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Unioncamere Veneto

CONSIGLIO REGIONALE DEL VENETO

Spending 'centre'

Role and dynamics of public finance in Italy and in Europe

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Overview

Prepared in collaboration with the Veneto Regional Council, the latest Unioncamere Veneto's report turns the spotlight on the role and dynamics of public finance, specifically identifying certain critical issues that clearly impact on the Veneto's economic system and making a comparison with the experience of other European countries.

The report is part of a series of research studies started six years ago that have addressed a variety of issues, such as the fiscal burden in Italy and its regions, regional variations in public expenditure and the ensuing injustices in terms of per-capita expenditure, the waste of money in some regions and the virtuosity of others, as well as errors in undifferentiated national policies to overcome economic disparities and gaps in local development.

It is before everyone's eyes that the current situation is severe. In the past five years, the tax burden and public debt have reached unprecedented levels, but the resources for services to the public are constantly dwindling due to a policy aimed at curbing expenditure imposed by the European Union, which has proven to be counterproductive for enterprises.

The cost of an inefficient 'public system' is evident, as we have emphasized repeatedly in recent years, but boosting Italy's competitiveness calls for structural solutions that mark a clear change compared to what has been done to date.

For this reason, we believe it is essential to contribute ideas and proposals to anyone who can help chart a new route, in the awareness that public expenditure reform can no longer be put off. The very survival of social and economic cohesion between communities and the country's overall sustainability are at stake.

The hope of the Chambers of Commerce of the Veneto is that this report can make a useful contribution to the ongoing debate and support those who are working on the reforms that Italy needs.

Venice, December 2013

Fernando Zilio
President of Unioncamere Veneto

Preface

This working paper continues the work of the *Observatory on Federalism and Public Finance* started in 2007 in collaboration with Unioncamere Veneto and aimed at gaining greater insight into the potential, advantages and implications deriving from a federal organization.

The results of research activities and information on the discussion platforms in which the Observatory's working group participates at regional, national and also European level, on federalism, fiscal policies and the roles of regional governments in European policies, are available on the web site www.osservatoriofederalismo.eu.

This new paper is an opportunity to specifically address the issue of public finance, with particular reference to public spending and national rationalization policies that have tried to eliminate those situations of waste and inefficiency which have severe adverse effects on the productivity and competitiveness of Italy's economic system as a whole.

We have already recalled how Italy's regions have been unjustly accused of covering up the waste and messy management of Italy's public finance: after the Provincial Districts and Mountain Communities, it is now the turn of Italy's Regions to take the blame. No one can shirk responsibility, but numbers too have their weight and it should be borne in mind that, in Italy, provincial district employees account for just 1.75% of the total number of civil servants, those of Mountain Communities for 0.21% and those of ordinary-statute Regions for 1.15%. The central government, on the other hand, accounts for 56% of civil servants, but little has been done (and I believe will be done) on this major spending item.

By contrast, we are proud to recall the efforts made by the Veneto's Regional Council, whose spending review allowed for a progressive reduction of spending by the regional assembly from 60 million Euros in 2010 to 44 million in 2012.

By reorganizing structures, cutting the number of managers, freezing staff turnover, eliminating residual debt and liabilities, and reducing reserve funds to a minimum, the 2012 final balance sheet drawn up by the President's Office last August realized savings and adjusted revenue and expenditure arrears totalling 5,336 thousand Euros. This considerable amount was returned to the Region's coffers with the recommendation to the Regional Council to allocate these sums to an extraordinary solidarity fund for the unemployed and new forms of poverty set up by the 2013 Finance Law.

This is a tangible sign that reviewing spending is possible and that institutions are able to be close to and show solidarity toward people living in dire need. The savings realized since 2011 and the clampdown on spending in 2013 determined by the new autonomy law have earned the Veneto's Regional Council the title of Italy's most virtuous legislative assembly in terms of cost and number of employees. While the Veneto was already at the top of the rating for the ratio of regional assembly employees to regional inhabitants (158 employees versus the 340 employees of Piedmont, a region with half a million less inhabitants than the Veneto, and the 168 of nearby Emilia-Romagna, which counts 80 thousand inhabitants less than Piedmont), the spending review has allowed the Veneto's Regional Council to be Italy's most virtuous also in terms of the number of top-level managers.

These considerations accompany a number of proposals discussed in this new essay, whose objective is to understand where public money is actually wasted.

We are convinced that responsible management of resources will only be achieved in Italy through full implementation of fiscal federalism. This is the only viable path to save Italy and its production system.

Venice, December 2013

Clodovaldo Ruffato
President of the Regional Council of the Veneto

This survey was promoted and carried out in the framework of the *Regional Observatory on Federalism and Public Finance*, established by the Regional Council of the Veneto and Unioncamere Veneto.

The survey was designed, and the data and legal sources were collected, processed and assessed by a team co-ordinated by Gian Angelo Bellati, Secretary General of Unioncamere del Veneto, and composed of Serafino Pitingaro, Giovanna Guzzo and Giorgia Gosetti di Sturmeck of the Centro Studi Unioncamere Veneto, with the support of Luca Romano, Alberto Cestari and Andrea Favaretto of the Centro Studi Sintesi, and Quirino Biscaro of the International Trade Academy Center of Advisory (ITACA).

We are especially grateful to all those who, as politicians or experts, participated in the meetings of the Observatory on Fiscal Federalism and contributed with their thoughts, ideas and suggestions to designing and writing this report.

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Introduction*

The *Observatory on Federalism and Public Finance* has been engaged in conducting studies and research into implementation of decentralization in Italy since 2007 and, along this path, it has addressed the issue of federalism by focusing in particular on the fiscal and tax system in a comparative framework.

The analysis of taxation, public spending and national policies aimed at solving the problems that plague public finance in Italy has played a central role in this effort, and the work that has gone into this *Working Paper* is intended to provide a general reflection on the data collected to date, in the awareness that the **cost and the efficiency of the 'machinery of government' have a considerable impact on the economic system and competitiveness of the country**.

As our studies have amply demonstrated, for example, the success of the German model depends not only on the performance of its businesses, but also, and - in our opinion - mainly, on the 'net domestic savings' resulting from a federal institutional structure and true accountability of local territories. However, it is also well known that **the main way through which Germany has accrued its net domestic savings is precisely the reduction of the costs of central government and the related public expenditure**.

It is no coincidence that this experience is the exact opposite of what has happened in Italy in the last decade, during which the effort to reduce public expenditure has been progressively limited to spending at the local level, hiding away from sight public spending at the central level, which has continued to grow steadily, for both staff and current expenses for 'general government'.

The result is before everyone's eyes: the road to **growth** is burdened by huge boulders that prevent investment and the recovery of the entire economic system. Just think of the inability to delegate responsibility to spending centres with the power to levy taxes; or to the impossibility to reward the virtuous and trigger a process of positive competition between entities; or even, the inability of the Italian public system to assess the effects of spending on the planning of investment policy.

* Gian Angelo Bellati, Secretary General of Unioncamere Veneto.

These characteristics make Italy's system a unique case among OECD and EU countries, both from an institutional and regulatory point of view. There are, in fact, structural anomalies whose scope and depth are such that they cannot be solved with minimal interventions. **There is a need for a radical reform that our political system does not seem to be able to accomplish.**

These anomalies include, for example, the process by which the government budget is formed: it uses a bottom-up approach in collecting the financial requirements from the various Ministries (including all the bodies that these control either directly or indirectly), reversing the conventional relationship between policy planning and the translation of the budget objectives set by the political actors in management and administrative terms (Parliament and especially the Government). The collection of the financial requirements is of an incremental nature and entirely lacks transparency. Not only does it neglect the political objectives of planning, but requires an increase in allocations based on historic spending parameters. Finally, there are absolutely no means to assess the effectiveness of the expenditure reported and to measure the effects in macroeconomic terms.

A close look at the data shows that these anomalies are reflected in the **record values of public debt and taxation.** The former is growing continuously and has rocketed to above 2,000 billion Euros: in 2013, it will amount to 133% of GDP. Finance Laws in recent years have tried to curb public spending. However, spending has continued to rise, going from 49.2% in 2008 to 51.9% of GDP in 2013 (net of the underground economy, this amount could reach 60%). Fiscal consolidation has been pursued through increased taxation, which in 2013 reached 44.3% of GDP (+1.7% over 2008 and which would amount to 55% net of the underground economy).

This is a historical record that the country is no longer able to bear and it is obvious, therefore, that **the urgency of cutting public spending is now desperate.**

No wonder, in this regard, that Italy ranks 139th (out of 148 countries) in the *Global Competitiveness Index* of the World Economic Forum for its efficiency in the use of public money.

The horizon has nothing encouraging in store for us despite the optimistic forecasts of the Italian Government. The memo updating the 2013 Economic and

Financial Document (*Documento di economia e finanza - Def*) outlines an improvement in public finances for 2014 and following years and includes, in particular, an increase in primary surplus and structural debt near zero.

However, **these perspectives are based on an overly optimistic trend of GDP**, which was estimated to be half a percentage point above the forecasts of the International Monetary Fund for each year from 2014 to 2017. The forecast of a stronger growth of GDP determines, in fact, a broadening of the tax base for taxes on income, consumption and labour and hence leads to higher estimated tax revenues and lower deficit without further increasing tax rates.

In addition to these reflections, there is also the consideration, significant by itself, of the incidence of the central component on the size of the total general government debt.

The essay that we are presenting intends to focus on and analyze the trends in Italy's central and local public spending in recent years, particularly as a result of the 'spread crisis' that from July 2011 has imposed an enormous effort on Italy to adjust national public accounts.

Firstly, it should be highlighted that Italy's public finances are currently characterized by **major imbalances in the distribution of revenue and expenditure** between the various levels of government. The central government, in fact, directly collects **52% of total public revenue**. This **percentage rises further to 78% if we consider tax revenue alone**, that is, the revenues used to finance public services, such as education, defence, justice, transport, as well as a significant share of the funding of the healthcare and welfare system. However, in the face of these enormous resources, the central government directly manages **only 24% of public expenditure** net of interest. By contrast, **local government manages 33% of primary expenditure, while relying on just 18% of public revenue.**

The evidence of this pathological deviation between a formally federal constitutional make-up and such a concentrated coordination of public finance has resulted in the decision to inquire further into the structure of the expenditure incurred by the central government, which can offer cognitive tools useful in the reform of Italy's general government, in line with more virtuous models based on comparative experience.

Particular attention has been devoted to the information available in the central government's financial report, by reconstructing the volume of expenditure for each Ministry, broken down by type of cost. Calculations showed that the actual expenditure for services by the central government stood at about **221 billion Euros** in 2012. **More than half of this aggregate is ascribable to the Ministry of Economy and Finance, which almost reaches 114 billion Euros**, followed by the Ministry of Education (45 billion Euros) and the Ministry of Defence (22 billion Euros). It should be noted that **personnel and intermediate consumption account for 98 billion Euros**: the remaining 123 billion Euros are distributed quite evenly between capital expenditure, transfers and other current expenses.

Despite the contrary opinion of those who say that one of the causes of the current inefficiency of general government is federalism, in our opinion, the data taken into account shows that **in Italy, the central government still manages national public finance and the federalization process is far from being completed.** The central government manages a significant share of public spending, which is empirically not the case in most federal countries.

In the last three years, central public expenditure in Italy, net of interest, amounted to an average of 23.9% of GDP. This value is even greater than that of a traditionally centralized country like France (20.8%), while all federal countries lie well below Italy. These gaps are even larger if we consider the public services directly managed by the central government. In order to approximate this aggregate, the expenditure for transfers to other levels of government was excluded from central primary expenditure (Regions, local government institutions, social security). In this way, France outranks Italy by far in 'actual' central expenditure with a value equal to 16.5% of GDP, but **Italy continues to rank before all other federal countries: its 'actual' central expenditure is equal to 10.8% of GDP**, compared with 8.9 % in Spain, 7.1% in Germany and 4.6% in Switzerland.

In addition, Italy stands out for the high percentage share of the **running costs** out of the total spending directly managed by central government. **This percentage reaches 70%,** against 29.7% in Germany, and **is equal to 7.5% of GDP,** as opposed to Germany's 2.1%. If Italy's central government were to allocate the same share of GDP to running costs as Germany and Switzerland, **it**

could save 82 to 85 billion Euros.

We could also add here one of the results of our previous working papers, i.e., **the almost 30 billion Euros in savings, which would result from applying the 'optimal level of spending' based on the Veneto model to all Italian regions**.

This data was further scrutinised by focusing on the spending of individual ministries, based on their accounting reports for the 2010-2012 period.

It emerged that in the three years considered the **sum of the running costs** and the costs for **operations and investment was reduced by 9,982 million Euros** (-2.3%). However, the savings were almost entirely at the expense of citizens and businesses, since the **reduction of running costs amounted to just 743 million Euros.** In addition, in almost all the Ministries, **the share of running costs out of the total increased to the detriment of the share of expenditure in operations/investment.** In particular, in 5 Ministries, the relative weight of the running costs varied between 40 and 60%; in addition, in 3 Ministries, every 1 euro spent in operations/investment cost more than 1 euro in terms of running costs.

The study also addressed the effects of the 'spread crisis' on the implementation of fiscal federalism in Italy.

It is clear that **the centralization of resources and the direct management of public functions by the central government are such that these are incompatible with a country with regional-based governance, let alone a federal make-up.** The consolidation of public accounts pursued since 2011 has seriously compromised local autonomy, creating major difficulties for local authorities as a result of the enormous effort that has been imposed on them.

The extent of this effort is obvious if one considers that, as a result of the cuts in the Finance Laws passed between the summer of 2011 and December 2012, **current expenditure was reduced by 34 billion Euros**, from 706 billion Euros budgeted in the autumn of 2010 to 671 billion recorded last spring. However, the distribution of these savings is heavily unbalanced and favours the central government. In percentage terms, in fact, **64% of the savings in public expenditure** in recent years **has been borne by local government, 19% by central government** and 17% by social security institutions.

On the revenue side, local revenues (**10 billion Euros**) have been diverted in recent years to central government and this gap will tend to grow further (central government +32 billion Euros; local government -12 billion Euros). In essence, between 2009 and 2012, local authorities increased their tax revenues by **16 billion Euros** in the face of cuts totalling **29 billion Euros**: **There was no substantial 'swap' between local taxes and transfers as promised by Law No. 42/2009.**

Obviously, these fiscal policy choices have greatly affected Italy's federal reform process, which in 2011, with the approval of the last decree implementing the fiscal federalism law, seemed at long last ready to open a new season in the financial and institutional relations between central government and local government.

In fact, the finance laws that have followed since then have **brought fiscal federalism to a stop** and not allowed it to yield the positive effects on public spending and administrative liability that were among the key principles and goals of this reform. On the contrary, the central government deemed it necessary to block fiscal decentralization and to consolidate the governance of public accounts, thus causing a **U-turn on the issue of local autonomy.**

1. Reducing public spending to boost investment*

1.1 Public spending and the legal and accounting shield of historic spending

Italy's public spending is a unique case among all OECD and EU countries from an institutional and regulatory perspective. There is extensive literature on its faults; perhaps the most on-target and straightforward diagnosis is that presented by the International Monetary Fund at the end of a mission in April 2007. It

'indicated among the particularly critical areas of the Italian budget system:

- an incremental approach in budget formation: the bulk of public spending is defined from year to year with marginal changes, without an in-depth review of the validity of spending programmes and with a poor correspondence between government priorities and budgetary choices;
- a lack of a clear medium-term orientation in the budget formation process;
- redundant preventive checks on the implementation of the budget, which limits flexibility in the use of financial resources by those responsible for spending, forcing them to attach greater importance to compliance with legal constraints rather than efficiency when delivering public services;
- a rather weak informative basis concerning the costs of the different spending programmes and their effectiveness in terms of results achieved;
- scarce attention to the results achieved with budget resources by political decision-makers, with particular reference to the results, and the costs of public spending programmes, as well as a system scarcely geared to account for results actually achieved.'[1]

There are structural anomalies whose scope and depth are such that they cannot be solved with minimal interventions and call for a radical reform. Let's have a look at these structural anomalies.

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* This chapter was written by Luca Romano.

[1] See Commissione Tecnica per la Finanza Pubblica, *Libro Verde sulla spesa pubblica 2007*, p. 104.

The budget is formed through an initial collection of data concerning financial requirements from Ministries, including the entities they control either directly or indirectly, thus reversing the conventional relationship between policy planning and the translation of the budget objectives set by the political actors in management and administrative terms (Parliament and especially the Government).

According to the IMF, the collection of requirements is of an incremental nature, absolutely lacks transparency and not only neglects the political objectives of planning, but also requires an increase in allocations based on historic spending parameters. The 'bottom-up' approach does not relate to civil society, citizens and local communities, but only to the local branches and central bodies of Ministries. A peculiar aspect of 'democracy' found solely at the administrative level is:

> 'The use of a 'top-down' approach: that is, a process, which starts from the setting of a target for the total aggregate of expenditure and then goes on to determine the allocations for the sub-items in such a way as to comply with the target (which contrasts with the 'bottom-up' approach in which the budget is derived from the sum or aggregation of all the requests from spending centres)[2];

The third anomaly, which is extremely well-known, but has never actually been eliminated, is the lack of tools to assess the effectiveness of reported spending and to measure the effects in macro-economic terms[3].

This lack of tools - which is actually dumbfounding if one considers how crucial ex-ante and ex-post evaluations are and the fact that these are required by governments, EU bodies at all levels and rating agencies to assess financial flows, but not by the Italian government - has led to tremendous consequences, whereby the so-called decade of public spending consolidation spanning from 1993 to 2003

> 'was pursued prevailingly by cutting interest on public debt and through the curbing of spending in public investment'[4]

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[2] Ibidem, p. 87.
[3] See Franco Zaccaria, *La spesa pubblica in Italia tra espansione controlli*, Franco Angeli ed., Milan 2005; Franco Reviglio, *La spesa pubblica*, Marsilio, Venice 2007; food for thought is also provided by Alberto Carzaniga, "Come riformare la Pubblica Amministrazione" in Luca Meldolesi (edited by), *Il Federalismo e le sue contraffazioni*, Guida, Naples 2011, p. 33 – 57.
[4] Zaccaria, cit, p. 161.

The difficulty that still persists in defining spending review plans that do not take the shape of outrageous cross-the-board cuts is due precisely to this fact, namely that the budgeting is carried out by aggregating expenditure requirements collected in an incremental manner based on historic spending, without any sort of assessment capable of ensuring some minimal independence[5] from the top echelons who run ministerial bodies.

> 'The 'systemic' nature of the problem of Italian public spending and the fact that many weaknesses appear to be common to all sectors of government lead to the conclusion that the resource allocation system and the formation of the government budget are basically inadequate. Some of the weaknesses to be remedied include: the not always complete transparency of the budget; the lack of a link between resources, priorities and objectives; resource allocation practices that rely excessively on the historical data and do not reward merit and results; the absence of a systematic review of the effectiveness and efficiency of existing policies; the scarce flexibility in the use of available resources; and finally the lack of a culture of accountability.'[6]

An analysis and a proposal for targeting cost savings to jump-start public investment can only start from here, from this huge constraint consisting of a 'white' coup by which the forming of the budget is in the hands of ministerial bureaucrats who have sealed off historic spending by means of a jungle of legislation so that

> 'The various spending programmes are still in place today as a result of a body of laws that has built up in the course of time, making it difficult to manage as well as to divert and target resources more efficiently in order to achieve targets.'[7]

That in fact prevents

'performance budgeting: namely, a budget in which the targets to be reached by every spending programme are clear *ex ante* and verifiable *ex post*, and where the link between resource allocation and results achieved is strong'[8].

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[5] An independent body is the logical corollary of the new wording of Article 81 of the Italian Constitution, which in 2012 introduced the obligation of a balanced budget. In theory, this omission could warrant recourse to courts of law because the formation of the government budget has serious shortcomings in constitutional terms.
[6] *Libro Verde*, cit. p. 87.
[7] Ibidem, p. 109.

It follows that the cycle of planning, management and control continues to be dominated by legal and accounting categories. Contrary to what is being maligned, Europe has not deprived the central government of the space to make political decisions. There is plenty of evidence at the level of EU institutions and Member States that it is possible to refocus administrative and control procedures to take results into account."[9]

This rather complicated introduction serves not so much as to shirk responsibility, but to explain the absurd nature of a proposal that: 1) bases cost savings on an assessment of the effectiveness of historic spending and 2) allocates savings to investment, one of the items most heavily hit by consolidation measures, because it entirely lacks the administrative protection that safeguards the running costs of the government budget.

Recently, Alberto Alesina and Francesco Giavazzi[10] have stigmatized the impossibility conjured up by Minister Saccomanni to cut public spending by 2.2% - i.e., 351 billion Euros net of interest on public debt, spending in pensions and public redundancy funds - to avoid an increase in VAT and the introduction of property tax on primary residences. In short, public spending is considered untouchable[11].

1.2 The first cracks: sectoral analyses

In the 2006-2008 period, under the Prodi II Government and Minister Tommaso Padoa Schioppa, the well-deserving effort of curbing government spending[12] failed to adopt the procedures outlined in the government's own

8 Ibidem, p. 104.

9 Paolo De Ioanna, *A nostre spese. Crescere di più tagliando meglio. La spending review nell'Italia sprecona*, Castelvecchi, Rome, 2013, p. 33 - 34. This expert says that "if you do not understand, master and manage appropriately the organizational ropes of the spending review, it appears to be very difficult to change the practices of the past," p. 31.

10 The two economists have even attacked the new State Accountant General, Daniele Franco, who has been unable to find where to make the cuts. See "*Coraggio, un taglio forte alla spesa*", Corriere della Sera, 16 June 2013.

11 The construction of this false myth has been uncovered only very recently by the pioneering work of Giuseppe Bortolussi, *Tassati e mazziati. Le tasse nascoste: quando lo Stato ci mette le mani in tasca due volte*, Sperling & Kupfer, Milan, 2011, Chapter 3, p. 105 – 141; Claudio Siciliotti, *Dare e Avere: Dall'analisi dei conti pubblici, una nuova stagione dei diritti e dei doveri*; Ipsoa, Milan, 2011.

12 In 2007, the Finance Law reorganized the Government Budget into missions and programmes and established the Technical Committee on Public Spending, chaired by Prof. Gilberto Muraro.

official documents to tear down the legal and accounting armour protecting historical spending. At least, however, the first cracks can be seen in the armour through the adoption of a criterion imposed from above. In April 2007, during a Cabinet meeting, Prime Minister Prodi outlined the five areas in which the spending review had to be conducted*:* Justice, Infrastructure, Interior, Education and Transport. It is worth noting these areas fall under the responsibility - though not exclusive - of the central government. Study groups were set up at the five ministries[13].

That project was not continued by the following Berlusconi and Monti governments and under the XVI parliamentary term the spending review was mainly directed at non-government spending items, such as healthcare, education and local government. However, the method is rather bizarre: although the Ministries are not directly empowered to integrate the spend analysis into their policies, nor to eliminate the regulatory muddle that underpins historic spending, the lever of savings is used to instruct them on how to carry out their functions.

It is a genuinely contradictory strategy, because it makes all functional structures of the central government fall under a form of accounting and financial supervision that becomes the real steering committee for all policies. In addition to emptying administrative spending structures of responsibility, the Ministries end up falling under a sort of 'receivership' and can no longer make 'policies' due to the overriding need to make savings.

Consolidation - which thus becomes sovereign - is executed through a very dangerous approach, by which the overarching criterion is purely technical and based on accounting, without any link, albeit weak, with policy-makers. This created a precedent, which was followed by a whole series of intrusions climaxed with the ECB's 'infamous' letter to the Italian government of 5 August 2011, which actually ousted national policy-makers from cost-saving procedures.

In addition to this sort of receivership from above - which is sovereign in cutting public spending - the 2006-2008 period of the XV parliamentary term was characterized by two other important government measures: the revision of the

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The Committee published a *Libro Verde sulla Spesa pubblica* - Green Paper on Public Spending (September 6, 2007) and, subsequently, the *Rapporto intermedio sulla revisione della spesa* - Interim Report on the Spending Review (13 December 13 2007).

[13] *Libro Verde*, cit. p. 108.

internal stability pact (2007) to reduce spending by local governments and the financing of certain public works sectors.

The implementation of a stability pact revised according to abstruse procedures[14], applied to the balance between the revenues and expenditure of municipalities, 'offers effective degrees of freedom to local and regional authorities, and it is necessary that they rely on an adequate autonomy to change the level of local levy.'[15] In other words, the application of the stability pact was supposed to be closely interdependent with the implementation of strong fiscal federalism. When asked how to cut debt, the President of the Technical Committee, Prof. Gilberto Muraro stated: 'By seriously implementing the fiscal federalism, which will be the real challenge of the next two years. Serious and full-fledged federalism is to replace a mere decentralization of functions and decisions taken centrally...'[16]

The second major line of action was to fund a program of strategic public works that had already been approved and included in the law called '*Legge Obiettivo*', but had not been fully funded yet.[17]

Let us draw the bottom line of a short parliamentary term that was nonetheless intense in its ambitions to consolidate public accounts, which between 2000 and 2006 had worsened greatly for two main reasons: the cost of debt service and the significant increase in the cost of general government employees.

More in detail, the most important measures of XV parliamentary term involved the formal creation of a higher level of accounting sovereignty, which pervades all functional aspects of spending, regardless of who the competent authority is, as in the case of local and health authorities.

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[14] "In detail, with reference to municipalities alone, the adjustments to be made by each municipality is calculated as the sum of the 2003-2005 three-year average of cash current expenditure multiplied by a specific annual coefficient (0.029 for 2007, 0.017 in 2008 and 0.013 in 2009) and, if negative (i.e., in deficit), the 2003-2005 three-year average of the cash balances (in absolute value) multiplied by a specific annual coefficient (0.33 for 2007, 0.205 in 2008 and 0.155 in 2009). This (possible) sum must then be compared with an amount calculated as 8% of the 2003-2005 three-year average of final cash expenditure: the adjustment (for 2007, 2008 and 2009) will be equal to the lesser of the two values. The net financial target to be achieved according to the ISP for the 2007-2009 period will then be calculated separately in terms of both cash and accrual, by summing the amounts of the adjustments made for each year at average balances by cash and accrual respectively, recorded in the 2003-2005 period." *Libro Verde*, cit. note 59, p. 102.

[15] Ibidem, p. 101. The 2007 Finance Law provided for the expansion of the additional income tax at municipal level and the transfer of the land registry function to the municipal level.

[16] These statements were made by Prof. Muraro in an interview to Alberto Gottardo, in "*Corriere del Veneto*", 14 September 2007.

[17] On investment, see MEF, *Politica economica e finanziaria. Glossario di due anni*, April 2008, p. 105 -116.

This austerity strategy aims to make allocations for public investment. Originally, the goal was to adopt the British spending review scheme, i.e., 'allocate additional resources to high priority programmes'[18].

In actual fact, no major priorities were set and some 'investments of no quality' were made, including the settlement of the debts of the Italian railways (FF.SS.). In the United Kingdom, the spending review was legitimised through a radical review of subsidies that allowed for the allocation of the resulting resources to social policies in the education and healthcare sectors.

By its own admission, the *Libro Verde* declares that austerity programmes are sustainable only by implementing 'sound and complete' fiscal federalism - which however remains though in a sort of limbo of good intentions.

This chasm created by consolidation strategies imposed from above and the lack of spending centres fully empowered through fiscal federalism will paradoxically end up penalising the most deserving. In the case of local authorities, the most heavily affected are municipalities in the Camposampiero area (Padua), who for a decade have worked on cutting costs to lower the tax burden, rather than to improve the balance.

This form of authoritarian austerity, devoid of parameters to measure true waste, i.e. standard costs, has led to a mock spending review*:*

> 'The spending review should be against cross-the-board cuts**...** There is no true spending review without standard requirements, and both the former and the latter lack any specific conclusive relevance for the purpose of determining the actual fiscal capacity of a local community.' [19]

In short, the work of Padoa Schioppa and Muraro started laying the foundations for a sectoral spending review, but completely missed both the objective of making spending centres accountable in a federal make-up, and, alternatively, the objective of allocating resources resulting from the spending review according to a new set of political priorities: the most deserving have been penalized by this approach in the healthcare sector, in local authorities, in education, and in a wide variety of local public services, including transport.

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[18] MEF – CTFP, *Rapporto intermedio sulla revisione della Spesa Pubblica*, December 13, 2007, p. 10.
[19] De Ioanna, cit. p. 40 - 41.

1.3 Tremonti's management and the dilemmas of fiscal federalism

The inauguration of the new government in the XVI parliamentary term, with Minister Tremonti, marked a clear change[20] from its predecessors. Law No. 196 of 2009 repealed the Technical Committee chaired by Gilberto Muraro and handed back the responsibility for oversight to the State General Accounting Office, thus eliminating any form of independent scrutiny, albeit feeble. The new Minister finally decided to make the formal structure of the State Budget compliant with European standards.

Tremonti's management had essentially two phases, the first before the debt crisis (2008-2010), during which the State Account General was assigned the task of conducting the review. This resulted in the huge report on the central government's spending (*Rapporto sulla spesa delle Amministrazioni centrali dello Stato* - 2009) and the launch of the COPAFF following the approval of Law No. 42 of 2009 on fiscal federalism.

The second phase, under the threat of speculative attacks on the Italian public debt, focused more on the spending review. A famous expert was called to the government headquarters in Rome to draw up a report, which however was followed by the hot summer of the spread crisis that made the political situation precipitate, leading to Mario Monti's technocratic government.

Minister Tremonti was perfectly aware of the burden of the legal-accounting system underpinning historic spending:

> 'There is rigidity, both in the budget formation process and in the management of resources, arising, for example, from the application of the criterion of current legislation in a context in which a substantial portion of expenditure is bound by laws and other parameters established by laws (about 93 per cent).'[21]

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[20] The criticism is spelled out in the Report's "Results": "The approach implied that the spending review would be entrusted to the public administration bodies concerned, who should streamline their procedures to comply with the new budgetary constraints by setting their own priorities and identifying the most effective and least productive expenditure items. This reaction of government bodies was not followed up to the extent expected," MEF, Rapporto sulla Spesa delle Amministrazioni centrali dello Stato. *Sintesi e conclusioni*, 2009, p. 2.

[21] Ibidem.

Secondly, he stigmatized the total lack of the use of reporting as a limit inherent in the purely formalistic and procedural management culture:

> 'Reporting is scarcely used either for the purpose of new budget programming or of the ex-post assessment of public spending. Some of these considerations contributed to the formulation of proposals that trickled into the bill to reform public accounting and finance currently being debated by Parliament'[22]

However, the real innovation of the XVI parliamentary term was the approval of the law on fiscal federalism, which was largely based on the Government report to Parliament called *Relazione sul federalismo fiscale* of 30 June 2010. It marks first and foremost an epistemological and cognitive break from the past: those responsible for allocating funds were no longer asked to provide for oversight; instead, an 'independent' observer was finally set up - namely, the COPAFF chaired by Prof. Luca Antonini and still in place - to start a herculean job of researching into how government money is spent.

The analysis finally focused on the disparities in the cost of goods and services, collecting details on spending made through 'transfers to regions and local authorities'. After Unioncamere Veneto's research into the fiscal residuum of Italian regions presented to the CALRE[23], the systematic study of regional and municipal spending marked the greatest revolution in the field of government public spending. More than sixty years after the foundation of the Italian Republic, it revealed the glaring absurdities linked to the differential costs of goods and services, the quantity and quality of the work performed by local general government employees, the allocations to in-house companies that are always in the red, and so on[24].

It is a shame that this timely and accurate clarification effort - which has already broken the taboo of historic spending, while still not managing to put in

[22] Ibidem.

[23] CALRE is the Conference of the Regional Legislative Assemblies of the European Union. In all, 74 regions from 8 countries belong to it. Together, these regions account for more than 200 million inhabitants. More specifically, CALRE consists of the parliaments of the Spanish communities, Italian regional councils, the federated states of Germany and Austria, the Portuguese regions of Açores and Madeira, Wales, Scotland and Northern Ireland in the United Kingdom, Åland Islands in Finland and Belgium community and regional chambers.

[24] An annotated compendium of all this can be found in Luca Antonini, *Federalismo all'italiana. Dietro le quinte della grande incompiuta*, Marsilio, Venice, 2013. It should however be noted that there is very little available on the web about sectoral analyses on standard costs.

place the fiscal mechanisms of Law No. 42 - was made by a company outside the scope of general government[25], and, therefore, is not an independent institutional body, like an authority, as provided for by constitutional law. How is it possible that the MEF, Banca d'Italia and the National Audit Office have not been able to put together an assessment body to perform this task, with the scientific and institutional legitimacy called for by such a significant public interest?

However, the greatest problem of Law No. 42 on fiscal federalism is the logic behind the regulatory architecture. In fact, centralization of the assessment on standard costs is linked to a precise provision by which the responsibility for levy lies with local authorities; in other words, it is a responsibility limited by the fact that the savings that a region or a municipality were to realize between the amounts collected and expenses, are taken by the central government for equalizing purposes and nothing is left to the body making the saving.

This is not fiscal federalism, but only a measure of public finance that adopts the parameter of standard costs in place of the manifestly scandalous parameter of historic spending. Having granted local government the power to collect and not that of saving one's own resources as a result of efficiency will definitely lead regions and municipalities to align expenditure with tax revenue, so as not to be deprived of resources due to equalizing purposes that risk reproducing current distortions.

1.4 Monti and Giarda's spending review: the return to the twilight zone

Many observers on both sides of the political spectrum agreed that by tossing fiscal federalism out the window, silencing the revolution of standard costs and returning to the oblivion of the spending review in genuine Padoa Schioppa/Muraro style, the Monti Government turned back time: re-creation of large expenditure aggregates, indiscriminate horizontal cuts, penalties for local

[25] For this purpose, the COPAFF appointed SOSE, a private company that already prepared the estimates of the sector surveys for the MEF.

general governments and[26] the return of obscure public spending by the central government.

The extensive research studies produced by the Minister for Relations with Parliament, Piero Giarda, which had been anticipated by both a full-bodied academic essay[27] and by the aforementioned report published in May 2010 on behalf of the MEF under Tremonti[28], take on the shape of documents coming directly from the government.

The new technocratic minister also noted that 1) the flow of expenditure is determined on the basis of administrative criteria separated from programming by political authorities:

'The changes in the mix of collective consumption spending (the heart of the central government's allocative function) have never been expressly defined by documents or decisions expressly qualified as strategic choices on the composition of the supply of collective consumption goods for the population'[29]

2) The destination of the flows from the 'centre' to local communities is not determined by standard criteria, but in an absolutely random and unverified way:

> 'Currently, all the regional and local authorities, regardless of the income level of their citizens or of the economic activity carried out in their territory, are funded - though to a different extent - by state transfers, which take the form of devolved government tax revenues produced locally or of direct transfers from the central government's budget based on allocation criteria that are predominantly inspired by some sort of principle based on requirement'.[30]

What the Minister states is terribly serious: it means that certain amounts of central government tax revenues can be allocated to the local communities using

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[26] Some, such as the measure concerning healthcare in the Lazio Region, made by Enrico Bondi after the budget had already been approved, were so technically inept as to worsen the situation that was supposed to be fixed. Cf. De Ioanna speaking of "brutal and retroactive outcomes" cit, p. 39.

[27] Piero Giarda, *Dinamica, struttura e governo della spesa pubblica: un rapporto preliminare*, Università Cattolica del Sacro Cuore, Quaderni dell'Istituto di economia e finanza, No. 104, September 2011.

[28] Piero Giarda, "Bilancio e patrimonio pubblico", report for trade unions and employers' associations participating in the working table for fiscal reform submitted to Minister Tremonti on 18 May 2011.

[29] Piero Giarda, *Dinamica*, cit. p. 28 – 30.

[30] Ibidem, p. 40.

methods that are not regulated, like a sort of ATM machine, thereby settling the debts of frighteningly indebted bodies:

> 'Decisions on public expenditure do not normally incorporate procedures that will impose the comparative evaluation of the benefits of the various activities financed with taxes or debt.'[31]

3) The 'driving forces' of growing expenditure are healthcare, general administration and environmental expenditure[32]. While the two entries relating to healthcare and the environment, especially in relation to catastrophic events, are in line with European and international trends, the presence of the item 'General Administration' contrasts with the situation in all other countries with characteristics similar to Italy's.

In conclusion, Giarda asks:

> 'How can a political and administrative system remedy the absence of direct indicators of whether there is little or no public interest in a particular spending program? (**...**) In any case, the public sector is in need of radical decisions to remedy allocative inefficiencies that are present in the production of public services as well as legislative and management inefficiencies in many spending areas with redistribution purposes.'[33]

The scholar's considerations are extremely accurate and meaningful. Then, however, the rising pressure on the Monti government, installed in November 2011 in the face of risk of default of the entire country, led to much more conventional choices. The Stability Law made 3.7 billion Euros in cuts in 2012, 10.5 billion in 2013 and 11.2 billion in 2014, in addition to 4 billion Euros in cuts to local authorities, and confirmed the 15 billion Euros in cuts made by Tremonti for the 2012-2014 period.

This marked the traumatic conclusion of twenty years of strategies intended to govern public spending. No effort has ever been made to set up an independent authority to control spending as provided for in the Constitution. The monopoly of information of the State General Accounting Office that has consolidated over

[31] Ibidem, p. 46.
[32] Ibidem, p. 43
[33] Ibid., p. 52 and p. 68.

the decades was confirmed[34]. There has been no success in scathing the legal and accounting armour surrounding historic spending, a layered sedimentation, 93% of which is built on existing laws, which no one is able to - or better - wants to dismantle. This constraint is so intrusive that it prevents the restoration of a proper hierarchy of command between government policy-makers, who decide how to allocate resources, and administrators below them.

Spending reviews without standard costs have resulted in indiscriminate cuts. When the standard costs will be put in place, fiscal federalism will have to follow, bearing in mind that incomplete accountability is another huge stumbling block which risks perpetuating the current distortion of the spending postings through 'equalization'.

1.5 Reducing public spending, saving and investing in growth

In an extremely interesting contribution, Carlo Bastasin was very convincing in explaining that the success of the German model lies in something that goes beyond the competitiveness of its enterprises in the context of globalization. In Germany, too, businesses are suffering from a lack of profitability and investment. It is not just an Italian feature. Similarly, Italian firms, as unequivocally documented by Marco Fortis, are faring well in international trade.[35]

The other pillar of success is 'net domestic savings', obtained through a federal institutional make-up and accountability of local communities. This net saving, in fact, is achieved by the same entities who then make the public and private investments needed to foster growth. Before the crisis and, a fortiori, after it broke out, the main item through which Germany accumulated its net domestic savings was the reduction of the costs of central government and of the public expenditure it directly managed. Exactly the opposite is happening in Italy: at the moment when the legal and accounting protection around historic public

[34] De Ioanna, *A nostre spese*, cit. p. 57.
[35] Carlo Bastasin, "Germania: il miracolo economico", in Luca Paolazzi and Mauro Sylos Labini (edited by), *L'Italia al bivio. Riforme o declino: la lezione dei paesi di successo,* Luiss University Press, Rome, 2013, p. 195.

spending had started to crack, conservative forces succeeded in confining this change to local authorities. Once again, a purely technocratic government has covered up central public spending, which has steadily grown for both personnel and current expenses concerning 'general administration'.

The result is three boulders on the road to growth: not making spending centres accountable for taxation, not rewarding those who know how to save through more efficient public facilities and a better organized civil service, and not knowing how to evaluate the effects of expenditure in relation to the political planning of investment. A paralysis of accumulation is likely to swallow up Italy's industrial system; as Prof. Alberto Quadrio Curzio stresses, recovery can come only if it is set in motion. The prerequisite is public investment with strong impact on the market.

2. From the Periphery to the Centre: the effects of the latest budget laws on local government*

2.1 The effects of the spread crisis on central and local public spending

An attentive study of the recent trend of the economic and political situation in Italy shows that the month of July 2011 marks one of the watershed moments in the financial and institutional relations between centre and periphery. That month saw a symbolic 'changing of the guard' between a federalist perspective and a centralist practice. Later, on 28 July 2011, the Council of Ministers approved the eighth and final decree implementing the Delegated Law of 2009 (save for amendments), namely the one concerning the reward and sanction mechanisms for regional and local authorities. However, it went almost unnoticed: for several weeks, the country was facing 'the spread emergency'. The growing gap in the yield of Italian government bonds versus German bonds was the clear signal - underscored by the following downgrades by rating agencies - of the negative judgment of financial markets concerning Italy. In fact, Italy, burdened with an enormous public debt[36], was sliding towards unreliability with an increased risk of insolvency. The Government had to hastily pass two finance laws in just a month and a half (Decree Law No. 98/2011 and Decree Law No. 138/2011).

However, these efforts were not enough: in the autumn, the spread continued to rocket reaching as high as 553 basis points on November 9th. Italy became the 'sick man of Europe' and the situation seemed so delicate as to fear even the very fate of Euro zone[37].

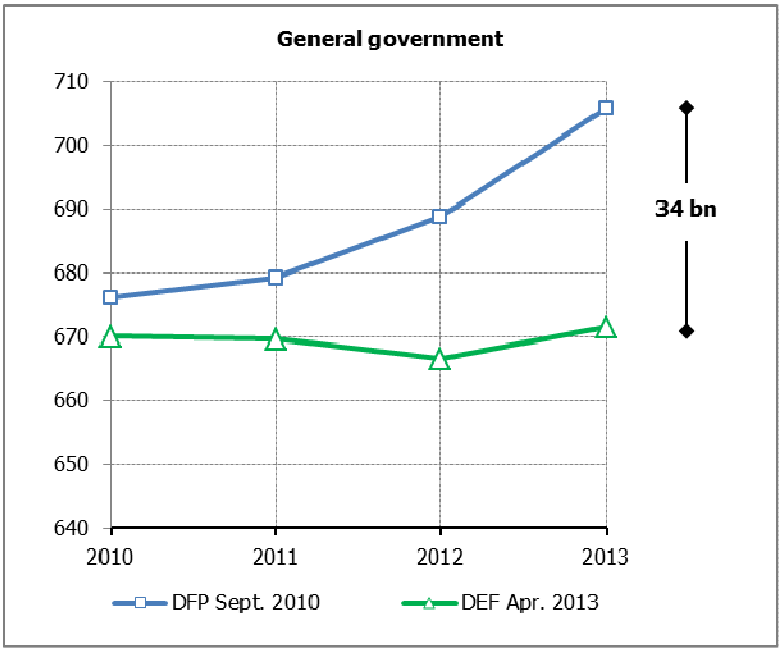
* This chapter was prepared by Centro Studi Sintesi based on statistics available as of 20 September 2013.

[36] Bellati G.A. – Crosta R., *Il federalismo contro la crisi. Perché la riforma federale ci salverà*, Marsilio, 2013.

[37] Bellati G.A. – Crosta, R., cit.

At the end of 2011, the change of government led to a further finance law ('Save Italy' Law); public finances had to be further corrected during 2012 with the decree on the spending review and the Stability Law. The closing of the excessive deficit procedure against Italy last May granted some leeway, which was used to launch measures such as the faster payment of amounts owed by the government to businesses (Decree Law No. 35/2013). However, the outlook for the end of 2013 and for 2014 remains uncertain: the recent memo updating the DEF (20September 2013) shows the progressive deterioration of the economy, an element that has brought the deficit/GDP ratio back to alarming levels.

Chart 2.1 - *Public spending estimates* during the crisis (in billion Euros)*



NB: DFP, Public Finance Document; DEF, Economic and Financial Document
(*) Current expenses excluding interest
Calculated based on ISTAT and MEF data

Starting from July 2011, the spread crisis has required a considerable effort to fix national public accounts, which has led to an increase in revenue and a reduction in public spending. In particular, a comparison of the Public Finance Document (DFP) of September 2010 with the Economic and Financial

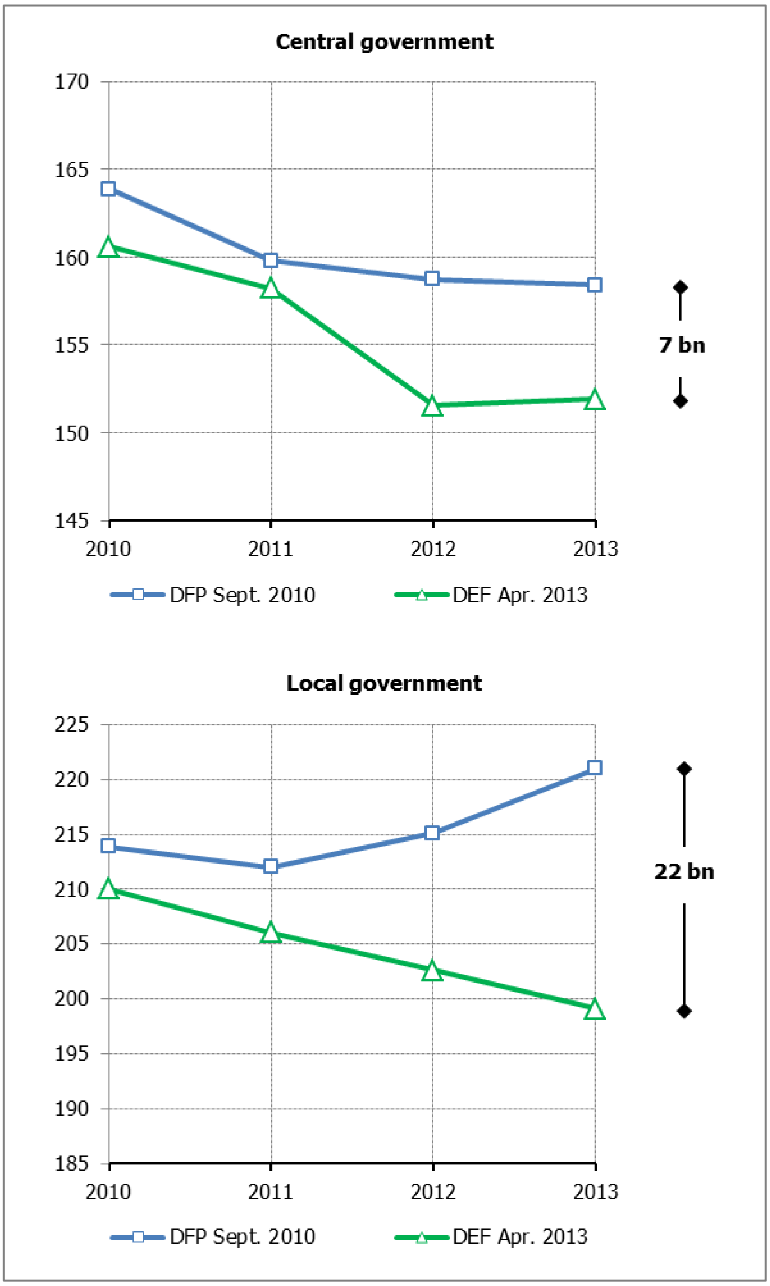
Document (DEF) of April 2013 clearly shows the extent of the effort in terms of reduction in public spending. With reference to current spending excluding interest referred to 2013, it should be noted that the value indicated in the DEF of April 2013 is about 34 billion Euros less than that stated in the DFP of September 2010[38]. In other words, as a result of the cuts made by finance laws passed between the summer of 2011 and December 2012, **current spending was reduced by 34 billion Euros**, from 706 billion Euros provided for in the autumn of 2010 to 671 billion Euros recorded last spring (Chart 2.1 and Tab. 2.1).

However, a more in-depth analysis of the documents shows that **the savings in expenditure of central government amounted to just 7 billion Euros;** most of the financial effort is attributable instead to local government, which registered a **cut in current expenses** of approximately **22 billion Euros** compared with forecasts made 30 months before (Chart 2.2): the trend in local expenditure registered a significant decrease from 221 billion Euros provided for by the DFP in September 2010 to 199 billion Euros in the DEF of April 2013 (Tab. 2.1). Completing the picture, social security agencies contributed about 6 billion Euros to the containment of primary current spending.

In percentage terms, the brunt of the savings in public spending in recent years can be broken down as follows: 64% **by local government**, 19% by the central government and 17% by social security (Chart 2.3). With respect to **investment**, the reduction for general government as a whole in 2013 was just 1.2 billion Euros: however, while it grew for central government (+1.9 billion Euros), **local government registered a significant decrease, amounting to 3.1 billion Euros** (Chart 2.4).

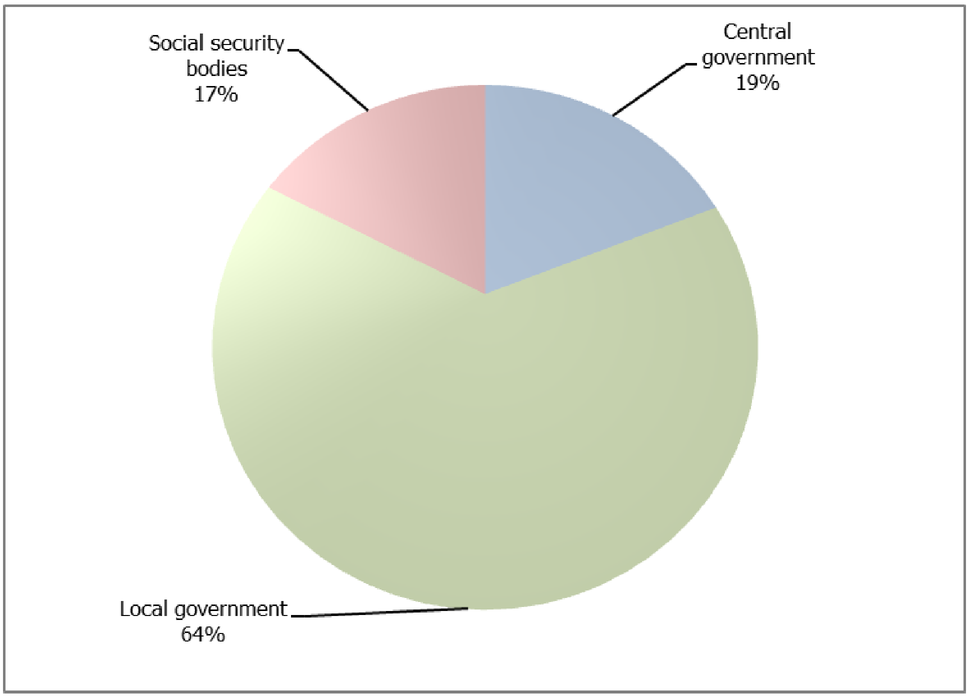
[38] As a result of the recent memo updating the DEF (September 2013), savings in spending in 2013 can be estimated at approximately 33 billion Euros; however, the document does not provide updated data by level of government, which could be useful for the purposes of this analysis.

Chart 2.2 - *Public spending estimates* during the crisis (in billion Euros)*



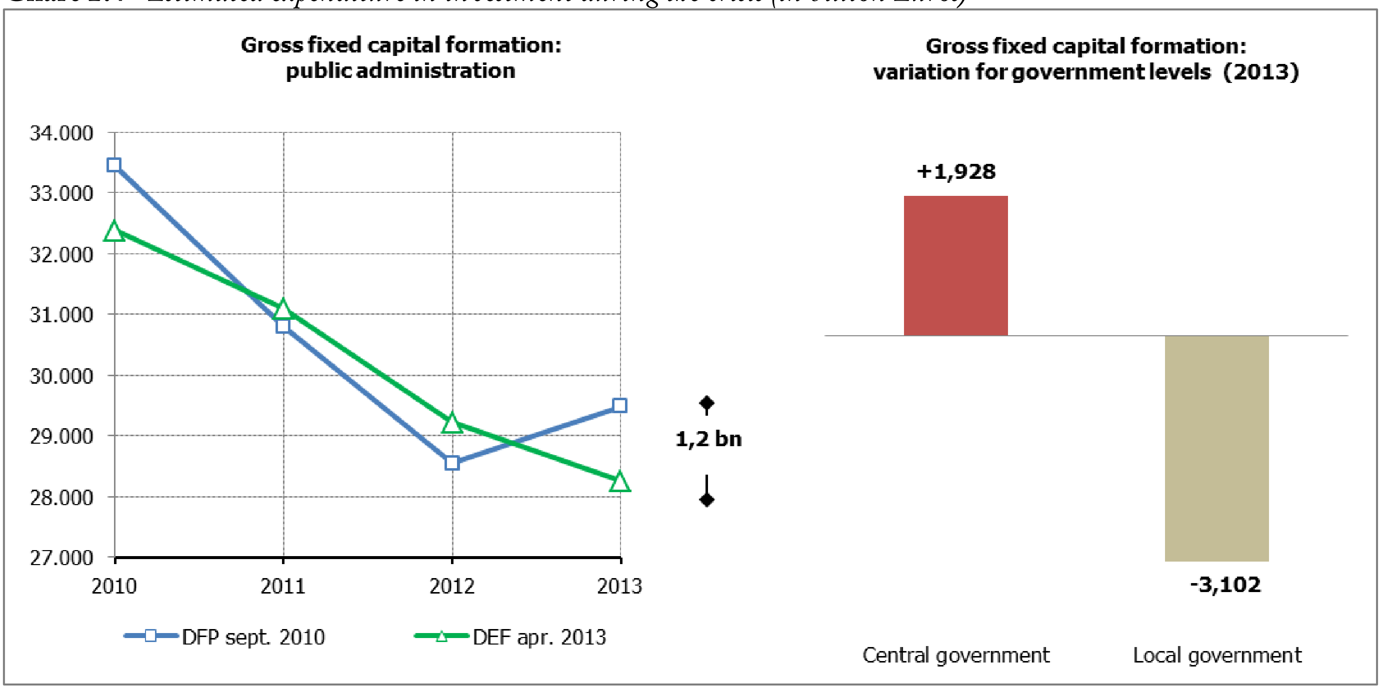
NB: DFP, Public Finance Document; DEF, Economic and Financial Document
(*) Current expenses excluding interest and resource flows to other levels of government
Calculated based on ISTAT and MEF data

Chart 2.3 - *Contribution to the reduction of public spending* of the main levels of government in the 2010-2013 period*



(*) Current expenses excluding interest and resource flows to other levels of government
Calculated based on ISTAT and MEF data

Chart 2.4 - *Estimated expenditure in investment during the crisis (in billion Euros)*



Calculated based on ISTAT and MEF data

Tab. 2.1 - *Contribution to reducing public spending* by the various levels of government during the crisis (in billion Euros)*

	2010	2011	2012	2013
(A) Situation as at September 2010				
Total GG, of which:	**676**	**679**	**689**	**706**
Central government	*164*	*160*	*159*	*158*
Local government	*214*	*212*	*215*	*221*
Social security bodies	*298*	*307*	*315*	*326*
(B) Situation as at April 2013				
Total GG, of which:	**670**	**670**	**667**	**671**
Central government	*161*	*158*	*152*	*152*
Local government	*210*	*206*	*203*	*199*
Social security bodies	*299*	*305*	*312*	*320*
(B-A) Difference in estimates				
Total GG, of which:	**-6**	**-10**	**-22**	**-34**
Central government	*-3*	*-2*	*-7*	*-7*
Local government	*-4*	*-6*	*-13*	*-22*
Social security bodies	*+1*	*-2*	*-3*	*-6*
Contribution to the reduction of spending				
Total GG, of which:	*100%*	*100%*	*100%*	*100%*
Central government	*53%*	*16%*	*32%*	*19%*
Local government	*62%*	*62%*	*56%*	*64%*
Social security bodies	*-15%*	*21%*	*11%*	*17%*

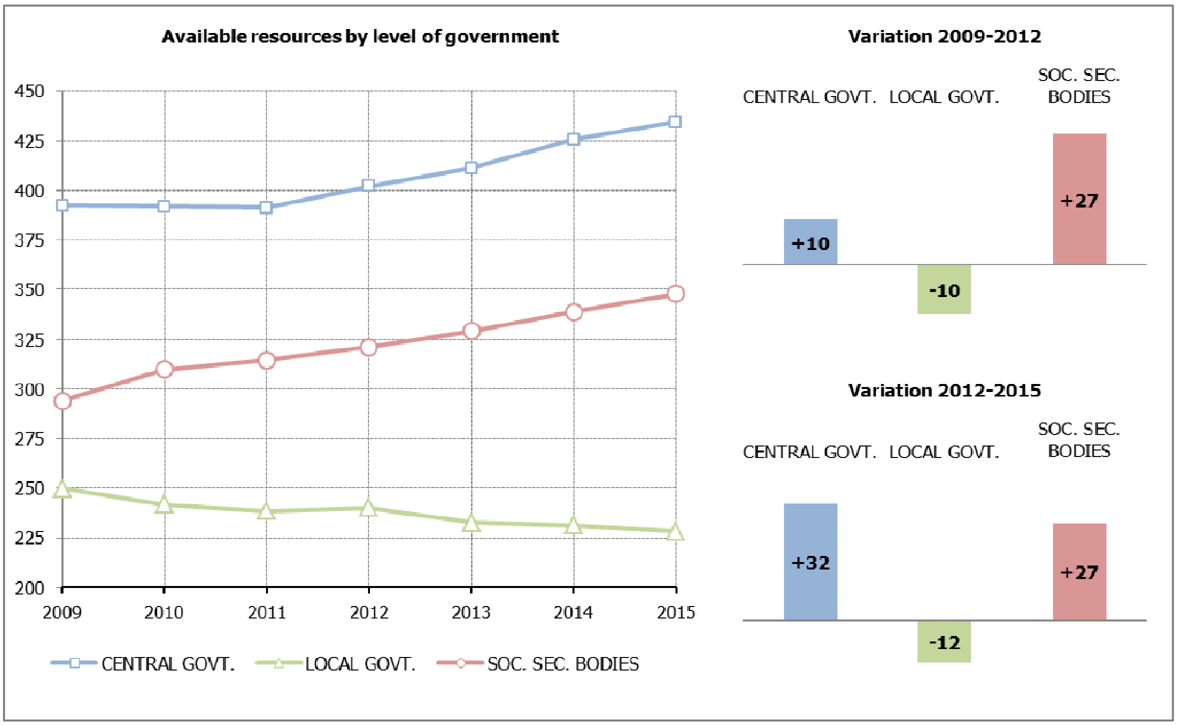
NB: A) Public Finance Document (DFP 2011-2013); (B) Economic and Financial Document (DEF 2013); GG= General Government
(*) Current expenses excluding interest and resource flows to other levels of government
Calculated based on ISTAT and MEF data

2.2 'Stolen' autonomy: toward a re-centralisation of spending

The finance laws, approved as a result of the spread crisis, have contributed to bringing the fiscal federalism reform process to a halt: in fact, it has not been able to yield the positive effects on public spending and administrative liability that were among the key principles and objectives of this reform. Obviously, with the winds of crisis, it was deemed appropriate to freeze fiscal decentralization and strengthen the governance of public accounts by the central government. Regions and local authorities have suffered a huge reduction in the resources allocated for the implementation of fiscal federalism; they have had to make do with the tightening constraints of the domestic Stability Pact, with negative consequences in terms of budget rigidity; they have had to raise local tax rates primarily to cope with the cuts in transfers and to meet the financial targets imposed by national legislation. The laws at central government level have intervened several times on local fiscal autonomy, creating fiscal hybrids, which have particularly affected the taxpayer: suffice it to mention here the share of IMU, the property tax, due to the central government and the automatic increase in the base rate of the regional surtax on the IRPEF income tax.

In addition, the available data confirmed not only that the federal reform process has come to a halt, but that there has actually been a reversal along the path to local autonomy. In fact, since the launch of the federal reform in 2012 (latest final results) **central government revenues increased by 10 billion Euros**, and those of social security institutions by 27 billion; instead, **the resources at the disposal of local government have been cut by 10 billion Euros**. In practice, a substantial exchange between local taxes and transfers as provided for by the delegated law on fiscal federalism has not occurred and **there has actually been a 'centralization' of local revenues** (Chart 2.5).

Chart 2.5 - *Trend and projection of revenues by level of government (billions of Euros)*

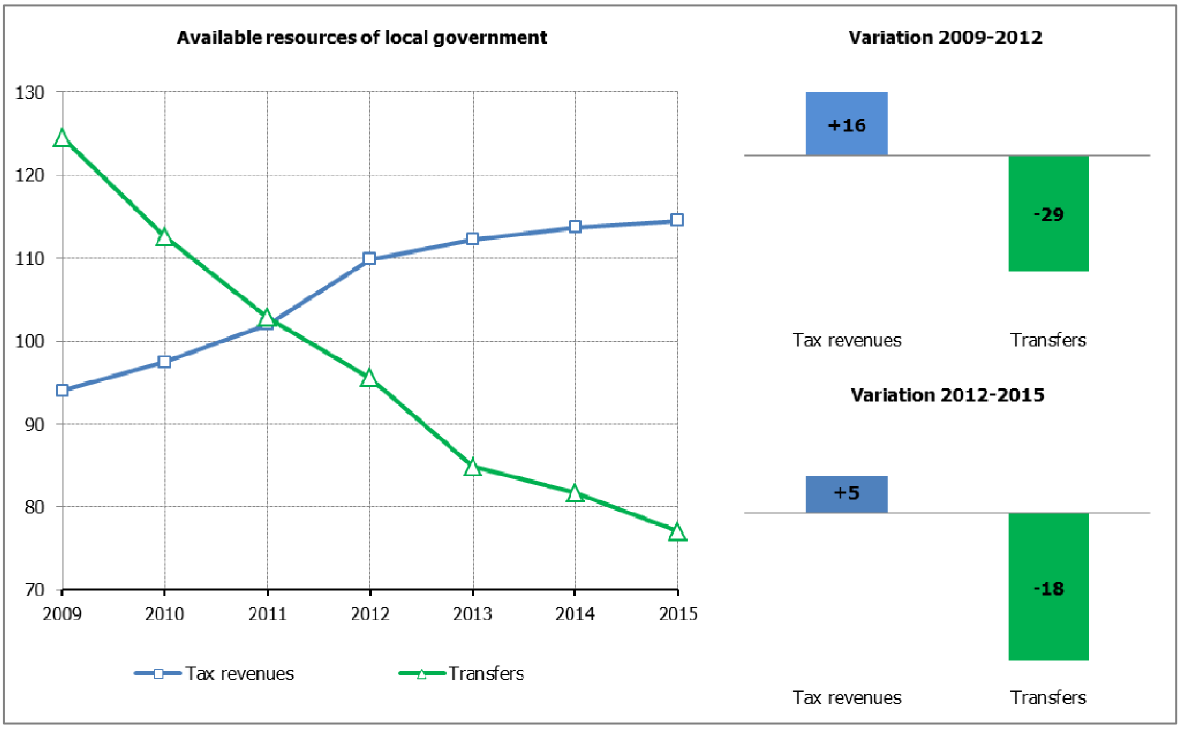


Calculated based on ISTAT and MEF data

Forecasts for future years indicate a consolidation of the current trend. In 2015, government revenues are expected to grow by 32 billion Euros over 2012, while the available resources for social security agencies will increase to 27 billion Euros. By contrast, the revenues of local government, based on available public finance data, will drop by another 12 billion Euros between 2012 and 2015. **In the whole period of time considered (2009-2015), regional and local authorities will witness an erosion of available resources estimated at around 22 billion Euros.**

However, against the backdrop of decreasing resources at the local level, the proceeds from local taxes will increase in order to compensate for the cuts to transfers made primarily by the central government (Chart 2.6 and Tab. 2.2). In the 2009-2012 period, the local government has increased its tax revenues (**+16 billion Euros**), but this increase has not been sufficient to fully make up for the cut in transfers (**-29 billion Euros**). If the regulatory scenario remains unchanged, the trend in the coming years will probably be characterized by **a weakening of the fiscal capacity of local government**, probably due to saturation of the room for manoeuvre on tax rates, and to a further drop in transfers as a result of the **coming into force of the cuts** to be made to the Italian national health fund and to local authorities pursuant to the finance laws approved in the 2011-12 period (Tab. 2.3).

Chart 2.6 - *Trends and projections for local authorities (in billion Euros)*



Calculated based on ISTAT and MEF data

The high degree of institutional uncertainty allows forming only a very tentative picture of the future financial and institutional relations between centre and periphery. Murkiness and a lack of a stable and comprehensive vision of the relationship between the central government and local authorities have negative effects in particular on communities and taxpayers. By way of example, it is worth pointing out that to date (September 2013) the deadline for the approval of budgets for the current year is set at 30 November, but municipalities still do not know where the cuts established by the spending review (2,250 million Euros) will hit, nor do they know which use will be made of the Municipal Solidarity Fund; also general guidelines on the service tax (which should take effect on 1 January 1 2014) are totally missing.

Tab. 2.2 - *Trend in available revenues by level of government (billions of Euros)*

	2009	2010	2011	2012	Var. 2012/2009
CENTRAL GOVT.					
Tax revenue	350	354	357	366	+16
Transfers	14	9	6	8	-6
Other revenue	29	29	29	28	-0
Total revenues	***392***	***392***	***391***	***402***	***+10***
LOCAL GOVT.					
Tax revenue	94	97	102	110	+16
Transfers	125	113	103	96	-29
Other revenue	31	32	34	35	+3
Total revenues	***250***	***242***	***238***	***240***	***-10***
SOCIAL SECURITY INSTITUTIONS					
Social security contributions	209	210	213	213	+4
Transfers	83	98	99	106	+23
Other revenue	3	2	2	2	-0
Total revenues	***294***	***310***	***314***	***321***	***+27***

Calculated based on ISTAT and MEF data

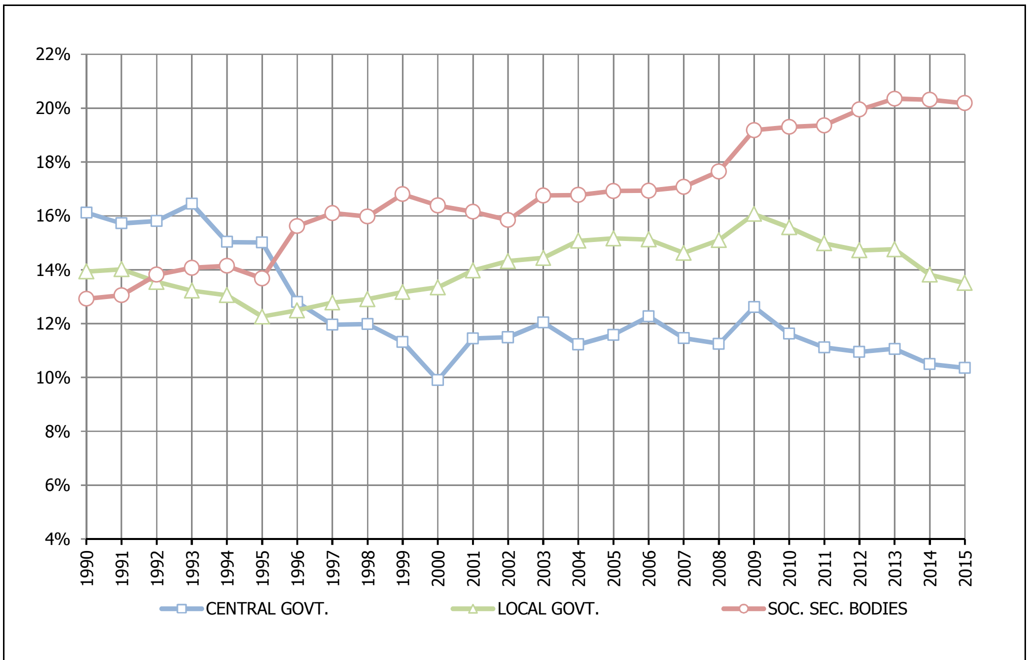
Tab. 2.3 - *Trend in available revenues by level of government (billions of Euros)*

	2012	2013	2014	2015	Var. 2015/2012
CENTRAL GOVT.					
Tax revenue	366	369	385	398	+32
Transfers	8	13	12	8	+0
Other revenue	28	29	29	29	+1
Total revenues	***402***	***411***	***425***	***434***	***+32***
LOCAL GOVT.					
Tax revenue	110	112	114	115	+5
Transfers	96	85	82	77	-18
Other revenue	35	36	36	37	+2
Total revenues	***240***	***233***	***231***	***228***	***-12***
SOCIAL SECURITY INSTITUTIONS					
Social security contributions	213	217	221	228	+15
Transfers	106	110	115	117	+12
Other revenue	2	3	3	3	+0
Total revenues	***321***	***329***	***339***	***348***	***+27***

Calculated based on ISTAT and MEF data

The data in the Government's public finance documents can provide, in any case, a useful framework of reference. In 1990, the distribution of public expenditure by level of government was very different from today's: the central government used to manage 16.1% of national GDP, local government 13.9 % and social security institutions 12.9%. Things changed significantly in the following years: from 1996, in fact, social security institutions accounted for the largest share of primary public expenditure (net of interest), which has now reached 20% of GDP (Chart 2.7).

Chart 2.7 - *Trend and projection of consolidated public spending by level of government (% of GDP)*

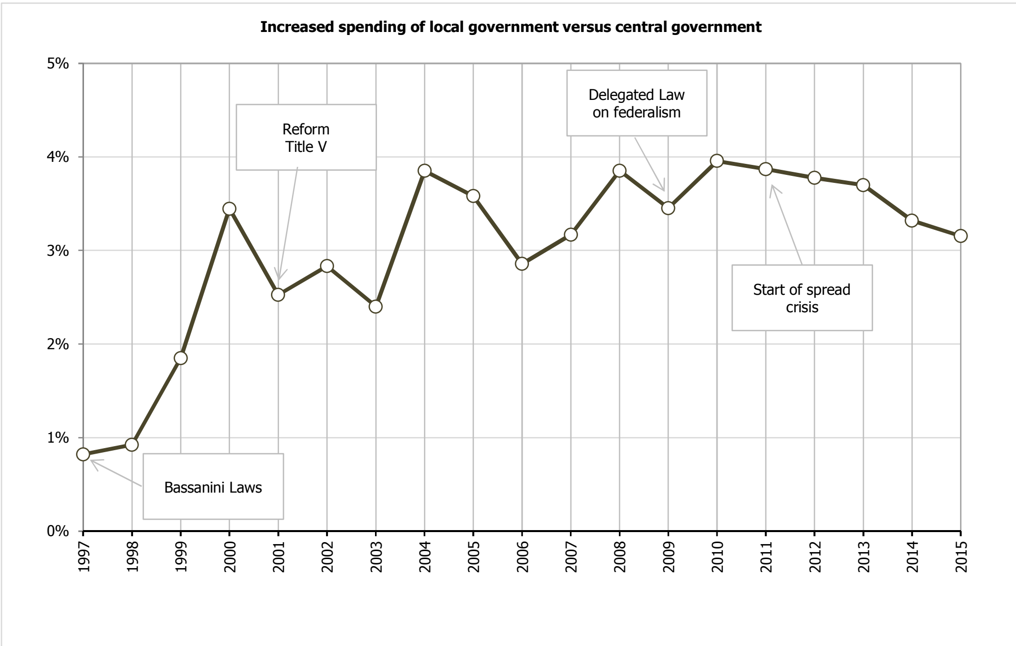


NB: Public expenditure net of interest and resource flows to other levels of government
Calculated based on ISTAT and MEF data

The following year (1997) came another change, with local government overtaking the central government: these were the years in which important functions (particularly, healthcare) were decentralized and local authorities were granted significant powers in terms of fiscal autonomy (IRAP, IRPEF surtax). The share of spending managed by regional and local authorities grew progressively in the following years and topped in 2009 (16% of GDP); by contrast, the scope falling under the competence of the central government shrunk until 2000, the year in which it fell below 10% of GDP (9.9%), and then plateaued around 11-12% in subsequent years.

However, since 2010, a slow but unrelenting **process of re-centralisation** of public spending has been under way, paradoxically in the very years in which the first steps towards fiscal federalism were being made. The spread crisis and following finance laws led to the downsizing of the weight and relevance of local government in the overall context of public spending. In 2010, local spending exceeded central spending by 4 percentage points of GDP (15.6% vs. 11.6%): with the current trend, this differential will decrease progressively to 3.2 points of GDP in 2015 (13.5% vs. 10.4%). This means that **local spending will decline much faster than central spending** (Chart 2.8).

Chart 2.8 - *The Centre-Periphery differential shrinks with the crisis (% of GDP)*



Calculated based on ISTAT and MEF data

A confirmation of the current trend of consolidation of central powers comes from the findings of the **Constitutional Reform Commission**, established on 11 June2013 to make proposals for the reform of the second part of the Constitution. The final report of September 17th included the proposal to return **some areas currently falling under the concurrent jurisdiction of the**

central government and regional authorities to the exclusive competence of central lawmakers: the document makes express reference to 'large transport and navigation networks', 'production, transport and national distribution of energy' and 'communication' and also suggests considering placing other areas currently managed by regional authorities under the competence of the central government.

Moreover, there is a special **safeguard clause** that would allow the central government to constantly intervene in matters of regional competence within the limits required by the safeguard of legal or economic unity, the implementation of programmes of national interest and major economic and social reforms. It is a proposal that can be agreed upon in principle but which, given precedents, **could legitimate the power of central government in its continued effort to downsize the role of local authorities**, putting an end to the fiscal federalism reform.

3. Spending differentials at central level: analysis by function and comparisons at European level*

3.1 Powers and resources of central government in Italy

The previous chapter highlighted the recent trends resulting from the latest finance laws that are progressively changing and centralizing the make-up of Italy's public finances. The federal reform, approved by Delegated Law No. 42/2009 and amended by subsequent implementing decrees, was supposed to consolidate the fiscal autonomy of regional and local authorities, to be accomplished also through the 'taxation' of government transfers. In other words, the extremely centralized Italian taxation system was supposed to be balanced in favour of local government, so as to complete spending decentralization as per the provisions of the reform of Title V of the Constitution.

Currently, Italian public finances are characterized by a **major imbalance in the distribution of revenue and expenditure** between the various levels of government. In fact, the central government collects directly 385 billion Euros, equal to 52% of the 736 billion Euros of total public revenue (Tab. 3.1 and Chart 3.1); **the percentage of central cash receipts rises further up to 78% considering tax revenue alone**, that is to say, the revenues needed to finance public services such as education, defence, justice, transport, as well as a significant share of the funding of the healthcare and welfare system. However, in the face of these enormous resources, the central government manages directly **just 24% of public expenditure** net of interest (Tab. 3.1 and Chart 3.2): the sphere of competence of central government covers mainly defence (100%), law enforcement and security (88%) and education (74 %).

* This chapter was written by Centro Studi Sintesi, based on the statistical data available as at 20 September 2013.

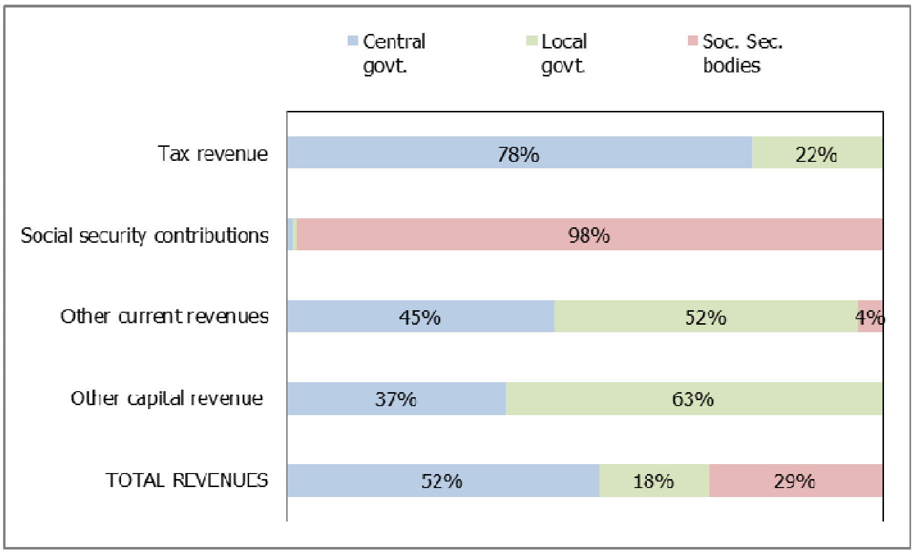
By contrast, **local government manages 33% of primary expenditure and can rely just on 18% of public revenue.** It should be noted that local government prevails over the central government in multiple functional areas, such as healthcare (99%), recreational, cultural and worship activities (89%), land use (83%), environmental protection (72%) and economic affairs (58%); the local government also holds significant shares of spending in general services (47%) and education (26%).

Tab. 3.1 - *Consolidated revenues and expenditure by level of government (year 2011, billions of Euros)*

	Central Govt.	Local Govt.	Social Sec.	Gen. Govt.
REVENUES				
Tax revenue	354	101	-	455
Social security contributions	2	1	213	217
Other current revenues	27	31	2	60
Other capital revenue	2	3	-	4
Total revenues	***385***	***136***	***216***	***736***
EXPENDITURE				
General services	34	30	-	64
Defence	25	-	-	25
Law enforcement and security	29	4	-	33
Economic affairs	27	37	-	64
Environmental protection	2	6	-	9
Homes and land use	2	10	0	12
Healthcare	1	114	0	116
Recreational, cultural and worship activities	1	7	-	8
Education	49	17	-	66
Social security	6	12	305	323
Total expenses *	***176***	***238***	***306***	***720***

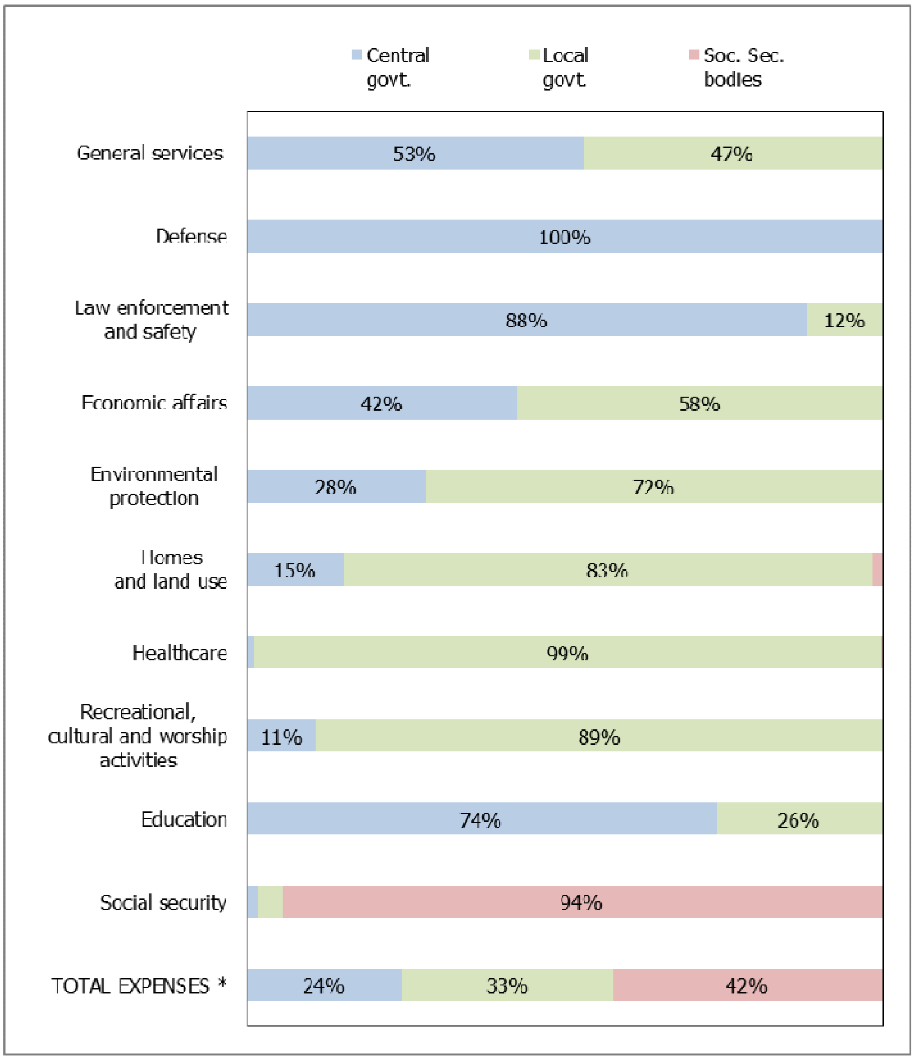
(*) Net of interest
Calculated based on ISTAT data

Chart 3.1 - *Where the resources come from... (year 2011, billions of Euros)*



Calculated based on ISTAT data

Chart 3.2 - ... *and how they are used (year 2011, billions of Euros)*



(*) Net of interest paid
Calculated based on ISTAT data

The imbalance in the distribution of resources, powers and responsibilities is clear: while it is true that the central government has always intervened ensuring the financing of local functions through transfers, it is also true that in recent years the resources to local authorities suffered remarkable cuts. The finance laws approved between the summer of 2010 and the end of 2012 have so far led to a **reduction in resources to regional and local authorities amounting to approximately 15 billion Euros**, plus an additional 10 billion Euros of indirect cuts due to tighter provisions of the Internal Stability Pact.

This report focuses on the role of central public expenditure within an institutional make-up like Italy's, which is struggling to find a consolidated balance between the central and local government, blocked by countless internal contradictions, among which the fact of having a formally federal Constitution and centralized coordination of public finance. In addition, as discussed above, the recent finance laws are based mainly on the reduction of local spending and only to a much lesser extent on cuts to central government. A detailed analysis of the structure of spending by the central government in Italy is therefore needed to gain insights that can be useful in the review and reorganization of Italy's general government.

Hence reference will be made to data on general government accounts provided by Istat and consistent with Eurostat data; the information used refers to 2011 because it is the latest year for which detailed data are available for **expenditure by function (COFOG)** and level of government. The context considered in this analysis refers solely to current spending, as it is the accounting aggregate that identifies the delivery of all public services, excluding the whole part of capital expenditure, which, by its own nature, is allocated for investment and development.

The current expenditure directly managed by the central government, net of interest and transfers to other levels of government, amounted to little less than **159 billion Euros** (Tab. 3.2); the main item is **expenditure on personnel** (**95 billion Euros**), which is mainly focused on education, law enforcement and defence.

Tab. 3.2 - *How central government spends money. Year 2011*

	Expenses for personnel	Intermediate consumption	Social benefits in cash	Current Trans-fers	Other current expenses	TOTAL CURRENT EXPENSES
General services	9,582	6,975	-	14,307	257	31,121
Defense	14,405	7,053	-	207	2,121	23,786
Law enforcement and security	21,449	4,199	-	109	2,064	27,821
Economic affairs	2,299	1,629	-	574	9,534	14,036
Environmental protection	515	435	-	11	452	1,413
Homes and land use	51	207	-	-	819	1,077
Healthcare	788	540	-	73	-23	1,378
Recreational, cultural and worship act	1,048	2,390	-	1,546	-832	4,152
Education	44,543	1,110	-	-	2,781	48,434
Social security	192	674	3,825	727	38	5,456
TOTAL	**94,872**	**25,212**	**3,825**	**17,554**	**17,211**	**158,674**

NB: Expenditure excluding interest and transfers to other levels of government
Calculated based on ISTAT data

Intermediate consumption follows with **25 billion Euros**, which include the purchases of goods and services required for the operation of general government as well as for the provision of some public services; this type of spending is concentrated in particular on defence, general services and law enforcement.

Central current expenditure is completed by **transfers to families and businesses** (17.5 billion Euros), almost entirely attributable to 'general services', and the residual heading of **other current expenses** (17.2 billion Euros), including contributions to production and amortization. Overall, these types of expenditure are worth almost **35 billion Euros, equal to 2 points of GDP**: this aggregate undoubtedly includes items which cannot be cut, but it nonetheless represents **a potential area of expenditure that can be addressed.**

The analysis by function and COFOG breakdown highlights potential critical spending areas, which may hide cases of waste and inefficiency. Most of the **general services** (central government share of 53%) is absorbed by 'Executive and legislative bodies, financial and tax activities and foreign affairs', equal to 25.5 billion Euros (Tab. 3.3): in particular, over 12 billion Euros of this item are spent in personnel and intermediate consumption for the management and provision of 14.3 billion Euros in current transfers. Defence (central government share of 100%) allocates 22.9 billion Euros out of a total of 23.8 billion to military defence, 14.1 billion of which for personnel and 7 billion Euros for intermediate consumption (Tab. 3.4).

Tab. 3.3 - *General services: detail of central government expenditure. Year 2011*

(in million of Euros)	Expenses for personnel	Intermediate consumption	Social benefits in cash	Current Trans-fers	Other current expenses	TOTAL CURRENT EXPENSES
General services	**9,582**	**6,975**	**-**	**14,307**	**257**	**31,121**
Executive and legislative bodies, financial and tax activities and foreign affairs	7,811	4,773	-	13,437	-482	**25,539**
International economic aid	22	8	-	841	4	**875**
General services	357	226	-	24	518	**1,125**
Basic research	416	219	-	5	92	**732**
Expenditure on research and development	18	10	-	-	17	**45**
General transfers between different levels of government	-	-	-	-	7	**7**
Transactions related to public debt	-	1,263	-	-	3	**1,266**
Other expenditure	958	476	-	-	98	**1,532**

NB: Net of interest

Calculated based on ISTAT data

Tab. 3.4 - *Defence: detail of central government expenditure. Year 2011*

(in million of Euros)	Expenses for personnel	Intermediate consumption	Social benefits in cash	Current Trans-fers	Other current expenses	TOTAL CURRENT EXPENSES
Defense	**14,405**	**7,053**	**-**	**207**	**2,121**	**23,786**
Military defense	14,125	6,991	-	-	1,812	**22,928**
Civil defense	40	21	-	-	72	**133**
Military aid abroad	-	36	-	207	-	**243**
Expenditure on research and development	1	-	-	-	219	**220**
Other expenditure	239	5	-	-	18	**262**

Calculated based on ISTAT data

Law enforcement and security (central government share of **88%**) includes some basic central government services: the main concern Police (16 billion Euros), Courts (5.9 billion Euros), Prisons (3.4 billion Euros) and Fire-Fighting (2.4 billion Euros). About 77% of the expenditure is absorbed by the cost of personnel (Tab. 3.5). **Economic affairs** (central government share of 42%) comprise a wide range of public interventions, mainly allocated to transport (8.4 billion Euros), the primary sector (1.5 billion Euros); in addition, this is the item that features the highest amount spent in R&D, with about 1.2 billion Euros (Tab. 3.6). **Environmental protection** (central government share of 28%) is an item in which the central government does not manage large volumes of expenditure: out of a total of 1.4 billion Euros, approximately 500 million Euros go to the protection of biodiversity and landscape (Tab. 3.7). A marginal item is also that of **Homes and land use** (central government share of 15%), which is slightly over 1 billion Euros (Tab. 3.8).

Tab. 3.5 - *Law enforcement and safety: detail of central government expenditure. Year 2011*

(in million of Euros)	Expenses for personnel	Intermediate consumption	Social benefits in cash	Current Trans-fers	Other current expenses	TOTAL CURRENT EXPENSES
Law enforcement and security	**21,449**	**4,199**	**-**	**109**	**2,064**	**27,821**
Police	12,784	2,118	-	3	1,171	**16,076**
Fire-fighting	2,041	141	-	-	217	**2,399**
Courts	3,914	1,617	-	-	342	**5,873**
Prisons	2,655	316	-	106	330	**3,407**
Other expenditure	55	7	-	-	4	**66**

Calculated based on ISTAT data

Tab. 3.6 - *Economic affairs: detail of central government expenditure. Year 2011*

(in million of Euros)	Expenses for personnel	Intermediate consumption	Social benefits in cash	Current Trans-fers	Other current expenses	TOTAL CURRENT EXPENSES
Economic affairs	**2,299**	**1,629**	**-**	**574**	**9,534**	**14,036**
General economic, trade and labour affairs	514	247	-	167	49	**977**
Agriculture, forestry, fishing and hunting	254	269	-	-	944	**1,467**
Fuel and energy	35	18	-	-	5	**58**
Mining, manufacturing and construction	39	36	-	32	425	**532**
Transport	677	564	-	135	6,964	**8,340**
Communications	109	34	-	6	753	**902**
Other sectors	17	20	-	-	247	**284**
Expenditure on research and development	544	353	-	234	112	**1,243**
Other expenditure	110	88	-	-	35	**233**

Calculated based on ISTAT data

Tab. 3.7 - *Environmental protection: detail of central government expenditure. Year 2011*

(in million of Euros)	Expenses for personnel	Intermediate consumption	Social benefits in cash	Current Trans-fers	Other current expenses	TOTAL CURRENT EXPENSES
Environmental protection	**515**	**435**	**-**	**11**	**452**	**1,413**
Waste treatment	-	160	-	-	22	**182**
Wastewater treatment	-	-	-	-	3	**3**
Pollution abatement	7	37	-	4	64	**112**
Protection of biodiversity and landscapes	240	33	-	5	226	**504**
Expenditure on research and development	231	121	-	2	44	**398**
Other expenditure	37	84	-	-	93	**214**

Calculated based on ISTAT data

Tab. 3.8 - *Homes and land use: detail of central government expenditure. Year 2011*

(in million of Euros)	Expenses for personnel	Intermediate consumption	Social benefits in cash	Current Trans-fers	Other current expenses	TOTAL CURRENT EXPENSES
Homes and land use	**51**	**207**	**-**	**-**	**819**	**1,077**
Housing development	3	-	-	-	345	**348**
Land use	-	121	-	-	414	**535**
Water supply	8	5	-	-	55	**68**
Other expenditure	40	81	-	-	5	**126**

Calculated based on ISTAT data

Healthcare, while being managed locally (central government share of 1%), falls under the concurrent jurisdiction of the central government and regional authorities. Central expenditure in this area, equal to 1.4 billion Euros, is allocated to research and to the financing of healthcare facilities that are directly run by the central government (Tab. 3.9). The eighth COFOG item (Tab. 3.10), dedicated to **recreational, cultural and worship activities** (central government share of **11%**) is extremely varied: it comprises generic recreational activities (1 billion Euros), support to culture (1.3 billion Euros), worship (1.4 billion Euros) and radio and television services.

Tab. 3.9 - *Healthcare: detail of central government expenditure. Year 2011*

(in million of Euros)	Expenses for personnel	Intermediate consumption	Social benefits in cash	Current Trans-fers	Other current expenses	TOTAL CURRENT EXPENSES
Healthcare	**788**	**540**	**-**	**73**	**-23**	**1,378**
Non-hospital services	157	291	-	10	-101	**357**
Hospital services	288	-	-	-	24	**312**
Public healthcare services	-	7	-	43	4	**54**
Expenditure on research and development	177	111	-	3	31	**322**
Other expenditure	166	131	-	17	19	**333**

Calculated based on ISTAT data

Tab. 3.10 - *Recreational, cultural and worship activities: detail of central government expenditure (year 2011)*

(in million of Euros)	Expenses for personnel	Intermediate consumption	Social benefits in cash	Current Trans-fers	Other current expenses	TOTAL CURRENT EXPENSES
Recreational, cultural and worship activiti	**1,048**	**2,390**	**-**	**1,546**	**-832**	**4,152**
Recreational activities	108	2,085	-	211	-1,397	**1,007**
Cultural activities	742	285	-	5	262	**1,294**
Radio and television services and publishing	1	10	-	-	235	**246**
Worship services and other services for comn	5	1	-	1,330	50	**1,386**
Expenditure on research and development	147	9	-	-	10	**166**
Other expenditure	45	-	-	-	8	**53**

Calculated based on ISTAT data

Education, along with Defence, Justice and Law enforcement, is one of the main functions managed centrally (central government share of 74%). More than 48 billion Euros of current spending are attributable almost entirely to pre-school, primary and secondary education. A total of 92% of the current expenses relate to personnel, while the costs for the school facilities and teaching material (attributable to intermediate consumption) are slightly over the 1.1 billion Euro mark, i.e., 2.3% of the relevant item (Tab. 3.11).

Tab. 3.11 - *Education: detail of central government expenditure. Year 2011*

(in million of Euros)	Expenses for personnel	Intermediate consumption	Social benefits in cash	Current Trans-fers	Other current expenses	TOTAL CURRENT EXPENSES
Education	**44,543**	**1,110**	**-**	**-**	**2,781**	**48,434**
Pre-school and primary education	18,829	457	-	-	1,237	**20,523**
Secondary education	24,852	467	-	-	1,454	**26,773**
Non-higher post-secondary education	232	12	-	-	12	**256**
Higher education	229	4	-	-	92	**325**
Expenditure on research and development	37	27	-	-	4	**68**
Other expenditure	364	143	-	-	-18	**489**

Calculated based on ISTAT data

In terms of **social security**, the central government plays a marginal role (2% share), since the main providers of social services are social security organizations. Overall, central government expenditure in this area amounted to 5.5 billion Euros, 3.8 billion of which referable to social benefits in cash (Tab. 3.12).

Tab. 3.12 - *Social security: detail of central government expenditure. Year 2011*

(in million of Euros)	Expenses for personnel	Intermediate consumption	Social benefits in cash	Current Trans-fers	Other current expenses	TOTAL CURRENT EXPENSES
Social security	**192**	**674**	**3,825**	**727**	**38**	**5,456**
Disease and disability	-	27	769	-	-	**796**
Old age	46	40	1,554	82	-75	**1,647**
Survivors	28	-	581	-	2	**611**
Family	-	231	921	39	-	**1,191**
Unemployment	3	-	-	-	-	**3**
Social exclusion	23	262	-	606	28	**919**
Other expenditure	92	114	-	-	83	**289**

Calculated based on ISTAT data

3.2 The figures concerning Ministries in Italy

The analysis of national accounts can be integrated through the information available in the central government's financial report. This document allows determining the spending of each Ministry, broken down by type of cost. It should be noted however that values diverge from the data on national accounts published by ISTAT and Eurostat due to methodological reasons.

Tab. 3.13 - *The expenses of Ministries: from 'official' spending to 'actual' spending (final data for 2012)*

	in million of Euros
(S1) Current expenses	**489,351**
Personnel	87,674
Intermediate consumption	10,527
Transfers	260,881
(I) Interest expense and finance income	81,385
Other current expenses	48,884
(S2) Capital expenditure	**45,653**
Gross fixed capital formation, purchase of land	5,034
Investment grants	26,398
Other capital expenditure	14,221
(S3) Repayment of financial liabilities	**214,334**
(ST) EXPENDITURE OF CENTRAL GOVERNMENT (S1+S2+S3)	**749,337**
Minus:	
(T1) Transfers to local government	128,310
(T2) Transfers to social security institutions	103,971
(SC) CONSOLIDATED EXPENDITURE OF CENTRAL GOVERNMENT (SC = ST-T1-T2)	**517,056**
(SE) ACTUAL EXPENDITURE FOR SERVICES (SC-S3-I)	**221,338**

Based on State General Accounting Office data

A thorough examination of the outlay of Ministries calls for a fundamental distinction between the total budgeted expenditure and what is actually allocated to services falling under their competence. In 2012, spending of the central government amounted to **749 billion** Euros: this aggregate, however, comprises **128 billion Euros** in transfers to local government (co-financing of healthcare and of the other functions performed by regional and local authorities) and **104 billion Euros** of payments to social security institutions, most of which required to cover expenditure for pension benefits. Excluding these items, the spending of Ministries amounts to 517 billion Euros (Tab. 3.13.

It should be noted that running costs (personnel and intermediate consumption) take up 98 billion Euros: the remaining resources are distributed for transfers to businesses and families and other current expenses (85.6 billion Euros) and for investment (37.5 billion Euros) (Tab. 3.14).

Tab. 3.14 - *Spending by Ministries - Final 2012 (million Euros)**

	ACTUAL EXPENDITURE IN SERVICES	Running costs	Spending in operations	Spending in investment
MINISTRY OF ECONOMY AND FINANCE	**113,988**	18,141	75,434	20,414
MINISTRY OF ECONOMIC DEVELOPMENT	**6,511**	280	533	5,698
MINISTRY OF LABOUR AND SOCIAL POLICIES	**1,232**	401	807	24
MINISTRY OF JUSTICE	**7,477**	6,696	580	201
MINISTRY OF FOREIGN AFFAIRS	**1,780**	904	862	15
MINISTRY OF EDUCATION, UNIVERSITY AND RESEARCH	**45,361**	40,116	2,980	2,266
MINISTRY OF THE INTERIOR	**11,983**	10,071	1,144	768
MINISTRY OF THE ENVIRONMENT AND PROTECTION OF THE TERRITORY AND SEA	**342**	156	81	105
MINISTRY OF INFRASTRUCTURE AND TRANSPORT	**6,437**	1,248	706	4,483
MINISTRY OF DEFENSE	**22,292**	18,312	1,316	2,664
MINISTRY OF AGRICULTURE, FOOD AND FORESTRY POLICIES	**1,295**	567	219	509
MINISTRY OF CULTURAL HERITAGE AND ACTIVITIES	**1,460**	948	166	346
MINISTRY OF HEALTH	**1,180**	363	813	4
TOTAL	**221,338**	98,201	85,640	37,497

** Due to methodological reasons, the data in the table diverges from those on national accounts disseminated by ISTAT and Eurostat and illustrated above*
Based on State General Accounting Office data

However, items that do not represent public services, such as interest charges and the repayment of financial liabilities, should be excluded from this aggregate. Based on these calculations, the actual spending on services by central government would be high anyway, amounting to about **221 billion Euros**. **More than half of this aggregate, in the neighbourhood of 114 billion Euros, is ascribable to the Ministry of Economy and Finance,** followed by the Education Ministry (45 billion Euros) and the Defence Ministry (22 billion Euros). It should be noted that staff and intermediate consumption account for 98 billion Euros: the remaining 123 billion Euros are distributed rather uniformly between capital expenditure, transfers and other current expenses (Tab. 3.14).

3.3 Central governments in (allegedly) federal countries: a comparison

After the spread crisis in the second half of 2011, the federal reform was progressively pushed to the margins of the political agenda. Despite the fact that the path to adopt the measures implementing the 2009 Delegated Law was formally completed in July 2011, most of the innovative elements of that regulatory design were set aside or literally had to yield to the needs of fiscal consolidation: in this respect, the most blatant example is that of the IMU tax, which was transformed from being a pillar of municipal taxation into a shared tax of both central and local government. The complex calculation of standard requirements of local authorities has not been applied yet to determine the equalizing resources for local authorities.

In spite of this, **federalism has been blamed** for being one of the main reasons of the current inefficiencies of Italy's general government and the main source behind bureaucracy, waste and irresponsible management. Implicitly, **it is taken for granted that Italy should be considered a real federal country**, like Germany, Spain and Switzerland. In fact, this is not the case: Italy is a country, which started a process of institutional decentralisation a few decades ago and this process is all but completed. It is a circuitous path that has not been shared. It has suffered numerous delays and setbacks. Few legislative and administrative powers have been decentralized and very little fiscal autonomy has been granted at the local level. **Central government is still the player that governs national public finance**, intervening promptly and periodically in spheres falling under the competence of local government. In addition, there still is no **Federal Senate** capable of effectively representing local authorities.

In Italy, central government still manages a considerable share of public spending, which is empirically unmatched in most federal countries. In the last three years, central public expenditure in Italy, net of interest, amounted to an average of 23.9% of GDP. This is a value even greater than that of a traditionally centralized country like France (20.8 %); all federal countries lie well below Italy (Tab. 3.15).

Tab. 3.15 - *Central government spending in some federal countries. Values in % of GDP (2010-2012 average)*

	Central primary spending (1)	Central transfers to other public institutions (2)	Central primary spending net of transfers (3 = 1-2)
France (centralized)	20.8%	4.3%	16.5%
Germany	13.3%	6.2%	7.1%
Spain	16.9%	8.1%	8.9%
Italy	23.9%	13.1%	10.8%
Switzerland*	10.3%	5.7%	4.6%

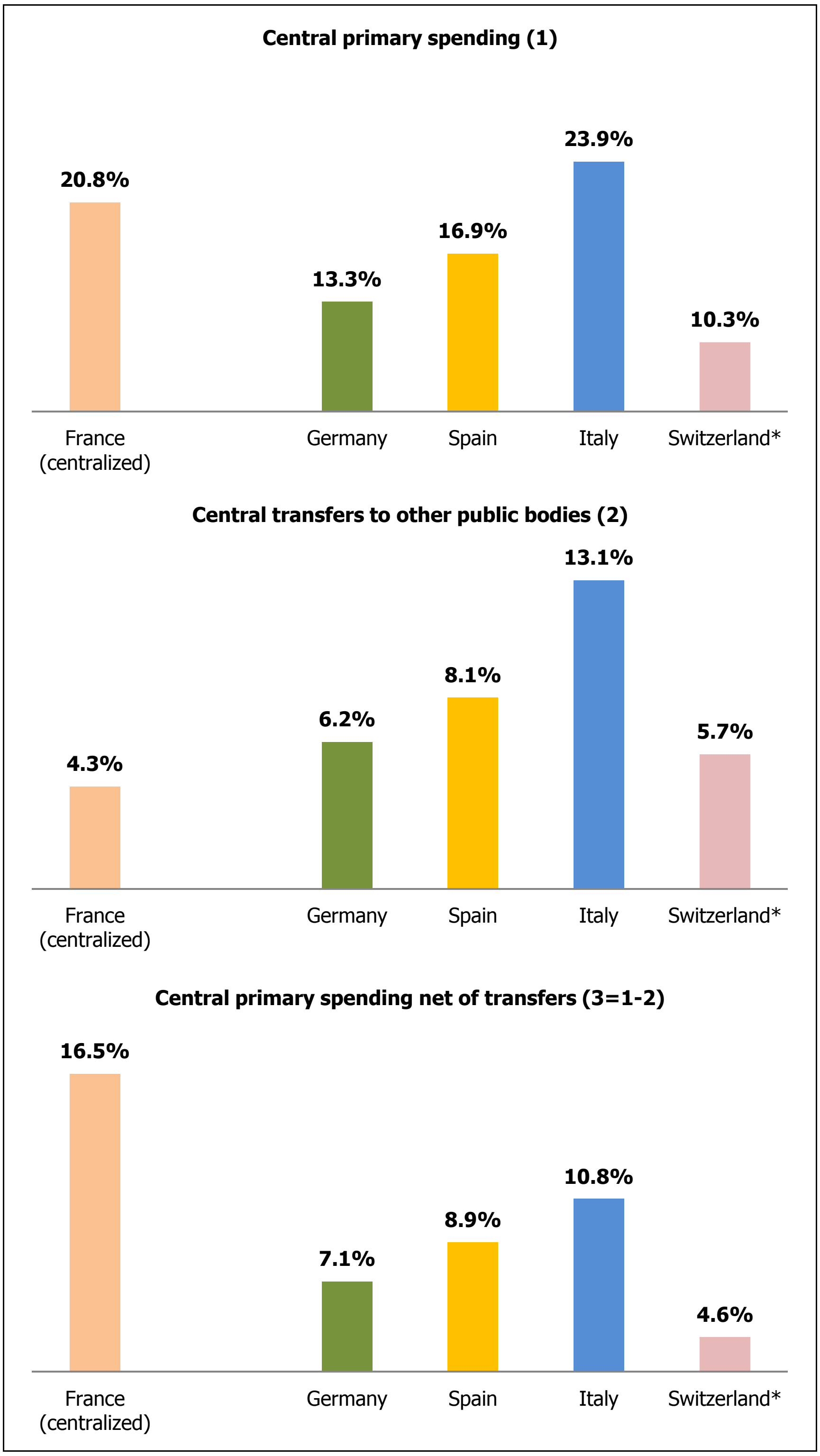
(*) Average for the years 2009-2011
(1) Net of interest
(2) To local government and social security institutions
Calculated based on Eurostat data

These gaps are even larger if we consider the public services directly managed by the central government. In order to approximate this aggregate, the expenditure for transfers to other levels of government was excluded from the central primary expenditure (Regions, local government institutions, social security). France excels by far in 'actual' central expenditure with a value equal to 16.5% of GDP, but Italy ranks before all the other federal countries: 'actual' central expenditure is equal to 10.8% of GDP, as compared to 8.9% in Spain, 7.1% in Germany and 4.6% in Switzerland (Chart 3.3).

Another element on which light needs to be shed is the internal breakdown of central government spending in various federal countries in Europe. Italy is characterized by a high percentage share of the running costs out of the total outlay directly managed by central governments. Running costs are costs for personnel and intermediate consumption: in particular, the latter item includes costs incurred by the general government for the purchase of goods and services on the market necessary to make the administrative machinery run (stationery, fuel, phone services, heating) and for the provision of some public services to the public. While considering running costs as waste is not correct, high levels of expenditure may signal critical management issues and inefficiency in the allocation of resources and the provision of services.

In the light of these facts, it should be noted that **almost 70% of the central spending in Italy is attributable to running costs**. This is a value well above 50.4% in Switzerland (but with a much more limited impact in terms of GDP), 37.2% in Spain and 29.7% in Germany. It is even higher than the 51.9 % recorded in a country as centralized as France (Chart 3.3). If we look at federal countries alone, Spain's central government spends, in proportion, more than Italy in investment (29.6% versus 11.2%), while the German central government spends almost 32% of its net budget for the provision of social security benefits (against 2.6% spent by Italy).

Chart 3.3 - *Central government spending in some federal countries. Values in % of GDP (2010-2012 average)*



(*) Average for the years 2009-2011
(1) Net of interest
(2) To local government and social security institutions
Calculated based on Eurostat data

Tab. 3.16 - *Structure of central government spending in some federal countries (average for 2010-2012)*

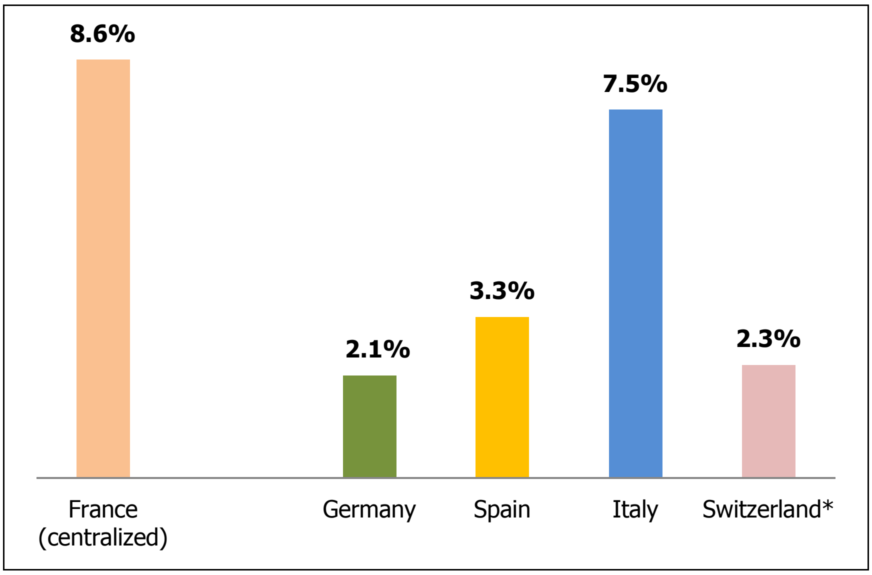
	France (centralized)	Germany	Spain	Italy	Switzerland*
In million Euros					
Running costs	170,175	54,357	34,266	117,938	9,654
Current transfers to private entities	36,516	32,893	12,444	17,386	2,683
Social security benefits	84,333	57,963	15,498	4,399	204
Other current expenses	18,933	8,000	2,619	10,672	2,081
Investments	18,111	29,827	27,257	18,967	4,534
Central primary spending**	**328,068**	**183,040**	**92,085**	**169,362**	**19,156**
Composition in %:					
Running costs	51.9%	29.7%	37.2%	69.6%	50.4%
Current transfers to private entities	11.1%	18.0%	13.5%	10.3%	14.0%
Social security benefits	25.7%	31.7%	16.8%	2.6%	1.1%
Other current expenses	5.8%	4.4%	2.8%	6.3%	10.9%
Investments	5.5%	16.3%	29.6%	11.2%	23.7%
Central primary spending**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**

(*) Average for the years 2009-2011
(**) Net of interest and transfers to local government and social security institutions
NB: The running costs comprise the costs for personnel and intermediate consumption
Calculated based on Eurostat data

Similarly, the **running costs** of central government in Italy reach much higher levels than those in other European federal countries: specifically, **Italy's central government** allocates an amount equal to 7.5% **of GDP** to this item (Chart 3.4%), more than double compared to Spain (3.3%) and over twice the level of expenditure in Germany and Switzerland (2.1% and 2.3% of GDP respectively). Compared to ten years ago, central running costs have not decreased and have actually risen from 7.4% of GDP in the 2000-2002 period to 7.5 % in the last three years. Central governments in Germany and Spain, too have registered a slight increase in running costs (+0.1% of GDP), but the latter remained considerably lower than those of Italy's central government. By contrast, in Switzerland and in France the running costs of central government have significantly decreased (Tab. 3.17).

The simple statistical exercise presented below can help 'translate' the running costs of central government in federal countries into monetary values. It is not a matter of estimating the efficiency of Italy's general government compared to that of other countries, but to refute, with numbers, the assumptions of those who implicitly consider Italy to be a federal country and blame decentralization, the federalist process and local authorities for the deficit in the national public accounts. If Italy's central government allocated the same share of GDP as Germany and Switzerland to running costs, it could save between **82 and 85 billion Euros** (Chart 3.5). Clearly, these savings are only theoretical, since part of these costs should be diverted to local government as a result of the actual delegation of responsibility in the management of general administration. Despite all of its unsustainability, this fact makes it possible to state that **Italy is witnessing a centralization of resources and direct management of public functions by the central government, in a manner which is incompatible with a truly federal setup of government.**

Chart 3.4 - *Central government running costs in some federal countries. Values in % of GDP (2010-2012 average)*



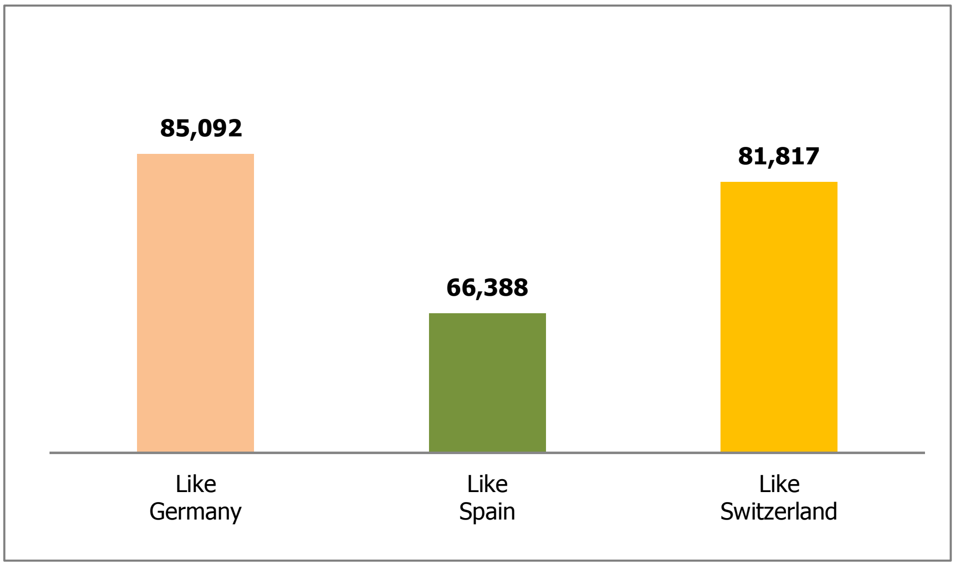
NB: The running costs comprise the costs for personnel and intermediate consumption
Calculated based on Eurostat data

Tab. 3.17 - *Central government running costs in some federal countries. Values in % of GDP*

	Average for 2000-2002	Average for 2010-2012*
France (centralized)	9.4%	8.6%
Germany	2.0%	2.1%
Spain	3.2%	3.3%
Italy	7.4%	7.5%
Switzerland*	2.6%	2.3%

(*) Average for the years 2009-2011 for Switzerland
Calculated based on Eurostat data

Chart 3.5 - *Central government running costs: hypothetical savings for Italy compared to other countries (million Euros)**



NB: The estimate was made assuming that Italy had running costs (in % of GDP) similar to those of other countries
(*) Calculations made on the basis of the 2010-2012 period
Calculated based on Eurostat data

4. Spending differentials at ministry level: an exploratory analysis*

4.1 The accounting reports of Ministries

After examining the differences in central government spending levels in a comparative perspective, one interesting effort is to investigate more closely into the composition and trends of central government spending with regard to the part falling under the various Ministries.

This analysis concerns only the 2010-2012 period because complete accounting reports of the Ministries have been made available only starting from 2010 (from 2008 only the total expenditure by Ministry is available and exclusively for the initial budget forecasts).

The annual totals of the complete accounting reports of the following Ministries were considered:

1. Agriculture, Food and Forestry Policies
2. Environment, Land and Sea Protection
3. Cultural Heritage and Activities
4. Defence
5. Foreign Affairs
6. Economy and Finance
7. Justice
8. Infrastructure and Transport
9. Interior
10. Education, University and Research
11. Labour and Social Policies
12. Healthcare
13. Economic Development

The nature of the data is such as to allow a fairly detailed analysis. The detailed analysis of all of the spending items is, however, a long and complex process considering the scope of the data matrix. Therefore, we will focus our inquiry on macro-aggregates (which corresponds to a specific and formal classification within

* This chapter was written by Quirino Biscaro.

the reports): that allows for interesting evaluations on the trends in central spending and especially on its compliance with basic criteria of effectiveness and efficiency.

The spending macro-aggregates formally available are the following:

1. Function
2. Operations
3. Investments
4. Common expenses (current and capital)
5. Charges and repayment of public debt
6. Other expenditure

However, we will analyze here only the first three items and consequently the total of reference will correspond to the sum of these macro-aggregates alone[39]. These are three types of spending that make it possible to fathom **the efficiency** (running costs) and **the effectiveness** (spending in operations/investment) of ministerial action. In addition, considering the approach of the analysis, it is also clear that there is no distinction between direct and indirect spending (transfers), since it would only have mere accounting relevance.

The remaining three macro-aggregates are not considered in this analysis because they are spending items, which by their nature do not lend themselves to effectiveness-efficiency assessments or even to strategies to curb central government spending. This is evident for the items that concern public debt as well as for the common expenses and other expenses, such as the coverage of deleted residual amounts, line-of-duty death and disability benefits, intervention following natural disasters and so on.

Considering the three macro-aggregates, the objective of the analysis is to assess the approach of each Ministry to incurring expenses for operations and investment, which mainly depend on the effectiveness of action at the central level, with respect to the expenses for running the 'central machinery' (running costs). More generally, the **analysis** aims **to determine whether the current strategies to curb public expenses reduce the running costs, to the benefit of the efficiency of the 'central machinery', or else if they reduce operations and investments, to the detriment instead of effectiveness.**

[39] The sum of the costs of the three items (function, operations and investment), equal on average to 423 billion Euros in the 2010-2012 period, accounts for about 60% of total costs, with an average of 724 billion Euros.

4.2 The structure of spending in Ministries

In the three-year period from 2010 to 2012, the sum of the running, operation and investment costs of Ministries dropped from 429,478 to 419,496 million Euros. It can hence be stated that the result of the Berlusconi Government (2010-2011) and Monti Government (2011-2012) was a **reduction** of three macro-aggregates by **9,982 million Euros**[40].

This trend, however, is only apparently positive. This can already be inferred from the analysis of the composition of expenditure, but the analysis of the trend of expenditure over time presented in the following paragraph will make it even clearer.

As regards the composition of expenditure, the following table shows the internal weight of the three macro-aggregates considered.

Tab. 4.1 - *Composition of spending of Ministries. Year 2012*

Ministry	Function	Operations	Investments	Total
Agriculture	44.4	25.0	30.6	100.0
Environment	15.6	35.7	48.7	100.0
Culture	56.8	23.3	19.9	100.0
Defence	86.1	1.6	12.3	100.0
Foreign Affairs	50.3	48.8	0.8	100.0
Finance	2.7	90.5	6.7	100.0
Justice	80.9	16.5	2.6	100.0
Infrastructure	18.4	22.6	59.0	100.0
Interior	45.2	52.6	2.2	100.0
Education	80.1	15.4	4.5	100.0
Labour	0.5	97.8	1.7	100.0
Healthcare	16.8	80.2	3.0	100.0
Development	4.8	5.3	89.9	100.0
Total	**20.9**	**71.4**	**7.7**	**100.0**

Based on RGS data - Accounting reports of Ministries

[40] Any discrepancies between the data in this chapter and those contained in chapter 3, both derived from the database of the State General Accounting Office, are attributable to different methods for the aggregation of basic data.

The 'horizontal' percentage composition (i.e., within the expenditure of each Ministry) leads to assume that there is a potential imbalance in spending items: in 2012 there were 6 Ministries out of 13 whose running costs accounted for the most part of the three spending items considered; in 5 of these cases, the share exceeded 50% of the total expenditure considered; in 12 out of 13 cases, the share of the running costs increased over the past three years.

It is quite evident that this depends on the way in which the aforementioned cuts were made (9,982 million Euros between 2010 and 2012).

Tab. 4.2 - *Trend in the spending of Ministries (absolute changes in the 2012-2010 period in millions of Euros)*

Ministry	Function	Operations	Investments	Total
Agriculture	-79.0	-51.4	-202.9	-333.3
Environment	-2.4	-34.2	-328.8	-365.4
Culture	20.8	6.0	-3.1	23.7
Defence	196.3	-18.7	-543.9	-366.3
Foreign Affairs	-62.6	-306.8	3.3	-366.1
Finance	-32.3	-8,234.6	-6,227.2	-14,494.0
Justice	213.9	45.4	-91.2	168.2
Infrastructure	-74.5	143.5	-1,096.9	-1,027.9
Interior	599.7	-5,769.7	-1,370.9	-6,540.9
Education	-1,716.4	-468.9	-11.4	-2,196.6
Labour	54.7	16,423.4	-1,792.6	14,685.5
Healthcare	3.6	-124.8	-47.9	-169.2
Development	135.1	-67.1	932.5	1,000.5
Total	**-743.1**	**1,542.2**	**-10,781.0**	**-9,981.9**

Based on RGS data - Accounting reports of Ministries

The three-year trend in spending shows that the reduction equal to 9,982 million Euros:

1. is relevant in absolute value[41], but in reality it is small in relative terms, i.e., -2.3% (over 2010);
2. it is practically shouldered entirely by users, in the sense that 9,239 million Euros were collected from expenditure in operations and investment; the reorganization of the running costs is limited to only 743 million Euros;
3. These modest savings are not even widespread, as there are no less than 7 Ministries (out of 13) that increased their running costs; of the 6 that cut these costs, only in 2 (Foreign Affairs and Education) the reduction was greater than that applied to operations and investment (considered in sum).

A consideration also needs to be made for the 'common expenses' and 'other expenses' macro-aggregates. Even though they are not the subject of this effectiveness/efficiency analysis, in absolute terms[42], these values are characterized by an increase in expenditure (6,381 million Euros), to the point that about 2/3 of the aforementioned reduction in running, operations and investment macro-aggregates was nullified.

4.3 The spending trend in Ministries: a shift-share analysis

The foregoing needs to be assessed more in detail with a *shift-&-share* analysis. From a methodological point of view, given any variable X that characterizes an organization - in turn included in a macro-organization - the trend of X can be explained both by specific and structural reasons:

1. specific: comparison between the trend of the variable X and the overall trend (all variables) of the organization to which the same variable refers (*internal trend of the organization);*
2. structural: comparison between the overall trend of the organization being studied and that of the macro-organization containing it (*trend between organization and macro-organization*).

[41] For example, the amount 'is worth' more than 2 points of VAT, or more than 2 years of IMU on the main residence of Italians.

[42] Although it is agreed that these are expenditure items, which cannot be discussed in terms of effectiveness and efficiency, according to a cold logic based on 'cash', these are nonetheless amounts borne by the country.

In applying the shift-&-share approach to this context, the **specific assessment** is equivalent to asking whether the running costs of a Ministry follows the overall spending trend of that same Ministry. The **structural assessment** leads to ask whether the total expenditure of a Ministry follows the overall trend (sum of the Ministries). At a glance:

1. *Specific analysis: comparison of the percentage change in the running costs of the Ministry and the percentage change of the total expenditure of the same Ministry*[43] *[comparison of trend within the Ministry: var(running costs of Ministry) - var(total expenditure of Ministry)]*
2. *Structural analysis: comparison between the percentage change of the total expenditure of the Ministry and the variation of the overall total of all Ministries [comparison of trend between the Ministry and central government as a whole: var(total expenditure of Ministry) - var(total expenditure of Ministries)]*

Tab. 4.3 - *Specific and structural analysis of spending of Ministries (% values). 2010 and 2012 comparison*

Ministry	Specific component*	Structural component**
Agriculture	8.3	-17.9
Environment	35.1	-35.3
Culture	0.8	3.7
Defence	2.7	0.7
Foreign Affairs	10.6	-14.8
Finance	6.3	-4.6
Justice	1.3	4.6
Infrastructure	8.2	-12.0
Interior	27.8	-19.5
Education	0.1	-1.7
Labour	-4.0	19.7
Healthcare	11.6	-7.9
Development	40.4	16.8

** var (OperMin) – var (TotMin)*
*** var (TotMin) – var (TotGeneral)*
Based on RGS data - Accounting reports of Ministries

[43] Please note that, according to the logic of this analysis, this is equal to the sum of the running costs, costs for operations and investment expenditure.

You will immediately notice that several Ministries (8) are structurally virtuous, as these are characterized by negative structural components; they are definable as 'structurally virtuous', because their total expenditure decreases to a greater extent (or increases less) compared to the spending of central government as a whole.

The sore spots are found in the specific assessment: it demonstrates that in 12 Ministries running costs dropped less (or increased more) than they did for the entire expenditure of the single Ministry.

The negative judgments that emerged from the analysis of the basic trend are hence confirmed.

4.4 Efficiency and effectiveness of spending in Ministries

In the light of the foregoing, the following question needs to be asked: do ministries consider the efficiency and effectiveness of operations? The answer seems obvious a priori, but let us proceed in an orderly manner.

In order to measure the **efficiency of ministerial spending**, let us consider the value of the running costs for every euro spent in operations and investments (considered in sum). Please note that this analysis is provided by way of example and is not exhaustive.

These data speak for themselves. **In 5 Ministries, producing a euro of operations/investment costs more than a euro of running costs**. The ratio is also very high for 2 other Ministries, in which no less than 80 cents are needed to produce 1 euro of operations/investment.

What should not be ignored, considering that it is essential in the perspective of this survey, is the fact that 12 Ministries (out of 13) tend to increase the ratio considered, consequently reducing the economic efficiency of their operation.

However, a consideration needs to be made with regard to this issue. There are 5 Ministries (Defence, Finance, Justice, Interior, and Education), which include the cost of personnel who work throughout the country among their running costs: military, tax police, judges, policemen and teachers. Leaving out the formal definitions that classify this cost as a running cost, and embracing a 'substantial' logic, one will certainly agree that in the eyes of citizens the work of said staff is not a running cost, but takes on the characteristics of an operation. To the extent that this consideration is shared, it is clear that for these 5 Ministries the aforementioned ratios would take on different values. This is certainly an aspect that deserves further investigation in a future survey.

Tab. 4.4 - *Running costs of Ministries for every euro spent in operations and investment (values in Euros). Year 2012*

Ministry	Running costs (Euros)	Diff. 2012-2011	Diff. 2012-2010
Agriculture	0.80	-0.03	0.13
Environment	0.18	0.02	0.07
Culture	1.32	0.03	0.02
Defence	6.19	1.42	1.03
Foreign Affairs	1.01	-0.04	0.21
Finance	0.03	0.00	0.00
Justice	4.23	1.11	0.27
Infrastructure	0.23	-0.05	0.02
Interior	0.82	0.20	0.32
Education	4.02	-0.05	0.02
Labour	0.00	0.00	0.00
Healthcare	0.20	0.00	0.03
Development	0.05	0.03	0.01

Based on RGS data - Accounting reports of Ministries

Let us now try to measure the **effectiveness of ministerial spending** - emphasizing once again that this analysis is provided by way of example and is not exhaustive. It is limited to the 5 Ministries mentioned above, because it is easy and intuitive to identify the reference targets of their spending. The effectiveness will be determined here by looking at the amount per capita (for each target), and not at the achievement of specific objectives, as otherwise it would be an extremely complicated debate with many different opinions and subjectivity would prevail over objectivity.

Having said that, the parameters taken as a reference are:

- Residents for Defence;
- Residents for Finance;
- Pending first-instance and appeal proceedings for Justice[44];
- Residents for Interior;
- Students for Education.

These will be the units of reference for the 5 Ministries considered, on the basis of which per-capita spending in operations/investment will be determined.

Tab. 4.5 - *Spending in operations and investment (per-capita values in Euros). Year 2012*

Ministry	Spending in operations+investment (Euros per capita)	Diff. 2012-2011
Defence	50.28	-14.97
Finance	3,163.53	-110.18
Justice (*)	133.07	-66.14
Interior	215.71	-77.96
Education	976.79	0.61

(*) Excluding activities related to penitentiaries
Based on RGS data - Accounting reports of Ministries

The data are extremely clear. **Spending in operations and/or investment per capita is lower in all 5 cases**, though to a different extent. It cannot be said with certainty that the effectiveness of the ministerial action decreases, but in any case it is extremely likely that it does.

The possible reflections are obviously not positive, especially if one considers that the spending in operations and investment per capita is the reason for the very existence of a central organization.

This first in-depth analysis on ministerial expenses does not focus on the grand total, but on aggregates, which on the one hand constitute the cost of the 'central

[44] For now, assessments considering penitentiaries have been excluded due to the incompleteness of the available data.

machinery', i.e., the running costs, and on the other, determine the effectiveness of central action, i.e., spending in operations and investment. As indicated in the introduction, the analysis was limited to these three types of expenditure also because the remaining items:

1. are of a nature such that these should not be involved in strategies to cut central public spending (the macro-aggregates for other expenses and shared expenses include, for example: the coverage of cancelled residual amounts, line of duty death and disability benefits, intervention following natural disasters);
2. cover expenses for and the repayment of public debt.

The starting point is the fact that between 2010 and 2012, the spending considered herein was cut by 9,981 million Euros. If the objective is the reduction of central spending, this is to be welcomed – of course, but the analysis shows that the data hides many shadows; indeed, the analytical result is definitely negative.

1. The composition of expenditure shows that the share of running costs is high and in some cases is clearly excessive;
2. The analysis of the trend clearly shows that, in the spending consolidation process, the most common attitude is to safeguard spending to 'run the structure', while spending to support ministerial programmes has been drastically cut;
3. In 12 out of 13 ministries, the 'machinery' that produces operations and/or investment in 2012 was less efficient than it was in 2010;
4. In 5 Ministries whose action is spread extensively across the country (Defence, Finance, Justice, Interior, Education), per-capita operations and/or investment expenditure (according to their respective reference targets[45]) decreased.

[45] Residents for Defence, Finance and the Interior; students for Education; pending first-instance and appeal proceedings for Justice.

5. Spending less is possible: potential savings with 'optimal costs'

The results of statistical analysis shown above clearly demonstrate the need for greater efficiency and a rationalization of the machinery of general administration, so as to facilitate the reduction of running costs. This goal should be achieved by applying **standard costs and requirements** to expenditure at all levels of government.

In the current state of things, the procedure to calculate and determine the standard requirements relating to the fundamental functions of local authorities is near completion (the process has been concluded for four provincial functions and for two municipal functions). Similarly, 2013 should be the year in which standard costs make their debut in the healthcare sector, though only on an experimental basis and in reduced form with respect to the original design. It is not superfluous to remember that the application of standard costs and requirements is intended to provide a gradual and definitive tool to go beyond the historical spending criterion.

However, it is clear that determining standard requirements is a technically complex effort. While appreciating the work of institutional actors involved in the accurate calculation of standard costs and requirements of each local authority, the results obtained by Unioncamere Veneto through an alternative procedure should be illustrated as well. To overcome the difficulties of determining standard costs and to channel together different levels of public spending in the various areas of the country to more sustainable targets, Unioncamere del Veneto has introduced the concept of '**optimal territorial spending**', combining three parameters:

- per-capita spending in intermediate consumption;
- average cost of personnel (civil servants);
- number of civil servants in relation to population.

More precisely, this is an evolution of the 'optimal costs' method developed by Unioncamere del Veneto a few years ago[46], which now takes into account the

[46] Unioncamere Veneto, *Responsibiliy and federalism. Figures, ideas and remarks to speed up the realization of fiscal federalism in Italy*, Working Paper No. 11, September 2009.

criteria of territorial/institutional homogeneity and the articulation of the running costs between centre and periphery.

The territory of reference for central government spending (relating to the 15 ordinary-statute regions) is Lombardy, since, based on preliminary statistical analyses, it provides for the most satisfactory combination between level of public spending and number of civil servants.

With regard to local government (relating to the 15 ordinary-statute Regions), the choice of the benchmark territory fell on the Veneto, since it has moderate levels of public spending, combined with good performance in terms of service quality (for example, in terms of basic levels of healthcare, and based on the first partial results on the standard requirements of municipalities).

The fact that the territories belonging to the ordinary-statute Regions were analyzed separately from autonomous Regions makes it possible to comply with one of the criteria mentioned above, namely that of territorial and institutional homogeneity. In other words, comparing the levels of spending of central government in ordinary-statute Regions with average expenditure in autonomous Regions would have produced results that were not homogeneous and not comparable. The same considerations apply to local government.

However, it was necessary to identify, by means of an appropriate statistical method, the surplus of expenditure of central government in the Lazio Region due to the presence of central government institutions related to the role of Italy's capital. For the purpose of calculating the optimal costs, the benchmark for the aggregate expenditure conventionally attributed to the 'Capital factor' is represented by the data referring to the peripheral bodies of central government in ordinary-statute regions (Tab. 5.1).

The territories belonging to the autonomous Regions were considered in their entirety, without distinguishing between central and local expenditure. Assuming that in all areas of the country the level of the quality and quantity of public services is the same, it was decided to apply to the autonomous Regions the average parameters for the complex of central and local governments of Lombardy and the Veneto.

After this long and necessary methodological introduction, it is now possible to comment on the data relating to the theoretical cost saving resulting from the application of optimal costs. **The running costs of general government could be reduced by 32 billion Euros, i.e., 13% less compared to the**

current structure. The total savings, equalling 2% of GDP, would be obtained by a 19% cut in central government and in central government institutions (-11,7 and -2.4 billion Euros respectively), a 16% cut of spending in autonomous Regions (-6.3 billion Euros) and by a 9% reduction at the expense of local government (Tab. 5.2).

Tab. 5.1 - *Optimal cost parameters for homogeneous territories. Year 2011*

	Civil servants per thousand inhabitants	Average spending for personnel (Euros)	Per-capita intermediate consumption (Euros)	*Reference territory*
Central government (1)	22.3	33,428	252	*(Lombardy)*
Local government (2)	21.5	32,496	1,539	*(Veneto)*
Autonomous Regions (3)	43.8	33,742	2,063	*(Lombardy-Veneto)**
Central government institutions (4)	*(The benchmark is given by peripheral bodies of the central government in the 15 ordinary-stature Regions)*			

(*) Mean values for the whole of central and local government in Lombardy and the Veneto
(1) Peripheral bodies of the central government in the 15 ordinary-statute Regions
(2) Regions and local authorities of the 15 ordinary-statute Regions
(3) Central and local government of the 6 autonomous Regions
(4) Estimated spending non-peripheral central government institutions
Processed by Unioncamere Veneto based on Territorial Public Accounts

Tab. 5.2 - *Application of optimal costs for homogeneous territories. Year 2011 (in millions of Euros)*

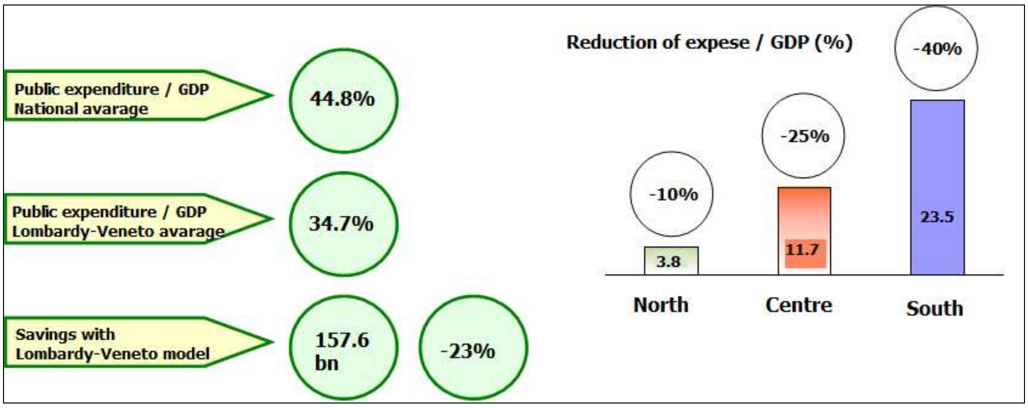
	Current running costs	Optimal running costs	Theoretical savings
Central government (1)	62,005	50,309	11,696
Local government (2)	124,384	112,735	11,650
Autonomous Regions (3)	38,120	31,893	6,228
Central government institutions (4)	12,606	10,228	2,378
TOTAL	**237,115**	**205,165**	**31,950**

(1) Peripheral bodies of the central government in the 15 ordinary-statute Regions
(2) Regions and local authorities of the 15 ordinary-statute Regions
(3) Central and local government of the 6 autonomous Regions
(4) Estimated spending non-peripheral central government institutions
Processed by Unioncamere Veneto based on Territorial Public Accounts

The rationalization of public spending, alongside the application of the standard costs at all levels of government, is probably a very strict yet necessary step to ensure Italy's economic and social cohesion. As pointed out repeatedly in previous working papers, the **necessary solidarity toward the economically less developed areas cannot be mistaken as a license to spend indiscriminately**. In Italy, territorial solidarity exists and is consolidated: otherwise, **if Italy were not a country based on solidarity, public expenditure could be reduced by almost 158 billion Euros, i.e., an overall decrease of 23%**. These results can be reached by applying the data on public spending based on the GDP of Lombardy-Veneto (34.7%) to other regions: Southern Italy would have to cut public spending by 40%, Central Italy by 25%, and Northern Italy by just 10% (Chart 5.1).

In conclusion, **the reform of public spending can no longer be dodged**. The very survival of social and economic cohesion between communities and the country's overall sustainability are at stake.

Chart 5.1 - *If Italy were not a country based on solidarity*



NB: Data refer to public spending net of interest, shareholdings and contributions and lending (average for 2009-2011)
Processed by Unioncamere Veneto based on Territorial Public Accounts

Statistical Appendix

Appendix 1 - *Forecasts for current expenditure* in comparison (million of Euros)*

	2010	2011	2012	2013	2014	2015	2016	2017
Central government								
DFP 2011-2013 (Sept. 2010)	163,883	159,786	158,722	158,419				
DEF 2011 (Apr. 2011)	160,508	159,579	156,844	155,810	156,356			
DEF 2012 (Apr. 2012)	160,661	159,500	157,841	155,643	155,581	156,455		
DEF 2013 (Apr. 2013)	160,603	158,216	151,540	151,900	150,139	153,203	154,347	155,150
Local government								
DFP 2011-2013 (Sept. 2010)	213,870	212,001	215,113	221,002				
DEF 2011 (Apr. 2011)	209,521	209,999	212,031	217,062	222,930			
DEF 2012 (Apr. 2012)	210,408	207,994	207,103	204,681	205,539	208,834		
DEF 2013 (Apr. 2013)	210,033	206,050	202,582	199,116	199,250	201,142	203,836	206,539
Social security bodies								
DFP 2011-2013 (Sept. 2010)	298,392	307,383	314,942	326,316				
DEF 2011 (Apr. 2011)	299,433	307,528	314,927	326,303	337,942			
DEF 2012 (Apr. 2012)	299,312	305,133	311,898	317,401	326,589	335,326		
DEF 2013 (Apr. 2013)	299,312	305,347	312,416	320,360	329,985	338,885	347,653	356,584
Total General Government								
DFP 2011-2013 (Sept. 2010)	676,145	679,169	688,777	705,737				
DEF 2011 (Apr. 2011)	669,462	677,107	683,802	699,175	717,228			
DEF 2012 (Apr. 2012)	670,381	672,627	676,842	677,725	687,709	700,615		
DEF 2013 (Apr. 2013)	669,948	669,613	666,538	671,377	679,373	693,230	705,836	718,273

(*) excluding interest and resource flows to other levels of government
Calculated based on ISTAT and MEF data

Appendix 2 - *Forecasts of spending in gross fixed investment (million of Euros)*

	2010	2011	2012	2013	2014	2015	2016	2017
Central government								
DFP 2011-2013 (Sept. 2010)	7,631	8,345	6,784	7,473				
DEF 2011 (Apr. 2011)	8,290	9,284	7,158	7,749	7,984			
DEF 2012 (Apr. 2012)	8,034	8,800	8,490	8,460	8,443	8,483		
DEF 2013 (Apr. 2013)	8,192	8,230	8,208	9,401	9,335	9,068	8,919	8,603
Local government								
DFP 2011-2013 (Sept. 2010)	25,717	22,648	21,851	22,081				
DEF 2011 (Apr. 2011)	23,373	21,946	20,206	20,047	20,158			
DEF 2012 (Apr. 2012)	23,858	22,832	21,462	20,978	21,269	21,540		
DEF 2013 (Apr. 2013)	23,862	22,519	21,062	18,979	18,939	19,333	19,707	20,109
Social security bodies								
DFP 2011-2013 (Sept. 2010)	100	-194	-84	-75				
DEF 2011 (Apr. 2011)	216	0	-350	20	50			
DEF 2012 (Apr. 2012)	326	398	1	53	101	149		
DEF 2013 (Apr. 2013)	326	348	-46	-123	-118	-112	43	49
Total General Government								
DFP 2011-2013 (Sept. 2010)	33,447	30,800	28,550	29,480				
DEF 2011 (Apr. 2011)	31,879	31,230	27,014	27,816	28,192			
DEF 2012 (Apr. 2012)	32,218	32,030	29,953	29,491	29,813	30,172		
DEF 2013 (Apr. 2013)	32,380	31,097	29,224	28,257	28,156	28,289	28,669	28,761

Calculated based on ISTAT and MEF data

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