The circulation of modern tax ideas in Italy 1950–1970

Cesare Cosciani and the introduction of personal income taxation

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Abstract

In 1973, Italy was among the last Western countries to introduce a mass-based personal progressive income tax (PIT). In other countries, PIT was implemented under the pressure of war financing or due to political demands for redistribution, but in Italy, it was the result of the work of a small group of technocrats led by economist Cesare Cosciani. The article argues that new economic ideas from the US played a key role in shaping the income tax adopted in 1973. The Italian traditional school of public finance, drawing upon marginalist economics, was highly skeptical of progressive and redistributive taxation and, after WWII, opposed the introduction of PIT. However, in the 1950s, despite being a respected member of the Italian school, Cosciani embraced modern public finance based on the theories of Keynes and Lerner. In 1963, he drafted a tax reform centered on a PIT with high countercyclical effects. Policymakers, however, influenced by traditional Italian economic knowledge, limited the tax to labor and business income. Following the identity between saving and investment, capital income was subject to a separate milder regime to stimulate national accumulation.

1. Introduction

In 2022, Italy ranked fifth among OECD countries for tax burden, with tax revenue at 43.0% of GDP, just behind France, Norway, Austria, and Finland. Italy's state involvement in the economy nowadays rivals Nordic welfare states. Such high extraction levels have been possible because all these countries introduced a mass-based personal income tax (PIT) at different points during the first half of the twentieth century. Modern income taxation is personal – meaning that the effective tax rate is adjusted to the personal and financial circumstances of the taxpayer; it is progressive and involves the majority of the population. These features make PIT not only the most redistributive element of modern tax systems but also a fundamental tool for economic policy. Despite the international success of PIT since the 1940s, the Italian mass personal income tax is a recent innovation that only dates back to 1973.

The literature on the rise of modern taxation has primarily focused on political processes or pivotal events (Genschel and Seelkopf 2022). Scholars have investigated the contractual nature of personal income tax (Levi 1988; Daunton 2001) and its connection with political institutions (Aidt and Jensen 2009). More recently, attention has been paid to political competition among social groups (Mares and Queralt 2015, 2020). The two World Wars are often pointed out as the origins of modern redistributive taxation (Scheve and Stasavage 2016). External pressures and economic efficiency are also important factors, such as the decision of the European Economic Community on the introduction of VAT in the late 1960s (Lynch 1998; Konishi 2018). None of these explanations, however, seem to explain the late introduction of PIT in Italy. While political competition among leading parties and international commitments might explain the timing of the reform, they cannot explain why Italian tax reformers opted for a mass-based PIT rather than further relying on indirect taxation or social security contributions. Value-added tax (VAT) was also introduced in Italy in 1973 at the same time as PIT, but its contribution to state revenue has been much smaller.

This article argues that the circulation of ideas and shifts in economic knowledge played a crucial role in adopting PIT in Italy. Until the 1950s, public finance was dominated by the marginalist economists of the Italian School of Public Finance, the Scienza delle Finanze (Buchanan 1960). They conceived taxation as a fee for the public goods and services supplied by the state levied proportionally to the value of national production. Optimal taxes were the ones that minimized the disruption of market equilibria and encouraged saving at the expense of consumption. These principles provided the economic justification for the contemporary Italian direct tax system, which relied on "real" income taxes. Unlike "personal" modern income taxes, real income taxes collected income at source and did not consider the taxpayer's global wealth or personal condition. Real taxes were proportional and did not include minimum allowances or exemptions for spouses or children.

After the Second World War and the end of the Fascist regime, the hegemony of the Italian School was challenged by the circulation of new economic ideas from the United Kingdom and the United States (De Cecco 2010). While most Italian public economists were staunch opposers of Keynes's theories, one senior member of the Italian School embraced new Keynesian public finance, Cesare Cosciani. During the 1940s, Cosciani advised finance ministers and business associations on several occasions with reports based on the teachings of the Scienza delle Finanze. However, in the early 1950s, he developed an interest in Keynesian models and introduced them in his lectures at a time when most Italian academia was hostile to Keynes's ideas. In 1962, when the new coalition government between

Christian Democrats and Socialists gathered a group of scholars to initiate the studies for a new tax reform, Cosciani was the obvious choice to coordinate the committee, thanks to his prestige as a senior scholar of Italian Public Finance. In this role, he designed a new tax system centered on a comprehensive mass-based personal progressive income tax along the US model.

Cosciani's new Keynesian beliefs played a crucial role in shaping the tax system implemented in 1973, but his victory was only partial. Following Keynes, he believed that progressive taxation of income and capital was instrumental for a stable and growing economy. However, following traditional economic views, other economists and policymakers were very wary of taxing capital income, fearing the effects on saving. As a result, capital income tax was subjected to a separate tax regime with different flat rates depending on the type of income (higher for dividends and private bonds, lower or null for state bonds and capital gains). In the article, I trace this change to Italian economic knowledge still being dominated by the tenets of the Scienza delle Finanze, first among them the identity between saving and investment. This belief was shared by public economists and extended to economic planners and left-wing parties.

The decision to introduce a mass-based progressive income tax precisely in 1973 proved pivotal. Between 1973 and 1985, Italian inflation systematically exceeded 10 percent, with peaks around 20 percent in 1974 and 1980. Inflation, coupled with the automatic indexing of wages established in 1975, pushed taxpayers' nominal incomes towards higher income brackets (and higher tax rates) while real income did not change, in a phenomenon called bracket creep. Despite the government's regular intervention in adjusting the tax code nominal values, the bracket creep resulted in an automatic increase of average tax rates, which turned PIT into the primary source of state revenue (Visco 1984, 127–49). Had the Cosciani Commission opted to conserve the previous generally proportional system or to extend VAT, the impact on the state budget would have been much different.

Despite PIT crucial role in state financing across the entire Western world, we still know very little about its implementation outside the UK and the US. In this paper, I intend to shed light on the introduction of PIT outside Western Anglo-Saxon countries by focusing on the case study of Italy. Modern fiscal knowledge originated in the US and the UK postwar and circulated to Western Europe (Hall 1989; Nützenadel 2005). In the Italian case, new tax ideas were crucial in shaping the general tax reform in the late 1960s.

The article contributes to three strands of literature. First, it sheds light on the role of economic knowledge in the shaping of economic and tax policies (Steinmo 2003). Structural change often determines the timing of institutional change, but this ultimately depends on the supply of ideas available. As Mark Blyth argues, "While exogenous material changes may help to explain why a particular institutional order becomes unstable, such infusions of instability do not in themselves explain how the new or modified order takes the form that it does" (Blyth 2002, 8). To understand the "specific forms that institutional change takes," we must study the economic ideas that made it intelligible. The argument is not that ideas are the ultimate determinant of tax innovation. Instead, economic knowledge provides a new playing field for political competition and interest groups to interact.

Secondly, the article contributes to the Italian debate on the delayed circulation of Keynesian ideas in Italy (Becattini 1984; De Cecco 1989). Paladini and Rodano (2003) have rightly pointed out the crucial role of a few public economists in the circulation of Keynesian economics in post-WWII Italy. In the article, I present two reasons public finance was crucial in reshaping Italian economics. The first had to do with the personal connections of Cesare Cosciani, who was very influential within the Italian business community and governmental circles before his conversion to Keynesianism. The second reason concerned the specificity of modern “Keynesian” taxation. While deficit spending was seen as a heresy in the Italian economic community, modern public finance promised higher revenue and containment of inflationary pressure without hurting economic growth.

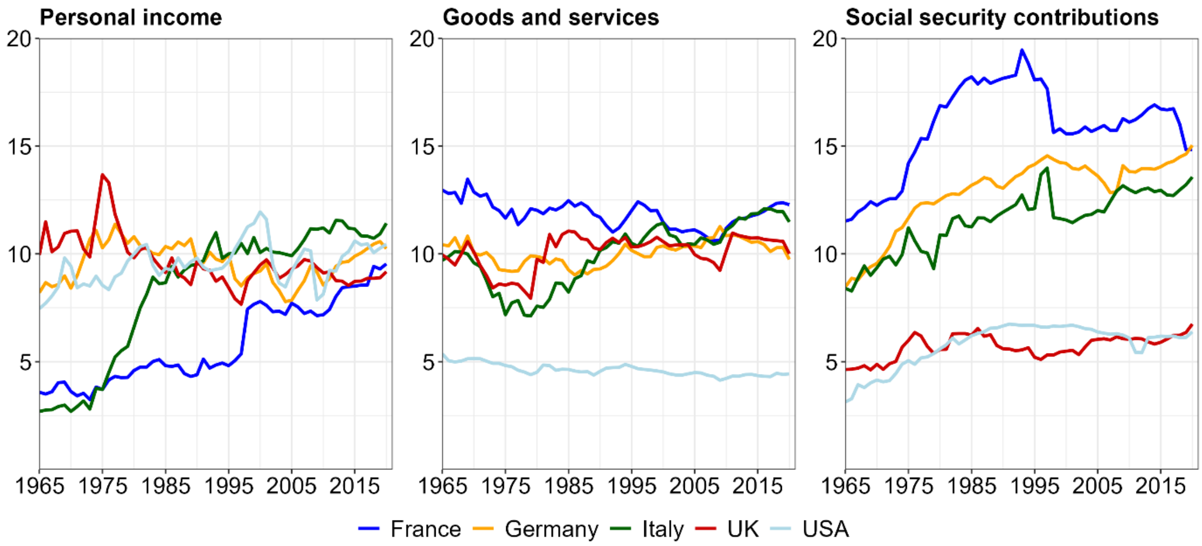
The concept of circulation plays a central role in my analysis. UK and US tax knowledge did not simply influence or penetrate the Italian context but acquired different characteristics interacting with local economic knowledge and political dynamics. Here, I will draw upon the approach of the history of knowledge to investigate how modern tax ideas circulated and evolved in the Italian context (Östling 2018). In this process, agency plays a key role. My argument is centered on the figure of Cesare Cosciani, the public economist who was the intellectual author of the 1973 tax reform. Cosciani’s interest in new economic knowledge from the US, thanks to his personal influence among the economic and business elite, proved crucial for the theoretical framework of tax reform.

Thirdly, my article contributes to the debate on fiscal transition in Italy during the 1960s and 1970s. An extensive literature by contemporary public economists stressed the shortcomings of the new system introduced in 1973 (Gerelli and Valiani 1984; Fausto 2023), especially with respect to the differential treatment of employees vis-à-vis self-employed, entrepreneurs, farmers, and rentiers (Pedone 1979). My contribution intends to shed light on the role of economic knowledge in shaping the evolution of the tax system. Due to the limited space available, I will not discuss political debates around the reform. Once the reform project was presented to Parliament in 1967, it became a central issue in Italian politics. However, contemporary discussions did not dispute the central features of the reform as designed by the Cosciani Commission – mass taxation, personality, and progressivity – but rather focused on tax rates, exemptions, and enforcement mechanisms.

Although the paper focuses primarily on ideas and discourses, it is essential to consider the evolution of income tax revenue in Italy and other major countries (France, Germany, the UK, and the US). Theoretical assumptions and statutory tax rates are important, but ultimately, what matters is the revenue produced by the tax system. For the period after 1965, I relied upon OECD tax revenue statistics, collected yearly based on homogenous budgeting categories. For the period before 1965, I relied as much as possible on individual national sources to isolate the income tax contribution in the different countries.

The paper is structured as follows. The second section reconstructs the circulation of new fiscal ideas between the US and Western Europe. Section three focuses on the figure of Cesare Cosciani and the circulation of new tax ideas in Italy between the 1950s and the 1960s. Section four discusses the transformation of personal income tax within the context of Italian economic knowledge.

Figure 1. The three pillars of modern taxation in major Western countries (revenue as a share of GDP)



SOURCE: OECD tax revenue statistics.

2. The rise of modern taxation

Income taxes appeared in Western Europe during the second half of the nineteenth century. The first permanent income tax was introduced in Britain in 1842. The tax, affecting only the very rich, was meant to convince the electorate and the taxpayers that the British tax system was equitable and did not favor any specific class (Daunton 2001, 77). Initially, the tax was strictly proportional, but at the beginning of the twentieth century, different rates were introduced for different types of income (Daunton 2001, 361): rates were higher for "unearned" income (rents and dividends) and lower for "earned" income (trade and salaries). In 1909, two years after the introduction of differentiation, the income tax also became progressive, with a standard rate for poorer taxpayers and an additional surtax for the wealthy.

Germany also did not have a unified income tax until 1920, but a modern income (*Einkommensteuer*) existed in Prussia since 1891. The tax was due by all citizens and was levied on taxpayers' global income with progressive tax rates. The exemption threshold was very high, so only roughly 30 percent of the Prussian population was subject to it (Schremmer 1989, 446). As stated by public economist Adolph Wagner, the Prussian income tax was likely to be the most efficient income tax in Europe, as not only did it rely on the global income of the taxpayer, but such income was taxed according to progressive rates and personal deductions (Wagner 1896, 164).

Post-unification Italy overcame the problem of state financing with a combination of foreign models and internal innovation. In 1864, a new tax system was extended to the newly unified country. Direct taxation was the cornerstone of the system, consisting of three different income taxes, each addressing different sources of income. Two of them focused on income produced by land and buildings. Income values, however, were assessed through a land. The real innovation in the Italian tax constitution was the tax on movable wealth (*imposta di ricchezza mobile*), which contributed to more than half of direct tax revenue (De Cecco and Pedone 1995, 274–78). The tax was designed along the British income tax, with different schedules depending on the type of income: capital, trade, and employment. Differently from the British model, Italian policymakers opted from the beginning for differentiation of the rates, higher for capital income and lower for labor, based on the idea that capital income had a higher ability to pay than labor income (Galeotti 1967, 412). The personal condition of the taxpayer did not play any role in determining the tax, making the taxes "real" as opposed to "personal" taxes like the British income tax. This regime was preferred as it required less administrative capacity than personal regimes (Galeotti 1967, 421–28).

The US can be considered a latecomer in introducing personal income taxation. Between 1861 and 1870, a federal income tax was implemented as a temporary war measure modeled on the British income tax, with flat rates and personal exemptions (Brownlee 2016, 63–64). With the approval of the Sixteenth Amendment in 1913, the way was finally open for the introduction of a permanent federal income tax. The system consisted of a standard flat rate of 1 percent with a very high deduction, which "excused virtually all middle-class Americans", and a progressive surtax ranging from 1 to 6 percent for wealthier taxpayers. Unsurprisingly, in 1913, the tax accounted only for 1.5 percent of state revenue (Brownlee 2016, 90, 292).

The financial challenges caused by the First World War led to a divergence between Britain and the other countries. In the UK, income tax grew significantly in terms of tax rates and the number of taxpayers becoming a modern PIT. Between 1914 and 1919, in the United Kingdom, the income tax exemption was reduced and tax rates for both the standard rate and the surtax dramatically increased, from 5.8 to 30 percent and from 2.5 percent to a range between 5 and 22.5 percent. Taxpayers increased from roughly 1 million to 4 million (Daunton 2002, 42, 47). In the 1920s, total tax revenue averaged 20 percent of national income, primarily thanks to the income tax (fig. 2). The US and Germany also reformed their tax systems but with less impressive results in terms of revenue. The US Revenue Act of 1916 increased the standard income tax rate from 1 to 2 percent and the maximum surtax rate from 6 to 10 percent (Brownlee 1985, 174, 191). Between 1914 and 1919, taxpayers increased from 300,000 to 4 million (U.S. Bureau of the Census 1975, 1110). In Germany, after the meager performance of the Reich's public finance during WWI, income taxation was handed over to the federal level, and a new federal income tax was introduced by Finance Minister Matthias Erzberger in 1920. Unlike the Prussian model, the new tax system reached marginal tax rates of 60 percent and affected roughly 25 million taxpayers (Buggeln 2022, 292, 297, 304).

There was also a rise in income taxation in Italy, but it was less significant, and it was accompanied by an increase in consumption taxes. A turnover tax (*imposta sugli scambi*) was introduced in 1919, together with a comprehensive personal progressive income tax was introduced on top of the existing real income taxes affecting only the very rich (*imposta complementare*). The taxable base for the personal income tax was simply the sum of the taxable income of the real taxes with a significant deduction that limited the tax to a few hundred thousand taxpayers. The personal income tax rates, reformed by the Fascist government in 1923, ran from 1 to 10 percent, while the flat rates of the real income taxes spanned from 12 to 24 percent (depending on the type of income). In terms of revenue, the new personal income tax played hardly any role in the financing of the state (Fausto 1993).

In the UK and the US, the Great Depression radically questioned existing tax regimes and opened the way to a new approach to public finance. In the nineteenth century, the primary purpose of taxation was to provide the revenue necessary to finance public expenditure. At the beginning of the twentieth century, it also acquired the function of redistributing income and wealth, mostly through progressive taxes. From the late 1930s, together with its traditional functions of funding the state and redistribution, taxation acquired a new crucial purpose, what economist Abba P. Lerner called "functional finance" (Lerner 1943). Lerner considered taxation from the point of view of its effects on the economy:

> The central idea is that government fiscal policy, its spending and taxing, its borrowing and repayment of loans, its issue of new money and its withdrawal of money, shall all be undertaken with an eye only to the results of these actions on the economy and not to any established traditional doctrine about what is sound or unsound… The principle of judging fiscal measures by the way they work or function in the economy we may call Functional Finance (Lerner 1943, 39).

These new ideas have been traditionally associated with the Keynesian revolution, but it would be more correct to state that John Maynard Keynes' *General Theory* provided the theoretical foundation for a set of policies that had been unsystematically adopted in the attempt to recover the economy during the Great Depression (Stein 1990). Embryonal elaborations on the effects of taxation on the general level of prices could also be found in the discussions on war financing in Britain during the First World War. However, it was only during the Second World War that the principles of functional finance were fully implemented in Britain (Keynes 1940) and in the US (Shoup, Friedman, and Mack 1943). For the purposes of this article, I will refer to these policies with the terms modern taxation and new public finance.

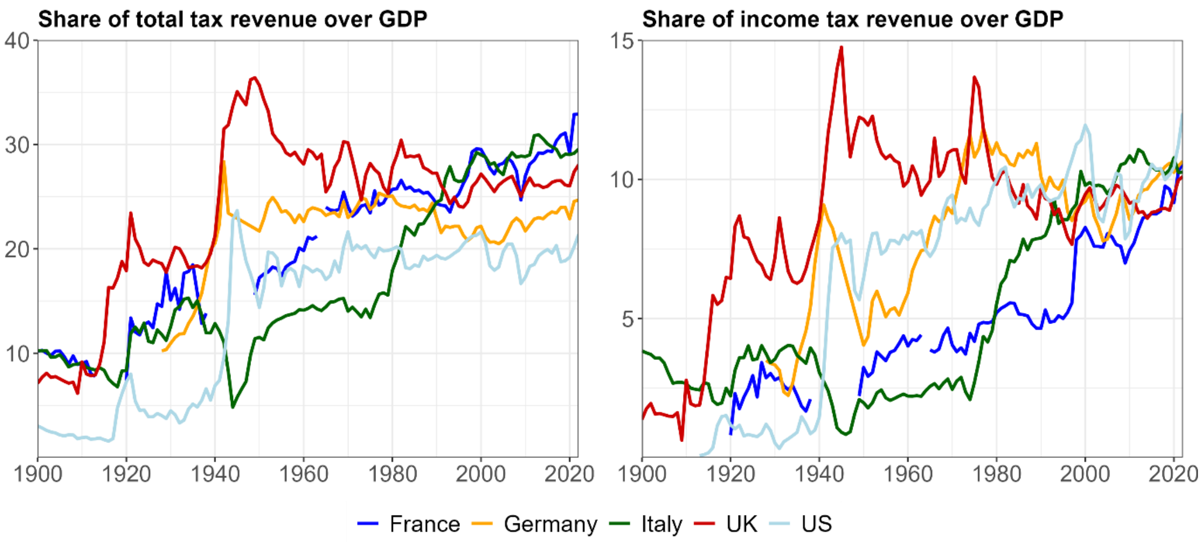
Under the new public finance, taxation becomes a means to stabilize national income. During an economic downturn, tax revenue must decrease proportionally more than national income to provide extra disposable income to the private sector, thus supporting aggregate demand. Conversely, during an economic boom, tax revenue must increase proportionally more to reduce disposable income and depress aggregate demand to avoid overheating and contain inflationary pressure. The revenue from progressive income and wealth taxes varies more than proportionally with a change in the taxable base, making them preferable over consumption taxes.

Progressive taxation also affects the economy by changing decisions to consume or save. The rich generally save large parts of their income, whereas the poor spend most of it on necessary consumption goods. A highly progressive tax will, therefore, reduce the income available to the rich, thus reducing saving and increasing the income available to the poor, thus encouraging consumption. Since, in a Keynesian scheme, consumption translates directly into aggregate demand, progressive taxation stimulates production and employment. As Keynes wrote, “If fiscal policy is used as a deliberate instrument for the more equal distribution of incomes, its effect in increasing the propensity to consume is, of course, all the greater” (Keynes 1936, General Theory, Chapter 8, p. 95).

By the end of the 1940s, all the countries we analyzed so far adopted a modern tax system except for France and Italy. The US and Britain fully implemented modern income taxes during the Second World War, along with the principles of functional finance. In the UK, the number of taxpayers rose from 9.7 million to 21 million between fiscal years 1937/8 and 1947/8. (Daunton 2002, 180). In the US, with the Revenue Act of 1942, a broad-based, highly progressive income tax became the centerpiece of the new tax regime. Between 1939 and 1945, the number of taxpayers increased from 3.9 million to 42.6 million. In Germany, the Weimar tax regime was substantially conserved under National Socialism, although tax rates were substantially increased under postwar Allied occupation (Buggeln 2022, 572). We do not have data for wartime, but in 1936, roughly 16.1 million taxpayers paid income tax out of a population of roughly 67.3 million. In 1950, taxpayers were 12.9 million out of a population of 50.6 million (Statistisches Bundesamt 1972, 103-237-238).

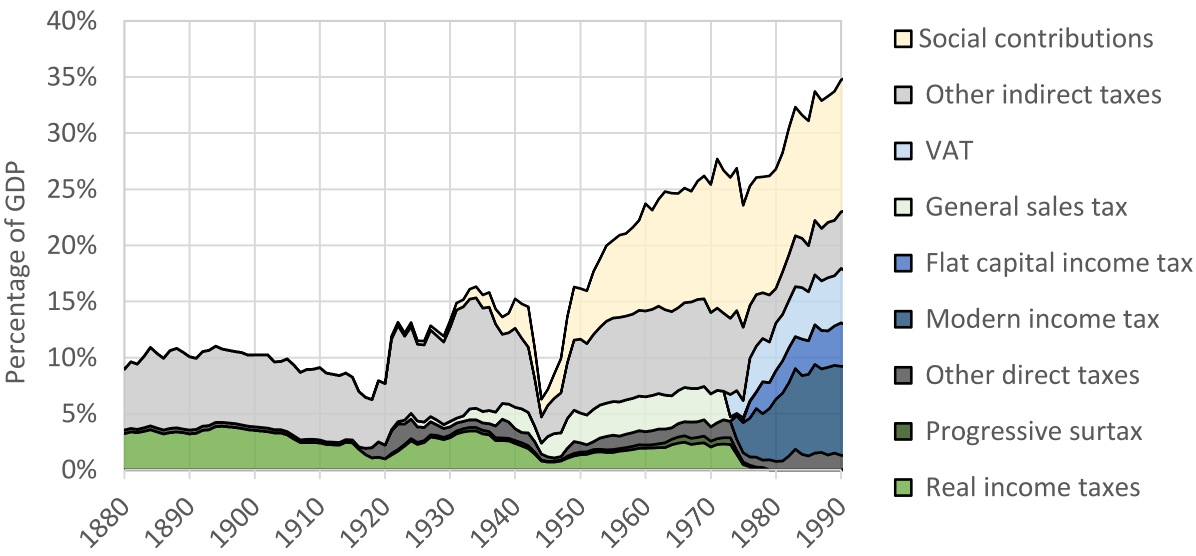
Conversely, Italy still relied on the double system of proportional income taxes for the middle class and small personal surtax for the very rich. As in the other countries, the postwar period in Italy was also dense with radical demands, but they translated into a confirmation of the existing system. The *Riforma Vanoni*, named after DC finance minister and public economist Ezio Vanoni, raised the maximum tax rate of the *complementare* to 50 percent, restructured the tax administration, and mandated tax return filing for everyone except employees. According to the first report following the reform in 1952, real income taxes impacted approximately 2 million households, while just over 1 million households paid the progressive surtax out of a total of 12 million households (Ministero delle Finanze 1953). At this time, direct tax revenue constituted only 20 percent of state revenue or 5 percent of GDP. Such disappointing outcome was due to a combination of hegemonical neoclassical economic thinking, which was extremely wary of progressive and redistributive taxation, and the weakness of the alternative provided by left-wing parties (Bozzi 2021).

Figure 2. Tax revenue in a major Western countries



SOURCES: tax revenue and GDP data after 1965 are from OECD. For the period before 1965, I relied on various national statistics. France: tax revenue from Flora (1983), pp. 299–301; GDP from Toutain (1987). Germany (West Germany between 1945 and 1991): tax revenue from Sensch (2013), Tables C01 and E01 – my series results from sum of the wage tax (*Lohnsteuer*) and the assessed income tax (*Veranlagte Einkommensteuer*); GDP from Ritschl and Spoerer (1997). Italy: tax revenue from Ragioneria Generale dello Stato (1969); GDP from Baffigi (2015). UK: tax revenue from Lanskey and O'Loughnan (2023); GDP from Thomas and Dimsdale (2017). US: U.S. Bureau of the Census (1975), Tables F1, Y343, Y399.

Figure. 3. Composition of Italian tax revenue 1880–1990



SOURCE: author's elaborations on data provided by Ragioneria Generale dello Stato 1969 and Ragioneria Generale dello Stato 1967-1996. I used the new GDP estimates from Baffigi (2015).

3. The Italian School of Public Finance

While Keynesian economists in the US and the UK provided theoretical support for mass-based income taxation, during the Fascist dictatorship and the war, Italy was isolated from international debates. When new economic ideas started to circulate, Italian economists showed a general lack of interest, with few open critiques (Becattini 1984, 26). The economic landscape was dominated by the followers of the Marginalist School, which had famous representatives in Italy, such as Vilfredo Pareto and Maffeo Pantaleoni (Dallera 2013). By the 1940s, the champion of orthodoxy was public economist Luigi Einaudi. Born in Piedmont in 1874, he was the chair of public finance at the University of Turin, which he divided with his teaching at the Bocconi University in Milan and since 1919 as senator of the Italian Kingdom (Faucci 1986). He firmly believed that production should prevail over redistribution and, therefore, the impact of taxation on national accumulation should be minimized.

Like many other economists of the Scuola Italiana, Einaudi considered taxation a payment for a service produced by the state, such as infrastructure, utilities, and protection. Since the state was a factor of production, it deserved its remuneration through taxation. Each lira of production, therefore, bore a debt to the state (Einaudi [1912] 1941, 13). Since each lira had to be taxed the same, saved lire would inevitably be taxed twice, once at the time of the creation of the capital and then every time the capital bore interest. To fully comply with the postulate of equality and avoid the double taxation of the same income, Einaudi argued that income going into savings should be exempted from taxation. The optimal tax system relied exclusively on proportional consumption taxation (*imposta sul reddito consumato*). He even envisioned a tax exemption on "primary consumption," meaning here essential goods and services. This was not to relieve the burden on poorer taxpayers but to make sure the "machine-man" was able to replenish itself through saving (Einaudi [1912] 1941, 56–57). Einaudi's ideal taxes were minimal. The rates of *imposta sul reddito consumato* should avoid the point beyond which the tax does not produce new revenue and instead reduces it due to its depressing effect on consumption (Einaudi [1912] 1941, 65–66).

With his theory, Einaudi claimed to have designed a tax system that drew its legitimacy not on political or moral grounds but on logic and economic efficiency. Logic and efficiency should also become the measure to assess existing tax systems. Indeed, not only was the *imposta sul reddito consumato* the most rational tax, but it was also the most economically efficient because it encouraged saving. The theory's core was elaborated in 1912, but the author continued to refine and expand it in the post-war years. In 1929, he further discussed the economic effects of the taxation of consumed income. He claimed that the tax would lead to the "better satisfaction of public needs consistent with the production of the most abundant national income stream" (Einaudi 1929, 75), meaning that taxation of consumed income would also encourage saving and capital accumulation.

These conceptions led Einaudi to support the existing system of direct taxation consisting of proportional income taxes: higher for capital income, which needed no extra saving to reproduce itself, and lower for labor, which needed more savings to pay for retirement and the reproduction of future workers. In the 1948 edition of his 1932 textbook on public finance, Einaudi praised the traditional "real" system of income taxation, which was reliable and simple to administer (Einaudi 1948, p. 167). Conversely, personal progressive taxation was dangerous as it could lead to the expropriation of the rich. Furthermore, progressive taxation lacked a rational justification. It was impossible to compare utility across individuals. Therefore, it was not necessarily true that the rich derived a smaller utility from the same income unit than the poor. Consequently, there was no justification for the principle advocated by John Stuart Mill of equality of sacrifice, according to which the rich should be taxed proportionally more than the poor (Einaudi 1940 [1938], 170–75). This view was shared among many economists of the Italian School (Fausto 2008, 301–2), and its fortune even reached the US through the works of James Buchanan (1960, 45–47).

Gino Borgatta, another economist within the Italian school of Scienza delle Finanze, shared Einaudi’s view in a contribution for the Economic Commission for the preparation of the Constituent Assembly in 1945: “In the current state of doctrine, progressivity still has no rational financial basis; it is a merely political fact, subject to a wide margin of arbitrariness and thus to injustice and economic damage.” And continued that progressive taxation would “upset savers” and be detrimental for the national income (Borgatta 1946, 278–79). Ernesto D’Albergo, at the time professor of Public Finance in Bologna, shared Borgatta’s concerns. After the destruction of physical capital due to the Second World War, fiscal policy had to encourage national saving to provide the resources to increase workers’ living standards (D'Albergo 1946, 459–60). Therefore, while progressivity was appropriate for capital-intensive economies like the US and UK, it was a threat to Italian recovery (D'Albergo 1946, 460). The abolition of the nominal register of shares introduced during WWII and the extension of flat-rate taxation to capital income could have increased national savings and foreign capital directed towards Italy.

These views, however, were not confined to academic economists. Angelo Costa, a leading industrialist and president of the Federation of Italian Industry (Confindustria), did not believe in taxation's redistributive function, which, according to him, must aim at the mere financing of state expenditure (Ministero per la Costituente 1946, 243–44). He was also skeptical about adopting a single personal income tax system after the German model because of the administrative challenges and the risk of personal exemptions on tax revenue.

The belief in the crucial role of saving was not limited to liberal economists. In his monograph on Einaudi’s thought, Francesco Forte stresses how the attention to a balanced budget and monetary stability as the main premises for the accumulation of savings was also shared by left-wing economist and Finance Minister Ezio Vanoni (Forte 1982, 136). Nonetheless, while in Einaudi, production prevailed over distribution, in Vanoni, redistribution played a fundamental role, if not in economic terms, at least in political terms (Magliulo 1991). This view was shared by a minority of public finance experts, such as the Christian Democratic reformers Salvatore Scoca (Scoca 1944). However, this group had limited opportunities to influence fiscal policy, which liberal economists dominated (Barucci 1978, 141). Even during the six years between 1948 and 1954 when Vanoni was Finance Minister, he could not produce a structural change in Italian taxation.

Of the three main functions of public finance, Italian public economists could only agree on the most traditional one, expenditure financing. By the middle of the century, the redistributive function of taxation was internationally accepted thanks to influential advocates such as Adolph Wagner, Edwin Seligman, and Henry Simons. However, in Italy, redistribution was supported by only an intellectual minority outside the traditional public finance establishment. Furthermore, redistribution could only justify some limited form of progressivity, but not a mass income tax like in Germany, the UK, and the US. As long as saving was considered the engine of economic growth, a general increase in tax rates remained taboo, with it the implementation of modern functional public finance.

4. Cesare Cosciani and the rise of modern taxation in Italy

Einaudi's ideas carried the day until the late 1950s. After the Second World War, while other European countries expanded the size of the state, Italy entered the golden age of Western economic growth with a tax system dating back to the 19th century. Italy was lagging behind both in terms of total revenue and income tax revenue (fig. 2). Although the situation of Italian direct taxation was subject to frequent criticism, only a few authors understood the need for a radical change in public finance.

Until the Second World War, Cesare Cosciani had a rather typical career within the Italian public finance tradition. Born in Trieste in 1908 when it was still the principal port of the Habsburg Empire, he studied public finance in the same city under two of Einaudi's students, Mauro Fasiani and Renzo Fubini (Da Empoli 1978). His first major work was a study of the effect of taxation on the supply of labor in conversation with the writings of Pantaleoni and Einaudi (Cosciani 1934). Starting in 1938, he divided his time between academia and the Association of Italian Joint Stock Companies (Assonime), for which he wrote several reports on tax issues. Assonime also supported Cosciani with the periodical publication of a press review of Italian and international publications in the field of public finance, the *Rassegna Stampa* (Campa ca 1985, 3).

In 1947, Cosciani participated in a ministerial commission for the study of a tax reform led by Vanoni. Here, he envisioned a tax system modeled along the British income tax, with a standard proportional tax for everyone and a progressive surtax for the very rich. The reasons for implementing the reform, however, still relied on existing arguments, such as the weak capacity of the Italian tax system to produce revenue and the unequal distribution of the tax burden (Cosciani 1948). In 1949, Cosciani was sent to London to write a report on the British income tax, which was eventually published by Assonime. He praised the British administration's efficiency and the taxpayers' morality. The large taxable base and the high tax rates not only made income tax a valuable source of revenue but also transformed taxation into a tool for income redistribution and dispossession of large fortunes (Cosciani 1949, 218–19). As a follower of the Italian tradition, however, Cosciani did not endorse such a high level of taxation, which he deemed harmful to entrepreneurship and saving.

During the 1950s, Cosciani shifted from the Italian tradition to embrace modern functional public finance. In 1941, he published a popular economics textbook based on the marginalist tenets of the time. In the new edition of 1954, however, after a few general definitions, the book opened with the Keynesian theory of national output, while the neoclassical theory was confined to a single chapter later in the volume. The book reproduced the famous aggregate demand-aggregate supply chart (fig. 4), with the characteristic 45 degrees supply curve, which could be traced back to Samuelson's textbook of 1948 (Cosciani 1954, 77). However, the use of the letter Z to indicate aggregate supply probably refers directly to the notation system of the *General Theory*. In the mid-1950s, Cosciani was one of the few Italian economists who understood and embraced the Keynesian theory.

His new adherence to modern public finance is marked in a few publications from the early 1960s. The first contribution was published in 1960 in the main Italian economic journal, the *Giornale degli Economisti*. The journal, which counted Maffeo Pantaleoni and Antonio de Viti de Marco as former directors, was the bastion of neoclassical economics in Italy. Cosciani's article stressed that, along with the funding of state expenses and the redistribution of income, taxation also had the function of increasing or reducing the purchasing power in the hands of the public. Taxation could contribute to the stability of prices and the growth of national income (Cosciani 1960, 446–47). In a complete rupture with the Italian tradition, for Cosciani, progressive taxation was the main tool to encourage economic growth:

> Apart from the desire to redistribute income and wealth, which is the primary cause of the existence of progressive income and inheritance taxes … these two taxes, together with other instruments, fiscal or otherwise, also constitute one of the valves of economic stability, inasmuch as by hitting higher incomes with a high propensity to save more strongly, the maneuvering of their rate can be an excellent means of directly influencing savings, either to curb them in times of depression or to leave them free to develop in the phase of economic expansion so as to implement compensatory forces with respect to spontaneous market forces (Cosciani 1960, 451–52).

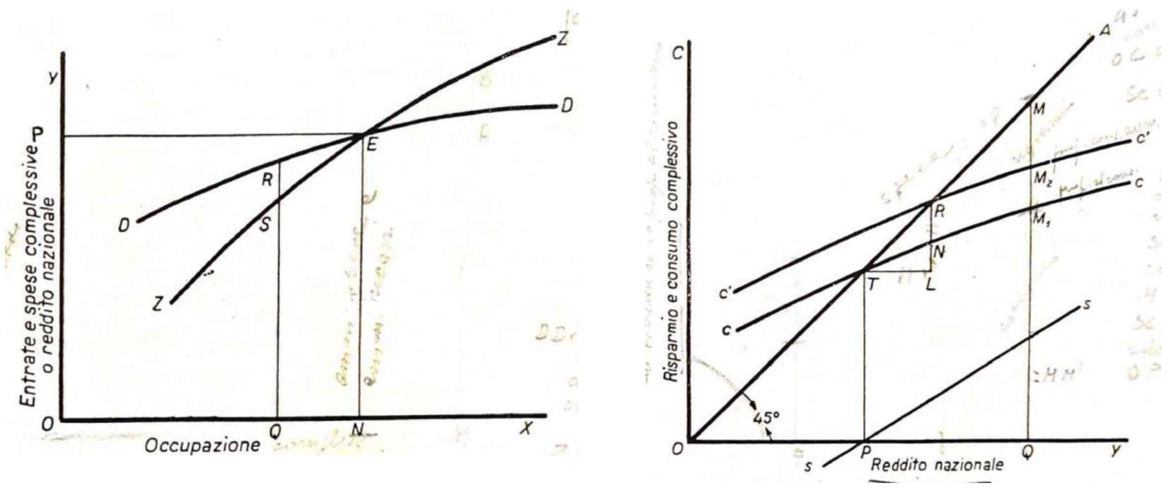
Cosciani's new ideas were concretized in a project for a tax reform drafted for the new center-left coalition in 1963. The Ministry of Finance instructed a commission that included the leading Italian scholars in public finance and tax law, chaired by Cosciani. In an internal document presented to the committee (Cosciani), later published as premise to the report of the commission (Cosciani 1964), Here, Cosciani stated the main goals of the reforms. Besides progressivity and simplification, the new tax system should also be able to stir economic growth and stabilize the business cycle. Cosciani stressed that taxation could also be used to increase saving, investment, and consumption, both at the national level and at the local level, with specific fiscal policies for less developed areas of the country (Cosciani, 7). The real rupture with the Italian tradition, however, was represented by the role of taxation in stabilizing income and the level of prices, which was now "universally recognized principle" (Cosciani 1962, 7-8).

There were two other external reasons for adopting progressive taxation. First, the Italian republican constitution of 1947 clearly stated that the tax system had to be progressive. The norm was unanimously approved, but it originated from the left wing of Christian Democracy (Bozzi 2021, 463–64). Second, as a member of the European Economic Community, Italy was required to harmonize her taxation system with the other European countries, primarily by replacing the old turnover tax (*imposta generale sull'entrata*) with a new value-added tax. Italian reformers used the opportunity of external pressure to extend the reform to income taxation, which, although recommended, was not required by the EEC directive (Lynch 2007). The introduction of VAT did not significantly affect Italian tax revenue. In fact, indirect tax revenue decreased in the years following the reform (fig. 1).

With only a few exceptions, most tax reform commission members supported Cosciani's position. Bruno Visentini, at the time influential vice president of the IRI, the holding of Italian state-owned industries, and soon-to-be Finance Minister in 1974, had previously supported the conservation of the double system of real income taxes and progressive surtax in a previous work on tax reform (Visentini 1948). In 1962, however, he presented a document to the Cosciani Commission where he advocated the introduction of a single progressive income tax (Visentini). Francesco Forte, member of the Cosciani commission and successor of Einaudi in the chair of public finance at the University of Turin, had partially embraced tax progressivity in 1952, implicitly rejecting Einaudi's argument on the interpersonal incomparability of sacrifice. However, Forte's progressivity was limited to a fairer distribution of the tax burden, while he rejected a general redistributive function aiming at leveling social conditions (Forte 1952, 310). By 1963, Forte moved to embrace redistributive taxation within the framework of Herny C. Simon, considering taxation necessary to preserve the market economy (Forte 1963, 764), which, however, fell short of the countercyclical income tax advocated by the new public finance.

By the 1960s, a new generation of economists and policymakers, epitomized by Cesare Cosciani, abandoned the old tenets of classical public finance defended by the Italian School and adopted a pragmatic approach to taxation and progressivity sensitive to foreign experiences. Economists like Vanoni and Forte endorsed progressivity, but only within the limits of a fairer redistribution of tax burden. As long as the classical identity between saving and investment held, there was no space for a general progressive income tax. According to Cosciani's thought, progressive taxation promised to bring not only fairness and social justice but also price stability and economic development.

Figure 4. Graphic representation of Keynesian models in Cosciani's texbooks



SOURCE: Cosciani (1954), 71 and 73.

5. Modern taxation in Italian fashion: The taxation of capital income

If Cosciani's works quietened theoretical discussions on income tax, the planning of the tax reform soon showed that its implementation was not less controversial. The crucial question was what to include in the new progressive income tax and how to deal with capital income. Cosciani, Forte, and Visentini agreed that capital income should be part of the taxable base of the new income tax. However, despite their recommendations, between 1973 and 1975, Italy was one of the first countries to implement a dual income tax:[1] dividends, interests from current accounts, interests from corporate bonds, interests from state bonds, and capital gains had each a different tax regime outside the taxable base of the personal income tax. The US model, which until then circulated only in theoretical circles, was hybridized with the specific context of Italian economic knowledge. Foreign ideas merged with the Italian priority on saving and capital accumulation.

Like most economists before Keynes, Italian public economists never questioned the identity between saving and investment. Based on this principle, higher savings would translate into higher investment and capital accumulation, eventually leading to economic growth. Moving from this, by the beginning of the twentieth century, Italian economists started to elaborate new theories of public finance, directly or indirectly aiming at maximizing saving. As we saw in the previous sections, these ideas quickly informed the mainstream of Italian economics, thanks to the work of economists such as Luigi Einaudi, even well after the end of the Second World War. A sign of the endurance of these ideas is the discussion of Einaudi's theory of taxable income in 1974 at a conference in Turin to mark the economist's birth anniversary. Here, two of the protagonists of the tax reform, Francesco Forte and Sergio Steve, still reflected on the taxation of consumed income and its importance for capital accumulation (Fondazione Einaudi 1974). Einaudi himself, shortly before dying, reaffirmed his stance against progressive taxation in 1960 (Einaudi 1960).

Similar positions can be found in parts of the business community. The Confindustria and its tax branch, Assonime, became particularly sensitive to the taxation of capital income after the center-left government introduced in 1962 a withholding tax on dividends, which in 1964 entirely substituted income taxation of dividends (Barbiellini Amidei and Impenna 1999, 753–55). Rather than a general opposition against the taxation of investment, however, the industrialists criticized the unequal tax treatment between bonds from the state and state-owned enterprises (partially or entirely exempted from taxation) and the tax regime for dividends, which was much more burdensome. The system, the president of Assonime complained, discouraged saving in venture capital and large firms (Assonime 1967, 26). Nonetheless, the association generally approved the proposed tax reform, praising the potential simplification of the system and its positive effects on business.

Much more skeptical about the reform was the industrialist Angelo Costa (president of the Confindustria between 1945 and 1955 and again between 1966 and 1970). In 1963, Costa wrote an extensive letter to Cosciani criticizing some of the core principles of the reform. Like Einaudi, he also questioned progressivity. However, he did so by moving from the principle of the ability to pay. In his view, the ability to pay strictly meant proportional taxation, with progressivity as a compensatory tool for taxes that cannot be adjusted to that principle. It followed that taxation should have no other goal but the financing of state expenditures since taxpayers' "fiscal honesty could not be expected in the presence

[1] Dual income taxation also includes capital gains, the Italian separate regime did not. See Sørensen (2010)

of redistribution" (Costa 1963, 4). Furthermore, he questioned the differentiation in the tax treatment of labor and capital income and the introduction of the surtax on the latter, adducing that modern insurance and workers' rights provided labor income with a higher ability to pay than capital income. He was also weary of the nominal register for stocks and instead suggested a separate flat tax on dividends and interests from bonds.

There was just as much skepticism among politicians about personal taxation of capital income as in academic and business communities. In 1964, Cosciani was appointed head of a new committee charged with drafting the bill for tax reform. At the end of 1966, the commission debated the inclusion of capital income within the personal progressive income tax in the presence of Finance Minister Luigi Preti. While Cosciani and Visentini presented their plan for including interests and dividends in the income tax, Preti advised a different solution. It is worth reading the minutes of the meeting:

> He [Preti] points out that he has also consulted, in this regard, some authoritative members of Parliament and that he has been convinced, under an aspect of mere political expediency, of the impossibility, at least for now, of sanctioning the obligation to declare the interest on bank deposits, bonds, and government securities, by stipulating their subjection to personal income tax and, for reasons of the functionality of such a taxation regime, proclaiming the non-existence of banking secrecy.[2]

To Cosciani and Visentini's insistence that the inclusion of such types of income constituted one of the cornerstones of the reform, Preti proposed the drafting of two texts, one including capital income and one exempting it, both to be presented to the cabinet.

We do not know how the discussion proceeded in the Council of Ministers, but we can expect a general rejection of Cosciani's and Visentini's proposals. A document by the office of Treasury Minister Colombo held in the Prime Ministers' papers at the Italian Central Archive stressed the need for a homogenous treatment of stocks, bonds, and current accounts to avoid unfair competition. It offered three arguments for excluding capital income from the personal income tax.[3] First, the administration would have been unable to implement a complicated system of nominal registration of stocks, bonds, and bank accounts, including the problem of bank secrecy. Second, taxing capital income within personal income tax would negatively affect the creation of savings: the inclusion was in radical opposition to "the requirements of a policy of economic development which finds its indispensable condition in a constant and intensive inflow of savings into the financing of production." Third, including personal taxation would encourage savers to bring their capital abroad to avoid taxation.

Indeed, the attention to saving was shared by the most progressive elements of the political spectrum, which were working on a development plan for the Italian economy, the so-called *programmazione economica* (economic planning). One of the pillars of the *programmazione* was the creation of extra savings to be invested in the provision of public services, the economic convergence

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[2] Assonime Historical Archive, b. 288, f. 15, Meeting 28 December 1966, pp. 5-6).

[3] Italian Central Archive, Presidenza del Consiglio dei Ministri, Ufficio Giuridico e del Coordinamento Legislativo, 1968-1969 Ministero delle Finanze, f. 68, no date, probably 1967 or 1968.

of underdeveloped areas, and the enlargement of employment (Lavista 2010, 315, 348). Even planners who generally supported a shift towards personal and progressive income taxation did not entirely endorse Cosciani's project. The very influential book *Ideas for economic planning* by left-wing economists Giorgio Fuà and Paolo Sylos Labini sketched a system of personal taxation of consumed income along Einaudi's conception. However, Fuà and Sylos's plan accompanied their tax on consumed income with a personal progressive tax on wealth (Fuà and Sylos Labini 1963, 74–75). Although redistributive, such a system did not conform to the principles of the new public finance advocated by Cosciani but instead echoed the tenets of the Scienza delle Finanze.

Italy hosted a large economic tradition encompassing all the main economic actors which was highly skeptical of redistributive taxation. Beyond the academic circle of Cosciani, we do not observe almost any circulation of modern fiscal ideas on functional finance. In the 1960s, the debate is still informed by the developments of the interwar period, with the Italian School of Public Finance on the one hand and the distrust of market mechanisms on the other hand. This multifaceted tradition had a crucial impact on the definition of modern income taxation in Italy. The foreign model admired by Cosciani hybridized with the local economic culture by incorporating its doctrinaire preoccupation with saving.

6. Conclusion

Italy was the last major country to implement modern income taxation before the rise of neoliberalism in the 1980s made it intellectually obsolete. While the country had a relatively high fiscal capacity for most of the 19th and 20th centuries, after the Second World War, it lagged behind its European partners both in terms of revenue and in terms of tax knowledge. One of the main reasons for that was the lack of support among public economists for modern income taxation, which had already been adopted in other Western countries. The Italian school of public finance maintained its hegemony over Italian economics throughout the first half of the twentieth century and rejected all attempts to introduce redistributive taxation.

The article argued that the circulation of new ideas about functional finance, thanks to Cesare Cosciani's works, provided the intellectual justification for reforming the tax system in accordance with the US and UK models. Cosciani’s project promised policymakers a system that would increase revenue, stabilize the business cycle, and encourage investment, which blunted the Italian economists’ traditional arguments against progressive taxation. While the timing of the reform depended on external pressures and political equilibria, the specific character of the reform and its emphasis on the centrality of PIT was exclusively the result of Cosciani’s efforts.

However, the endorsement of US functional finance fell short in the taxation of capital income. While Cosciani and the other members of the commission advocated for a comprehensive income tax that would include dividends, capital gains, and interests from current accounts and bonds, Italian policymakers echoed the arguments of the Italian school of public finance, opting for a separate and milder regime for capital income. Although these beliefs were stronger among conservatives, they were shared by all the main parties. By 1975, Italy was among the first countries to implement a dual income tax system, with a progressive income tax for labor and business income and a proportional tax for capital income.

Nonetheless, the reform was a striking success in terms of revenue. Between 1973 and 1983, Italian tax revenue as a percentage of GDP increased from 23 to 34 percent (OECD revenue statistics), primarily due to the rise in personal income tax. VAT, which was introduced at the same time, actually resulted in a decrease in revenue. The increase happened almost automatically thanks to the rise in nominal (and to a lesser extent also real) incomes during the inflation years between 1975 and 1985. Had Italy introduced mass progressive taxation ten years later, it would have missed out on this sudden increase in tax revenue. This was ultimately possible thanks to Cosciani’s specific role in elaborating new economic ideas and translating them into policies.

Despite the rise of progressive income tax, more and more groups have been exempted from it, either informally, by tolerating tax evasion or formally, by increasing the number of separate tax regimes (rents, farmers, some categories of self-employed). Economist Antonio Pedone successfully labeled the two groups, those who evade/avoid the tax and those who duly pay, the *evasori* (evaders) and the *tartassati* (overburdened) (Pedone 1979). Such discrimination already existed in the pre-1973 system, but the massive increase in revenue made it a central issue in Italian political debate for the decades to come.

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