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The Gamble of Fiscal Federalism in Italy

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THE GAMBLE OF
FISCAL FEDERALISM
IN ITALY

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Abstract

The implementation of fiscal federalism in Italy will witness an essential aspect of the functioning of the constitutional reforms of 2001 taking shape, i.e. the independent raising of financial resources by local government within the framework of coordinating principles laid down by national law. Also because the question of fiscal federalism, i.e. the allocation of resources among different levels of government, raises a constitutional issue of paramount importance that goes to the very heart of the form of state. It concerns the relationship between central and local politics, the common need to have resources to fund public services and, above all, the guarantee that all citizens can enjoy their civil and social rights equally.

Keywords: constitution; federalism; finance; fiscal; Italy; local; national; public services; resources; rights.

The Gamble of Fiscal Federalism in Italy

Tommaso E. Frosini

With the 2001 reform of the Italian constitution, in particular Title V dealing with relations between central and local governments, Italy has taken its first steps toward a federal system. In fact, Italy has gone from a regional system in which central government enjoyed all the powers, combined with a limited role for local government, to a system that can best be described as “federal-like,” as the federalization process has not yet been completed, especially in terms of establishing a house of parliament representing the interests of the regions, provinces and municipalities.

A significant step toward the development and growth of the federal system in Italy will undoubtedly occur through implementation of fiscal federalism governed by Article 119 of the constitution. Until now, there has been a structural anomaly: the federal system has been achieved only in terms of administrative functions (Bassanini Law) and legislative powers (reform of Title V of the constitution), while the whole issue of funding has remained as it was before, based essentially on a model of grants issued by the central government. The effect of this asymmetry is that public spending (excluding pensions and interest) is divided equally between central government on the one hand and regions/local authorities on the other, although the latter raise less than 18 per cent of tax revenues. Thus, there is a weak link between taxation and spending. Centralized government may well have been checked but federalism has not been created.

From this perspective, the Italian situation is similar to that of Spain in the 1980s, when the new democratic constitution granted greater legislative and administrative functions to the autonomous communities there, but not the power to levy taxes. This lack of a link between spending and taxation led to public expenditures spiralling out of control. The remedy was fiscal federalism, which was quickly and resolutely introduced shortly afterward.

By contrast, in Italy, central government continues to be the paymaster of last resort. It is clear that a federal system that does not also incorporate fiscal federalism will not be very effective. Maintaining a model essentially based on grants from central government in a country that has witnessed a decentralization of significant legislative powers since 2001 creates serious confusion, disassociates spending from taxation, generates an institutional situation that makes it almost impossible to keep public accounts under control and fosters duplication of programs and services, inefficiencies and little accountability. This defect damages the system like a virus as the figures on public spending by central and local governments over the past few years demonstrate.

Constitutional Background and Italian Federalism

Briefly, before examining the issues associated with fiscal federalism and its implementation, it is worth explaining the “federalist-like” system that exists in Italy today. The constitutional reforms of 2001 significantly overhauled the relationship between the legislative powers of the state and those of the regions. Article 117 of the constitution sets out the exclusive jurisdiction of the state (for example, foreign policy, defence and armed forces, the administration of justice, immigration, etc.) and the concurrent jurisdictions of the state and the regions, whereby the former lays down the basic principles in a national law and the latter specify the contents in more detail through regional laws (for example, foreign trade, health care, scientific research, etc.). All other matters not specified in the constitution fall within the jurisdiction of the regions, which in effect amounts to a residual jurisdiction in their favour.

The 2001 constitutional changes did not just concern the distribution of legislative powers between the state and the regions. Other issues were addressed too, the most important of which, and quite representative of the entire system, is the principle enshrined in the first paragraph of Article 114 of the constitution: “The Republic is composed of Municipalities, Provinces, Metropolitan Cities, Regions and State”. This meant the state, regions, metropolitan cities, provinces and municipalities are all at the same level, thereby overturning the previous approach that saw the state as above everyone and everything.

But is Italy a federal country? If one considers the classic federal countries, perhaps Italy cannot be considered to have a federal system. There are no elements of strong autonomy for constituent units as, for example, in the United States and Germany (e.g. relationship between constituent parts and local authorities, involvement of constituent parts in any constitutional revision process and role in the administration of justice). However, if we consider the constitutional reform of 2001, the regions and local authorities have become bodies that together with the state make up the Italian Republic and that enjoy legislative and administrative autonomy guaranteed directly by the constitution. The central government cannot limit their autonomy if it is within the boundaries permitted by the constitution itself.

Compared to the past, the central government has more limited powers to intervene to safeguard the unity of the system and to limit the authority of local government. What the 2001 constitutional reforms lack are transitional provisions that guarantee the changeover to the new system. These are slow processes. For example, regional authorities were envisaged by the 1948 constitution but they were actually created only in 1970.

Today, the most important factors are:

- a) The actual implementation of the reform.
- b) Negotiation and sharing among central government, regions and local authorities.

- c) The interpretation of the Constitutional Court, which decides on the constitutionality of laws.

Law 42, passed on May 5, 2009, is key to promoting this implementation process and already contains in its title a reference to “fiscal federalism.” Is this perhaps the Italian route to federalism?

The implementation of fiscal federalism, whose details will be explained shortly, involves an essential aspect of the functioning of the constitutional reforms of 2001 taking shape, i.e. the independent raising of financial resources by local government within the framework of coordinating principles laid down by national law as foreseen in the first paragraph of Article 119 of the constitution: “Municipalities, Provinces, Metropolitan Cities and Regions shall have financial autonomy with respect to revenues and expenditures.”

The second, third and fourth paragraphs of Article 119 of the constitution specify as follows, respectively:

- a) Local authorities, from this standpoint equivalent to the regions, may set and levy their own taxes and revenues (“Municipalities, Provinces, Metropolitan Cities and Regions shall have independent financial resources. They set and levy taxes and collect revenues of their own, in compliance with the Constitution and according to the principles of co-ordination of State finances and the tax system. They share in the tax revenues related to their respective territories.”)
- b) National laws must establish equalisation funds without restrictions as to how they may be used (“State legislation shall provide for an equalization fund, with no allocation constraints, for the territories having lower per capita taxable capacity.”)
- c) The overall resources raised from the foregoing sources must be such as to fully fund the functions of the regions and local authorities (“Revenues raised from the above-mentioned sources shall enable Municipalities, Provinces, Metropolitan Cities and Regions to fully finance the public functions attributed to them”).

The ruling principles of local taxation have thus been significantly modified in light not only of the wording of the new Article 119, but also of the indispensable link that Title V establishes between the same Article 119 and Article 117 of the constitution, granting the state exclusive legislative power over national taxes (paragraph 2, sub-paragraph e) and granting the state and the regions concurrent jurisdiction in relation to “coordination of the public finances and taxation system” (paragraph 3), evidently granting the regions residual exclusive jurisdiction over regional and local taxes.

It must be said that, from the standpoint of the method, implementing Article 119 within the framework of the new Title V of the constitution calls for a deep transformation of the Italian state, perhaps the most radical one in decades. It means committing a vast number of regions and local authorities to be able to rigorously manage resources, increase the efficiency and productivity of their facilities for providing services, assess performance and adopt “carrot

and stick” policies capable of fostering ability, merit, quality and productivity. It also means putting in place an essential tool to attain the transformation of the institutional and administrative system, which has often been announced in the past (and to some degree started), but which has never been fully achieved.

As well, the question of fiscal federalism, i.e. the allocation of resources among different levels of government, raises a constitutional issue of paramount importance that goes to the very heart of the form of the state, because it concerns the relationship between central and local politics, the common need to have resources to fund public services and, above all, the guarantee that all citizens can equally enjoy their civil and social rights.

It is important to note that the essential levels of civil and political rights remain in the sphere of national legislative jurisdiction.

Since 2001, both regions and local authorities (provinces, metropolitan cities and municipalities) have enjoyed autonomy directly guaranteed by the constitution. As for legislative powers, both the state and the regions can pass laws on the subjects that fall within their jurisdiction, allocating “administrative functions” to local authorities, according to the principles set by the constitution (in summary: the subsidiarity principle). However, the state has exclusive legislative power for a series of matters that touch upon regional jurisdiction, including identification of the fundamental functions of local authorities. The distinction between fundamental functions and administrative functions of local authorities is not a simple one. Therefore, through the fundamental functions clause, the state can significantly limit the legislative autonomy of regions concerning the exercise of administrative functions.

For a series of historical and financial reasons, local authorities are not generally in favour of regional power. They prefer to engage in direct dialogue with the central government, and they prefer the far-reaching and thorough intervention of the state when it comes to fundamental functions. This also has an impact on financial relations. It is, therefore, not completely correct to state that the Italian system follows a hierarchical structure: central government – regions – local authorities. This naturally makes the financial system for the operations of the regional and local authorities more complicated.

Law No. 42 and the Implementation of Fiscal Federalism

Article 119 of the constitution, and hence Italian fiscal federalism, is to be implemented through delegated legislation whereby parliament entrusts the national government – through Law No. 42 /2009 – “Delegation to the government in the matter of fiscal federalism further to Article 119 of the Constitution” – with the task of adopting legislation to establish and organize fiscal federalism. It should be said that the principle that informs the law is “institutional loyalty among all levels of government,” which applies to the whole process of implementation of fiscal federalism, as well as the principle of “participation by all public adminis-

trations in attaining the objective of the national public finances consistent with the restrictions imposed by the European Union and international treaties.”

The federalism in the constitution is thus a “joint” one, in which healthy competition among areas is not a *bellum omnium contra omnes* (war of everyone against everyone), but a system of co-operation, emulation and subsidiarity aimed at creating the best conditions for the effective protection of all citizens’ rights, securing sustainable growth for the nation as a whole through harnessing the energy and resources of each regional and local community, adapting management choices and mechanisms to the peculiarities of each community, re-establishing political accountability for resources and spending, fostering the productivity and efficiency of public institutions and enhancing the synergy between private initiatives and public action, all within the logic of horizontal subsidiarity.

Given the complexity of the law that has been passed, its main criteria and principles can be summarized in these 10 points:

1. It is provided that the move to the new system must not lead to a greater fiscal burden for citizens. The greater taxation powers of the regions and local authorities will correspond to a reduction in the taxation imposed by the central government commensurate with local government’s greater fiscal autonomy. The overall tax burden should not increase and every transfer of central government functions to local government should be accompanied by the transfer of human resources and facilities to avoid duplication of functions or additional costs.
2. Fiscal autonomy entails:
 - the end of the grants system based on historical spending and the gradual move to a system based on standard needs.
 - the introduction of effective taxation and spending powers for local governments, meaning there will be taxes whose content the regional and local authorities may determine, within the limits and framework laid down by law. In essence, these are: i) derived taxes, or taxes established by the state but whose revenue the regions and local authorities are entitled to; ii) regional and local surtaxes (a given proportion of the revenue remains with the geographic area that generated it; iii) own taxes properly speaking, in the sense of taxes established by the regions and local authorities themselves.
 - a series of regional and local taxes that assure flexibility, room for manoeuvre and territoriality, with the latter criterion expressing more than the others the ethos of the system that it is sought to introduce, since it assigns a central role to the concept of territory in its many meanings. This ensures a link between where tax revenues come from and where they are spent.
 - the possibility for more efficient administrations that manage to contain costs, services being equal, to fine tune their taxes (for example, reducing the rates or introducing deductions or exemptions).

In particular, to finance essential levels of services (especially health, education and welfare), regions will have the following available to them: i) regional taxes to be determined on the basis of a link between the type of tax and the service provided; ii) a personal income tax (IRPEF) surtax; iii) regional share of VAT receipts; and iv) specific shares of the equalization fund. On a transitional basis, expenditures will be financed by revenues from the existing regional production tax (IRAP) until it is replaced by other taxes. The provinces and municipalities will have their own taxes, shares of revenue, surtaxes and dedicated taxes linked to domains such as tourism or urban mobility.

- a connection between the tax and the function performed by the authority (principle of correlation between taxation and benefits).
3. As regards standard needs and costs, funding for the regions and local authorities must be based not on historical spending, which could also include waste and inefficiency, but on costs calibrated with regard to a public administration's average level of efficient management. Reference is to be made to the costs borne by an administration that provides services and performs functions respecting average efficiency parameters. In other words, the effective need in relation to each service rendered is to be taken into account. Therefore, the councillors will have to answer to the electorate for any costs over and above the level established as the benchmark.
 4. Equalization is based on the following suppositions:
 - overcoming the criterion of historical spending.
 - reference to standard needs and costs for expenditure in connection with essential levels of service that must be guaranteed throughout the country and for the fundamental functions of local authorities.
 - full equalization for authorities with the lowest tax revenue generating capacity per capita as regards expenditures in connection with essential levels of service and the fundamental functions of local authorities, as always within the limits of standard needs and costs. Equalization means bridging the gap between the different areas of the country, guaranteeing essential services to the citizens of each region in accordance with the principle of social solidarity, thereby assuring that the least well off regions can provide services to their citizens with minimum uniform levels. For local public transportation, reference will be made to the national benchmark and the associated standard needs.
 - equalization of the differences in capacity to generate tax revenues must be done without changing the order and without impeding modifications over time, depending on how the economic picture develops. In short, the wealthiest region, province or municipality before equalization must contribute to the equalization fund, but may

not after equalization end up being poorer than another area that previously had fewer resources. For example, if the revenues pro capita from taxation are 100 in a wealthy region and 70 in a poorer region, equalization can take place to achieve some balance and guarantee essential services for everybody. However, equalization cannot be so extensive as to produce an outcome whereby because of it the resources pro capita in the first region end up being 80 and those in the second one 90, perhaps only because the second region spends more and in a worse way.

- the regions may redefine equalization for the local authorities in their territory, subject to agreement with those authorities.
5. In order to afford guarantees for local authorities, Law No. 42 /2009 provides for:
 - taxes established by the state or region in their capacity as holders of legislative power, subject to a significant degree of flexibility and respect for the local authority's own autonomy.
 - sharing of national and regional taxes, to assure the stability of the local authority.
 - full equalization based on standard needs for expenditure in connection with fundamental functions.
 6. The system of rewards and sanctions envisages:
 - rewarding virtuous conduct and behaviour that demonstrates efficiency in the exercise of fiscal powers and in financial/economic management.
 - penalizing the bodies that do not achieve an economic/financial balance or do not provide essential levels of service, including disqualification from office for the management in charge of local authorities suffering from a financial crisis and, in the worst cases, the option for the state to step in directly itself. Irregularities that cause serious financial difficulties amount to violations of law for the relevant regional managers.
 7. The convergence pact is a mechanism through which the central government, subject to joint discussions and assessment at a so-called "unified conference of state and regions," sets out a path for dynamic coordination (which must be submitted to parliament with the national economic and financial planning document) to achieve the objective of a convergence between standard costs and needs, as well as service targets that the local authorities must adhere to. In the event of a failure to attain the objective, the central government establishes the reasons for this and takes suitable corrective action through a special purpose "plan to attain convergence objectives."
 8. Transitional provisions envisage the establishment of metropolitan areas whose autonomy in matters of revenue and expenditure should be commensurate with the complexity of the broader functions assigned to

them. Moreover, other fundamental functions are identified in addition to those already exercised by the province concerned. They are:

- general planning of the territory and infrastructure networks.
- structuring of coordinated systems for the management of public services.
- promotion and coordination of economic and social development.

The transitional provisions also set out the procedures governing the establishment of metropolitan cities through a referendum to be held in the provinces in which the cities of Turin, Milan, Venice, Genoa, Bologna, Florence, Bari, Naples and Reggio Calabria are located. It is further provided that a specific legislative decree will regulate the resources to be allocated to the city of Rome for its role as the national capital. Finally, municipalities will be granted a series of specified administrative functions in addition to those that they already exercise.

9. The following principles will govern coordination of the various levels of government:
 - transparency in the different capacity per capita to generate tax revenue before and after equalization so as to highlight financial flows between bodies.
 - a role for each region and local authority in observing the stability pact.
 - introduction of a series of rewards and sanctions for, respectively, the most and least virtuous bodies.
10. In order to implement the fifth and sixth paragraphs of Article 119 of the constitution, Law No. 42/2009 provides:
 - specific rules for allocating additional resources and adopting special measures in favour of given regions and local authorities to remove particular forms of economic and social imbalance (the measures are financed by the state budget, European Union grants and national co-funding).
 - implementation of the sixth paragraph of Article 119 of the constitution on the transfer of state assets to the regions and local authorities.

Coordination of Fiscal Federalism

A “parliamentary commission for the implementation of fiscal federalism,” comprising 15 deputies and 15 senators appointed by the speakers of both houses of parliament, will give opinions on draft implementing legislation, to check progress on implementing Law No. 42 /2009 itself, submit observations and provide the government with whatever evaluation might be useful in drawing up implementing legislation. The commission is to be dissolved at the end of the transitional phase. The commission is to liaise with the regions and local authorities and, to this end, a committee of their representatives is to be set up. Should the government decide not to follow the opinion of the

joint parliamentary commission or those of the other relevant parliamentary commissions, it must submit the text concerned to both houses of parliament and make a statement thereon before them; after 30 days, the government may adopt the legislation in final form.

Further, a “joint technical commission for the implementation of fiscal federalism,” set up at the Ministry of Finance as an advisory body, is to provide advice to the government and local authorities as well as obtain and analyze whatever information may be necessary for the drafting of the implementing legislation. And finally, a steering body in the shape of the “permanent conference for the coordination of the public finances,” comprising all of the institutional players involved in the process of achieving fiscal federalism, will check the new financial order of the regions and local authorities, the adequacy of resources and the consistency of data. It performs an advisory role and is the forum for sharing information among all concerned.

The commitment of central and local governments to fight tax evasion and avoidance is acknowledged, including rewards for the regions and local authorities that achieve positive results in this area in terms of increased tax revenues.

It is provided that the regions with special constitutional status and the autonomous provinces shall contribute the objectives of equalization and solidarity, shall exercise the rights and duties associated therewith and shall adhere to the internal stability pact and EU obligations in the manner to be set forth in legislation implementing their respective regional and provincial constitutions. Any new functions allocated to them will be funded by sharing revenues from national taxes and excise duties. Within the framework of the State-Regions Conference, a round table is established between the central government and each single region with special constitutional status and each autonomous province, in order to assure their participation in achieving equalization and solidarity and observing the internal stability pact. This forum also serves to assess the consistency of the financial resources allocated to the said regions and provinces after the entry into force of their constitutions in order to check coherence with the new system of public finance.

The transitional phase for regions: in respect of the equalization fund, there will be a gradual move away from the grants given to the single regions in 2006-2008 to the principle of standard needs. The new equalization system will operate once the financial aspects of the essential levels of services and fundamental functions have been determined with the switch to the principle of standard needs within five years. For non-essential needs, levels of funding will have to progressively depart from historical spending within five years, but in cases where regions cannot objectively bear the change, the state may adopt corrective action in the form of compensation, nevertheless only for a maximum of five years. On a transitional basis, regions will not have to bear any shortfall between projected and real revenues.

The transitional phase for local authorities: the state and the regions will

fund the additional administrative functions transferred to the local authorities as well as those that the latter already perform. The system of historical spending is to give way to one based on financing standard needs within a period of five years for expenditures connected to fundamental functions and other spending. Until such time as the rules on fundamental functions take effect in full, the functions performed by provinces and municipalities are financed on the basis that 80 per cent of expenditures are to be considered as fundamental and 20 per cent as not fundamental.

Finally, there are financial saving clauses providing that:

- the new system of public finance is to be compatible with the growth and stability pact.
- the reform and implementing legislation must not lead to any new or greater burden on public finances.
- the transfer of functions must be accompanied by a transfer of personnel, to avoid the duplication of functions.

Very briefly, it is meant to guarantee

- financial independence and accountability for all levels of government.
- granting of independent resources to regions and local authorities in accordance with the principle of territoriality.
- prohibition against adopting measures in relation to the taxable base and rates for taxes that do not pertain to one's own level of government;
- an adequate degree of fiscal flexibility through establishing a basket of taxes and shares of taxes payable to the regions and local authorities, the composition of which is made up to a significant extent by taxes that allow room for manoeuvre;
- fiscal flexibility spread over a number of taxes with a stable taxable base and distributed in a generally uniform manner throughout the country, to enable all regions and local authorities (including those with the lowest revenue-generating capacity) to fund – through harnessing their own potential – spending levels beyond merely the essential services and functions associated with local authorities;
- reduction of national taxation commensurate with the increased taxation powers of the regions and local authorities linked to a corresponding reduction in the central government's human resources and facilities;
- regulation of local taxes in a way that allows horizontal subsidiarity to be fully exploited;
- territoriality of taxes, neutrality of taxation and a ban on the exporting of taxes.

In relation to a taxable base not subject to taxation by the state, regional law may: a) introduce regional and local taxes; b) decide the changes to tax rates or tax relief that municipalities, provinces and metropolitan cities may adopt in the exercise of their own autonomy; a region may share the revenue from regional taxes and its part of national taxes with local authorities.

Upcoming Challenges

What will be the main problems associated with the application of the law on fiscal federalism? The end of the system whereby the central government transferred funds to local governments implies a massive undertaking: all state funds aimed at financing regions and local authorities are to be replaced by revenues raised as a result of the fiscal autonomy enjoyed by those same regions and local authorities, with the only exceptions being equalization funds and special measures.

The application of Law No. 42 /2009 will be important to establish how federal Italy has really become.

Consider the following examples.

If most of the regional funding ends up being guaranteed by sharing the revenue from national taxes, the autonomy of regions will be limited. As a matter of fact, revenue sharing is not substantially that different from grants. On the contrary, the autonomy of the regions will be stronger if they mainly depend on their own taxes or surtaxes rather than revenue sharing. The same is true for local authorities, which are further limited by the fact that they do not have legislative power.

If the so-called “special measures” provided for by the constitution for specific local government bodies become a form of additional and permanent equalization, there will be no drive toward efficiency for the public administration. If special measures are limited in scope and time, the less virtuous too will improve their efficiency. The main difficulties in enforcement will lie in the sharp differences between certain geographical areas of Italy. North and South exhibit strong economic and infrastructure differences. The unemployment rate in the South is much higher, while per capita income is much lower. Tax evasion is higher there, too. The net average household income in 2006 in the North was almost 31,000 euros compared with only 23,500 euros in the South. The phenomenon of the underground economy is mostly concentrated in the South, which accounts for 45 per cent of the total.

The transitional phase, which will last no less than seven years, will involve an attempt to reduce the infrastructure deficit of the least wealthy areas as well as increase the efficiency of public administration. Another example is costs for health care are generally higher in the South but many people living there move to the North to receive public medical care.

More coordination and collaboration among national, regional and local authorities is envisaged as it is necessary to avoid duplication of activities, and hence of spending. Bodies that efficiently act to fight tax evasion will receive additional resources. Already today, municipalities can keep part of the higher receipts stemming from their efforts in tax collection. The enforcement of the law will be accompanied by the transfer of a meaningful set of assets from the state to regions and local authorities.

Lastly, there is the issue of special regions. For historical reasons, five of the 20 regions in Italy enjoy a special degree of autonomy guaranteed by five separate constitutional laws (Valle d'Aosta, Trentino Alto Adige, Friuli Venezia Giulia, Sicily and Sardinia). Each constitutional law also guarantees that the regions concerned have significant fiscal autonomy. The law on fiscal federalism requires the state to have "open negotiations" with special regions (especially the first two named above, which are the richest) to involve them in the equalization process to help the less wealthy areas.

Alongside the rationalization of expenditures through benchmarking, the second plank of the fiscal federalism reform is increasing the fiscal autonomy of local authorities through a series of provisions foreseen in Law No. 42 /2009, ranging from principles and guidelines to be followed in the delegated legislation to the more detailed provisions specifically set forth in Articles 12 and 21, the latter concerning the transitional phase. The value of fiscal autonomy can be deduced, for example, from Sub-paragraphs A and E of Article 2.2, which place autonomy in generating tax revenues, accountability at all levels of government and the allocation of resources on the basis of territoriality at the top of the list of principles that the law itself seeks to achieve. But also the provisions in subparagraph U on tax assessment and collection that assure efficient methods for direct allocation and automatic payment, seem to point in the direction of local taxation, especially if read in conjunction with the rewards on offer for virtuous behaviour and efficiency in the exercise of taxation powers as per subparagraph Z.

Overall, therefore, local taxation should acquire more weight as compared to national taxation within a framework in which the total tax burden should fall, thanks to the beneficial effects of cuts in spending, or at the very least, rationalization. In any event, the Constitutional Court has ruled out that any reform of the financial independence of local government, and specifically the regions, can operate to decrease their resources without affording them alternative means of raising revenue, taking into account the overall financial picture in light of the functions exercised, rather than just single taxes or items of income (Judgments 29/2004, 241/2004, 381/2004, 431/2004 and 155/2006).

Tax revenues should also play a greater role in the context of local finances as a consequence of greater autonomy in levying taxes, and as a result of the power that the regions enjoy to introduce local taxes in relation to a taxable base not already subject to regional or national taxation (Articles 7.1.b.3 and 12.1.g).

Naturally, these are just general principles destined to be incorporated into and elaborated on in detailed delegated legislation. That said, they can serve as interpretative tools in cases of judicial review in light of the provisions of Article 119 of the constitution and can be relied on by the Constitutional Court in this regard.

The entry into force of Law No. 42 /2009 and associated delegated legislation should resolve the issue of the relationship between a region's legislative power

and local authorities' regulatory autonomy in tax matters. The Constitutional Court's view that legislation governing the basic framework for local taxes is a precondition for local authorities to exercise their own regulatory powers should open the way to rules on three levels operating on two planes, national and local or regional and local, as the Court itself has stated.

What remains to be seen is whether, in the wake of Law No. 42 /2009 and the first pieces of delegated legislation, the issue of the types of sources of funding for local authorities has been addressed. Initially, the Constitutional Court ruled that for non-tax funding, the state could act "in conformity with the new division of competencies and new rules," also without the need to first enact a coordinating national law (Judgment 16/ 2004), only to then admit shortly afterward that the maintenance of existing funds and their financing was lawful as was the making of changes to the legal framework that had established them (Judgments 320/2004, 423/2004, 36/2005 and 225/2005).

As for the transfers specified in the current Article 119 of the constitution, i.e. the equalization funds, special measures and additional resources, the Court has already laid down some essential markers. The fund must be used solely for bodies that have a lower tax revenue generating capacity and the grants must not be subject to restrictions on their use.

The Court then held that, regardless of the provisions of subparagraph E of the second paragraph of Article 117 of the constitution and the state's exclusive jurisdiction in the equalization of financial resources, the regions could set up or replenish funds devoted to special measures and additional resources whenever they exercised planning powers for areas within their remit (Judgments 16/2004 and 49/2004). The Court held that state funds divided among the regions (Judgment 370/2003) or among regions and local authorities (Judgment 49/2004) or among local authorities circumventing the regional level were unconstitutional and ruled out the transfer of resources conceived and given effect to by methods other than those envisaged by the fifth paragraph of Article 119 of the constitution, methods that owed much to past practice when national law and the way the Ministry of the Interior was run allowed virtually any form of transfer of resources to local authorities on the basis of essentially discretionary distributions.

It is not clear whether the Court considers that only national law impinging on the financial independence to raise revenue and spend funds infringes on the fifth paragraph of Article 119 of the constitution, or whether it considers that this is also the case for provisions that are not binding, as regards spending, but nonetheless create a general dependence on state revenue fall foul of the constitution. It appears that grants from the central government that by their very nature or structure have nothing to do with the types covered by the fifth paragraph of Article 119 of the constitution are admissible even though they come with restrictions as to their use provided that they concern matters falling within the state's exclusive remit.

The interpretation thus far given by the Constitutional Court regarding the limits to state grants that can be made consistent with Article 119 of the constitution would seem to bring to the fore the division of legislative power enshrined in Article 117 of the constitution. This might well do justice in the specific cases that the Court had to consider in light of the principle of sincere co-operation, but risks depriving the strictly financial and fiscal rules in Article 119 of the constitution of any binding force, thereby opening up an avenue of parallel funding.

It remains to be seen whether, following the entry into force of Law No. 42 /2009 and associated delegated legislation, that approach can be maintained or whether a more rigid assessment will be employed for the extremely detailed rules in both bilateral and trilateral situations.

Any assessment of the degree of implementation of fiscal autonomy must start from what the actual situation is, which can be summarized as follows:

The municipalities can currently rely on the following taxes: municipal property tax, electricity surtax, municipal advertising tax, waste disposal tax, dedicated taxes and a personal income tax surtax.

The provinces likewise can rely on a personal income tax surtax and a share of the electricity surtax, as well as motor vehicle registration tax, motor vehicle insurance tax, a share of landfill taxes, and a waste disposal tax surtax for environmental protection and health functions.

Conclusion

In summary, the new structure of economic-financial relations between central and local governments seeks to overcome the grant system of funding and endow regions, provinces, municipalities and metropolitan cities with greater independence in levying taxes and spending resources, subject to observing the principles of solidarity and social cohesion. Key principles of fiscal federalism are, firstly, coordination of taxation centres with spending centres, thereby automatically ensuring that regional and local bodies will be more accountable for their spending and, secondly, replacement of historical spending based on continuity with spending levels reached the previous year with standard spending.

To become operative, fiscal federalism requires a series of measures that will take at least seven years: two for implementation and five for transition. The law creates an ad hoc commission for drafting the contents of the implementing decrees, to be ready within two years after the entry into force of the law, as well as a permanent commission for financial coordination. -

The funding of the functions transferred to the regions through the implementation of fiscal federalism will obviously lead to the cancellation of the relevant appropriations from the state's budget, including personnel and operating costs.

An equalization fund with no restrictions on its use will be set up to help regions with reduced revenue-raising capacity, as required by Article 119 of the constitution.

Fiscal federalism introduces rewards for bodies that assure high quality services and imposes a tax burden below the average for that of other bodies at its own level of government providing equal services. Conversely, bodies with weak performance can be sanctioned by imposing a ban on hiring personnel and discretionary spending. At the same time, those bodies have to clean up their balance sheets through disposing of part of their real and personal property and using their taxation powers to the maximum allowed.

Should a region or local authority fail to achieve the economic-financial balance and objectives set for it, automatic sanctions are also imposed on executive and administrative organs. Specifically, managers in charge of a local authority which is declared to be insolvent will be disqualified from office.

Turin, Milan, Venice, Genoa, Bologna, Florence, Bari, Naples and Reggio Calabria will become metropolitan cities. Rome, the Italian capital, which already enjoys special legislative, administrative and financial autonomy within the limits prescribed by the constitution, will obtain a special status in the months to follow.

The implementation of fiscal federalism must be compatible with the financial commitments undertaken with the stability and growth pact. In conclusion, the implementation of fiscal federalism is a gamble that needs to pay off for the sake of progress for the Italian economy and institutions.

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