of increasing the discretion of the regions in terms of rate and of recognising also the power of introducing some forms of tax relief. The standard rate of 0.9% is increased by the amount necessary to compensate the abolition of State transfers and of the regional sharing of the State excise on petrol. Each region is empowered to increase the new standard rate by 0.5 percentage points in 2013, 1.1 in 2014, to 2.1 in 2015. Instead, decreasing the rate is not subject to any limit. Thus, after the transitional period, each region will have the power to set its income tax rate t_{ry} within the range:

$$0 \leq \quad t_{ry} \leq 0.9\% + x\% + 2.1\%,$$

   where x% is the percentage points increase necessary to replace the State grants and the regional revenue from petrol tax-sharing, which will be both abolished. It is worth noticing that the increase in the standard rate con not go above 0.5 percentage points for liable incomes falling in the first bracket of the State progressive income tax. Over the first bracket the rate can be graduated, up to the maximum, but respecting the tax brackets of the national tax. The regions are also empowered to increase the national tax credits for spouse and children and to introduce tax credits for social purposes in substitution of any existing form of subsidy, grant and voucher (the latter measure is supposed to enhance horizontal subsidiarity).

2. The regional VAT sharing is also modified. The intention is to transform it, from being *de facto* a transfer to a strict tax-sharing, especially with concern to the principle of individual proportionality. Art. 4 of the legislative decree 68/2011 disposes that, starting from 2013, the allocation of the revenue to regions should follow the "territorial principle", by which it is meant that each region must receive a share of the tax effectively arising in its territory. The point where the VAT revenue is effectively generated is identified with the place where goods (and generally also services) are sold to subjects, which, for some reasons, cannot deduct the VAT included in the passive invoice. The latter will primarily be non-VAT registered persons,

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[18] Gastaldi, Longobardi and Zanardi (2009) provide a comparative economic analysis of the two forms of overlapping taxation.

Università di Bari
Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

that is to say final consumers. But they can also be VAT entities that are not entitled to (full) deduction of VAT on their purchases (no-market public or private entities, firms providing exempted services, like banks and hospitals and so on). The decree disposes that the point of effective VAT generation should be determined using the information derivable from the VAT tax files and other databases of the fiscal administration. The rational of such an attempt is to envisage a system in which the SCG is given a right incentive to collaborate in the administration of the tax and, in particular, in fighting tax evasion. This incentive is lacking when the tax is distributed according to some economic proxy independent of the effective tax revenue generated in the jurisdiction. It is surely a challenge because in no other country such a system has been successfully experimented. We'll come back to this question in the conclusive part of the paper.

3. The decree 68/2011 grants the regions the possibility to reduce the rate of IRAP without any limit, down to zero. Regions are also granted the right to introduce tax allowances. The revenue effects of the rate reductions and of the introduction of allowances must be borne by the region itself. In particular, it must be assured that the reduction will not affect the amount of equalising transfers. Peculiarly enough, a region deciding to decrease its IRAP rate is not entitled to augment the standard rate of the IRPEF surcharge more than 0.5 percentage points.

4. Different measures are directed to provide appropriate incentives to the participation of regions in fighting evasion. It is recognised the right of the region to keep for its budget the entire increase in revenue of "cohabitated" taxes, including the regional VAT sharing, deriving from the reduction of evasion.

Municipal finance

The reform of municipal finance is supposed to be fully into force in 2014, after a transitional period of three years. The main innovations are the following.

1. A new municipal property tax is introduced (IMU-Municipal Tax on Immobile Property), in substitution of both the present municipal property tax (ICI) and the personal income tax (IRPEF) levied on the imputed rent of the real estate which does not produce an actual income (because not rented), with the exclusion of owner-occupied houses. For non-rented immobile property the standard rate is 0.76%: municipalities are entitled to modify it within the range +/- 0.3. For rented properties, because they still remain subject to income taxation, the standard rate is lower, 0.38%, with a range of regional discretional change of +/- 0.2. The tax is levied at the higher rate also when the immobile properties are used as assets in business activities: the region has however the faculty to apply the reduced rate.

2. When real estate property is rented, the owner must include the rental income she receives in the IRPEF tax base. With the reform she is now offered the possibility to opt in substitution for a withholding tax with a flat rate of 21% (19% when the rental contract is stipulated according to special schemes regulated by law). The municipalities will receive a share equal to 21.7% of the withholding tax revenue. If, instead, the taxpayer has not opted for the withholding tax, and pays IRPEF, the municipality, curiously enough, will receive the entire revenue (a 100% sharing tax).

Università di Bari
Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

3. A municipal VAT sharing is introduced. The revenue is allocated by distributing per-capita the regional revenue. The fulfilment of the individual proportionality criterion is thus in doubt[19].

4. The municipal surtax on IRPEF is confirmed with the range 0-0.8% for tax variation. The rate are gradually "de-frozen" starting from 2011.

5. A municipal share (30%) of revenue of the registry tax (and other fees that are absorbed in the main tax) on the value of sales of real estate is introduced.

6. The entire revenue (100%) of registry tax and stamp duty on contracts of real estate lease is introduced.

Provincial finance

The reform should be implemented in 2012. The main innovations are as follows.

1. The tax on cars' insurance over which, as we have seen, at the moment the provinces do not exert any discretional power, and are thus considered a disguised form of tax-sharing, is modified. The provinces are empowered to set their rate within the +/- 3.5 percentage point around the standard rate of 12.5%.

2. A provincial sharing of the personal income tax is introduced[20]: the provincial ratio will be determined at the level necessary to fully compensate the cut of the transfers from the State.

3. The provincial surcharge on the State excise on electricity is abolished.

The new financial relations between regions and local authorities

Implementing law 42, the decrees 23 and 68 establish that also the transfers from regions to municipalities and provinces must be substituted with tax resources. The loss of the regional grants will be compensated at the municipal level with a share of the regional surcharge on IRPEF and, at the provincial level, with a share of the revenue from the regional vehicle tax.

Going through the above description we may count 11 different forms of tax co-occupation. They are reported in Table 13.

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[19] Blöchliger and Petzold (2009, p. 5 note) argue that "arrangement where tax receipts are distributed on the basis of a close proxy should fulfil the criterion (e.g. a consumption tax whose distribution relies on household income or a corporate income tax whose revenue in distributed according to the number of employees)". It is clearly debatable if a per-capita distribution could still be considered a meaningful proxy for the production of VAT revenue.

[20] It can be mentioned that a provincial IRPEF sharing already exists, but is considered in all respects a transfer, even by the same administration (Interiors) in charge of administering it.

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Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

	Table 13. The forms of tax co-occupation in the new system of financial intergovernmental relations in Italy
	State-Regions co-occupation
1	Regional surcharge on IRPEF
2	VAT regional sharing
	State-Municipalities co-occupation
3	Sharing the witholding tax on rental income
4	IRPEF on rental income (100 % devolution)
5	VAT municipal sharing
6	Municipal surtax on IRPEF base
7	A municipal share (30%) of revenue of the registry tax
8	Registry tax and stamp duty on contracts of real estate lease (100% devolution)
	State-Provinces co-occupation
9	Provincial share of IRPEF
	Region-Municipalities co-occupation
10	Municipal share of the regional surcharge on IRPEF
	Region-Provinces co-occupation
11	Provincial share of the regional vehicle tax

4. Open questions

4.1 The rationale and the politics of tax decentralisation

A huge movement from transfers to different forms of tax "co-occupation" qualifies therefore the present reform of intergovernmental fiscal relations in Italy. Starting from '80s a climate of diffuse criticism towards derivative finance has spread. On economic grounds the prevailing opinion ascribes to the decentralisation of tax power positive effects in terms of fiscal consolidation. The basic idea is that the alignment of expenditure and fiscal functions would enhance responsibility and accountability, and would thus promote fiscal discipline. On political grounds two main forces have been in action. Firstly, a political party (Lega Nord) in the North of the Country has been constructing its electoral consensus on the claim "taxes must remain in the territory where they are paid". Secondly, SCGs, of any political colour, have been asking more effective independence from higher level governments and developed an increasing intolerance towards any undue form of interference in their autonomous decisional sphere as well as towards unannounced unilateral changes in the provision of funds. It should be stressed that local governments, on the one hand, require more certainty in terms of availability of resources, but, on the other hand, they are also very reluctant to assume the

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Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

responsibility to tax their electorate. That's why forms of tax co-occupation, and especially the tax-sharing arrangements that are politically the mildest form of tax involvement, are preferred to fully autonomous taxes.

Another important factor, which contributes to explain the movement towards tax co-occupation, is the firm belief of the last governments (of both political sides) in the necessity to involve the sub-national governments in the assessment of the tax. This founded on the conviction that a local government has an informative advantage that can be precious in contrasting evasion. Having the local government as a cohabitant of the tax becomes, thus, an indispensible premise for its involvement in the tax administration.

All these factors, together with the objective difficulty in envisaging new forms of local taxes on economic tax bases not already occupied by the central government, contribute to explain the resulting specific architecture of the new intergovernmental fiscal relations in Italy.

In this conclusive part of the paper three main questions are raised. The first is if, as a final result, the reform is likely to augment effectively the tax autonomy of SGSs. The second is connected with the needs of coordination within some of the main schemes of tax co-occupation and, in particular, the PIT. Finally, we turn to the question of the new strategy that has been chosen to share the VAT among levels of government.

4.2 Will the reform effectively produce more tax autonomy?

The degree of tax autonomy implied by any single main form of tax revenue in force in the last year preceding the beginning of the implementation of the reform (2010) is compared with those expected in the year when the reform will be fully operative at every level of government (2014) in Table 14. We can see that out of 16 main forms of tax revenue in force in 2014, 8 are "new", in the sense that they substitute transfers. In all these cases the new tax item is constituted by a tax-sharing arrangement: in 7 cases out of 8 it qualifies as "strict tax-sharing" (d.1, the arrangement fulfils all four B-P requirements), while in the remaining one the tax share is just apparent, concealing, in fact, a transfer (G, because B-P criteria are not fulfilled). It is well known that tax-sharing does not confer SCGs more autonomy in any meaningful sense with respect to transfers. In a perspective of fiscal federalism, the only appreciable advantage of a tax-sharing formula with respect to a transfer is in terms of the effective entitlement over the resource. While a transfer remains in the domain of the donor, which can, thus, change the amount transferred when the cut is considered necessary, say for consolidation purposes - as it has happened twice in Italy in the last three years - the guarantees assured to SCGs by tax-sharing arrangements are likely to be stronger on both political and institutional grounds. We would expect, in fact, that changing the formula of tax-sharing would require the consensus of the receiving government. In a sense Italian SCGs have won their battle: as we have mentioned, what they really wanted was not more autonomy, with the relative implications in terms of political risk assumption, but more certainty over the effective availability of the resources.

Looking at the remaining items of Table 14, we see that in 5 cases the position of the item in the OECD ranking has not changed: the item was classified in the b.2 category and there it has been left. In 2 cases the tax item (a d.1 and a b.2) has been abolished. At the end only in one case the tax item results upgraded in the OECD ranking: the provincial tax on cars' insurance that moves from d.1 to b.2.

It must be noticed, however, that the OECD taxonomy can not capture a main result of the reform in terms of tax autonomy conferred to regions. As far as IRAP and the regional PIT surtax are concerned, the enlargement of the range of possible tax rate changes and the possibility to introduce tax relieves, while enhancing effective tax power at regional level, do

Università di Bari
Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

not change the nature of the two local taxes. The latter, thus, do not go up in the OECD ranking.

We have mentioned that what really matters in terms of accountability and responsibility is the tax power at the margin. Thus the question becomes if, at the margin, there will be enough scope in the new system to allow the SCG to finance with autonomous tax effort expenditure needs exceeding the "normal" ones, either because of inefficiencies in the provision or because local preferences justify a change in the allocation of resources in favour of public goods.

Table 14. An evaluation of the effects of the reform in terms of effective tax autonomy of Italian SCGs

	2010	2014
Regions		
Regional share of VAT revenue	G	d.1
Regional Business Tax (Irap)	b.2	b.2
Regional tax rate on PIT (Irpef) base	b.2	b.2
Vehicle tax	b.2	b.2
Regional share of the state excise on petrol	d.1	abolished
Muncipalities		
Local property tax (2010 ICI, 2014 IMU)	b.2	b.2
Sharing the witholding tax on rental income	-	d.1
IRPEF on rental income (100 % devolution)	-	d.1
VAT municipal sharing	-	G
A municipal share (30%) of revenue of the registry tax	-	d.1
Registry tax and stamp duty on contracts of real estate lease (100% devolution)	-	d.1
Municipal surtax on IRPEF base	d.1	b.2
Municipal share of the regional surcharge on IRPEF	-	d.1
Provinces		
Tax on cars' insurance	d.1	b.2
Tax on cars' registration	b.2	b.2
Surcharge on electricity excise tax	b.2	abolished
Provincial share of IRPEF	-	d.1
Provincial share of the regional vehicle tax	-	d.1

If we look at the regional level, the main source of autonomous fiscal effort is given by the surtax on IRPEF. This is because political reasons prevent regions to rely on IRAP, whose burden is even expected to decrease, while the possible contribution of the vehicle tax is objectively limited. At the municipal level the importance of the property tax as possible source of revenue has been depleted by the exclusion from the base of the owner-occupied houses, so that at the moment non-residents pay a significant portion of the tax. Hence, also at the municipal level the most important means of autonomous fiscal effort remains the surtax on IRPEF base.

In principle at both the regional and the municipal level, the range for potential rate changes in income surtaxes becomes of some relevance with the reform. Probably the technical space for discretionary tax choices is not the real obstacle to an effective exercise of (marginal)

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Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

tax autonomy: what is still missing in today's Italy is an institutional culture of tax autonomy. The central level government still fears that the electorate could attribute to its responsibility tax increases at a decentralised level. This attitude explains why last years' governments have several times intervened to freeze local tax rates and also why in the implementation of law 42 the government has been very cautious in according effective tax autonomy to SCGs. A fully accountable system in which the electorate can distinctively attribute tax responsibilities to each level of government and each level of government has full consciousness of this (she knows that he knows), so that nobody can play to pass the buck, is something still unknown in the Italian political and institutional life.

4.3 Co-habiting the PIT: some equity profiles

PIT co-habitation appears thus at the hart of the new system of tax relations between levels of government built with the reform. About the equity implications of such a co-habitation an intensive discussion had been already opened in Italy in the last few years. The relevant questions pertain both to the sphere of vertical and horizontal equity.

When regional and municipal surtaxes were introduced, the dominant opinion, at least at the academic level, was that they should have been of a flat type, in order to reduce the impact of sub central discretion on the overall structure of progressivity of the income tax.[21] Instead, regions started introducing progressive rate schedules, often with a class-based rate progressivity (instead of the bracket-base system adopted at the national level, as in most countries)[22]. The question of the legitimacy of such choices was raised in front of the Constitutional Court, which recognised the reasons of the regions.

It is largely admitted that the traditional approach, according to which redistributive function should be reserved to the central level, can be considered obsolete - both because preferences for redistribution may vary from one local community to another and because, as a matter of fact, it is impossible to assign redistributive function to a single level of government (Boadway and Shah, 2009, p. 72-73). However, it could still be maintained that the SCGs involvement in redistribution should regard instruments and policies other than the PIT. The overlapping of the choices of different governments in determining the structure of progressivity of the income tax without any coordination can, in fact, determine an erratic path of the effective total marginal rate, with unpredictable effects in terms of incentives to work.

In Italy a measure of coordination has now been introduced with the reform, which, as already mentioned, has established that, when adopting a progressive surtax, the region has to adhere to the bracket-based system and to respect the structure of brackets established at the central level.

In terms of horizontal equity the question is to which extent differences can be admitted in tax incidence on equal incomes depending on the place of residence. While, as far as vertical equity is concerned, the reform has contributed to ameliorate the situation, it has, instead, exacerbated the problem concerning horizontal equity, by recognising to the region the discretion to increase tax credits for children and spouse.

[21] It is worth remembering, however, that a sub-central surtax on the PIT base, even if flat, affects the degree of overall progressivity. Gastaldi, Longobardi and Zanardi (2009, p. 168) show that a flat surtax reduces the overall degree of progressivity in the sense of Kakwani and, instead, increases the redistributive effect in the sense of Reynolds-Smolensky.

[22] In 2008 eight regions out of twenty had introduced a progressive rate schedule, having six of them adopted the class-base system (Gastaldi, Longobardi and Zanardi, 2009, p. 168).

Università di Bari
Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

4.4 The Italian planned experiment of VAT decentralisation according to tax files information

Allocating central VAT to SCGs according to the place where VAT is actually paid is not a good criterion, because VAT is paid in the place of legal residence of the firm, generally different from the place where it undertakes the activity. Thus, in many countries, VAT is allocated among levels of governments using some proxies of the tax base or revenue, such as final consumption, manpower, payroll and so on. In this case the revenue accruing to any single SCG is independent from the contribution it may have assured in the administration of the tax.

As mentioned, in Italy, at the moment, a great attention is paid to the design of appropriate incentive mechanisms to involve SCGs in the assessment of the tax. As far as VAT is concerned, the Italian reform draws a new system to decentralise VAT according to the identification of the place where the transaction that has generated the revenue has been undertaken. The underlying vision is that VAT does not produce revenue until it impacts on an agent that has not the possibility to deduct the VAT paid on purchases. Simplifying, we could say that B2B transactions do not generate revenue, while B2C transactions do. If so, VAT would be a pure consumption tax. However, in practice, also some B2B transactions generate revenue. This happens when the VAT registered entity cannot (fully) deduct VAT on purchases, essentially because it does not produce for the market (public administrations and private non-profits entities) or because it undertakes exempted operations. For this reasons VAT domain does not coincides with final consumption. A share of VAT is levied, in fact, on intermediate consumption or investment[23].

Some years ago in Italy a new box was introduced in the VAT return, where the taxpayer has to register separately the sells to final consumers, indicating also the region where the operation has taken place (the so called VT box in the VAT returns). The data have been checked and their reliability has improved from year to year. Now the intention is to use this data set to allocate to regions the VAT revenue generated by B2C operations. As far as the other VAT components are concerned, the administration is considering the possibility to use other data base. The one of IRAP returns, for example, provides a good information on the territorial distribution of all productive activities, considering both market and non market agents.

It is a difficult challenge, because apparently there are not similar experiences at the international level which could help and the technical problems are relevant. The risk is that the resulting mechanism would not appear enough rigorous and transparent, undermining its legitimacy in front of the interested SCGs.

5. Conclusions

The paper has tried to provide some insights into the current reform of the system of intergovernmental relations in Italy. The reform is mainly characterised by a movement from transfers to different forms of tax co-occupation, which is intended to enhance autonomy and, as a consequence, accountability and responsibility of SCGs. Using the OECD taxonomy about tax autonomy, it has been shown that the effective increase in “infra-marginal” tax autonomy of SCGs produced by the reform will be quite modest. At the margin, however, where autonomy really matters, there could be enough room for the exercise of effective discretion. The main problem is that both the central government and the SCGs fear the

[23] According to estimates produced by the EU Commission some years ago, on average in the Union 1/3 of VAT was levied on intermediates and investments.

Università di Bari
Dipartimento di Scienze Economiche e Metodi Matematici
Southern Europe Research in Economic Studies - S.E.R.I.E.S.

decentralisation of tax power: the former because it feels that, at least in the transitional period, the electorate might not properly distinguish the different fiscal responsibilities, the latter because they would prefer not to tax their electorate, even if they strongly ask for more stable and predictable sources of finance with respect to the current system of grants.

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