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Tax credits an introduction and the USA practice

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One among many available policy instruments

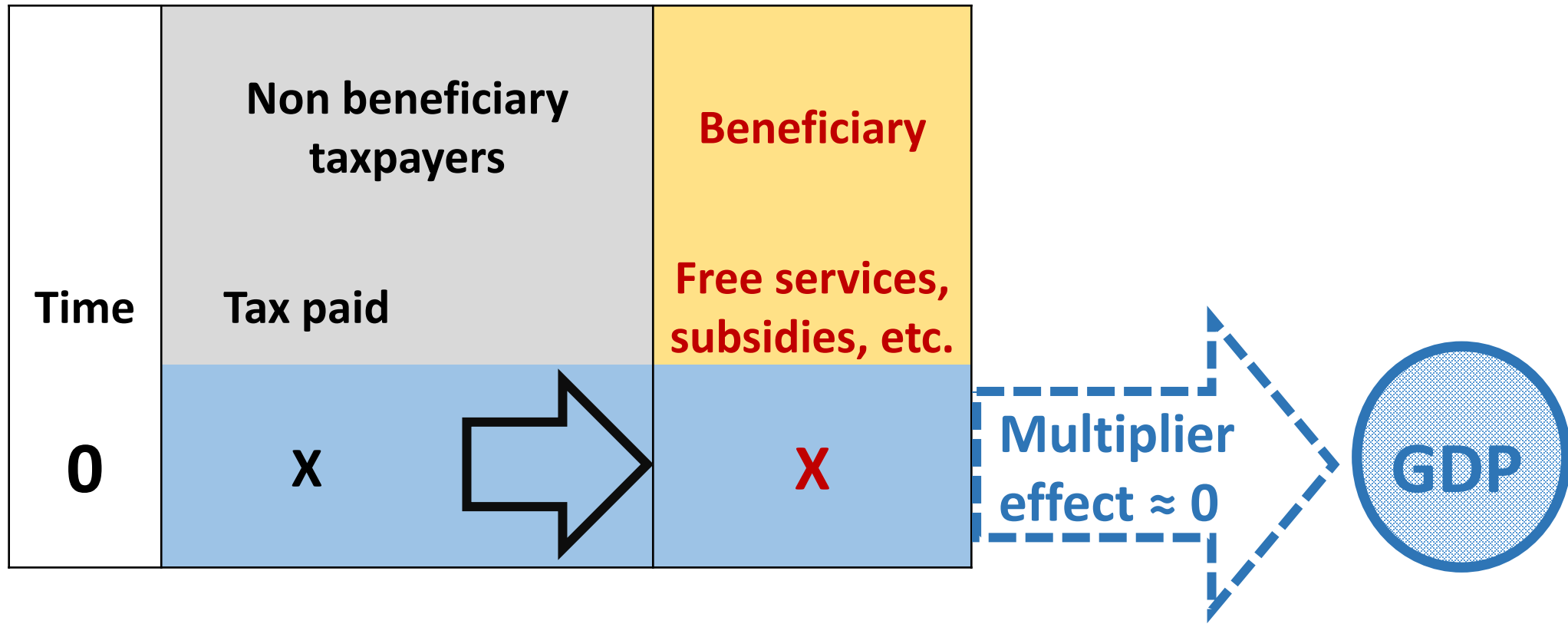
Government may deliver **merit and public goods** in several ways, in particular:

- **Directly**, through public expenditure
- **Subsidising** prices and/or firms (where allowed by state aids discipline)
- Stimulating private to purchase the same goods and services through **tax credits (TC)** and other incentives (tax expenditures, etc.)

All the previous measures must be **funded** by compensating revenues, cuts on other items of the public budget or through borrowing or issuing money (where allowed)

Funding public expenditure, subsidies, etc.

Direct public expenditure and **subsidies** must be financed contextually, thus the **overall multiplier effect** is small or null

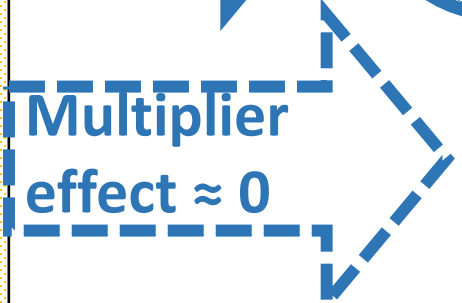
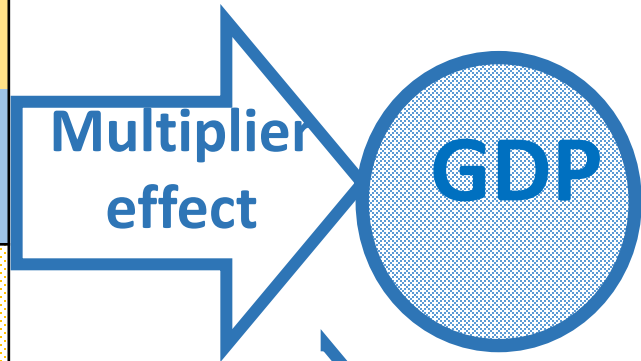
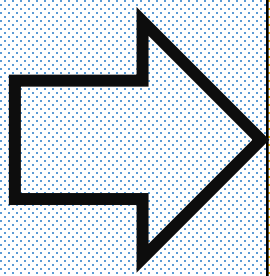


Funding tax credits

Since **TC** arise **after** private spending, they can be funded by **future** sources of financing, thus the **impact multiplier effect** is large

This is the main **advantage** of **TC** over other policy measures

Time	Non beneficiary taxpayers Tax paid	Beneficiary of TC		
		TC	Tax liabilities	Net tax Incentivised expenditure
0		k X		
1	X	-X	X	0
2	X	-X	X	0
...	...	...	...	...
k	X	-X	X	0



Other advantages of TC

Private expenditure incentivised by TC is strictly **voluntary**

It implies less **crowding-out** risks (i.e. larger **additionality**)

Larger **multiplicative effects** on GDP, since expenditure do not pair corresponding public revenues **instantaneously** (tax reductions may be claimed by the beneficiary only in the **future**)

Less **inflationary** risks, since TC do not increase current **liquidity**

Wide **policy consensus**, since taxpayers do incentivised expenditures **voluntarily** (hopefully selecting goods and services in a well functioning **market**)

Many empirical studies assess that TC are **more effective** than other incentives

Some drawbacks of TC

Fine targeting of measures is challenging, since expenditure is **voluntary**

The final outcome of TC depends crucially on the **take-up** of incentives, which is **hardly predictable** (as well as its overall burden for the public budget)

Beneficiary may be unable to exploit TC fully if his/her **future fiscal liabilities** are not large enough

Thus TC mainly benefit **richest** taxpayers and those less **liquidity constrained**

To overcome the former two drawbacks, TC should be **monetised** or **transferred** (voluntarily) to other taxpayers who expect to have large fiscal liabilities in the future

Some (good) USA practices

USA government has made use of **monetised** and **transferable TC** since many years, even as a substitute for some **social benefits**

EITC (earned income TC) program is the main benefit for poor households since the seventies

CTC (children TC) helps families with children

R&D TC promotes investment and innovation (also adopted in most European countries)

TC have sustained the show business for many years (also in UE, India, etc.)

IRA (Inflation Reduction Act) broadens TC for private **green expenditure**

EITC and CTC

For each dollar **earned working**, EITC assigns a TC to **poor** taxpayers

Since a working poor likely does not expect to accrue tax liabilities in the future, he/she can receive **cash in advance** for his/her TC from banks and specialised agencies

The same applies to TC on **children**

This practice has many advantages:

- poor **households pay** for better housing, education, health care, etc. (which the government **should provide**) according to their **preferences** and needs
- **regular employment** promoted (since EITC depends on **certified** earned income only)
- TC are **straightforward**

TC on R&D and for entertainment industry

TC is proportional to companies' **expenditure** (with many special cases)

TC can be **compensated** through **association agreements** between firms (some having TC in excess, the others having enough fiscal debt)

It is possible to **sell** the TC to specialised agencies after **certification** from the IRS

A **market** for TC developed and many platforms for the **exchange** of TC arose

Savers can **invest** in TC (**save** assets)

Similar TC schemes exist in the **EU**, but only TC for show business can be generally monetised (also in **Italy**)

TC provided (and extended) by IRA

The IRA was adopted in August 2022 and is **heterogeneous package** of measures to dampen down the effects of **inflation** and **relaunch** the USA economy

IRA provides or extends a number of TC on **green** goods and services (heat pumps, rooftop solar, high-efficiency electric appliances, electric vehicles, etc.) and on house green renovation up to \$14.000 per year per household

It also extend the possibility to **transfer** existing TC (more **eligible** subjects)

Concluding remarks

TC is utilised to **stimulate** the economy (together with other policy tools) in **many countries** and particularly in the USA

The possibility to **transfer and monetise** TC in excess of own tax liabilities is an essential feature of **successful TC** schemes

There are many **advantages** (and few **drawbacks**) in opening a **market for TC**

Secondary market for TC charges only **little** additional burden on the public budget (assuming that only few TC are **non payable**, otherwise beneficiary would be fully **irrational** when they undertake incentivised activities)

The risk of **excessive cost** of TC schemes can be avoided also by limiting taxpayers **eligibility** and setting a **ceiling** to available payable funds

USA taxpayers are generally allowed to trade their TC.

Why **EU nationals** should not?

**Many thanks
for your attention**