

Case Study (Full Report)

Tax Expenditures in Germany

Mark Hallerberg , May 2014

Introduction

This report considers the transparency of tax expenditures in Germany. It begins with the reporting that appears in the annual budget. It then considers one document in particular, the so-called *Subventionsbericht*, or Subsidy Report, which includes information on tax expenditures. Germany is appropriately known as a federal republic, with many governmental functions carried out at the state (*Land*) or local levels. The state level is especially important for taxation. While there have been repeated efforts to centralize the administration and collection of tax at the federal (or *Bund*) level, it is the state governments that carry out these functions in practice. Therefore this report follows its initial discussion of the federal report with comparisons of the various state reports, whose coverage in practice is less detailed and more varied than the federal report. It also evaluates the main civil society alternative to the federal Subsidy Report, the Kiel Subsidy Report. It considers the role of the Federal Audit Court (*Bundesrechnungshof*) and concludes with a brief discussion of the growing role of the European Union in the monitoring of tax expenditures.

Federal Budget and Federal Budget Process

The annual budget for 2012 included a table displaying the “20 largest tax privileges,” which appears on pages 89 and 90 of the seventh section. The first column provides the name and the legal basis for each tax privilege; the second lists the corresponding number in the second annex of the federal Subsidy Report; the third reports the function according to usual classifications; and the fourth provides the reduction in tax collection for the years 2012, 2011, and 2010.

For example, the top tax expenditures concern energy production, and the linked production of energy and heat appears as number 53 in the last Subsidy Report. It reduced tax income 2.3 billion euros in each of the last three years. The Finance Ministry provides the estimates. Interviewees did not know of any explicit review of the accuracy of their estimates.

More generally, three of the four top tax expenditures that cost the government at least 1 billion euros are related to energy; the exception is for cultural activities, which cost 2.18 billion euros in 2012.

This format of highlighting the top 20 tax privileges appeared under the last budget of the previous government as well, which was for 2009, and featured the same column structure. The top item in that list was a tax reduction for ecological renovations to homes.

The reporting of the federal budget has legal basis in the budget law (*Bundeshaushaltsordnung*)¹, but the Finance Ministry included the 20 largest tax expenditures in the annual budget beginning in 2005 and has ordered them according to their size beginning in 2008.²

There are some additional details from the Bundestag worth mentioning here concerning the way that it handles tax expenditures. Any bill that has financial implications needs to provide estimates of the costs.³ This includes tax expenditures. The Finance Ministry provides the estimates, which usually cover the next five years. There may be debates about the costs, with external groups such as interest groups providing their own estimates, but the parliamentarians treat the Finance Ministry estimates as the most important. All such bills that pass must appear in “*Einzelplan 60*” at the end of the year, which brings together all tax income and notes all changes to tax law in a given year, including any tax expenditures.

In terms of public input, the party groups in parliament decide who testifies at a given hearing. Hearings of the Finance Committee, which is the main committee that deals with taxation, are public. But one has to gain the favor of a party group to testify. In practice, interest groups that represent tax professionals as well as taxpayers do appear regularly before the committee. Interviewees had not heard of a “freedom of information” law or requirement, but they also asked why this would be necessary –the government already provides the appropriate figures.

Federal Subsidy Report

Legal framework. The law that establishes the Subsidy Report is now 45 years old. It was passed on 8 June 1967, at the same time as a stimulus package, and is known formally as the *Gesetz zur Förderung der Stabilität und des Wachstums der Wirtschaft* (StWG). This was a reaction to reports in the press that subsidies had increased in the preceding years, especially in election years. The Finance Minister at the time, Franz-Josef Strauß, justified the subsidies as a requirement of membership in the European Community. During the recession it became clear that there would need to be budget cuts, and there was hope that, if one identified subsidies, it would be easier to cut them. Economics Minister Schiller pushed the idea of a report to be issued every two years.⁴ Indeed, in practice the federal government has published the Subsidy Report approximately every two years as initially planned; there have been 23 such reports. More information appears below for the latest two reports, which the federal government published on 13 January 2010 and 8 August 2011.

According to the latest Subsidy Report, this law provides the legal basis more generally for the definition of a “tax expenditure.”⁵ The focus is on measures that directly or indirectly benefit an economic sector or an enterprise. Whether a measure is a tax subsidy in practice, and therefore whether

¹ See <http://www.gesetze-im-internet.de/bho/>

² *Bundesrechnungshof, Bericht nach § 99 BHO über die Transparenz von Steuersubventionen*, Bundesrechnungshof, 15 April 2008, p. 36.

³ The legal basis for this requirement is the *Gemeinsame Geschäftsordnung der Bundesregierung* (§ 44 GGO).

⁴ See Kurt Simon, “Der korrumpierte Wähler – Subventionen haben ein zähes Leben,” *Die Zeit*, 22 December 1967; Wolfgang Pohle, “Angst vor dem Pferdefuß: Stabilitätsgesetze – Vorstufe zum Dirigismus,” *Die Zeit*, 17 March 1967; and “Subventionend: Risiko für alle,” *Der Spiegel*, 24 April 1967.

⁵ German Finance Ministry, *Dreiundzwanzigster Subventionsbericht: Bericht der Bundesregierung über die Entwicklung der Finanzhilfen des Bundes und der Steuervergünstigungen für die Jahre 2009-2012*, 2011, p. 8; pp. 91-2, reprint of relevant section of the 1967 law.

the measure is included in the Subsidy Report, is a decision the Ministry of Finance makes together with any relevant line ministry.

Once the Finance Ministry produces the final text, the German Cabinet officially approves the report before it is provided to the legislature. There are many discussions within the government about what should be included in the Subsidy Report. Once it gets to a cabinet vote, however, it has generally been noncontroversial.⁶ The Finance Committee of the lower house then discusses the report. In practice, the committee takes a vote that it acknowledges the Subsidy Report, and the vote is usually unanimous. The committee does not consider the report itself to be controversial.

Timing

The Subsidy Report should be published approximately every two years, but there is not a set time during the budget process when it is to be published. The Finance Ministry publishes the Subsidy Report, as does the Bundestag.

Content

The Subsidy Report covers all kinds of subsidies, not just tax expenditures. It begins with an overview how subsidies have developed during the period covered in the report. Looking at the last two reports, it is clear that this introduction is an opportunity for the government to explain its perspective on these developments. The 2010 Subsidy Report, which covered the period 2007-2010, noted that subsidies dropped some from 2007 to 2008, but then increased strongly through 2010. It emphasized the connection with measures to alleviate the economic crisis as the reason for the increase. Similarly, the 2011 Subsidy Report notes that subsidies had declined since the previous report. The economic crisis is of course mentioned, but the overall mood is that the government is successfully reducing subsidies.

The third section that comes after the introductory remarks focuses on tax expenditures. It presents the government's goals and concepts; in the 2011 Subsidy Report, for example, this list includes the point that subsidies should not provide permanent support for a given group. It then presents a summary of changes to existing tax expenditures, and it lists a few new tax expenditures. Anything that affects the Land governments is supposed to receive approval in the *Bundesrat*, which is where Land governments are represented. Since most taxes are shared, changes in tax law usually require passage through both houses of parliament. This includes tax expenditures. The 2011 Subsidy Report lists four changes to tax expenditures for the energy sector and one change for the airline industry.

The fifth section of the Subsidy Report examines the development of subsidies more generally (both spending and taxation) according to five economic areas: agriculture, nutrition, and consumer protection; private economy, which includes energy; transportation; housing; and savings and property accumulation. The sixth section discusses the main guiding principles of subsidy policy of the government and summarizes the implementation status of the subsidy policy guidelines. The seventh section discusses help at the European level.

In terms of lists of tax subsidies, Overview 3 on page 15 provides the 20 largest tax expenditures. This "greatest hits" list appears in the federal budget as well, of course, but a difference is that the Subsidy

⁶ Michael Bröcker, "Staat verteilt 30 Milliarden," *Rheinische Post Düsseldorf*, 12 January 2010.

Report includes somewhat different numbers: the total for one year (2012) for all levels of government as well as the numbers for the federal government alone. When one considers all levels of government, it is clear that culture receives the most tax expenditures, or a little over 4 billion euros in 2012. A little more than half that amount (2.2 billion) comes from the Bund. In addition, the total for the top 20 at the Bund level is almost 15 billion euros, while the overall total is nearly 23 billion euros. To put this in context, expected total revenues in 2012 were anticipated to be about 280 billion euros, so the overall total of tax expenditures reported amounts to about 8 percent of revenues, or about 3.5 percent of GDP.⁷The top 20 tax expenditures also represent 90 percent of the tax expenditures the government reports in Annex 2 later in the Subsidy Report.

This second annex (Anlage 2) covers only tax expenditures and is about 16 pages long in a Subsidy Report that runs to a total of 256 pages in 2011. It presents the concept used to measure them. The reporting itself is more detailed than in the annual budget: it includes a description of the tax expenditure, the type of help, the amount for the past three years, as well as estimates for the upcoming year both at the federal level and at all levels; the legal basis; and whether the tax expenditure is limited or unlimited in time frame. They are organized according to area (e.g., transportation), then the type of tax (e.g., personal income tax). Overall in the 2011 Subsidy Report, there were 103 tax expenditures that amounted to 26.9 billion euros, with 17.1 billion at the federal level.

There are additional expenditures that appear under the label “special tax regulations” that appear in the third annex (Anlage 3). These are organized according to type of tax. For example, the money paid as church tax is not included as income tax. Such measures are sometimes large; the regulation on church tax cost the German government 2.8 billion euros in 2011, of which 1.2 billion accrued to the federal government. As the Kiel Subsidy Report notes (more on this report below), reductions in the value-added tax for some types of food and the exemption for rents from rental property are not included in the Subsidy Report. An interesting part of this section is that payments to, and income from, the German railways are . . . not considered “state help” because of the legal basis of the railways. While the Subsidy Report lists these items, it does not consider them “tax expenditures.”

There are other parts to the Subsidy Report that have some relevance. The fourth annex includes a list of new tax expenditures and their legal basis. The fifth details what the states (or *Länder*) are doing in terms of reporting their subsidies (more on this below). The sixth annex describes in more detail what the government means by “subsidy” and how this differs from other state help. The 2011 Subsidy Report notes that the definition of a “tax expenditure” it uses comes from the 20th report. A tax expenditure exists, according to the report, only if it has a “subsidy” character to it. This means that it cannot capture all special tax rules (p. 94). A subsidy is something that affects private industry. There is also a brief discussion of how their definition differs from the one the Kiel Institute uses (more on the Kiel report below). The seventh annex provides more information on financial help.

The final relevant part of the Subsidy Report is Annex 8, which provides more detail about each of the tax expenditures mentioned in Annex 2. It lists the provisions of the expenditure; the goal of the expenditure; the legal basis through history (e.g., the first one, which is for people over 55 who cannot work, first became law in 1925, then was changed in 1984, 1996, 2001, and 2004); whether it expires; its financial volume; the division across the federal government, states, and localities; the type of subsidy;

⁷ Aggregate figures are from *Bundesrechnungshof, Bemerkungen 2011 zur Haushalts- und Wirtschaftsführung des Bundes*, 2011.

the measures taken; degression (does the subsidy decline over time); how it is evaluated; and the perspective for the future. The listing of both expiration dates (or the lack of them) and degression, some hope, will spur governments to consider making them both temporary and diminishing over time.

Availability

The last version is easily found online at the German Finance Ministry. The Web address is listed in Table 1. The 23rd report's summary is available in English as well.⁸

Press reports

The press generally covers the publication of each Subsidy Report. This study surveys the newspaper articles that appeared after the last two reports.

After the 2010 Subsidy Report, the main national newspapers covered it. There were some common themes: a discussion of the biggest items; a debate about whether the current government would cut them, if it does cut them, which ones to cut. The government's argument that subsidies increased because of the crisis was duly noted.⁹

After the 2011 Subsidy Report, articles in *Die Welt*, *Frankfurter Rundschau*, *Handelsblatt*, *Spiegel*, and *Tagesspiegel*, all repeated the main message of the report that subsidies decreased.¹⁰ There were exceptions that went into some depth and were also more critical. An article in the national *Süddeutsche Zeitung* discusses the general problem of effectively addressing subsidies. The author notes that the headline-grabbing statement of the federal government that subsidies decreased by 20 percent for the reporting period from 2009-2012 is misleading. As the financial crisis in 2009 saw a huge increase in German government subsidies to support various industries, saying subsidies went down compared to 2009 does not say much about the trend of subsidies. Comparing the data for 2012 with the pre-crisis year of 2008 shows very little difference in the amount of German government subsidies. Measured as a percentage of GDP, the subsidy rate has been constant for years. The article further notes that the Kiel Report finds subsidies five times as high as the official government report because the government report does not count many subsidies, such as those for public transportation, labor market programs, or subsidies to auto drivers.¹¹ Similarly, an online slide show from the same newspaper emphasizes the main industries that received subsidies.¹² Finally, editorials in the *Frankfurter Allgemeine Zeitung* and the *Süddeutsche Zeitung* both compare the report to the Kiel Report and note that the government's data seem to underestimate the total number of tax expenditures. They also note that the reduction in

8 See http://www.bundesfinanzministerium.de/Content/EN/Standardartikel/Topics/Fiscal_policy/Articles/2012-09-25-subsidy-report-23rd.html

9 Examples include Thomas Öchsner, "Kohle für die Kohle," *Süddeutsche Zeitung*, January 11, 2010; Robert Birnbaum and Antje Sirleschtov, "Steuerdiskussion: Die Quadratur des Kreises," *Der Tagesspiegel*, January 13, 2010; and Roland Pichler, "Krise treibt Beihilfen auf Höchststand," *Stuttgarter Zeitung*, January 13, 2010.

10 Nachrichten Kompakt, "Die Welt: Bund drosselt Subventionen," 4 August 2011; Spiegel: Subventionen des Bundes sinken, 24 July 2012; Frankfurter Rundschau. 03 August 2011; Handelsblatt. "Staat spart durch das Ende der Abwrackprämie," 25 July 2011; Der Spiegel 30/2011; "Bund kürzt Subventionen Förderung sinkt auf 22,6 Milliarden Euro," 10 August 2011, *Der Tagesspiegel*.

11 Claus Hulverscheidt, "Wenn der Staat Milliarden verteilt," *Süddeutsche Zeitung*, 4 August 2011.

12 "Subventionsbericht der Regierung – Stütze für Schnapsbrenner," *Süddeutsche Zeitung Online*, 3 August 2011.

subsidies is due to cutbacks after the crisis, not due to a commitment to reduce tax subsidies more generally.

State Subsidy Reports

As the federal Subsidy Report makes clear, while the federal government estimates that about two-thirds of tax expenditures for the 20 largest expenditures appear at the federal level, while another one-third come at the state level. In the list of 103 tax expenditures, there are a few that are only at the state level. I Inheritance tax breaks that amounted to 235 million euros in 2011 at the subnational level are an exception, but in general there is little detail about what happens at the subnational level in the federal Subsidy Report.

At the same time, it is important to note that many of the main money-makers in terms of taxes in Germany are shared taxes, where different levels of government receive pre-set percentages of certain types of tax, such as the income tax and the value-added tax, and where the laws are made at the federal level but then require state approval by the upper house in each Land. For this reason, the state government reports generally focus on the expenditures side instead of the tax side.¹³

Nevertheless, the potential usefulness of such reports is clear. There are ways for subnational governments to extend tax expenditures. The business tax is levied only at the subnational level, for example, and anecdotal evidence suggests that exemptions for some types of businesses are common. This tax is at the local level and not the state level, and so there is competition within the state governments, not just between them.

Table 1 provides data for all the Subsidy Reports that appear at different levels of government. Where possible, it indicates the first year the report was done; the year of first publication; whether the report is currently published; whether it includes tax expenditures and if so, what their definition is; notes about each report; and the Web address (if available). First, the large states of Baden-Württemberg and Bavaria (since the late 1960s), Hesse (since the late 1970s), and North-Rhine Westfalia (since the early 1970s) have published such reports over several decades. The 11 states that made up the former West Germany (including Berlin) have introduced such a report at some point, while three of the five new states formed in the former East Germany have done so as well. Three states appear not to have such a report active; they have not produced one since 2008.

In terms of content, there are several separate definitions of “subsidies” that appear in the 13 states with their own reports. Six use the federal definition, four the Kiel definition, one uses a definition produced by the Institute of Public Economics from the University of Cologne, and the remainder use their own.

The most recent one came in Brandenburg, which was published in 2011, and why it was adopted and how it was explained to the public is of interest. One party in particular, the Free Democratic Party, advertised the passage of the law mandating the production of a Subsidy Report as a success for the party in increasing transparency. The Finance Ministry also made a similar claim, noting that the

¹³ Personal correspondence, Finance Ministry of Rhineland-Palatinate, 23 October 2012.

adoption of this report was a success because it contributed to transparency. It is very hard to know whether these claims swayed voters.

The Kiel Subsidy Report

The Kiel Institute for the World Economy, which is an economic institute based at the University of Kiel, produces a separate report. Academics write it, and the Institute published the first one in 1979. It also produced an English language version in 1987, which provides some background on the need for an external report and why Kiel decided to write one.¹⁴ Reasons provided include: the federal Subsidy Report may miss some of the subsidies at other levels of government and that the definition of “subsidies” has not been consistent across federal reports, with each revision reducing the size of overall subsidies.

If one compares the latest versions of the documents, there are several key differences with the federal government report. First, the Kiel Report covers explicitly subsidies at the federal, state, and EU level, so it presents a more comprehensive picture than any of the individual reports. Second, its definition of a subsidy is broader. However, it is largely based on the federal report; the main difference is which part of the federal report it covers as “subsidies.” The federal report counts only the first and second annexes of its document as “subsidies,” while the Kiel Report includes the items in the third annex of the federal report as well. Among these tax rebates in the Kiel Report only are reduced tax rates for encouraging saving for retirement; the church tax rebate; charitable tax deductions; tax deductions to medical services; and not taxing social services.

The press coverage mainly cites the Kiel Report as an alternative measure of subsidies when reporting on the publication of the German government’s Subsidy Report. Wire reports and press articles generally note that the economic analysis of the Kiel Report shows that there is a significantly higher level of subsidies than the government report shows. Neither the *Frankfurter Allgemeine Zeitung* nor the *Handelsblatt* had explicit stories on the Kiel Report when it was first published. It is generally reported on when discussing the federal report that came later and generally included in the wire stories on the federal report as well.

Federal Court of Auditors (*Bundesrechnungshof*)

This audit court has two opportunities to publicize tax expenditures.

First, it issues an annual report. The court focuses on the legal aspects of tax expenditures: Have the taxes been raised according to the law? This report generally appears in November. The latest report has comments on the top 20 tax expenditures in the annual federal budget.

Unlike the federal budget, which simply lists tax expenditures, the annual report sums the total of the top 20 to 15.6 billion euros in 2010 and the total of all tax expenditures to 17.6 billion euros. It also states in one sentence that there are another 9.9 billion euros of tax breaks not reported in the federal government’s Subsidy Report that are quantifiable. This information is not the central message of the annual report; it appears on page 306 of a 317-page document. There is an additional comment on page

¹⁴ Karl-Heinz Jüttemeier, “Subsidizing the Federal German Economy: Figures and Facts, 1973-1984,” Kiel Working Papers, No. 279, 1987.

308 that exemptions mean significant losses of revenue for the federal government under the personal income tax, as well as a comment that there are tax benefits for energy on page 59 and on page 315.

The annual report is routinized in terms of organization and content, and it provides limited scope to highlight specific issues. But the court has a second opportunity to publicize tax expenditures: it has the right to issue rulings on particular matters, including tax expenditures, which can come at any time. According to Article 99 of the *Bundeshaushaltsordnung*, the court itself can decide to make a ruling on parts of the budget it deems worthy of consideration. For example, in February 2011 it issued an opinion on tax reductions for craftsmen/artisans and other family-based businesses. It noted that the Finance Ministry indicated in 2010 that the costs of these deductions amounted to over 4 billion euro. It ruled that the goals that the tax reductions were supposed to reach were not being met, and it recommended that the government eliminate the tax break. The court's recommendation received some press coverage, including especially in the construction industry that was likely to be most affected. The court is known for its independence, and it makes the decision whether to issue a recommendation.

Similarly, in April 2008 the court issued a special report on the transparency of tax expenditures. It argued in particular that the government should provide more detail on the actual effects of tax expenditures.¹⁵ The Budget Committee of the Bundestag reacted to the court's report and asked the government to provide more details in December 2008. The Finance Ministry agreed to follow this advice.¹⁶

European Union

The formal task of this study was to investigate the reporting of tax expenditures within Germany. After in-person interviews, it became clear that the European Union plays an increasingly large role in Germany. When the Bundestag debates a new tax expenditure, the question the members usually ask is whether the European Union will accept it. There is concern that the European Commission will rule a given expenditure to be against state aid rules. The members of the Bundestag do not call up the commission to ask for an opinion; rather, the staff combs through earlier rulings by the European Court of Justice. There are cases where a member would like to support a new tax expenditure, but where the government says no and cites a European Court of Justice precedent as the reason why the tax expenditure should not move forward. According to one interviewee, considerations of the European level rather than the publication of the federal report is the main restriction on further tax expenditures.

¹⁵ Bericht nach § 99 BHO über die Transparenz von Steuersubventionen, Bundesrechnungshof, 15 April 15 2008.

¹⁶ Bemerkungen 2009 zur Haushalts- und Wirtschaftsführung des Bundes, Bundesrechnungshof, p. 214.

Table 1: Summary of Subsidy Reports (Kiel, Federal, and State)

<i>Land</i>	<i>First Published</i>	<i>Last Published</i>	<i>Last Period Covered</i>	<i>Definition Based On</i>	<i>Web Link</i>
IfW Kiel	1979	2010	2000-09	Bund definition + additional subsidies	http://www.ifw-kiel.de/pub/kd/2010/kd479-480.pdf
Bund	1967	2011	2009-12	Stability and Growth Act of 1967	http://www.bundesfinanzministerium.de/Web/DE/Themen/Oeffentliche_Finzen/Subventionspolitik/subventionspolitik.html
Baden-Württemberg	1969	2011	2009-11	Bund	http://www.mfw.baden-wuerttemberg.de/sixcms/detail.php/253989
Bayern	1969	2011	2011-12	Bund	Received current one as e-mail attachment
Berlin	1989?	2010	2009-11	Bund + additional Berlin flow chart	https://www.berlin.de/sen/finanz/n/haushalt/download/index.html
Brandenburg	2011	2011	2009-11	FiFo Köln	http://www.mdf.brandenburg.de/cms/detail.php/bb1.c.270981.de
Bremen	2004?			§§23 Land Budget Law	http://www.finanzen.bremen.de/sixcms/detail.php?gsid=bremen53.c.1702.de
Hamburg	2002	2011	2010	§§23 Land Budget Law	http://www.hamburg.de/zuwendungsbericht/ http://www.hamburg.de/pressearchiv-fhh/210456/pressemeldung-2002-08-27-fb-zuwendungsbericht.html
Hessen	14/10/1978	2011	2009-11	IfW Kiel	http://starweb.hessen.de/cache/haushalt
Mecklenburg-Vorpommern	NA	NA	NA	NA	
Niedersachsen	1998	2012	2011-15	Bund	http://www.mf.niedersachsen.de/portal/live.php?navigation_id=1007&article_id=1430&psmand=5 http://edok.ahb.niedersachsen.de/07/357131134.htm
Nordrhein-Westfalen	2002	2007	2005 - 2007	1998 State Audit Court Expert Commission	Not available online
Rheinland-Pfalz	1994	2011	2008 - 2011	IfW Kiel	http://www.fm.rlp.de/startseite/finanzen/finanzhilfebericht/
Saarland	2007	2009	2006-2009	IfW Kiel	http://www.saarland.de/29756.htm
Sachsen	NA	NA	NA	NA	
Sachsen-Anhalt	2004	2004	2000-2004	IfW Kiel	http://www.sachsen-anhalt.de/fileadmin/Elementbibliothek/Bibliothek_Politik_und_Verwaltung/Bibliothek_Ministerium_der_Finanzen/Dokumente/Subventionsbericht/Bericht_528248.pdf
Schleswig-Holstein	1990	May 2004	2001-2004	Bund	http://www.landtag.ltsh.de/infothek/wahl15/umdrucke/4600/umdruck-15-4687.pdf
Thüringen	2001	May 2012	2008 - 2010	Bund	https://www.thueringen.de/th5/tem/haushalt/subventionsbericht/

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