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Italy government tensions flare up over tax reform

Divisions in Italy's government widened on Tuesday when the rightist League deserted a cabinet meeting that approved the framework of a contested tax reform promised to the European Union.

The bill, aimed at reducing income taxes and simplifying the system, was initially promised by the end of July as part of Rome's Recovery and Resilience Plan (PNRR), but had been held up by coalition tensions.

These erupted on Tuesday when the League, a key component of Prime Minister Mario Draghi's national unity government, protested the bill could lead to an unacceptable increase in taxation and that it had not had time to examine it properly.

The League's decision not to participate in the cabinet meeting is the clearest rift in Draghi's administration since it was formed seven months ago.

Draghi told reporters it was "a serious gesture" which it was up to League leader Matteo Salvini to explain.

The main bone of contention is a planned review of real estate values which the League fears will trigger higher levies for home-owners.

"At this moment increasing taxes for Italians even by a single euro is not an option," Salvini told a news conference.

Draghi said the government had no intention of raising taxes and stressed that the reform was in an extremely preliminary stage and there would be plenty of occasions for ministers and parliament to discuss it further.

"This is a very general framework which we will need to fill with the details," he said, adding that overhauling Italy's tax system would take "many years."

After the bill has been approved by both houses of parliament it must be implemented within 18 months.

"The tax reform is among the key elements in the PNRR to tackle the structural weaknesses of the country and constitutes an integral part of the recovery we aim to trigger with the help of EU funds," says a government document accompanying the bill.

Updating the taxable value of real estate, which is often far below real market values, has been recommended to Italy by the European Commission.

The bill stipulates levies on real estate will not change before 2026, and Draghi called the planned review of house values "a statistical exercise" in the name of transparency, which was not connected to taxation.

Italy also plans to align rates of tax on financial investments with corporate income tax over the medium term, a draft of the bill seen by Reuters showed.

The tax rate on financial investments, except for government bonds, is currently higher than tax on corporate income (Ires).

The government's latest budget targets presented last month contain leeway for additional spending of 1.2% of national output, or more than 22 billion euros ($25.5 billion) next year.

A big part of this sum will be used to fund tax cuts in the fiscal reform, a government source said.