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Recommendation for a

COUNCIL RECOMMENDATION

on the 2023 National Reform Programme of Italy and delivering a Council opinion on the 2023 Stability Programme of Italy

{SWD(2023) 612 final}

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THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Articles 121(2) and 148(4) thereof,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies[1], and in particular Article 5(2) thereof,

Having regard to Regulation (EU) No 1176/2011 of the European Parliament and of the Council of 16 November 2011 on the prevention and correction of macroeconomic imbalances[2], and in particular Article 6(1) thereof,

Having regard to the recommendation of the European Commission,

Having regard to the resolutions of the European Parliament,

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

Having regard to the opinion of the Economic and Financial Committee,

Having regard to the opinion of the Social Protection Committee,

Having regard to the opinion of the Economic Policy Committee,

Whereas:

(1) Regulation (EU) 2021/241 of the European Parliament and of the Council[3], which established the Recovery and Resilience Facility, entered into force on 19 February 2021. The Recovery and Resilience Facility provides financial support to the Member States for the implementation of reforms and investments, entailing a fiscal impulse financed by the EU. In line with the European Semester priorities, it contributes to economic and social recovery and to the implementation of sustainable reforms and investments, in particular to promote the green and digital transition and make the Member States' economies more resilient. It also helps strengthen public finances and boost growth and job creation in the medium and long term, improve territorial cohesion within the EU and support the continued implementation of the European Pillar of Social Rights. The maximum financial contribution per Member State under the Recovery and Resilience Facility was updated on 30 June 2022, in accordance with Article 11(2) of Regulation (EU) 2021/241.

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1 OJ L 209, 2.8.1997, p. 1.

2 OJ L 306, 23.11.2011, p. 25.

3 Regulation (EU) 2021/241 of the European Parliament and of the Council of 12 February 2021 establishing the Recovery and Resilience Facility (OJ L 57, 18.2.2021, p. 17).

(2) On 22 November 2022, the Commission adopted the 2023 Annual Sustainable Growth Survey[4], marking the start of the 2023 European Semester for economic policy coordination. The European Council endorsed the priorities of the survey around the four dimensions of competitive sustainability on 23 March 2023. On 22 November 2022, on the basis of Regulation (EU) No 1176/2011, the Commission also adopted the 2023 Alert Mechanism Report, in which it identified Italy as one of the Member States that may be affected or may be at risk of being affected by imbalances, and for which an in-depth review would be needed. On 14 December 2022, the Commission adopted an opinion on Italy's 2023 draft budgetary plan. On 22 November 2022, the Commission also adopted a recommendation for a Council recommendation on the economic policy of the euro area, which the Council adopted on 16 May 2023, as well as the proposal for the 2023 Joint Employment Report analysing the implementation of the Employment Guidelines and the principles of the European Pillar of Social Rights, which the Council adopted on 13 March 2023.

(3) While the EU economies are showing remarkable resilience, the geopolitical context continues to have a negative impact. As the EU stands firmly with Ukraine, the EU economic and social policy agenda is focused on reducing the negative impact of energy shocks on both vulnerable households and companies in the short term, and on keeping up efforts to deliver on the green and digital transition, support sustainable and inclusive growth, safeguard macroeconomic stability and increase resilience in the medium term. It also focuses heavily on increasing the EU's competitiveness and productivity.

(4) On 1 February 2023, the Commission issued the Communication *A Green Deal Industrial Plan for the Net-Zero Age*[5] to boost the competitiveness of the EU's net-zero industry and support the fast transition to climate neutrality. The plan complements ongoing efforts under the European Green Deal and REPowerEU. It aims to provide a more supportive environment for scaling up the EU's manufacturing capacity for the net-zero technologies and products required to meet the EU's ambitious climate targets, as well as ensuring access to relevant critical raw materials, including by diversifying sourcing, properly exploiting geological resources in Member States and maximising the recycling of raw materials. The plan is based on four pillars: a predictable and simplified regulatory environment, speeding up access to finance, enhancing skills, and open trade for resilient supply chains. On 16 March 2023, the Commission also issued the Communication *Long-term competitiveness of the EU: looking beyond 2030*[6], structured along nine mutually reinforcing drivers with the objective to work towards a growth enhancing regulatory framework. It sets policy priorities aimed at actively ensuring structural improvements, well focused investments and regulatory measures for the long-term competitiveness of the EU and its Member States. The recommendations below help address those priorities.

(5) In 2023, the European Semester for economic policy coordination continues to evolve in line with the implementation of the Recovery and Resilience Facility. Fully implementing the recovery and resilience plans remains essential for delivering the policy priorities under the European Semester, as the plans address all or a significant subset of the relevant country-specific recommendations issued in recent years. The 2019, 2020 and 2022 country-specific recommendations remain equally relevant also

4 COM(2022) 780 final.
5 COM(2023) 62 final.
6 COM(2023) 168 final.

for recovery and resilience plans revised, updated or amended in accordance with Articles 14, 18 and 21 of Regulation (EU) 2021/241.

(6) The REPowerEU Regulation[7] adopted on 27 February 2023 aims to rapidly phase out the EU's dependence on Russian fossil fuel imports. This will contribute towards energy security and the diversification of the EU's energy supply, while increasing the uptake of renewables, energy storage capacities and energy efficiency. The Regulation enables Member States to add a new REPowerEU chapter to their national recovery and resilience plans in order to finance key reforms and investments that will help achieve the REPowerEU objectives. They will also help boost the competitiveness of the EU's net-zero industry as outlined in the Green Deal Industrial Plan for the Net-Zero Age and address the energy-related country-specific recommendations issued to the Member States in 2022 and, where applicable, in 2023. The REPowerEU Regulation introduces a new category of non-repayable financial support, made available to Member States to finance new energy-related reforms and investments under their recovery and resilience plans.

(7) On 8 March 2023, the Commission adopted a communication providing fiscal policy guidance for 2024. It aims to support the preparation of Member States' stability and convergence programmes and thereby strengthen policy coordination[8]. The Commission recalled that the general escape clause of the Stability and Growth Pact will be deactivated at the end of 2023. It called for fiscal policies in 2023-2024 that ensure medium-term debt sustainability as well as raise potential growth in a sustainable manner. Member States were invited to set out in their 2023 stability and convergence programmes how their fiscal plans will ensure that the 3% of GDP deficit reference value is adhered to as well as plausible and continuous debt reduction, or for debt to be kept at prudent levels in the medium term. The Commission invited Member States to phase out national fiscal measures introduced to protect households and firms from the energy price shock, starting with the least targeted ones. It indicated that, if support measures needed to be extended because of renewed energy price pressures, Member States should target such measures much better than in the past towards vulnerable households and firms. The Commission proposed that the fiscal recommendations would be quantified and differentiated and be formulated on the basis of net primary expenditure, as proposed in its Communication on orientations for a reform of the EU economic governance framework[9]. It recommended that all Member States should continue to protect nationally financed investment and ensure the effective use of the Recovery and Resilience Facility and other EU funds, in particular in light of the green and digital transition and resilience objectives. The Commission indicated that it will propose to the Council to open deficit-based excessive deficit procedures in spring 2024 on the basis of the outturn data for 2023, in line with existing legal provisions.

(8) On 26 April 2023, the Commission presented legislative proposals to implement a comprehensive reform of the EU's economic governance rules. The central objective of the proposals is to strengthen public debt sustainability and promote sustainable and

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7 Regulation (EU) 2023/435 of the European Parliament and of the Council of 27 February 2023 amending Regulation (EU) 2021/241 as regards REPowerEU chapters in recovery and resilience plans and amending Regulations (EU) No 1303/2013, (EU) 2021/1060 and (EU) 2021/1755, and Directive 2003/87/EC (OJ L 63, 28.2.2023, p. 1).

8 COM(2023) 141 final.

9 COM(2022) 583 final.

inclusive growth in all Member States through reforms and investment. The proposals aim at providing Member States with more control over the design of their medium-term plans, while putting in place a more stringent enforcement regime to ensure that Member States deliver on the commitments undertaken in their medium-term fiscal-structural plans. The objective is to conclude the legislative work in 2023.

(9) On 30 April 2021, Italy submitted its national recovery and resilience plan to the Commission, in accordance with Article 18(1) of Regulation (EU) 2021/241. Pursuant to Article 19 of Regulation (EU) 2021/241, the Commission assessed the relevance, effectiveness, efficiency and coherence of the recovery and resilience plan, in accordance with the assessment guidelines of Annex V to that Regulation. On 13 July 2021, the Council adopted its Decision on the approval of the assessment of the recovery and resilience plan for Italy[10]. The release of instalments is conditional on a decision by the Commission, taken in accordance with Article 24(5) of Regulation (EU) 2021/241, that Italy has satisfactorily reached the relevant milestones and targets set out in the Council Implementing Decision. Satisfactory fulfilment presupposes that the achievement of preceding milestones and targets has not been reversed.

(10) On 2 May 2023, Italy submitted its 2023 National Reform Programme and its 2023 Stability Programme, in line with Article 4(1) of Regulation (EC) No 1466/97. To take account of their interlinkages, the two programmes have been assessed together. In accordance with Article 27 of Regulation (EU) 2021/241, the 2023 National Reform Programme also reflects Italy's biannual reporting on the progress made in achieving its recovery and resilience plan.

(11) The Commission published the 2023 country report for Italy[11] on 24 May 2023. It assessed Italy's progress in addressing the relevant country-specific recommendations adopted by the Council between 2019 and 2022, and took stock of Italy's implementation of the recovery and resilience plan. Based on this analysis, the country report identified gaps with respect to those challenges that are not addressed or only partially addressed by the recovery and resilience plan, as well as new and emerging challenges. It also assessed Italy's progress on implementing the European Pillar of Social Rights and on achieving the EU headline targets on employment, skills and poverty reduction, as well as progress in achieving the UN's Sustainable Development Goals.

(12) The Commission carried out an in-depth review under Article 5 of Regulation (EU) No 1176/2011 for Italy and published its results on 24 May 2023[12]. It concluded that Italy is experiencing excessive macroeconomic imbalances. In particular, while there have been some improvements, vulnerabilities related to high government debt and weak productivity growth, in a context of labour market fragilities and some weaknesses in financial markets, which carry cross-border relevance, persist. Italy's long-standing vulnerabilities have receded somewhat over recent years but remain significant and are not expected to unwind quickly. Persistent low productivity growth has been a key factor behind Italy's protracted weak economic growth, which slows down government debt deleveraging, dents employment opportunities and impacts banks' balance sheets. The government debt ratio further declined in 2022 along with

[10] Council Implementing Decision of 13 July 2021 on the approval of the assessment of the recovery and resilience plan for Italy (ST 10160/21; ST 10160/21 ADD 1; ST 10160/21 ADD 1 REV 1; ST 10160/21 ADD 1 REV 2; ST 10160/21 ADD 1 REV 2 COR 1).

[11] SWD(2023) 612 final.

[12] SWD(2023) 634 final.

the economic recovery. However, it remains high and constitutes a substantial fiscal sustainability challenge. The public debt ratio is forecast to further decline by 2024 but to increase in the medium term in the absence of consolidation measures. The government has implemented further measures to support the resilience of the financial sector and non-performing loans have significantly declined, but banks are still significantly exposed to the sovereign. Some progress has been made with policies to tackle imbalances, but sustained efforts are warranted and the implementation of the RRP remains the key policy priority as it includes comprehensive reforms and significant investments. Putting the high government debt on a firm downward path, in a context of rising debt servicing costs and rising age-related costs, requires a multipronged approach relying on prudent fiscal policies with adequate primary surpluses, growth-enhancing investments and reforms, greater tax compliance as well as an efficient use of national and European resources. Italy is facing challenges that, alongside a continued strong implementation of the RRP, would benefit from additional policy efforts, notably in the areas of taxation, fiscal framework and pension systems as well as in the areas of demography, labour market, and energy.

(13) Based on data validated by Eurostat,[13] Italy's general government deficit decreased from 9.0% of GDP in 2021 to 8.0% in 2022, while general government debt fell from 149.9% of GDP at the end of 2021 to 144.4% at the end of 2022. On 24 May 2023, the Commission published a report under Article 126(3) TFEU;[14] the report discussed the budgetary situation of Italy, as its general government deficit in 2022 exceeded the 3% of GDP Treaty reference value, while its general government debt exceeded the 60% of GDP Treaty reference value and did not respect the debt-reduction benchmark. The report concluded that the deficit and debt criteria were not fulfilled. In line with the Communication of 8 March 2023,[15] the Commission did not propose to open new excessive deficit procedures in spring 2023; in turn, the Commission stated that it would propose to the Council to open deficit-based excessive deficit procedures in spring 2024, on the basis of the outturn data for 2023. Italy should take account of this in the execution of its 2023 budget and in preparing the Draft Budgetary Plan for 2024.

(14) The general government balance has been impacted by the new statistical treatment of some housing renovation tax credits, now recorded as capital transfers and mostly accrued to 2021-2022[16]. It was also impacted by the fiscal policy measures adopted to mitigate the economic and social impact of the increase in energy prices. In 2022, such revenue-decreasing measures included measures to control general system charges in the electricity and gas sectors, reduction of the VAT rate on gas, reduction of excise duties on fuel prices, reduction of social security contributions for workers below a certain income threshold; while such expenditure-increasing measures included subsidies to electricity and gas companies, expansion of the 'social bonus' for electricity and gas bills for low-income households, means tested allowances for workers, pensioners and unemployed persons and an increase, by 2% in October 2022 in advance of the statutory inflation-related indexation normally due in 2023, of old-

13 Eurostat-Euro Indicators, 47/2023, 21.4.2023

14 COM(2023) 631 final, 24.5.2023.

15 COM(2023) 141 final, 8.3.2023.

16 The new statistical treatment implied an upward revision of the deficit by 1.8 percentage points of GDP in 2021. In 2022, the tax credits involved by the new statistical treatment are estimated to have had a deficit increasing impact of 2.6 percentage points of GDP.

age pensions. The cost of these measures was partly offset by new taxes on windfall profits of energy producers and suppliers and revenues from the offset mechanism on the price of electricity produced from renewable sources and from the application of a compensation mechanism in the electricity sector, deemed to implement Council Regulation on an emergency intervention to address high energy prices adopted on 6 October 2022. The Commission estimates the net budgetary cost of these measures at 2.5% of GDP in 2022. The general government balance has also been impacted by the budgetary cost of temporary protection to displaced persons from Ukraine, which is estimated at 0.1% of GDP in 2022. At the same time, the estimated cost of COVID-19 temporary emergency measures dropped to 1.1% of GDP in 2022, from 3.4% in 2021, as the government phased out the majority of the measures taken in response to the COVID-19 crisis.

(15) On 18 June 2021, the Council recommended that in 2022 Italy[17] use the Recovery and Resilience Facility to finance additional investment in support of the recovery, while pursuing a prudent fiscal policy. Moreover, Italy should preserve nationally financed investment. The Council also recommended Italy to limit the growth of nationally financed current expenditure.

(16) According to the Commission estimates, the fiscal stance[18] in 2022 was supportive, at -3.2% of GDP. As recommended by the Council, Italy continued to support the recovery with investments financed by the Recovery and Resilience Facility. Expenditure financed by Recovery and Resilience Facility grants and other EU funds amounted to 0.9% of GDP in 2022 (0.4% of GDP in 2021). Nationally financed investment provided a neutral contribution to the fiscal stance.[19] Italy therefore preserved nationally financed investment, as recommended by the Council. At the same time, the growth in nationally financed primary current expenditure (net of new revenue measures) provided an expansionary contribution of 2.4 percentage points to the fiscal stance. This significant expansionary contribution included the additional impact of fiscal policy measures to mitigate the economic and social impact of the increase in energy prices (additional net budgetary cost of 2.2% of GDP), as well as the costs to offer temporary protection to displaced persons from Ukraine (0.1% of GDP). Italy therefore sufficiently kept under control the growth in national financed current expenditure.

(17) The macroeconomic scenario underpinning the budgetary projections in the Stability Programme is realistic in both 2023 and 2024. The government projects real GDP to grow by 1.0% in 2023 and 1.5% in 2024. By comparison, the Commission 2023 spring forecast projects a slightly higher real GDP growth of 1.2% in 2023 and somewhat lower, at 1.1%, in 2024, mainly due to a smaller contribution of investment, which the

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17 Council Recommendation of 18 June 2021 delivering a Council opinion on the 2021 Stability Programme of Italy, OJ C 304, 29.7.2021, p. 53.

18 The fiscal stance is measured as the change in primary expenditure (net of discretionary revenue measures), excluding Covid-19 crisis-related temporary emergency measures but including expenditure financed by non-repayable support (grants) from the Recovery and Resilience Facility and other EU funds, relative to medium-term potential growth. For more details see Box 1 in the Fiscal Statistical Tables.

19 Other nationally financed capital expenditure is projected to provide an expansionary contribution of 0.3 percentage points of GDP. This is explained by the increase in expenditure related to tax credits for building renovation works, which is recorded as a capital transfer.

government projects to grow by 3.4% year-on-year while the Commission forecasts to grow by 1.8%.

(18) In its 2023 Stability Programme, the government expects that the general government deficit ratio will decrease to 4.5% of GDP in 2023. The decrease in 2023 mainly reflects the reduction in capital transfers related to tax credits supporting private investment in housing efficiency, a decrease in compensation of employees due to the retroactive renewal of public contracts for the period 2019-2021, for which a substantial part of the arrears was recorded in 2022, a reduction in subsidies on production in conjunction to lower tax credits to electricity and gas companies and lower interest expenditure mainly explained by lower yields on government bonds indexed to inflation. According to the Programme, the general government debt-to-GDP ratio is expected to decrease from 144.4% at the end of 2022 to 142.1% at the end of 2023. The Commission 2023 spring forecast projects a government deficit of 4.5% of GDP for 2023. This is in line with the deficit projected in the Stability Programme. The Commission 2023 spring forecast projects a lower general government debt-to-GDP ratio, of 140.4% at the end of 2023. The difference is due to higher nominal GDP growth in the Commission forecast.

(19) The government balance in 2023 is expected to continue to be impacted by the measures adopted to mitigate the economic and social impact of the increase in energy prices. They consist of measures extended from 2022 (in particular: subsidies to electricity and gas companies, measures to control general system charges in gas sector, reduction of the VAT rate on gas and reduction of social security contributions for workers below a certain income threshold) and new measures such as a heating bonus for all households for the period October-December 2023. The cost of these measures continues to be partly offset by taxes on windfall profits of energy producers and suppliers. Taking these revenues into account, the net budgetary cost of the support measures is projected in the Commission 2023 spring forecast at 1.0% of GDP in 2023[20]. Most measures in 2023 are targeted to the most vulnerable households or firms, although the majority of the energy support measures do not fully preserve the price signal to reduce energy demand and increase energy efficiency. As a result, the amount of targeted support measures, to be taken into account in the assessment of compliance with the recommendation for 2023, is estimated in the Commission 2023 spring forecast at 0.7% of GDP in 2023 (compared to 1.2% of GDP in 2022). Finally, the 2023 government balance is expected to benefit from the complete phasing out of COVID-19 temporary emergency measures of 1.1% of GDP.

(20) On 12 July 2022, the Council recommended[21] that Italy ensures in 2023 a prudent fiscal policy, in particular by limiting the growth of nationally financed primary current expenditure below medium-term potential output growth[22], taking into account continued temporary and targeted support to households and firms most vulnerable to energy price hikes and to people fleeing Ukraine. At the same time, Italy should stand ready to adjust current spending to the evolving situation. Italy was also recommended to expand public investment for the green and digital transitions, and for energy

[20] The figure represents the level of annual budgetary cost of those measures, including current revenue and expenditure as well as – where relevant – capital expenditure measures.

[21] Council Recommendation of 12 July 2022 on the National Reform Programme of Italy and delivering a Council opinion on the 2022 Stability Programme of Italy, OJ C 334, 1.0.2022, p. 96.

[22] Based on the Commission 2023 spring forecast, the medium-term (10-year average) potential output growth of Italy is estimated at 6.4% in nominal terms.

security taking into account the REPowerEU initiative, including by making use of the Recovery and Resilience Facility and other Union funds.

(21) In 2023, the fiscal stance is projected in the Commission 2023 spring forecast to be contractionary (+2.6% of GDP), in a context of high inflation. This follows an expansionary fiscal stance in 2022 (-3.2% of GDP). The growth in nationally financed primary current expenditure (net of discretionary revenue measures) in 2023 is projected to provide a contractionary contribution of 0.9% of GDP to the fiscal stance. Therefore, the projected growth of nationally financed primary current expenditure is in line with the Council recommendation. The projected contractionary contribution of nationally financed primary current expenditure is due, in substance, to the reduced costs (by 1.5 percentage points of GDP) of the support measures (targeted and untargeted) to households and firms in response to energy price hikes. The main drivers of growth in nationally financed primary current expenditure (net of new revenue measures) are the increase in pension expenditure due to the indexation to previous-year inflation and the further recently adopted cuts to the labour tax wedge for low- and medium-income earners. Expenditure financed by Recovery and Resilience Facility grants and other EU funds is projected to amount to 1.4% of GDP in 2023, while nationally financed investment is projected to provide an expansionary contribution to the fiscal stance of 0.1 percentage points[23]. Therefore, Italy plans to finance additional investment through the Recovery and Resilience Facility and other EU funds, and it is projected to preserve nationally financed investment. It plans to finance public investment for the green and digital transitions, and for energy security, such as investments in the rail network, renewable energy, hydrogen, electricity grids and sustainable mobility, the protection of land and water resources as well investments related to the cloud infrastructure for the public administration, which are partly funded by the Recovery and Resilience Facility and other EU funds. In light of the devastating floods that hit Italy in May 2023, the cost of direct emergency support related to those floods will be taken into account in subsequent assessments of compliance and will in principle be considered as one-off and temporary measures.[24]

(22) According to the Stability Programme the general government deficit is expected to decline to 3.7% of GDP in 2024. The decrease in 2024 mainly reflects a reduction in expenditure for intermediate consumption and for tax credits to electricity and gas companies. The programme expects the general government debt-to-GDP ratio to decrease to 141.4% at the end of 2024. Based on policy measures known at the cut-off date of the forecast, the Commission 2023 spring forecast projects a government deficit of 3.7% of GDP in 2024. This is in line with the deficit projected in the programme, although the Commission forecast does not include planned deficit-increasing measures amounting to 0.2% of GDP, for which the details are not yet known. The Commission 2023 spring forecast projects a lower general government debt-to-GDP ratio, of 140.3% at the end of 2024. The difference is due to higher nominal GDP growth in the Commission forecast.

(23) The Stability Programme envisages the phasing out of all of the energy support measures in 2024. The Commission also assumes full phasing out of energy support

[23] Other nationally financed capital expenditure is projected to provide a contractionary contribution of 2.3 percentage points of GDP. This is explained by the expected reduction in spending for tax credits for building renovation works.

[24] See for the definition of a one-off measure the 2015 Public finance report.

measures in 2024. This hinges upon the assumption of no renewed energy price increases.

(24) Council Regulation (EC) No 1466/97 calls for an annual improvement in the structural budget balance toward the medium-term objective by 0.5% of GDP as a benchmark[25]. Taking into account fiscal sustainability considerations[26] and the need to reduce the deficit to below the 3% of GDP reference value, an improvement in the structural balance of at least 0.7% of GDP for 2024 would be appropriate. To ensure such an improvement, the growth in net nationally financed primary expenditure in 2024 should not exceed 1.3%, as reflected in this recommendation. At the same time, the remaining energy support measures (currently estimated by the Commission at 1.0% of GDP in 2023) should be phased out, contingent on energy market developments and starting from the least targeted ones, and the related savings should be used to reduce the government deficit. Based on Commission estimates, this would lead to a growth in net primary expenditure lower than recommended for 2024.

(25) Assuming unchanged policies, the Commission 2023 spring forecast projects net nationally financed primary expenditure to grow at 0.8% in 2024, which is below the recommended growth rate. In light of the devastating floods that hit Italy in May 2023, the cost of direct emergency support related to those floods will be taken into account in subsequent assessments of compliance and will in principle be considered as one-off and temporary measures.

(26) According to the programme, government investment is expected to increase from 3.3% of GDP in 2023 in to 3.8% of GDP in 2024. The higher investment reflects higher nationally financed investment and investment financed by the EU, including through the Recovery and Resilience Facility. The programme refers to reforms and investments, that are expected to contribute to fiscal sustainability and sustainable and inclusive growth. These include the reform of the procurement code, which is also part of the Recovery and Resilience Plan and the tax system included in the enabling law of March 2023.

(27) The Stability Programme outlines a medium-term fiscal path until 2026. According to the programme, the general government deficit is expected to decline to 3.0% of GDP in 2025 and to 2.5% by 2026. The general government deficit is therefore planned to not exceed 3% of GDP from 2025. According to the programme, the general government debt-to-GDP ratio is expected to decrease from 141.4% at the end of 2024 to 140.4% by the end of 2026.

(28) Italy's tax wedge on labour has remained high at all income levels compared to other EU Member States, despite the reduction of personal income taxes implemented in 2022. In addition, the extension of the flat-rate regime to the self-employed raises concerns over the equity and efficiency of the tax system. The introduction of a new flat-rate regime on earning increases for 2023 also raised complexity. In March 2023, the government adopted a new enabling law for a general reform of the tax system. It

[25] Cf. Article 5 of Council Regulation (EC) No 1466/97, which also requires an adjustment of more than 0.5% of GDP for Member States with a government debt exceeding 60% of GDP, or with more pronounced debt sustainability risks.

[26] The Commission estimated that Italy would need an average annual increase in the structural primary balance as a share of GDP of 0.85 percentage points to achieve a plausible debt reduction or ensure that government debt is kept at prudent levels in the medium term. This estimate was based on the Commission autumn 2022 forecast. The starting point for this estimate was the projected government deficit and debt for 2024 which assumed the withdrawal of energy support measures in 2024.

is expected to tackle some long-standing weaknesses, including by reducing taxes on labour and rationalising and streamlining tax expenditures and corporate taxes. When implementing this reform, it is crucial to preserve the progressivity of the tax system, reduce complexity, increase incentives to work, strengthen tax compliance and ensure budget neutrality. In this regard, there is potential to increase revenues from other sources that are less detrimental to growth, such as property, VAT and authorisation for the use of state-owned coastal assets, in order to reduce the tax burden on labour in a budget-neutral way. There is also scope to improve the design of environmental taxes, which, despite relatively high revenues, does not sufficiently promote the transition to cleaner technologies, also due to the extensive use of environmentally harmful subsidies. Furthermore, it is important to address a long-standing challenge that is not included in the enabling law, namely the largely outdated cadastral values, which serve as a basis for calculating property tax.

(29) In accordance with Article 19(3), point (b) and Annex V, criterion 2.2 of Regulation (EU) 2021/241, the recovery and resilience plan includes an extensive set of mutually reinforcing reforms and investments to be implemented by 2026. The implementation of Italy's recovery and resilience plan is underway, however with increasing risk of delays. Italy submitted 3 payment requests, corresponding to 151 milestones and targets in the plan and resulting in an overall disbursement of EUR 42 billion (the amount refers to the first two payment requests, while the third one is under assessment). Proceeding swiftly with the implementation of the plan and the negotiation of its amendment is essential due to the temporary nature of the Recovery and Resilience Facility in place until 2026. It is important for Italy to strengthen administrative capacity, particularly at subnational level, to deliver on the commitments of the plan, while an effective and fully operational governance framework remains key for a smooth and timely implementation of the plan. It continues to be crucial to identify potential delays and implementation issues early on and to take timely action to address them. In accordance with Article 14(6) of Regulation (EU) 2021/241, on 31 March 2023, Italy expressed its intention to request additional loan support under the Recovery and Resilience Facility. The negotiation on the addendum and the REPowerEU chapter is ongoing, although Italy has not submitted any official proposal. The swift inclusion of the new REPowerEU chapter in the recovery and resilience plan will allow additional reforms and investments to be financed in support of Italy's strategic objectives in the field of energy and the green transition. The systematic and effective involvement of local and regional authorities, social partners and other relevant stakeholders remains important for the successful implementation of the recovery and resilience plan, as well as other economic and employment policies going beyond the plan, to ensure broad ownership of the overall policy agenda.

(30) The Commission approved most of Italy's cohesion policy programming documents in 2022 and some in 2023. Proceeding with the swift implementation of the cohesion policy programmes in complementarity and synergy with the recovery and resilience plan, including the REPowerEU chapter, is key to achieving the green and digital transition, increasing economic and social resilience as well as achieving balanced territorial development in Italy.

(31) Beyond the economic and social challenges addressed by the recovery and resilience plan, Italy faces a number of additional challenges related to energy policy and the green transition, particularly on the uptake of renewables, gas transmission, energy efficiency, the provision and acquisition of green skills and sustainable mobility.

(32) Renewable capacity grew very slowly over the past year, and the share of fossil fuels in the energy mix remains significant. To accelerate the uptake of renewables, Italy has adopted some amendments to the existing framework that regulates the permitting and authorisation process for renewables. Further efforts are needed to ensure coherence between the administrative and legislative framework at both national and regional level and their relevance to state-of-the-art energy technology. For example, all related norms could be consolidated into a unique text (*Testo unico*); at the same time, the guidelines that subnational authorities follow to evaluate projects need to be updated. Lastly, further investments are needed to upgrade the national grid and construct interconnections between the mainland, Sicily and Sardinia to allow for the expected higher generation capacity and absorb the related increase in renewable output.

(33) Bottlenecks in the gas network remain. Italy is discussing investments with partners in North Africa to increase the import capacity of existing pipelines and gas interconnectors. This would help diversify imports and therefore strengthen security of supply. However, further investments are needed to remove bottlenecks in the existing domestic network, which does not have the transmission capacity to distribute new gas intake from the south to the north of the country. Investment into fossil fuel infrastructure needs to be limited to the strictly necessary and be designed to be future-proof, to avoid lock-in into technologies that are not consistent with the climate objectives or increasing the cost of the energy transition.

(34) Italy's consumption of natural gas has dropped by 19% in the period between August 2022 and March 2023, compared with the average gas consumption over the same period in the last 5 years, beyond the 15% reduction target. Italy could keep pursuing efforts to temporarily reduce gas demand until 31 March 2024[27]. Measures to improve the energy efficiency of buildings need to be targeted. Italy's building stock has considerable energy efficiency potential, in particular with regard to the large share of old and energy-intensive buildings. Existing measures in the recovery and resilience plan could be complemented by measures such as targeted incentive schemes to increase energy efficiency in worst-performing buildings, including commercial buildings and public housing, while ensuring that vulnerable households are reached and avoiding regressive effects. These measures would benefit in particular small, medium and microenterprises that often lack the technical and financial capacity to improve their energy efficiency. The same measures would also help reduce energy poverty, which could be further tackled by other measures, for instance via one-stop shops that provide personalised services for energy savings. Energy efficiency gains would also benefit from an increase in market surveillance on ecodesign and energy labelling.

(35) Infrastructure gaps and environmentally harmful subsidies, including road transport, remain substantial and discourage the transition towards more sustainable transport solutions. For instance, the average number of charging outlets remains below the EU average. Environmentally harmful subsidies include the flat-rate taxation of company cars available for private use and the reimbursement of excise duty on diesel used in freight. Continuing efforts to roll out charging stations and remove those subsidies is key to consolidating the market for zero-emission vehicles.

[27] Council Regulation (EU) 2022/1369 and Council Regulation (EU) 2023/706.

(36) Labour and skills shortages in sectors and occupations key for the green transition, including manufacturing, deployment and maintenance of net-zero technologies, are creating bottlenecks in the transition to a net-zero economy. High-quality education and training systems that respond to changing labour market needs and targeted upskilling and reskilling measures are key to reducing skills shortages and promoting labour inclusion and reallocation. To unlock untapped labour supply, these measures need to be accessible, in particular for individuals and in sectors and regions most affected by the green transition. In Italy, both high- and low-skilled occupations that are key for the green transition are affected by shortages. At the same time, training support often does not reach the workers most likely to be affected by the green transition. The lack of green skills in the public sector, in particular at local level, is also holding back green investments. Italy faces wide regional disparities that risk being exacerbated if local labour markets are not able to grasp the opportunities of the green transition. Moreover, boosting green skills, including for sustainable soil management, would be key in fighting the effects of climate change, in particular aggravated flooding and persistent droughts.

(37) In light of the Commission's assessment, the Council has examined the 2023 Stability Programme and its opinion[28] is reflected in recommendation (1) below.

(38) In view of the close interlinkages between the economies of euro area Member States and their collective contribution to the functioning of the Economic and Monetary Union, the Council recommended that the euro area Member States take action, including through their recovery and resilience plans, to (i) preserve debt sustainability and refrain from broad-based support to aggregate demand in 2023, better target fiscal measures taken to mitigate the impact of high energy prices and reflect on appropriate ways to wind down support as energy price pressures diminish; (ii) sustain high public investment and promote private investment to support the green and digital transition; (iii) support wage developments that mitigate the loss in purchasing power while limiting second-round effects on inflation, further improve active labour market policies and address skills shortages; (iv) improve the business environment and ensure that energy support to companies is cost-effective, temporary, targeted to viable firms and that it maintains incentives for the green transition; and (v) preserve macro-financial stability and monitor risks while continuing to work on completing the Banking Union. For Italy, recommendations (1), (2) and (3) contribute to the implementation of the first, second, third and fourth euro area recommendations.

(39) In light of the Commission's in-depth review and this assessment, the Council has examined the 2023 National Reform Programme and the 2023 Stability Programme. Its recommendations under Article 6 of Regulation (EU) No 1176/2011 are reflected in recommendation (1) below. Policies referred to in recommendation (1) help address vulnerabilities linked to high government debt and weak productivity growth. Recommendation (2) contributes to addressing recommendation (1). Policies referred to in recommendation (1) contribute to both addressing imbalances and implementing the recommendations for the euro area, in line with recital 38.

HEREBY RECOMMENDS that Italy take action in 2023 and 2024 to:

1. Wind down the energy support measures in force by the end of 2023, using the related savings to reduce the government deficit. Should renewed energy price increases necessitate support measures, ensure that these are targeted at protecting

[28] Under Articles 5(2) and 9(2) of Council Regulation (EC) No 1466/97.

vulnerable households and firms, fiscally affordable, and preserve incentives for energy savings.

Ensure prudent fiscal policy, in particular by limiting the nominal increase in nationally financed net primary expenditure in 2024 to not more than 1.3%.

Preserve nationally financed public investment and ensure the effective absorption of RRF grants and other EU funds, in particular to foster the green and digital transitions.

For the period beyond 2024, continue to pursue a medium-term fiscal strategy of gradual and sustainable consolidation, combined with investments and reforms conducive to improved productivity and higher sustainable growth, to achieve a prudent medium-term fiscal position.

Further reduce taxes on labour and make the tax system more efficient by adopting and duly implementing the enabling law on tax reform while preserving the progressivity of the tax system and improving fairness, in particular by streamlining and reducing tax expenditures, including VAT and environmentally harmful subsidies, and by reducing the complexity of the tax code. Align the cadastral values with current market values.

2. Ensure an effective governance and strengthen the administrative capacity, particularly at subnational level, to allow for a continued swift and steady implementation of the recovery and resilience plan. Swiftly finalise the REPowerEU chapter with a view to rapidly starting its implementation. Proceed with the speedy implementation of cohesion policy programmes, in close complementarity and synergy with the recovery and resilience plan.

3. Reduce the reliance on fossil fuels. Streamline the permitting procedures to accelerate the production of additional renewable energy and develop electricity interconnections to absorb it. Increase the capacity for internal gas transmission to diversify energy imports and strengthen security of supply. Increase energy efficiency in the residential and corporate sectors, including through better targeted incentive schemes, addressing in particular the most vulnerable households and the worst-performing buildings. Promote sustainable mobility, including by removing environmentally harmful subsidies and speeding up the roll-out of charging stations. Step up policy efforts aimed at the provision and acquisition of the skills needed for the green transition.

Done at Brussels,

For the Council
The President