Senato della Repubblica

Ufficio Valutazione Impatto
Impact Assessment Office

FOCUS

Fiscal Expenditures. Incentives, deductions and exemptions: how many exist? Who benefits from them?

September 2017

Together with the update memo to the DEF Economic and Financial Document, in a few days the Government will be publishing its First Preliminary Report on Fiscal Expenditure*: exemptions, deductions, tax credits, and favourable tax rates that the executive has been tasked with "reducing, eliminating or reforming", acting specifically on measures that are "unjustified" or "superceded". For years now, the European Union Council has been asking Italy to reduce its "use and generosity of exemptions and preferential treatment". The National Reform Plan (PNR) has scheduled an* ***overhaul*** *for 2017 and 2018.*

Italy has hundreds of measures that are 'classified as ***tax expenditures, involving tens of millions of taxpayers****. However, surveys carried out in recent years on the exact number of incentives to be overhauled, the amounts paid out to beneficiaries and the various consequences on income, have all painted a different picture.*

This research paper provides an update on what data and information is available and what is missing, starting from work carried out by the Committee that assists the Government in monitoring tax expenditure: in 2016, adding up State and local taxes, experts found a total of ***as many as 610 different measures, with a financial impact equal to -€76.5 billion****,* ***and yet no information is available on 67.5% of State tax expenditure****.*

Starting Point

On the topic of tax spending, Legislative Decree no. 160 in 2015 mentions two tools: a ***Preliminary Report*****,** which is a government document of a political nature, and which is due

Table 1. Tax expenditure broken down by tax. Year 2017

Tax	Impact 2017 (millions of euros)
IRPEF	38,550.8
Excise	2,687.9
VAT	2,047.9
Registration	1,961.1
Tax credits	1,664.5
Registration e other indirect taxation	1,600.5
Substitute tax	1,338.5
IRPEF / IRES	967.0
IVA IRPEF IRAP	914.5
IRPEF / IRES	666.6
IRES	647.3
Cadastral tax	559.6
Mortgage tax	363.2
Registration and mortgage/cadastral	198.7
Stamp duty	161.8
Insurance tax	73.0
Registration tax	32.0
Withholding on financial income	25.3
Registration and mortgage/cadastral tax	18.0
Stamp duty, registration and misc.	17.8
IRES IRAP	10.5
Registration, mortgage and cadastral tax	8.9
Government concessions	5.5
Inheritance tax	1.5
Consumption tax?	1.0
Gift tax	1.0
IVIE	0.8
Inheritance, mortgage/cadastral tax, stamp duty and misc.	0.5
Registration tax and misc.	0.2
Gift and mortgage/cadastral tax	0.2
IRES / IVA	0.1
Overall total	**54,526.0**

Source: UVI. Based on data from the 2016 Report

to be published imminently, and the technical **Annual Report**, drafted by a committee of fifteen experts, which lists all of the measures in effect and is attached to the statement of estimates of income in the National Budget. The initial *Technical Report* was published in 2016.

Analysis

The International Monetary Fund defines *tax expenditures* as **income that the State forgoes** through selective measures in favour of certain categories. For the OECD, they are defined as **public expenditure implemented through the tax system.**

In domestic Italian law, it is "any form of exemption, exclusion, reduction in taxable income or of taxes, or favourable treatment resulting from applicable law."

According to the 2016 Committee Report, **Italy had 610 tax expenditure** measures in place: 468 measures regarding State taxes, and 166 regarding local taxes.

Of these, 24 expired in 2016, while 43 new State tax expenditure measures were brought in between 1 January 2015 and 30 June 2016**.**

Adding together the financial impact of the various measures identified in the *Report*, the **tax authorities will be collecting €54,526 million less for the year 2017.** Including local tax incentives, this amount rises to **76.5 billion**.

The **main public policies** pursued in Italy through tax expenditure are for:

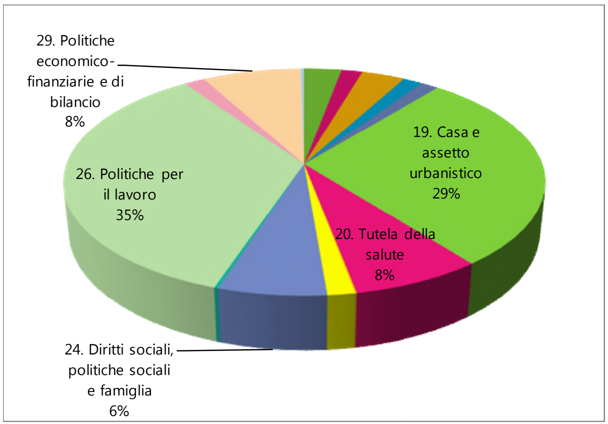
• **Employment** policies (mission 26), for which around 35% of resources were set aside in 2017, corresponding to €19,206 million

• The **home and town planning** (mission 19), accounting for ca. 29%, equal to €15,603 million

• **Health protection and economic/financial and budgetary policies** (missions 20 and 29), for which around 8% is earmarked (respectively, €4,118 million and €4,221 million)

• **Social rights and social/family policies** (mission 24), which accounted for 6% of resources (€3,395 million).

Figure 1. Financial impact (%) by mission



Source: UVI. Based on data from the 2016 Report

Resources equal to **€46,543 million (ca. 85% of the total)** are allocated to these five sectors.

The numbers dilemma: previous surveys

A number of surveys of tax expenditure have been conducted in recent years, albeit with different criteria, methods and results.

In 2011, the Working Group on Tax Erosion set up by the Ministry of the Economy and Finance – known as the Vieri Ceriani Committee – identified **720 different tax expenditure measures**, with an overall financial impact of **between -€227 and -€254 billion.** It was not, however, possible to carry out an *ex post* quantification for **457 of these 720 measures**.

The statement of estimates of income in the National Budget also features a Notes to the Accounts which includes a list of tax expenditure in effect. In 2011, the same year that the Vieri Ceriani committee report came out, it listed **242 (compared with 720).**

The Notes to the Accounts for the year 2015 listed **282 tax expenditure measures;** in **2016** – the year that the new Committee of Experts carried out its survey – this rose to **296** (**compared with 468** tax authority measures noted in the *Annual Report*). Lower income forecast: **€175.1 billion for the year 2016**, and 161 billion for 2015.

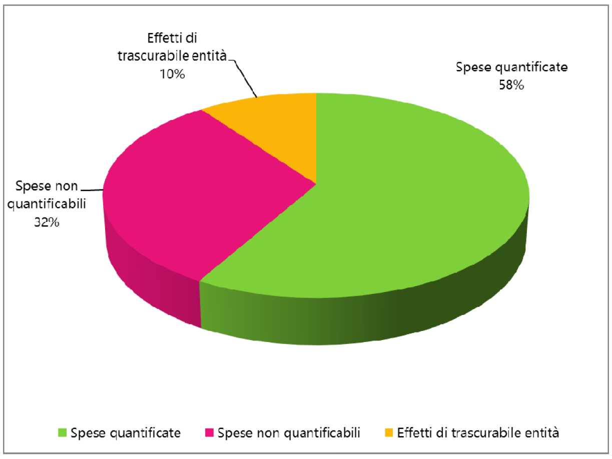
In its 2016 *Report on Tax Expenditures*, the Committee chose not to provide a value for the overall lowering of income, "in the belief that the obstacles and disadvantages of a simple totting up are too great to overcome". Out of **468** state incentives examined, **316 (67.5%) did not feature any indications** on charges, beneficiaries and *per capita* amounts.

The data: not always complete

No financial values were provided for many of the incentives that the Committee identified: **just 273 State tax expenditure measures out of 468 were actually "quantified"** (58%).

For **42%** of the measures, **it had not been possible to indicate values,** either because they were deemed unquantifiable incentives (148 measures, accounting for 32%) or because they were termed as having "an impact of a negligible amount," albeit without providing any figures (47 measures, corresponding to 10%).

Figure 2. Exhaustiveness of the financial data



Source: UVI. Based on data from the 2016 Report

The riddle of "negligible amounts"

The 43 State tax expenditure measures introduced since 2015 generated an overall financial sum of **€3,583 million for the year 2017**.

Eighteen of these new measures were deemed to have a "negligible amount" of financial impact, while a further two are termed "unquantifiable" Despite this, technical reports have on occasion entered the **impact of amounts that are not insignificant** onto the public finance balance sheets. Here are four examples:

- **Measure no. 448** (Substitute tax, preferential exclusion of assets from corporate tax arrangements): the technical report states negative financial effects on an accruals basis of **€46.7 million** for 2017; **€49.2 million** for 2018; **€51.8 million** for 2019; **€54.3 million** for 2020; and **€54.3 million** for 2021

- **Measure no. 77** (Incentives for investing in SMEs): the Notes to the Accounts projected negative financial effects equal to **€44 million** for 2016, **€25.5 million** for 2017, and **€17.5 million** for 2018

- **Measures no. 457 and 466** (Tax credit for the installation of video surveillance systems and for scrapping motorhomes): authorized expenditure equal to a total of **€20 million** for 2016 alone (on an accruals basis). The *Report* defined it as having "an impact of a negligible amount" over the three-year period 2017-2019

- **Measure no. 459** (50% VAT deduction for the purchase of A or B Energy Class residential properties): based on the technical report, negative financial effects on an accruals basis are forecast of **€18.4 million** for 2017 and **€10.5 million** from 2018 to 2026.

Looking at the details. Who benefits from these incentives?

The financial effects and pool of beneficiaries were stated for **just 152 State tax expenditure measures (out of 468)**.

Distribution of these 152 measures indicates that:

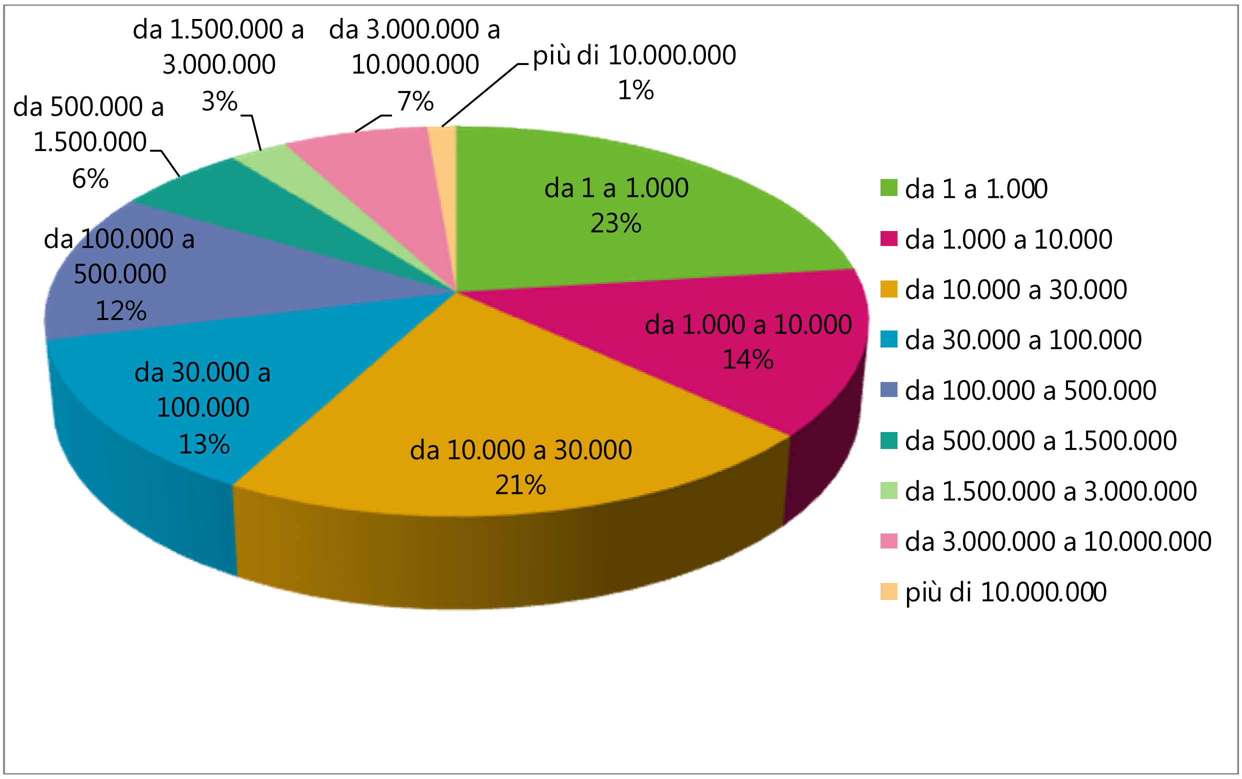
- 23% are oriented towards a beneficiary pool that encompasses **fewer than a thousand people**
- 21% covers a slightly larger pool, **of between 10,000 and 30,000**
- 14% covers **between 1,000 and 10,000 beneficiaries**
- 13% benefits a number of between **30,000 and 100,000 taxpayers**

More than half of these 152 tax incentives – 88 of them, corresponding to **58%** – **concerns fewer than 30,000 individuals**. The actual number of users is, in any event, extremely low: some 518,000, equal to **0.46%** of those entitled.

Table 2. Tax expenditure measures divided by bands of beneficiary, measures per band, individuals covered and amounts

Frequency band	Number of measures per band	Total beneficiaries per band	Value of the measures by band (million euros)
From 1 to 1,000	35	12,331	145
From 1,000 to 10,000	21	79,245	445
From 10,000 to 30,000	32	426,390	860
From 30,000 to 100,000	20	1,011,540	1,691
From 100,000 to 500,000	19	3,939,781	3,300
From 500,000 to 1,500,000	9	7,920,108	3,396
From 1,500,000 to 3,000,000	4	8,228,709	1,997
From 3,000,000 to 10,000,000	10	48,664,524	15,209
Over 10,000,000	2	43,049,460	6,743
Quantified total	**152**	**113,332,087**	**33,785**
Unquantified total	**316**	**-**	**-**
Overall value of measures without an indication of frequency	-	-	20,741
Overall total	**468**		**54,526**

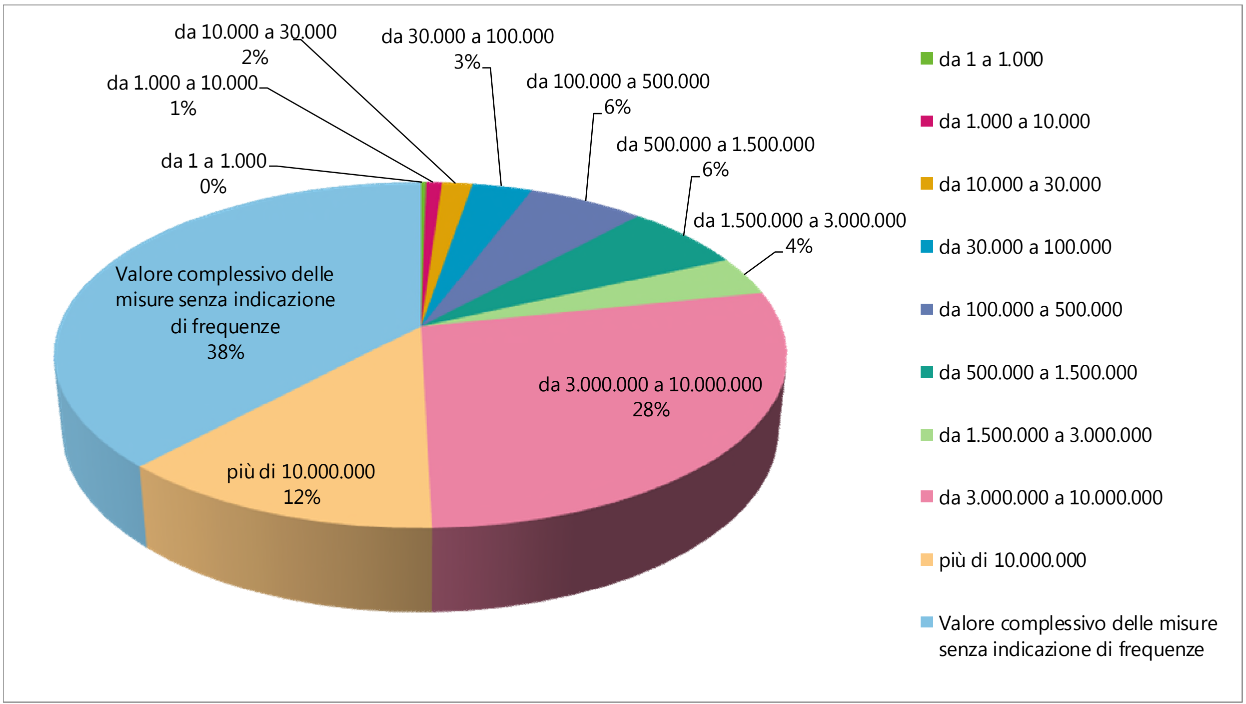
Figure 3. Distribution of tax expenditureS measures by class (beneficiary frequency)



Source: UVI. Based on data from the 2016 Report.

Forty percent of resources associated with the 152 measures for which information is available is focused on the categories of 3 million individuals and upwards. Twenty-two percent of resources (around €11 million) are earmarked for categories of up to 3 million. Owing to a lack of data, it is not possible to perform this analysis on the remaining 360 measures.

Figure 4. Distribution of tax expenditure amounts by frequency band



Source: UVI. Based on data from the 2016 Annual Report on Tax Expenditure

Just two measures register frequencies of more than 10 million beneficiaries:

Measure no. 124 (Deduction of the cadastral rent of a property unit nominated as the **main residence**, and associated fixtures) concerns **26.1 million taxpayers**, generating a per capita financial benefit of €141.4 . **The tax authorities will be receiving €3,691 million** less over the three-year period 2017-2019.

Measure no. 154 (Deductions for **spending on healthcare**, medical expenses and specific care, as well as spending on specialist services) affects **16.9 million people**, and has a financial impact equal to €180 per taxpayer. The impact on the State balance sheet corresponds to **€3,051 million**.

For the few. Between 0 and 200 beneficiaries

The list of tax expenditure with which the lowest number of beneficiaries is associated, albeit with the highest per capita benefits (€60,000 and up):

- **Measure no. 58 - Deduction for coops and their consortia of amounts split between members** by way of repayment or higher earnings – generates individual financial effects equal to **€74,556** and benefits **169** IRES-paying individuals
- **Measure no. 225 - Tax credit for the acquisition of ambulances and fire-fighting vehicles** by non-profit organizations and voluntary associations – entails financial benefits worth **€87,970** for each of its **133 beneficiaries**
- **Measure no. 42 - Tax credit on remote heating systems** fuelled by biomass and geothermal energy – involves per capita incentives worth **€121,827** for **197 users**
- **Measure no. 66 - Flat-rate tax on income from ships on the international register** – generates a financial effect equal to **€144,444** for each of its **90 beneficiaries** (IRPEF/IRES)
- **Measure no. 75 - Exemption from IRES of corporate income generated by property leasing** – offers a financial advantage of **€195,556 and benefits 90 parties** (IRES/IRAP)
- **Measure no. 120 - Total deductibility of funds for funding research, by way of contribution or gift** – has a per capita financial impact equal to **€242,550** for the **77 IRES payers who benefit from it**
- **Measure no. 64 - Flat-rate tonnage tax** – entails per capita financial effects equal to **€291,139** for its **79 IRES** recipients
- **Measure no. 427 - Mortgage and cadastral register tax applied to a set amount** for contributions to closed-end real estate funds – generates per capita effects worth **€635,714** to the benefit of **14 parties**
- **Measure no. 95 - Tax credit for independent producers** of audiovisual works – entails per capita financial benefits worth **€961,538** and **26 incentivized taxpayers**.

Conclusions

In recent years, Italy has made significant progress in adopting international **best practice**, **for example by stating tax expenditure separately in the accounts**. The publication of an *Annual Report* is also a major step towards fiscal transparency.

A number of uncertainties do however remain, as may be evinced from the results of the various surveys **on the number and nature of tax expenditure, financial values, and the parameters used for classification**.

Technical analyses are not yet available regarding the *ex post* impact of tax expenditure measures and their effectiveness in terms of the objectives for which they were introduced.

Compared with previous surveys, **the *2016 Annual Report* is characterized by**:

- The **limited overall value** attributed to the measures identified (State and local taxes), equal to -€76.5 billion for the year 2017

- The high percentage (67.5%) of State measures for which **not all quantitative data has been supplied**

- **A lack of comparisons**, as statutorily envisaged, between tax expenditure in effect for more than five years and spending programmes that have the same end-purposes

- **A lack of analysis requested regarding the micro-economic** effects of individual tax expenditure measures and their repercussions on the social context.

Comments

The effectiveness of public policy pursued through tax expenditure should be verified more closely by:

- Drafting surveys that adopt **homogeneous methodological criteria**

- Implementing procedures and surveys **for each measure** in order to **ascertain the overall financial and *per capita* impact, the effects registered *ex post* and over time, who the recipients are, what objectives are pursued** and **the effectiveness of the measure**

- Focusing attention on tax expenditure measures in operation in order to **verify the effectiveness and relevance of the assessments that led to them being introduced**

- Evaluating whether the **existing legislative framework and the tools already in place** are actually appropriate to supplying political decision-makers with the support that they need to implement the envisaged overhaul

- Assessing whether the annual budgetary manoeuvre is the best route for the overhaul, or whether an *ad hoc* **tool might be preferable, for example, an annual Law Bill on tax expenditure.**

This dossier

- offers an **overview** on Italy's tax expenditures
- reviews **guidelines and recommendations** by international bodies **and the main Italian and European legislative references**
- focuses **special attention on the first *Annual Report on Tax Expenditure (2016)***, as attached to the National Budget for the year 2017 and the Multi-year Budget 2017-2019
- Performs its **own analysis** to provide a number of elements for assessment.

Credits

This research paper is the work of

GIUSEPPE DELRENO

ALESSANDRA DI GIOVAMBATTISTA

VALERIA BEVILACQUA

with the contribution of

NADIA CLEMENTI and GLAUCO CHIYAKI SESTA

Senate of the Italian Republic

Focus is edited by

UVI – UFFICIO VALUTAZIONE IMPATTO

Senate of the Italian Republic

uvi@senato.it

This work is distributed under a Creative Commons Attribution - Noncommercial - NoDerivs 4.0 International Licence