

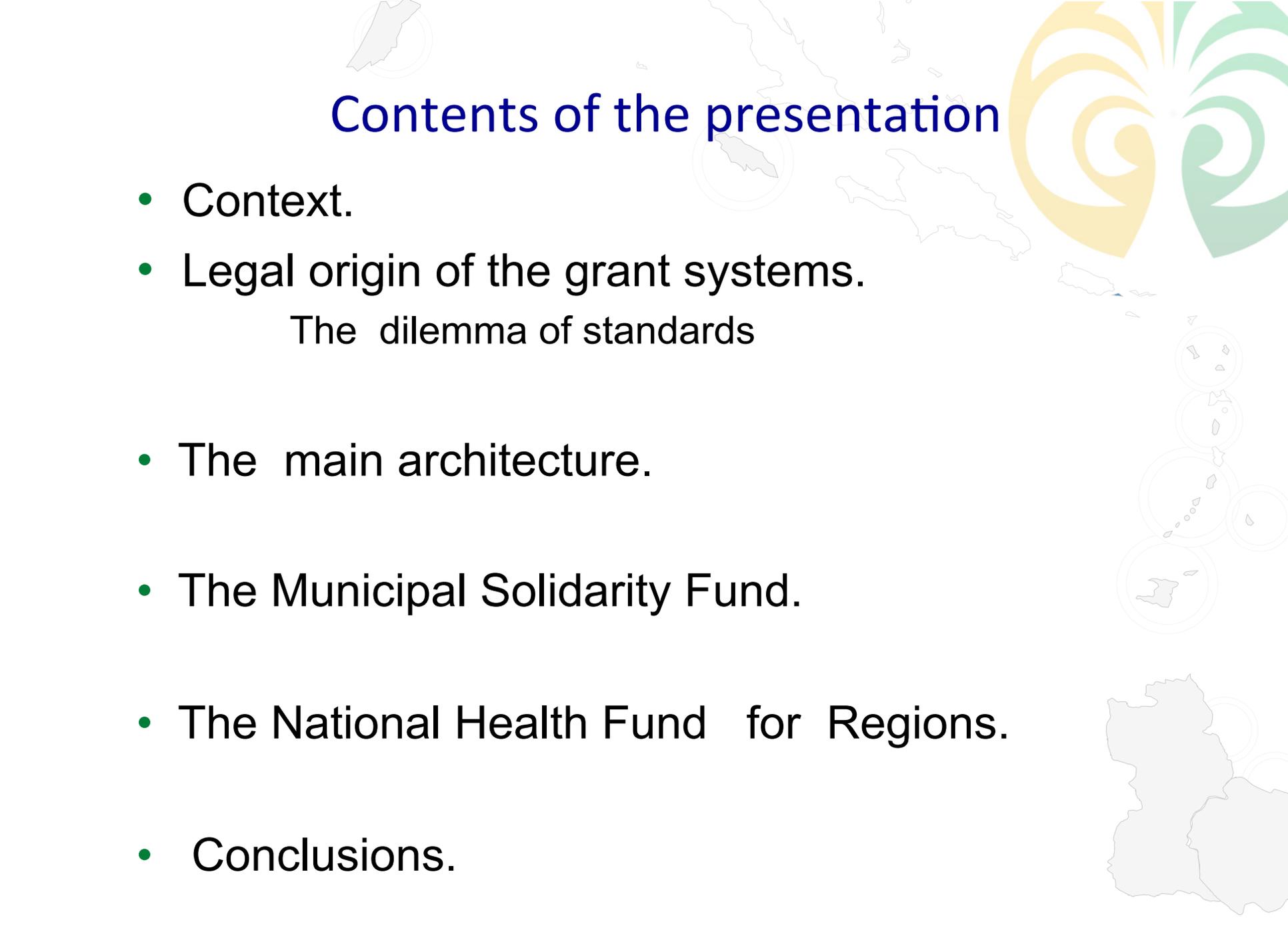


Ambition beyond feasibility? Equalization transfers to regional and local governments in Italy

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Contents of the presentation

- Context.
- Legal origin of the grant systems.
The dilemma of standards
- The main architecture.
- The Municipal Solidarity Fund.
- The National Health Fund for Regions.
- Conclusions.

Context

- At the municipal level is very similar to the Spanish one.
- Many, 8,000, municipalities. Big and small, very different.
- Same legal/institutional framework.
- Municipalities are represented by the the *Associazione Nazionale Comuni Italiani* (ANCI). Very powerful.
- ANCI has a clear small-medium sized municipality orientation. Big municipalities have mainly a veto power.
- Municipalities are also involved in the “Federalism of the Executive”. Particularly, through the *Conferenza Stato-città ed autonomie locali* and the *Conferenza Unificata*.
- However, in this ambit their large number is a factor of weakness.

The legal origin

- The Constitution of 2001 assigns (Article 117) to the central government the:
determination of the basic level of benefits relating to civil and social entitlements to be guaranteed throughout the national territory.
- Not spelled too clearly, but sends two messages with reference to regional and local services:
The determination of standards of service provision for fundamental functions.

The guarantee of provision.

Interpreting the legal origin: the dilemma of standards

- Basically, the constitutional aims at implementing the principle of inter jurisdictional equity.
- Residence should not have impact on access to public services and on the cost of accessibility.
- It implies, necessarily, the use of standards. The Italian constitution refers also to *garanteing*.
- The practice, also in Italy as in the rest of the world, is to use standards to determine total grants, without forcing their implementation, because
 - in a decentralized system is hard/not congruent to impose standards to subnational governments.

The inter-jurisdictional equity principle

$$\frac{\sum_1^t E_{c,d,ef,..j}}{R_{j,wy}} = k$$

Various subscripts are parameters that define standards.

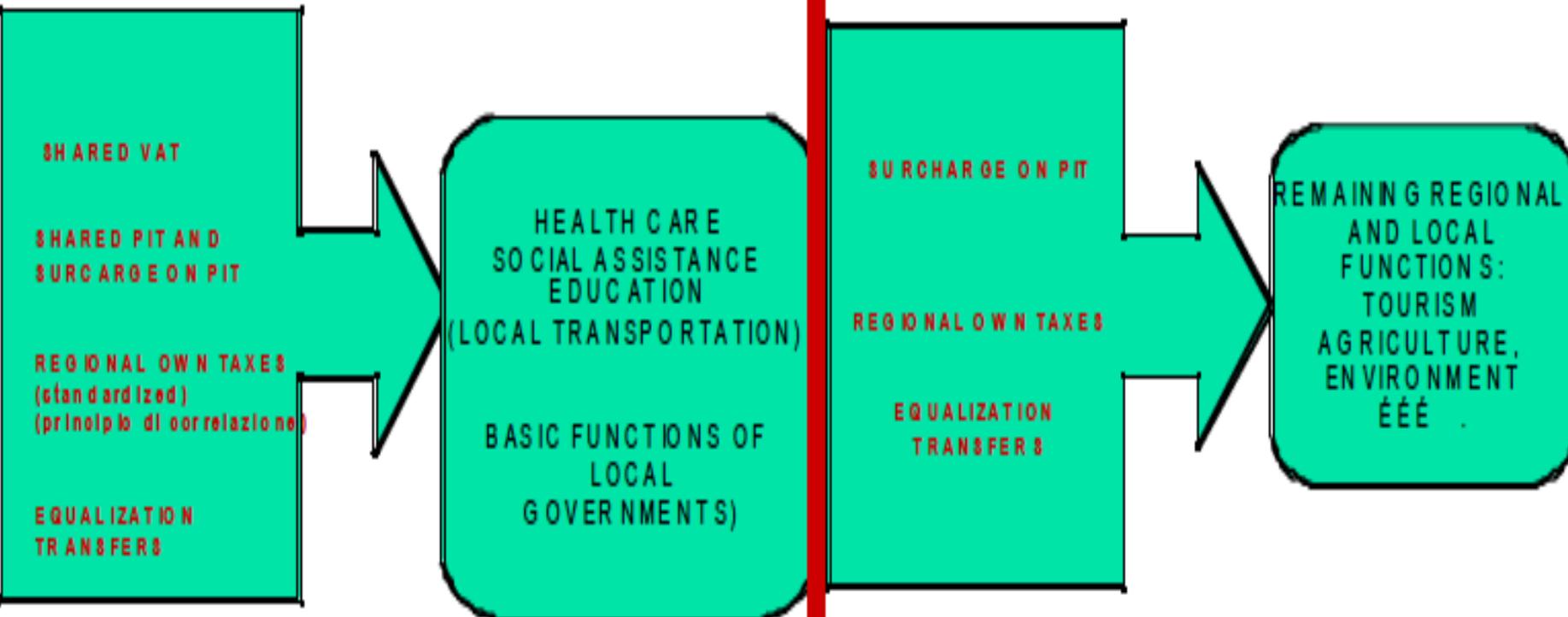
Equality of K implies a strict interpretation of inter-jurisdictional equity.



IMPLEMENTATION OF 2001 CONSTITUTION

Essential Services

Other Services



EQUALIZATION TRANSFERS BASED ON STANDARD COSTS REFERRED TO ESSENTIAL LEVELS OF SERVICE PROVISION

EQUALIZATION TRANSFERS BASED ON FISCAL CAPACITY

The Municipal Solidarity Fund (MSF)

- Is mostly a horizontal equalization fund, fed by a varying percentage - 22,43% for 2017- of the municipal property tax (IMU/TASI) with almost no central government supplement.
- Has three components:
 - a) is the so-called historical share, TI. It is the difference between central transfers before MSF, minus its share of IMU/TASI going to the Fund.
 - b) fills the gap between standard needs and fiscal capacity:
$$TF_i = SN_i - FC_i,$$
 - c) equalizes fiscal capacity with reference to non fundamental functions. $TC_i = AC - FC_i$

In total $TS_j = iTI_j + fTF_j + cTC_j.$

Smoothing the equalizing impact

- Government is worried about excessive change.
- Keeps the historical component at a high level.
- Also reduces the weight of fiscal capacity.
 - Less than 50% of it is taken into account.

Smoothing the equalizing impact

Year	Historical Component α	Parameters Equalization Target β	Weight to basic functions γ	Weights of components		
				Historical component i $(1-\beta+\alpha\beta)$	Equalization needs f $(1-\alpha)\beta\gamma$	Equalization of fiscal capacity c $(1-\alpha)\beta(1-\gamma)$
2015	0,800	0,458	0,700	0,908	0,064	0,027
2016	0,700	0,458	0,700	0,863	0,096	0,041
2017	0,600	0,500	0,800	0,800	0,160	0,040
2018	0,450	0,500	0,800	0,725	0,220	0,055
2019	0,300	0,500	0,800	0,650	0,280	0,070
2020	0,150	0,500	0,800	0,575	0,340	0,085
Since 2021	0,000	0,500	0,800	0,500	0,400	0,100

Standard needs

- Determined according the so called Regression Cost-Based Approach (RCA)
 - Needs are defined with reference to past expenditure.
 - They are the expected value of the model.
 - After sterilization of variables impacting on actual expenditure, but considered to not reflect standard needs.

Regression analysis

- “Pure” expenditure functions: output cannot be measured
 - $y = \alpha_0 + \alpha'X + \gamma'W + \delta'Z + \eta'T + \varepsilon$
 - X are demand and supply variables;
 - W are cost and price (normalizing) variables;
 - Z represents choices about provision (direct production, local utilities, consortiums);
 - D are regional dummies (efficiency varies between regions).
- “Increased” expenditure functions :output cannot measured, but provision of service is identified
 - $y = \alpha_0 + \alpha'X + \gamma'W + \delta'Z + \eta'T + \lambda'D + \zeta$
 - D indicating when the service is provided.
- cost functions, when output is identified
 - $y = \alpha_0 + \alpha'X + \gamma'W + \delta'Z + \eta'T + \theta'C + \psi$
 - W includes output indicators;
 - C are clusters of demand variables.

Detail on variables and weights

Variables	Administration	Local police	Urban services	Local public transport	Social services	Kinder gardens	Education	Garbage collection and disposal
Population variables (1)	43%	9%	10%	5%	20%			
Physical/territorial variables (2)	19%	18%	47%	38%				
Idiosyncratic demand variables (3)	28%	54%	41%	15%	8%			
of which tourism(4)	14%	18%	9%	5%				
Modes of provision (5)		7%		36%	5%	16%		2%
Characteristics of service provided (6)						40%	44%	13%
Demand Clusters (7)						35%	51%	34%
Input prices (8)	10%	12%	2%	6%	4%	9%	5%	1%
Regional dummies (9)				64%		48%		

Sterilization of variables

1. Huge, non justified, discretion involved in the exercise.

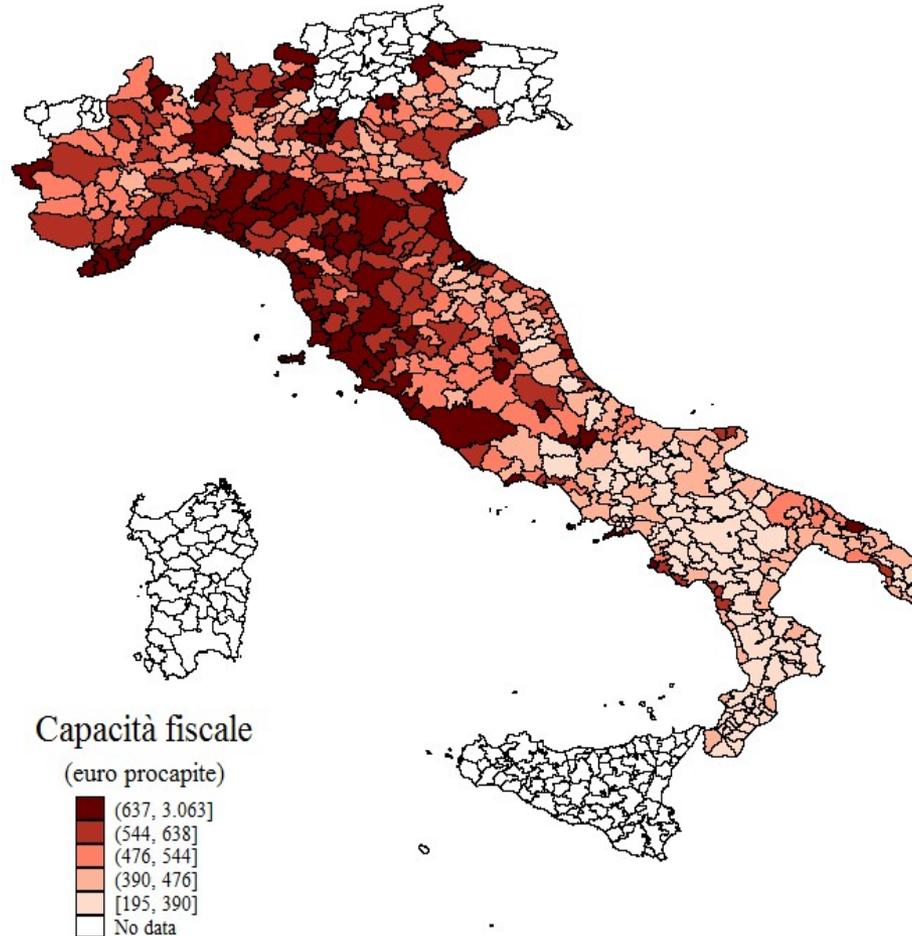
2. Distortion. Example: city uses a local public utility.

- Leads, supposedly, to a reduction of expenditure, reflecting a more efficient way of operation.
- The coefficient associated would be negative.
- If dummy is kept in the calculation of standard needs, we are within the logic of the model.
- However, municipalities with public utilities spend less and have lower standard needs. Will receive less.
- Hence, a perverse incentive.
- Sterilizing the dummy, brings in a correct incentive, but we are no more in a standard needs determination framework.

The determination of fiscal capacity

	Collections	Weights	Standardization
Imu-Tasi (property tax)	12.957	45	Representative tax system RTS
Surcharge to the personal income tax	2.547	9	
Correction for evasion/erosion (<i>Tax gap on Imu-Tasi</i>)	356	1	
Garbage collection/disposal fee	7.107	25	No standardization
Other taxes charges and fees (Residual fiscal capacity)	5.661	20	Regression Analysis
Total fiscal capacity	28.629	100	

Fiscal capacity by clusters of municipalities



Collection and elaboration of information

- Data is collected by means of two extremely large surveys filled by municipalities.
 - The first survey refers to service provision and is 13 pages long;
 - the second one refers to financial and personnel data and is 20 pages long (samples of surveys on request).
- Direct collection of such a big amount of information from beneficiaries/losers is a very impressive effort.
- It raises, however, a few problems.
- The system has a strong built-in incentive to manipulate information.
- Control and validation of data.
 - Presently, control is done statistically with singling out of outliers and subsequent request of additional information.
 - The system also imposes a high burden on small municipalities that can not be able to provide the right information.

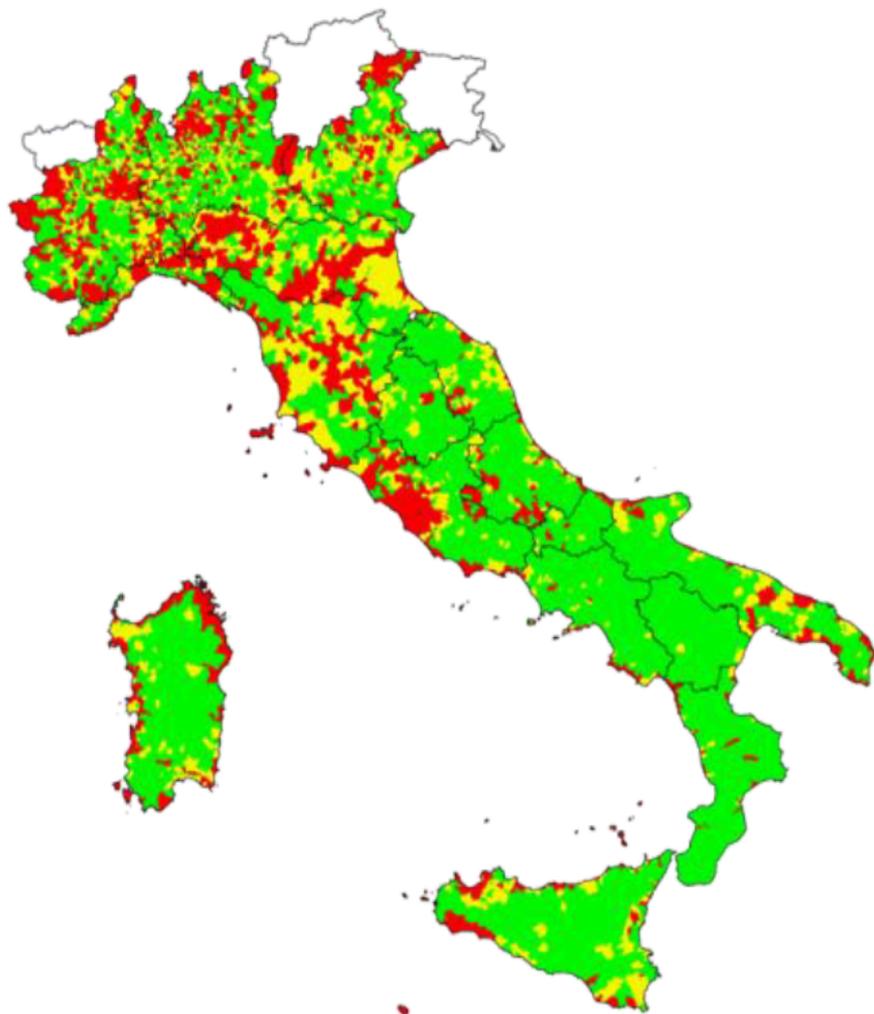
Determination of individual allocations

Very simply done

Allocation coefficients for expenditure, a_{sni} , are determined by summing up, for each municipality standard needs calculated for each category of expenditure and by dividing the sum by the corresponding national total.

- $\sum SN_{ji} / \sum SN_J = a_{sni}$
- The same procedure for fiscal capacity
- $\sum FC_{ji} / \sum FC_J = b_{sni}$
- Net allocation is then the difference: $a_{sni} - b_{sni}$

The results of Municipal Solidarity Fund



Green areas : winners

Red areas: 'no hope' losers.
Historical component is negative. They loose even before entering.

Yellow areas: 'no lost hope' losers:
the negative equalization component is larger than the positive historical component.

The results of Municipal Solidarity Fund in percapita

Municipality	Area	Tourist	Population 31/12/2016	MSF Total allocation	MSF Per capita
Napoli	S		974.074	246.696.640	253
Palermo	S		674.435	91.656.940	136
Messina	S		238.439	61.180.215	257
Catania	S		314.555	39.326.689	125
Taranto	S		201.100	24.336.809	121
Genova	N		586.655	17.300.423	29
Pozzuoli	S		81.661	17.197.513	211
Torre del G o	S		86.275	16.872.350	196
Salerno	S		135.261	16.700.085	123
Foggia	S		151.991	15.302.997	101
Monza	N		122.671	-13.144.064	-107
Firenze	N	x	382.808	-14.173.591	-37
Verona	N		258.765	-14.739.604	-57
Rapallo	N	x	29.796	-18.386.031	-617
Brescia	N		196.480	-19.746.188	-100
San Remo	N	x	54.807	-20.423.150	-373
Padova	N		210.401	-37.898.940	-180
Bologna	N		386.663	-41.045.798	-106
Milano	N		1.345.851	251.817.720	-187
Roma	C		2.864.731	420.764.982	-147

Equalization of Regions: The National Health Fund

- Health represents 75 percent of regional expenditure.
- Definition of standards started long time ago: LEAs.
- LEAs used to ensure that regions are effectively providing levels and types of care that are considered essential.
- The system is relatively centralized with high level of central intervention and monitoring.
- Help negotiate the total amount of the Fund.
- The Fund is financed with standardized revenue from big regional taxes, plus central government grants.

Equalization for Regions: the National Health Fund

Areas of activity (LEAs)	Share on total (%)	Allocation indicators
Preventive care	5	Population
Outpatient care, of which	51	
Pharmaceuticals	11,6	Population weighted by age group, with annual ceilings
Specialist care	13	Population weighted by age group
Clinics, ambulance, etc.	18	Population
General practitioners	7	Population
Inpatient care (Hospitals)	44	50 % population; 50% population weighted by age group

Equalization for Regions: the National Health Fund



- Behind the appearances
 - The Fund is completely negotiated between the central government and the regional governments.
 - Within the State-Regional Governments Conference.
 - Parliament rubber stamps the agreements, but is no happy.

Conclusions

- The determination of standards needs is a Herculean task, particularly with municipalities.
- No surprise that Municipal Solidarity Fund achieves only partially its aims.
- Results are, more or less, in line with other countries engaged in similar equalization grants systems.
- Standardization of expenditure needs has not been achieved and I wonder how it can be achieved in the practice.
- Opposition to the Fund is increasing and the Association of Municipalities has already demanded the temporary freezing of its operation.
- Political constraints can be harder to overcome than technical obstacles.