Federal Ministry
of Finance

24th Subsidy Report of the Federal Government

Federal Government report on the development of federal financial assistance and tax benefits for the years 2011 to 2014

Summary

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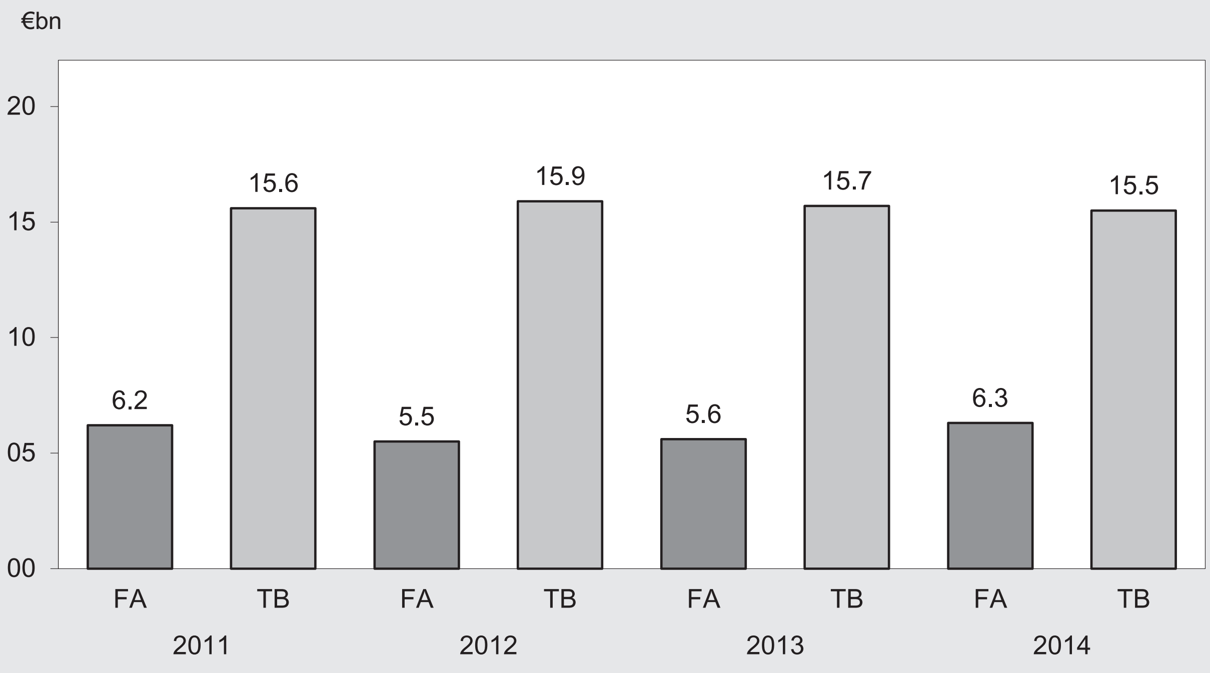
I. Introduction

In accordance with section 12 of the 1967 Stability and Growth Act (*Gesetz zur Förderung der Stabilität und des Wachstums der Wirtschaft*), every two years the Federal Government submits to the Bundestag and Bundesrat a Subsidy Report that provides an overview of federal financial assistance and estimated revenue shortfalls resulting from tax benefits. The report is submitted in conjunction with the government draft of the federal budget.

The Federal Government's 24th Subsidy Report outlines trends in federal financial assistance and tax benefits during the 2011–2014 period. This English-language summary report presents the main findings of the full report. The full report is available in German on the website of the Federal Ministry of Finance, **www.bundesfinanzministerium.de**.

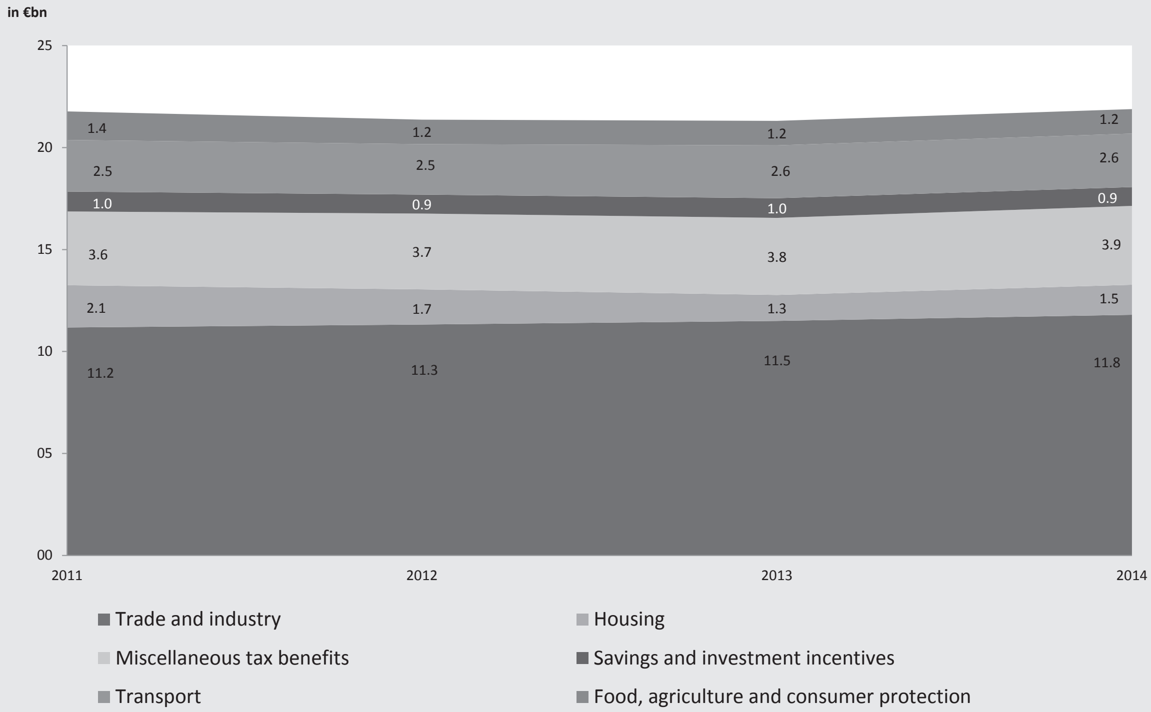
Annual total subsidies remained constant over the course of the reporting period at €21.8 billion (in both 2011 and 2014; see Figure 1). Total financial assistance over the 2011–2014 period, as well as total tax benefits during this period, are lower than the corresponding totals contained in the 23rd Subsidy Report and are slightly below pre-crisis levels.

Figure 1: Federal financial assistance (FA) and tax benefits (TB), 2011 to 2014



In 2013, approximately 54% of all federal subsidies went to trade and industry. Federal subsidies in this category have increased from just under €11.2 billion in 2011 to just under €11.8 billion in 2014. Financial assistance targeting the energy sector is the main factor driving this increase.

Figure 2: Federal financial assistance and tax benefits by economic sector, 2011 to 2014



II. Subsidy policy and definitions

During the reporting period, the Federal Government's subsidy policy has been influenced primarily by decisions taken in connection with the *Energiewende*, or the transformation of Germany's energy system. The Federal Government's aim with the *Energiewende* is to secure a reliable and economically viable energy supply that is both climate- and environment-friendly, without compromising the German economy's competitiveness.

The Federal Government has pursued a differentiated subsidy policy based on (a) the current stability of the German economy and (b) the priorities associated with the implementation of the *Energiewende*. As a result, it has reduced certain subsidies slightly while temporarily topping up or introducing new forms of financial assistance to businesses and consumers, especially in the energy sector. These latter subsidies aim to accelerate the implementation of the *Energiewende* and to safeguard and strengthen the competitiveness of energy-intensive businesses. The measured reduction of subsidies in certain areas coupled with higher subsidies in other areas has caused total subsidies to remain basically constant over the reporting period. In sum, total subsidies for the current reporting period are below the total contained in the 23rd Subsidy Report, and slightly below pre-crisis levels. This trend means that subsidy policies have made a positive contribution to fiscal consolidation while simultaneously safeguarding and enhancing the competitiveness of the German economy. As a result, these policies form part of the Federal Government's pursuit of growth-friendly consolidation.

2.1 Subsidy policy principles and the importance of subsidy reduction

Germany's budget rule, which has applied since 2011, lays down the legal framework for ensuring sustainable fiscal policies over the medium and long term. The budget rule stipulates that structural new borrowing must be gradually reduced to 0.35% of GDP by 2016. The Federal Government's budget preparation process came into compliance with the 2016 cap already in 2013. In order to ensure long-term compliance with this target, all functions performed by state must be regularly reviewed to ensure that they are necessary, and all measures that impact public finances must undergo suitable cost-benefit analysis. Accordingly, subsidy policy based on these principles involves the systematic review of financial assistance and tax benefits, with reviewed measures subject to adjustment or elimination as appropriate. This contributes both to the fulfilment of quantitative consolidation targets as well as to the more efficient and effective use of public finances. The Federal Government's regular Subsidy Reports provide the information needed for this review of subsidies. It presents federal financial assistance and public tax benefits in quantitative terms and analyses them with regard to their objectives and how attainment of those objectives is measured.

Apart from serving as a special means to facilitate economic stability, subsidies can function under certain conditions as a legitimate instrument of fiscal policy in the social market economy. The decisive factor here is their impact in terms of economic growth, distributive policy and competition, and increasingly also in terms of their impact on the environment. Subsidy policy must therefore take into account positive and negative external effects – including the distribution of such effects – as well as potential knock-on costs. Time-limited, degressive public assistance can help level out regional disparities, provide incentives and start-up funding to encourage new market entrants, accelerate the development and launch of new products, and simultaneously facilitate necessary structural change.

However, subsidies always require special justification, together with regular evaluations of their efficiency and success. This is because long-term favourable arrangements that benefit one side at the expense of others generally have adverse effects: for example, by altering relative prices over a sustained period, subsidies can lead to economic distortions and the misallocation of resources. Subsidised companies can crowd competitive companies out of markets. Furthermore, subsidies pose the risk of creating a culture of dependence, or a "subsidy mindset", with the result that recipients fail to make the necessary adaptations and show less initiative to tackle structural challenges. These problems can delay crucial structural adjustments, cause a loss of international competitiveness, and impede economic growth and employment.

Subsidies also require special justification with a view towards any potential adverse impacts on the environment. Subsidies that damage the environment place a double burden on public budgets: first, they cause extra government spending and/or revenue shortfalls in the present; and second, they increase the costs of eliminating harmful effects on health and the environment in the future. For this reason, the Federal Government regularly assesses whether subsidies that make short-term sense can be replaced over the medium term with market-based solutions that are not dependent on government budgets.

2.2 Definition of subsidies

The subject matter of the Subsidy Report has been stipulated on an unaltered basis since 1967 by section 12 of the Stability and Growth Act. Financial assistance is defined for this purpose as federal funds allocated to agencies outside the federal administration and deployed for the benefit of private businesses or economic sectors. Tax benefits, in turn, are special tax rules that lead to a reduction in public revenue.

In accordance with the statutory mandate, the definition of federal subsidies focuses on assistance to private businesses and economic sectors. Section 12 of the Stability and Growth Act specifically describes financial assistance as federal funds used to provide sectoral support, adjustment assistance and productivity/growth assistance for businesses and economic sectors. Assistance that does not fall into these categories is designated as miscellaneous financial assistance. Indirect subsidies are also included; these comprise assistance that directly reduces the price of certain goods or services for private households but that can be indirectly assigned to trade and industry. Examples here include assistance for residential construction or for private old-age pensions known in Germany as “Riester pensions”.

A similar definition is applied to tax benefits, which are classified in the same way as financial assistance. A special tax regulation is regarded as a subsidy and hence as a tax benefit for the purposes of the Subsidy Report if it directly or indirectly benefits specific sectors or subsectors of the economy. Tax benefits also include special tax regulations that directly benefit business and industry over the general public.

Special tax regulations that are not classified as subsidies according to this definition but that have an equivalent effect are listed for informational purposes in Annex 3 of the full version of the 24th Subsidy Report. These consist of regulations that indirectly benefit business and industry in general – such as the income tax allowance for employee discounts – as well as regulations that do not assist business and industry but rather benefit – directly or indirectly – some other identifiable sector of society. The latter mainly comprise concessions for non-profit organisations, registered associations, churches, political parties, the healthcare sector and social insurance funds.

Federal expenditures on general tasks of the state such as funding for basic research do not count as subsidies, although it can be difficult to draw the line in individual cases. Grants and capital injections for federal enterprises are likewise not included. Federal guarantees also do not count as subsidies; the main reason for this is the typically low risk of recourse to such guarantees, making an outflow of fiscal resources highly unlikely. Although federal guarantees did record a tremendous increase as part of the measures taken to rescue banks during the financial crisis, the probability of default can be classified as low in these cases as well. Furthermore, such measures aim more to safeguard the overall economy’s ability to function smoothly rather than to support a separate sector of the economy, much less an individual company. It is indisputable that state intervention was necessary in the case of the bank rescues, a fact that also makes it unsuitable to classify such measures as financial assistance. In any case, federal and other guarantees are reported elsewhere, for example in the financial reports regularly published by the Federal Ministry of Finance.

In accordance with its specific purpose, the Subsidy Report reflects only those government functions that involve the use of federal funding or tax benefits to influence the economy. Information on specific policy areas is provided in other Federal Government reports.

Both the question of which specific arrangements are to be classified as subsidies as well as the general definition of subsidies for the purpose of the Subsidy Report are a recurring subject of academic and political debate. In accordance with the provisions of the Stability and Growth Act, a relatively narrow definition of subsidies is used for the Subsidy Report. The Subsidy Report’s general focus on assistance for private enterprises and economic sectors means that large areas of the federal budget are excluded that could be classified as subsidies using other definitions. The Federal Government regularly reviews the definition of subsidies as well as the subject matter covered by the Subsidy Report based on section 12 of the Stability and Growth Act.

III. Development of subsidies

The Subsidy Report's analysis and discussion of financial assistance focuses on the use of federal funding. Tax benefits, on the other hand, are reported on from different perspectives. The report shows firstly the total size of the tax revenue shortfall from tax benefits adopted by the federal legislature and secondly the size of the shortfall incurred at federal level. The Subsidy Report therefore also includes estimates of revenue shortfalls for other than federal jurisdictions. From a budget policy perspective, the focus is on federal-level revenue shortfalls and expenditure.

In addition to reporting on the development of federal subsidies from 2011 to 2014 (section 3.1), this chapter also provides an overview of the development of federal, *Länder* municipal, ERP and EU subsidies (section 3.2). The information on the development of subsidies provided below forms an important basis for assessing subsidy policy in general, and federal subsidy policy in particular. Various methodological points need to be kept in mind when analysing and evaluating the figures. Any critical appraisal of subsidy policy should be performed with separate regard to the various policy instruments, objectives and subsidy areas.

3.1 Development of federal subsidies in the reporting period from 2011 to 2014

Total subsidies during the reporting period range from €21.3 billion to €21.8 billion. Total financial assistance over the 2011–2014 period, as well as total tax benefits during this period, are lower than the corresponding totals contained in the 23rd Subsidy Report and are slightly below pre-crisis levels.

> Compared with 2011, financial assistance in 2012 declined by €700 million to €5.5 billion. Total financial assistance will increase again in 2014 due to topped up and newly introduced assistance programmes, especially in the energy sector and mainly in connection with the expansion of the building refurbishment programme to reduce CO_2 emissions (called the CO_2 Building Refurbishment Programme) and a programme to compensate energy-intensive companies for higher electricity prices resulting from emissions trading (called Electricity Price Compensation). For the entire reporting period, financial assistance accounts for 27% of all subsidies.

> Federal-level tax benefits will remain basically constant across the entire reporting period as well (at €15.6 billion in 2011 and €15.5 billion in 2014).

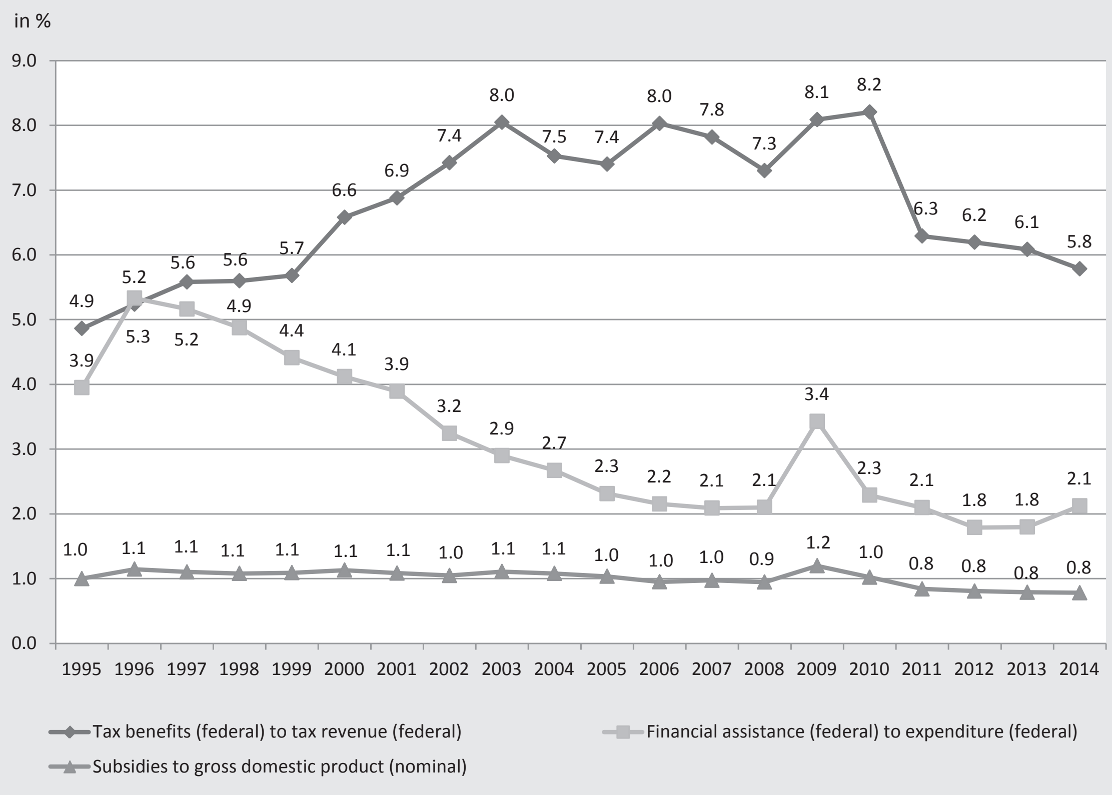
Table 1: Development of federal financial assistance and federal-level tax benefits, 2011 to 2014 (in € million)[1]

	2011			2012			2013			2014		
Category	Financial assistance Actual	Tax benefits	Total	Financial assistance Actual	Tax benefits	Total	Financial assistance Budget	Tax benefits	Total	Financial assistance Govt. draft	Tax benefits	Total
1. Food, agriculture and consumer protection	877	560	1,437	657	530	1,187	680	535	1,215	636	540	1,176
2. Trade and industry (excluding transport)												
2.1 Mining	1,448	-	1,448	1,288	-	1,288	1,229	-	1,229	1,290	-	1,290
2.2 Energy efficiency and renewable energy	313	-	313	386	-	386	438	-	438	945	-	945
2.3 Technology and innovation subsidies	682	-	682	461	-	461	530	-	530	521	-	521
2.4. Assistance for specific economic sectors	170	-	170	9	-	9	23	-	23	24	-	24
2.5. Regional structural measures	404	446	850	411	453	864	408	278	686	398	155	553
2.6 Other measures	372	7,343	7,715	324	7,991	8,315	341	8,229	8,570	283	8,158	8,441
Total (2)	**3,389**	**7,789**	**11,178**	**2,879**	**8,444**	**11,323**	**2,969**	**8,507**	**11,476**	**3,461**	**8,313**	**11,774**
3. Transport	496	2,035	2,531	475	2,000	2,475	563	2,029	2,592	561	2,062	2,623
4. Housing	1,017	1,055	2,072	1,101	622	1,723	1,001	272	1,273	1,337	135	1,472
5. Savings and investment incentives	435	541	976	386	544	930	354	611	965	300	624	924
6. Miscellaneous financial assistance and tax benefits[2]	-	3,616	3,616	-	3,716	3,716	-	3,779	3,779	-	3,867	3,867
Total (1) to (5)[3]	**6,214**	**15,596**	**21,810**	**5,498**	**15,856**	**21,354**	**5,567**	**15,733**	**21,300**	**6,295**	**15,541**	**21,836**

1 Totals may contain differences due to rounding
2 Primarily tax benefits that directly assist private households but affect important sectors of trade and industry
3 Tax benefits estimated

To present subsidies in relation to economic and fiscal policy trends, various subsidy ratios are shown in Figure 3. Financial assistance as a percentage of federal public spending decreased continuously from 1996 to 2008 before rising in 2009 in response to the global financial and economic crisis. Financial assistance stands at an all-time low, accounting for between 1.8% and 2.1% of federal spending across the reporting period. Tax benefits as a percentage of tax revenue will post a decline across the period covered by this Subsidy Report, falling from 6.3% in 2011 to 5.8% in 2014. This change is attributable both to the decrease in tax benefits mentioned above and to the increase in tax revenue after surmounting the financial and economic crisis (a denominator effect). The ratio of total subsidies (financial assistance plus tax benefits) to GDP, which held steady at 1.0% 1.1% for many years starting in 1997, fell to 0.8% in 2011 and will remain at this historically low level throughout the entire reporting period.

Figure 3: Subsidy ratios



Development of federal subsidies by category

In 2013, approximately 54% of all federal subsidies went to trade and industry. Subsidies in this category have increased from just under €11.2 billion in 2011 to just under €11.8 billion in 2014. The main factor leading this increase is assistance for energy-intensive companies (through electricity price compensation described above).

Federal subsidies in the transport sector will increase slightly during the reporting period, from €2.5 billion in 2011 to €2.6 billion in 2014. The transport sector accounts for roughly 12% of all subsidies and is the third largest subsidy category behind trade and industry and miscellaneous subsidies. The main factors driving this slight increase are an increase in financial contributions for maritime transport and expanded funding for combined transport terminals and rail connections.

Trends in subsidies for housing reflect two contradictory developments: on the one hand, financial assistance is increasing, mainly due to expanded funding for the CO_2 Building Refurbishment Programme; on the other hand, tax benefits are being reduced. The decline in tax benefits is attributable chiefly to the discontinuation of the owner-occupied homes premium (*Eigenheimzulage*). Taken together, subsidies for housing will decline by €600 million over the reporting period to €1.5 billion in 2014.

Federal subsidies in the category of food, agriculture and consumer protection will decrease from €1.4 billion in 2011 to €1.2 billion in 2014. This decline is based mainly on the expiration of the *Grünlandmilchprogramm*, a programme that granted assistance in 2010 and 2011 for the purpose of stabilising incomes and bridging liquidity shortfalls in the dairy industry.

Financial assistance in the category of savings and investment incentives will decline slightly during the reporting period, while tax benefits will rise. The main cause of this increase in tax benefits is a rise in the number of individuals eligible for tax relief in connection with fully funded private pensions (known as “Riester pensions”), while the decline in financial assistance is being led by a decrease in the overall volume of the home ownership savings premium (*Wohnungsbauprämie*). Taken together, subsidies in the category of savings and investment incentives will total €0.9 billion in 2014.

Miscellaneous tax benefits will post a mild increase over the reporting period, rising from just over €3.6 billion to just under €3.9 billion. The largest items in this category are the reduced tax rate for cultural and entertainment services and the tax exemption for statutory or collectively agreed bonuses for working Sundays, holidays or nights.

Development of federal financial assistance and tax benefits

There are a total of 62 federal financial assistance items; of these, the 20 largest individual items account for roughly 93% of total financial assistance in 2013. Sales and decommissioning assistance for coal mining will remain the largest individual item throughout the reporting period.

Table 2: The 20 largest federal financial assistance items

No.	Chapter	Brief description of financial assistance item	No. in Annex 1 of 24th Subsidy Report	2014 Govt. draft € million	2013 Target € million
1	2	3	4	5	6
1	09 03	Subsidies for the sale of German coal for electricity generation and to compensate impacts of capacity adjustment	13	1,172	1,111
2	12 25 60 92	KfW subsidy for energy-efficient building refurbishment measures	58	1,117	759
3	16 02 60 92	Subsidy for individual measures to promote renewable energy use	18	443	387
4	10 03	Joint Task "Improvement of Agrarian Structures and Coastal Protection"[1]	11	401	401
5	09 02	Joint Task "Improvement of Regional Economic Structures"[1]	36	398	408
6	12 09	Utilisation of distance-based commercial vehicle toll	52	392	395
7	09 01	Central Innovation Programme for SMEs (ZIM)[1]	21	385	383
8	60 92	Electricity price compensation	17	350	0
9	12 25	Premiums under the Home Ownership Savings Premium Act (*Wohnungsbauprämiengesetz*)	62	300	354
10	12 25	Urban development subsidy[1]	53	156	181
11	60 92	Energy efficiency fund[1]	16	133	29
12	10 01	Subsidies for agricultural accident insurance funds	1	125	150
13	09 03	Adjustment benefit for coal miners	14	118	118
14	09 02	Support for small and medium-sized enterprises, liberal professions and vocational training[1]	37	118	119
15	12 02	Subsidy for combined transport terminals	51	107	107
16	04 05	Incentives to promote film production in Germany	42	70	70
17	09 02	Interest subsidies under ERP assistance schemes	25	63	64
18	08 20	Subsidies for the Federal Spirits Monopoly Administration (BfB)	8	58	80
19	12 02	Financial contributions for maritime transport	48	58	58
20	09 02	Venture capital investment grants	28	39	30

1 Stated amount only a portion of budget amount

Like financial assistance, tax benefits are concentrated within a small number of categories (see Table 4). In 2013, trade and industry accounts for the largest share of federal tax benefits at roughly 52%, followed by miscellaneous tax benefits (approximately 24%); as such, tax benefits are largely concessions that directly benefit private households and influence economic activity in key sectors. The third largest category of tax benefits targets the transport sector (nearly 13%). Thus the marked shift in the relative importance of various categories of tax benefits – which had already become evident in the 23rd Subsidy Report – is continuing: tax benefits for the transport sector and miscellaneous tax benefits have gained substantially in importance, while the significance of tax benefits targeting the housing sector has waned. Due to the discontinuation of the owner-occupied homes premium, tax benefits for the housing sector now account for less than 2% of total tax benefits.

In 2014, the 20 largest tax benefits will account for just under 86% of the total revenue shortfall at federal level (see Table 3). The largest individual item from the federal perspective is the *Spitzenausgleich*, i.e. a tax benefit for companies bearing significant cost burdens due to electricity duty; this benefit will cause a €2 billion revenue shortfall at federal level in 2014.

Table 3: The 20 largest tax benefits

No.	No. in Annex 2 to 24th Subsidy Report	Brief description of tax benefit		Revenue shortfall (€ million) Revenue year 2014 Total	Federal
1	98	Section 12 subsection 2 nos 1 and 2, annexes 49, 53 and 54 and section 12 no 7 UStG	Reduced rate of VAT for cultural and similar services	3,630	1,937
2	94	Section 3b EStG	shift bonuses	2,625	1,116
3	63	Section 10 StromStG	Tax relief for business enterprises most severely affected by electricity duty	2,000	2,000
4	53	Section 37, 53 EnergieStG,	Energy duty relief for electricity generation	1,800	1,800
5	38	Section 35a subsection 3 EStG	Reduced tax rate on renovation work	1,520	646
6	91	Section 10a EStG/Division XI EStG (Sections 79-99 EStG)	Subsidy of private pensions through premiums (subsidy amount)	1,150	489
7	66	Section 12 subsection 2 no 10 UStG	Reduced tax rate for public transport	1,100	587
8	61	Section 9b StromStG	Tax relief for business enterprises for electricity consumption in excess of 50 MWh for operational purposes	1,000	1,000
9	99	Section 12 subsection 2 no 11 UStG	Reduced tax rate on overnight accommodation from 1 Jan 2010	965	515
10	62	Section 9a StromStG	Reduced rate for specific processes	720	720
11	52	Section 37, 51 EnergieStG	Reduced energy duty rate for specific processes	615	615
12	100	Section 12 subsection 2 no 6 UStG	Dental technicians	525	278
13	78	Section 27 subsection 2 EnergieStG	Aviation fuel	500	500
14	19	Section 57 EnergieStG	Agricultural diesel	400	400
15	50	Section 26, 37, 44, 47 EnergieStG	Tax relief for mineral oil producers	300	300
16	55	Section 53b EnergieStG	Partial energy duty relief for combined heat and power generation	300	300
17	35	Section 8c EStG	Restructuring and corporate group clause	300	85
18	21	Section 2 InvZulG 2010	Investment grants for equipment	281	132
19	26	Section 7g subsection 5 and 6 EStG	Depreciation arrangements for small and medium-sized businesses	281	71
20	44	Section 13a ErbStG	Relief for recipients of businesses and shares of corporations in cases of inheritance/gifts	275	-
1 to 20			**Total**	**20,287**	**13,491**
			% of tax benefits listed in Annex 2 to the 24th Subsidy Report	87.3%	85.8%

Table 4: Development of tax benefits for the years 2011 to 2014, by category

	Category	Tax revenue (€ million)							
		2011		2012		2013		2014	
		Total	Federal	Total	Federal	Total	Federal	Total	Federal
1.	**Consumer protection, food and agriculture**	**604**	**560**	**575**	**530**	**580**	**535**	**585**	**540**
2.	**Trade and industry (excluding transport)**	**9,914**	**7,789**	**10,354**	**8,444**	**10,527**	**8,507**	**10,306**	**8,313**
2.1.	Mining	-	-	-	-	-	-	-	-
2.2.	Energy and raw material supply	-	-	-	-	-	-	-	-
2.3.	Technology and innovation subsidies	-	-	-	-	-	-	-	-
2.4.	Assistance for specific economic sectors	-	-	-	-	-	-	-	-
2.5.	Regional structural measures	942	446	969	453	591	278	331	155
2.6.	Trade and industry in general (excluding 2.1, 2.2, 2.3, 2.4 and 2.5)	8,972	7,343	9,385	7,991	9,936	8,229	9,975	8,158
3.	**Transport**	**2,633**	**2,035**	**2,501**	**2,000**	**2,541**	**2,029**	**2,586**	**2,062**
	Of which: - Aviation fuel	500	500	500	500	500	500	500	500
	- Other transport	2,133	1,535	2,001	1,500	2,041	1,529	2,086	1,562
4.	**Housing and urban development**	**2,483**	**1,055**	**1,466**	**622**	**640**	**272**	**320**	**135**
	Of which - Section 7h, i EStG	90	38	85	36	80	34	80	34
	- Section 10f, g EStG	15	6	15	6	15	6	15	6
	- Owner-occupied homes premium	2,378	1,011	1,366	580	545	232	225	95
5.	**Savings and investment incentives**	**1,273**	**541**	**1,280**	**544**	**1,437**	**611**	**1,467**	**624**
6.	**Miscellaneous tax benefits**[1]	**7,281**	**3,616**	**7,481**	**3,716**	**7,611**	**3,779**	**7,786**	**3,867**
	Total (1) to (6)	**24,188**	**15,596**	**23,657**	**15,856**	**23,336**	**15,733**	**23,050**	**15,541**

1 Primarily tax benefits that directly assist private households but affect important sectors of trade and industry

3.2 Overall development of subsidies by jurisdiction

In accordance with the mandate laid down in the Stability and Growth Act, the Subsidy Report shows federal-level financial assistance and tax benefits for each budget year. Supplementary to this, Table 5 provides an overview of trends in federal, *Länder* and municipal subsidies as well as subsidies from the European Recovery Programme (ERP) and the European Union. As in past reports, data for *Länder* and municipality subsidies, for ERP financial assistance, and for EU market-related expenditure are not available for the full reporting period.

The information on *Länder* financial assistance was provided by ZDL, the central data office of the *Länder* finance ministries. Municipal financial assistance is extrapolated from an RWI report (see 13th Subsidy Report, paragraphs 60 to 62), and estimates are based on the development of *Länder* financial assistance. *Länder* and municipal-level tax revenue shortfalls – like federal-level shortfalls – are estimated by the Federal Ministry of Finance. EU agricultural spending and ERP financial assistance are also included.

To avoid double counting, the financial assistance figures reported by the *Länder* are reduced by the amount of the federal share of *Länder* financial assistance already accounted for under federal financial assistance. The figures reported by the *Länder* are based on a uniform framework tailored to the purposes of federal subsidy reporting. This framework differs from the definitions used by individual *Länder* to compile data on subsidies. It was developed on the basis of the general framework recommended by the Working Committee on Budget Law and the Arrangement of the Budget System. It is a purely technical solution used to capture approximate figures for *Länder* financial assistance that falls under the definitions applied in the federal Subsidy Report. As the budget headings included are not examined more closely regarding the extent to which they constitute financial assistance, these figures are only indicative of the development of *Länder* subsidies.

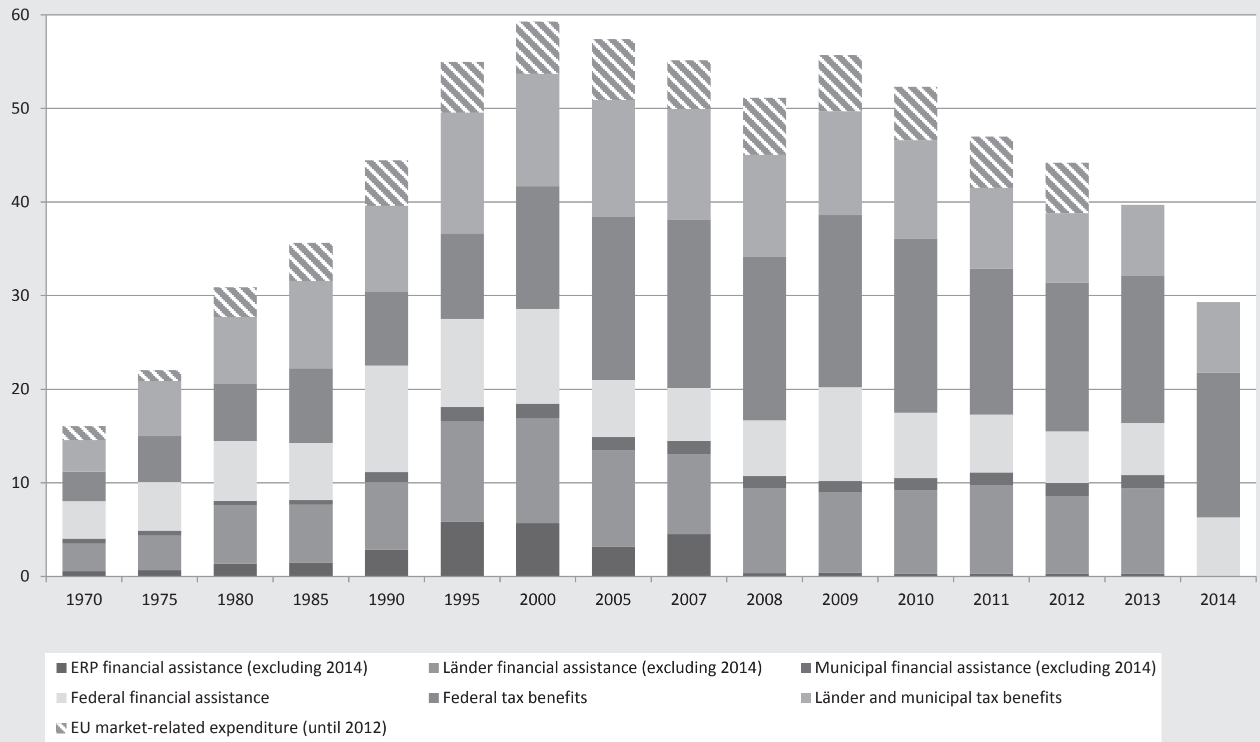
Table 5: Reported total volume of federal, *Länder*, municipal, ERP and EU[1] subsidies (€bn)

	1970	1975	1980	1985	1990 [2]	1995	2000	2005	2008	2009	2010	2011	2012	2013	2014
1. Financial assistance															
Federal	4.0	5.2	6.4	6.1	7.3	9.4	10.1	6.1	5.9	10.0	7.0	6.2	5.5	5.6	6.3
Länder [3]	3.0	3.7	6.2	6.2	7.2	10.7	11.2	10.3	9.1	8.6	8.9	9.5	8.3	9.1	
Municipal[4]	0.5	0.5	0.5	0.5	1.1	1.5	1.6	1.4	1.3	1.3	1.3	1.3	1.4	1.4	
2. Tax benefits															
Federal	3.2	5.0	6.1	8.0	7.9	9.1	13.1	17.4	17.5	18.4	18.6	15.6	15.9	15.7	15.5
Länder and municipal	3.4	5.9	7.2	9.3	9.2	12.9	12.0	12.5	10.7	11.1	10.5	8.6	7.4	7.6	7.5
3. ERP financial assistance[5]	0.6	0.7	1.4	1.5	2.9	5.9	5.7	3.2	0.4	0.4	0.3	0.3	0.3	0.3	
4. EU market-related expenditure	1.5	1.1	3.2	4.1	4.9	5.4	5.6	6.3	6.1	6.0	5.7	5.5	5.4		
Total (1) to (4)	**16.1**	**22.0**	**30.9**	**35.6**	**40.3**	**34.6**	**40.0**	**40.1**	**50.8**	**55.8**	**52.3**	**47.0**	**44.2**	**39.7**	**29.3**

1 Former Federal Republic of Germany 1970-1990; Federal Republic of Germany including former German Democratic Republic from 1991
2 Including financial assistance for former East German *Länder* in supplementary budgets (excluding section B of the third supplement to the 1990 federal budget).
3 Source: Zentrale Datenstelle der Landesfinanzminister (ZDL)
4 Municipal data: Estimated based on development of *Länder* subsidies
5 From 2008: Changeover from total loan amount to interest relief granted in connection with applications approved in current year, over total term of loan or of other funding measures.

Total subsidies measured using this methodology declined slightly between 2011 and 2013, from €47 billion to just under €40 billion (however, the latter figure does not include EU market-related expenditure, for which no data were yet available for 2013 – see Table 5). This mild decline is due mainly to lower federal financial assistance, tax benefits, and EU market-related expenditure. Compared with 2011, EU market-related expenditure in 2012 fell by €100 million to €5.4 billion. As in the previous three years, ERP financial assistance stands at just over €300 million in 2013. From 2008, the figures for ERP funding no longer represent the total loan amount, but rather only the subsidy amount, which is derived mainly from reduced interest rates. This change in methodology changed the overall total by approximately €4 billion in 2008; this must be kept in mind when interpreting long-term trends.

Figure 4: Reported total volume of federal, *Länder*, municipal, ERP and EU subsidies, 1970 to 2014



IV. Fiscal policy measures and their impact on tax benefits

4.1 The Federal Government's tax policy strategy

The Federal Government's tax policy strengthens the drivers of economic growth while securing stable government revenue. Factors that help secure government revenue include the fight against tax fraud and tax dumping as well as the reduction of tax bureaucracy. Taken together, these principles aim to achieve sustainable financing for expenditures that serve the interest of society at large. The Federal Government's pro-growth tax policies ensure employment and fair taxation. This creates a reliable tax environment and enhances people's productivity.

The financial and economic crisis of recent years is still making itself felt in public budgets, mainly due to the significant expansion of government debt during the crisis years. The consolidation of public budgets therefore remains one of the central tasks of fiscal policy. For this reason, Germany is doing its utmost to achieve its objective of a structurally balanced government budget. The positive trend in tax revenues in recent years, for example, has helped reduce net borrowing.

As a matter of principle, subsidies are not meant to be permanent. The Federal Government therefore aims to undertake regular reviews of tax exceptions and to eliminate them whenever possible. Cutting back tax benefits can play a key part in the consolidation of public finances and can help boost the efficiency of the state while safeguarding its fiscal capacity.

One of the Federal Government's tax policy priorities is to make tax law more user-friendly. Additional simplifications of tax law have been implemented since the publication of the 23rd Subsidy Report, including the 2011 Tax Simplification Act as well as legislation amending and simplifying business taxation and travel expenses law. These improvements benefit private citizens, businesses and public administration. In this way, the Federal Government has modernised tax law and reduced unnecessary red tape.

4.2 Improving the structure of public revenues

In Germany, constitutional rules stipulate that, from 2016 onwards, structural new borrowing must not exceed 0.35% of GDP. The Federal Government's budget preparation process came into compliance with this cap already in 2013. Measures taken in recent years to improve the structure of public revenues have contributed to this positive outcome. In order not to jeopardise Germany's post-crisis economic recovery, the Federal Government has not introduced any new taxes or raised any existing taxes during the period covered by the 24th Subsidy Report. Stable economic growth and higher employment levels help ensure a stable tax base and higher tax revenues.

Tax benefits have declined slightly during the period covered by this report. Furthermore, tax revenue shortfalls have been declining since 2006 when the owner-occupied homes premium was eliminated (from -€9.314 billion in 2006, to -€1.366 billion in 2012, to -€225 million in 2014).

4.3 Changes in existing tax benefits

Four tax benefits mentioned in the 23rd Subsidy Report are no longer cited in the current report, because these were of a temporary nature. In addition, the restructuring clause (*Sanierungsklausel*) dealing with the offsetting of losses under section 8c of the Corporation Tax Act was suspended by section 34 subsection (7)c of the Corporation Tax Act. According to the decision taken by the European Commission on 26 January 2011, the restructuring clause constituted unlawful state aid that was incompatible with the internal market.

The tax benefit changes contained in this report mostly involve tax modifications that have a financial impact on tax benefits already cited in previous Subsidy Reports. Some examples include:

- As part of December 2011 legislation implementing the EU Recovery Directive, a new rule was introduced in connection with supplementary pension schemes as governed by section 10a of the Income Tax Act. The new rule requires persons indirectly eligible for government pension savings grants to make a minimum contribution of at least €60 per year to maintain their eligibility for such grants.

- Legislation amending the Energy Tax Act, Electricity Tax Act and Aviation Tax Act was adopted on 5 December 2012 that restructures tax relief for combined heat and power generation. These amendments included an extension of the Spitzenausgleich (a tax benefit for manufacturing companies bearing significant cost burdens due to electricity duty), which was originally set to expire at the end of 2012.

- The Transaction Tax Amendment Act, adopted on 25 October 2012, extended the tax exemption for fully electric passenger vehicles to all other classes of fully electric vehicles (for example, commercial vehicles and light vehicles of the N1 and L categories). The legislation also extended the duration of the tax exemption from five to ten years. This change took effect on 12 December 2012 and applies retroactively to all electric vehicles registered between 18 May 2011 and 31 December 2015.

4.4 New tax benefits

One new tax benefit was adopted during the reporting period covered by the 24th Subsidy Report:

Under the Transaction Tax Amendment Act, a special tax base and a lower rate of insurance tax was adopted from 2013 onwards for multi-risk agricultural insurance, which insures against damage to agricultural products caused by the weather-related natural hazards of hail, storms, heavy frost, heavy rainfall or flooding and/or certain weather-related damage to glass covering mounted over agricultural products in agricultural or horticultural enterprises. This new benefit adds roughly €40 million to total subsidies.

V. Background information on federal subsidy policy

5.1 Legal basis of subsidies

The legal basis for financial assistance consists primarily of rules enacted by the executive branch. This is the case for 43 of the 62 items of financial assistance cited in the current Subsidy Report, although it is also important to take into account contracts that the Federation concludes with the KfW development bank in connection with the implementation of individual programmes. In addition, 15 financial assistance items are based on specific statutory provisions that go above and beyond budget law provisions. Four financial assistance items are provided for in the budget itself. By their very nature, all tax benefits have a statutory basis.

Legal basis		Primary legislation	Secondary legislation, guidelines or treaty	Annual decision (budget)	Total
Financial assistance	Number	15	43	4	62
	%	24.2	69.4	6.4	100
Tax benefits	Number	102	-	-	102
	%	100			100

A statutory basis makes the granting of tax benefits transparent to the public. The criteria for granting funding are openly disclosed to potential applicants. The specific details of the approval process are uniformly regulated and verifiable. This provides legal certainty for both the general public and the public administration.

At the same time, however, providing subsidies with a statutory foundation generally leads to their perpetuation. Because of the large amount of government and parliamentary effort involved, it is relatively rare for subsidies based on primary legislation to be changed or revised. The result is a tendency to protect existing subsidies. Annual budget negotiations frequently provide the impetus to change certain guidelines, for example when a change in resource allocation necessitates certain adjustments in the granting of subsidies.

In all, 27 of the financial assistance items included in this report – which account for 43.5% of the total – also qualify as state aid under EU law. This shows that the definitions of state aid and subsidies are closely related, but also that it is wrong to equate the two. For example, the financial assistance for housing and urban development does not constitute state aid, because it does not affect trade in the internal market.

5.2 Objectives of subsidies

The Federal Government's subsidy policy guidelines underscore the importance of clear objectives. Without clearly defined objectives, it is impossible to assess whether a subsidy is the most efficient means to the desired end.

Pursuant to the Stability and Growth Act, subsidies are classified according to their objective as sectoral support, adjustment assistance and productivity/growth assistance. In addition to these three categories, there are miscellaneous financial assistance and tax benefits that do not fit clearly into a specific category. Classification generally tends to be difficult and is not always clear-cut.

In 2014, sectoral support will make up only a very small share of total financial assistance, at 1% (see Table 6). Adjustment assistance, which will account for nearly half of all financial assistance in 2014, is centred on (i) joint Federation/*Länder* tasks to promote regional industry and agriculture and (ii) assistance to the coal industry. Financial assistance for purposes such as promoting private sector innovation is classified as productivity and growth assistance. This latter category will account for 13.3% of all financial assistance in 2014. Miscellaneous financial assistance covers subsidies that do not fit clearly into a specific category (about 12% of total financial assistance in 2014). This category includes such items as funding for individual measures to promote the use of renewable energy and measures to improve energy efficiency. Assistance for private households that indirectly benefits trade and industry will account for approximately 26.4% of all financial assistance in 2014. In particular, such assistance includes funding for energy-efficiency building retrofits and premiums under the Home Ownership Saving Premium Act.

With regard to tax benefits, Table 6 shows only the federal share. Sectoral support accounts for the largest portion at approximately 49.1% in 2014. This includes, for example, energy and electricity tax benefits for companies in the manufacturing sector that were introduced as part of ecological tax reform legislation in order to maintain the international competitiveness of the manufacturing sector. Adjustment assistance, which at just under 3% makes up only a relatively small share of tax benefits, includes investment allowances for businesses in eastern Germany as an instrument of regional economic policy. Productivity and growth assistance, which includes such items as interest subsidies to enhance the capital base of small and medium-sized businesses, will make up 17.4% of tax benefits in 2014. Miscellaneous tax benefits (21.8%) include, in particular, reduced rates of value-added tax in various sectors. Tax benefits for private households (8.8% of total tax benefits in 2014) that indirectly assist trade and industry are comprised mostly of the owner-occupied homes premium (which is being phased out), deductible renovation costs and savings incentives.

Table 6: Federal financial assistance and tax benefits for business enterprises, economic sectors and private households

Category	2011 Actual[3]		2012 Actual[3]		2013 Budget[3]		2014 Govt. Draft[3]	
	€ million [1)]	%	€ million [1)]	%	€ million [1)]	%	€ million [1)]	%
Financial assistance								
For businesses and economic sectors	4,839	77.9	4,090	74.4	4,208	75.6	4,635.7	73.6
of which:								
Sectoral support	77	1.2	67	1.2	84	1.5	62	1.0
Adjustment assistance	2,806	45.2	2,627	47.8	2,619	47.0	2,984	47.4
Productivity/growth assistance	1,218	19.6	811	14.8	898	16.1	836	13.3
Miscellaneous financial assistance	738	11.9	585	10.6	607	10.9	755	12.0
For private households[2]	1,375	22.1	1,408	25.6	1,360	24.4	1,661	26.4
Total financial assistance	**6,214**	**100**	**5,498**	**100**	**5,568**	**100**	**6,296**	**100**
Tax benefits								
For businesses and economic sectors	13,391	85.9	14,079	88.8	14,237	90.5	14,169	91.2
of which:								
Sectoral support	6,753	43.3	7,621	48.1	7,614	48.4	7,636	49.1
Adjustment assistance	761	4.9	615	3.9	539	3.4	445	2.9
Productivity/growth assistance	2,737	17.5	2,631	16.6	2,781	17.7	2,701	17.4
Miscellaneous tax benefits	3,140	20.1	3,212	20.3	3,303	21.0	3,387	21.8
For private households[2]	2,205	14.1	1,777	11.2	1,496	9.5	1,372	8.8
Total tax benefits	**15,596**	**100**	**15,856**	**100**	**15,733**	**100**	**15,541**	**100**
Federal financial assistance and tax benefits								
For businesses and economic sectors	18,230	83.6	18,169	85.1	18,445	86.6	18,805	86.1
of which:						0.0		
Sectoral support	6,830	31.3	7,688	36.0	7,698	36.1	7,698	35.2
Adjustment assistance	3,567	16.4	3,242	15.2	3,158	14.8	3,429	15.7
Productivity/growth assistance	3,955	18.1	3,442	16.1	3,679	17.3	3,537	16.2
Miscellaneous financial assistance and tax benefits	3,878	17.8	3,797	17.8	3,910	18.4	4,142	19.0
For private households[2]	3,580	16.4	3,185	14.9	2,856	13.4	3,033	13.9
Overall total	**21,810**	**100**	**21,354**	**100**	**21,301**	**100**	**21,837**	**100**

1 Totals may contain differences due to rounding
2 Indirectly assist business enterprises and sectors of the economy
3 Figures for tax benefits are mostly estimated revenue shortfalls. Actual figures are also available in some cases for 2011 and 2012.

5.3 Financial character of assistance

Financial assistance can be provided in the form of grants, loans and debt service assistance, with grants accounting for the predominant share. Loans granted directly from the federal budget have long been of secondary importance. This is partly because in order to provide loans, the Federal Government uses financial institutes that in most cases receive an interest subsidy to implement the programme concerned. The interest subsidy can be paid either on an ongoing basis – for each annual instalment of a loan – or cumulatively for the total amount of assistance approved. The majority of such federal interest subsidies are paid on an ongoing annual basis. The programmes involved – such as KfW loans under the CO_2 Building Refurbishment Programme – therefore constrain fiscal policy for subsequent years. In some cases, the constraining effect extends beyond the medium-term financial planning horizon of Federal Government and can span a time frame of up to 10 years from the year of approval. In the year of approval, the Federal Government enters into a multi-year commitment based on a budgetary authorisation granted for that specific purpose. These commitments do not lead to corresponding expenditures until subsequent years.

A common feature of tax benefits is that they directly reduce tax revenue. The result is that joint taxes provide joint financing for federal, *Länder* and municipal tasks. Tax benefits that are not subject to a proportionate rate of taxation result in a different subsidy amount for the beneficiary depending on the applicable individual tax rate.

Premiums such as the owner-occupied homes premium, the investment allowance and the employee savings premium are paid out in a fixed amount regardless of the applicable tax rate. For the recipient, therefore, a premium has the same effect as financial assistance. The difference with tax benefits, however, is that there is always a statutory entitlement. Unlike financial assistance, the total subsidy amount is not determined and recorded on the basis of specific budgets.

VI. Subsidy policy guidelines and their implementation

6.1 The Federal Government's subsidy policy guidelines

The Federal Government follows subsidy policy guidelines that serve to enhance the subsidy system's transparency, accountability and governance. The guidelines constitute a voluntary commitment by the Federal Government in connection with subsidy measures under its remit. In this way, they make a crucial contribution to improving the performance evaluation of subsidies.

Subsidy policy guidelines
(as agreed in the Federal Cabinet decision of March 2006)

> New subsidies are granted only if they are the best-suited instrument, and are efficient on a cost-benefit basis, compared with other measures.

> New subsidies are granted preferably as financial assistance and are to be financed from savings elsewhere.

> As a rule, new financial assistance is to be both temporary and degressive by design.

> The objectives of financial assistance must be formulated in a way that makes it possible to evaluate the success of such measures.

> Federal subsidy policy takes into account the impact of subsidies on growth, distributive policy, competition and the environment.

> Existing tax benefits are to be reviewed with a view to replacing them with financial assistance or other measures that place a smaller burden on public finances.

> Time limits and, in general, degression rules are to be introduced for existing financial assistance items as well as financial assistance items not yet designed to be temporary and degressive.

New subsidies must undergo especially rigorous scrutiny before they are introduced, because entrenchment hinders later change. Recipients often claim that subsidies are the only feasible option, although in some cases the same outcome can be achieved at far lower cost by other means, such as regulatory measures. Against this background, and given the ongoing need to consolidate public finances, all new subsidies – including tax benefits – must be immediately, permanently and fully offset by savings elsewhere.

Tax benefits often have the same effect as a spending programme and indeed are sometimes referred to as "tax expenditures". However, tax benefits have a number of disadvantages compared with financial assistance. They are not capped (by budget appropriations) and are not part of annual budget negotiations. In most cases the size of the revenue shortfall can only be estimated. Tax benefits can generate deadweight losses, tend to become entrenched, and run the risk of quickly ceasing to be regarded as subsidies. Tax expenditures financed from joint tax revenues have the same effect as joint tasks carried out with federal, *Länder* and municipal funding in accordance with the respective formula for allocating tax revenue. Changes in the law in such cases require the consent of the Bundesrat.

For all of these reasons, tax benefits prove difficult to reform and control. That is why new subsidies – to the extent that they are necessary – should preferably be granted as financial assistance.

In contrast to tax benefits, the Federal Government generally possesses greater authority when it comes to modifying existing financial assistance. Financial assistance can be modified in many cases on the basis of Federal Government guidelines or administrative agreements. Objectives must be precisely specified and continuously monitored. If the targeted objective has been attained or is no longer justified, if it cannot be attained with the type of measure in question, or if there is another, better means of attaining the objective, then a subsidy must be discontinued without delay. It is also essential to prevent separate measures from having contradictory effects or cancelling each other out.

Long-term subsidies for specific economic sectors can lead to subsidy dependence, and this risk is enough in itself to make ongoing review of subsidies imperative. Long-term subsidies also carry a greater risk that they will be perpetuated even after they have outlived their justification. In addition to potential adverse external effects, the resulting deadweight losses ultimately lead to a net welfare loss for the economy as a whole and to unnecessary burdens on taxpayers. These adverse outcomes can be mitigated or prevented by designing subsidies to be temporary and degressive.

The basic principle that financial assistance must be time-limited by design enables the Federal Government to review the effectiveness of assistance measures and, where appropriate, to discontinue or re-design them. While certain government functions are based on statutory or even constitutional provisions that cannot and should not be rendered time-limited by government decision, the Federal Government can nevertheless establish framework plans or administrative agreements, particularly for functions like these. This provides the occasion and opportunity to regularly review how these functions are carried out.

The rule that all financial assistance items must be temporary by design allows these same opportunities to be put into place for measures which have hitherto not been subject to time limits.

6.2 Implementation of the subsidy policy guidelines

As a rule, the subsidy policy guidelines must be taken into account every time a financial assistance item or tax benefit is created or modified. For example, in 2008 and 2009, when the Federal Government was assembling the stimulus packages to respond to the global financial and economic crisis, it ensured from the outset – and in compliance with European rules – that targeted, fast-acting support measures for specific economic sectors were limited to the crisis years wherever possible. This was especially the case for measures that involved federal spending. Almost all financial assistance to combat the crisis was therefore time-limited by design. Following the guidelines remains an ongoing task, particularly in order to ensure that total subsidies are scaled back to pre-crisis levels on a sustained basis.

Furthermore, carrying out regular cost-benefit analyses that take external effects into account and designing subsidies to be temporary and degressive also makes a key contribution to fiscal consolidation efforts, which remain necessary to ensure sustained compliance with Germany's constitutional debt rules and the EU Stability and Growth Pact. This is a further reason why the Federal Government continues to attach great importance to performance evaluations for subsidies.

In line with the subsidy policy guidelines, the "golden rules" laid down in the current government's 2009 Coalition Agreement establish key benchmarks for the Federal Government's fiscal policy strategy. Budgetary principles with immediate effect on subsidy policy include the following:

> All functions performed by the state must be reviewed in terms of their necessity, and no expenditure categories may be exempted from cost-benefit analysis or consolidation efforts.

> The impact of all new items affecting public finances must be disclosed in full. As a rule, the costs for new items must be offset within the same departmental budget.

> Policy objectives must be based on qualitative criteria to a greater extent than before.

> In future, the Federal Cabinet will lay down binding budgetary parameters in advance that will provide the basis for the Federal Government's internal preparation of departmental budgets.

In the current year, for the second time since the new top-down approach to budget preparation was introduced in 2012, the Federal Cabinet laid down binding revenue and expenditure ceilings for the ministries as parameters for the government's draft federal budget for 2014 and financial plan to 2017. This approach ensures that the Federal Government establishes overarching policy objectives at an early stage and defines clear priorities. Setting ceilings for individual policy areas facilitates the regular critical review of each departmental budget's expenditure structure and fosters a clearer differentiation between primary and secondary priorities. This improves accountability, particularly with regard to selectively granted government assistance.

Furthermore, subsidy policies that are carried out in line with budget principles and subsidy policy guidelines serve to enhance the efficiency and effectiveness of subsidies and thereby help to improve the quality of public spending. Improving the efficiency and effectiveness of public spending and revenue is particularly crucial given the need to cope with the effects of demographic change and to maintain a structurally balanced budget. For this reason, many OECD countries are currently taking action to further improve the transparency and effectiveness of their expenditure and revenue systems. Efforts are also being undertaken at European level to improve the quality of public finances and to place a stronger focus on fostering institutional structures in Member States that serve to boost efficiency and effectiveness. As in other European countries, Germany's commitment to complying with its constitutional debt rules is another factor that heightens the necessity of improving the transparency and effectiveness of public finances.

Time limitation

A total of 39 financial assistance items (62.9%) are time-limited, of which 16 (25.8%) are in the final funding phase. The latter are measures for which time limits have already taken effect but funding obligations remain to be fulfilled.

		Total items subject to time limits	Of which: in final funding phase	Annual decision/ no time limit	Total
Financial assistance	Number	39	16	23	62
	%	62.9	(25.8)	37.1	100
Tax benefits	Number	13	3	89	102
	%	12.7	(2.9)	87.3	100

Overall, one third of financial assistance items are not time-limited. There are various reasons for this. In some cases, the measures concerned pre-date the adoption of the subsidy guidelines and remain in force unaltered. Other measures are implemented on the basis of annual budget resolutions, without specific guidelines. In addition, a small number of measures are based on direct parliamentary stipulations.

In the case of tax benefits, which always have a statutory basis, only a small number – 13 out of 102 tax benefits – are time-limited. The time-limited tax benefits comprise (i) measures for which time limits were stipulated upon adoption and (ii) tax benefits for which a subsequent decision was made to discontinue them because they had outlived their purpose or had been superseded by a follow-up arrangement.

Degression

Financial assistance is subject to degression in various forms. First, degression can apply for the recipient. Degression in such instances means that the assistance, which is granted for multiple years, decreases in absolute terms over time. This form of degression aims mainly to prevent recipients from becoming habituated to and dependent upon the subsidy. Second, degression can apply for the subsidising authority, which means that the total outlay for the assistance decreases over time. This objective can also be attained – even if the size of individual grants is held constant or even increased – by restricting the number of grants.

Compared with financial assistance, the scope for applying degression to tax benefits is very limited. Because the criteria for receiving tax benefits are fixed by law, degression can be applied only through statutory limitations of individual amounts on a case-by-case basis.

In the period covered by this Subsidy Report, 12 of the financial assistance items not in the final funding phase feature a degressive structure. These consist mostly of financial assistance items that are reduced in size by cutting the amount allocated in the budget. Where degression is applied in this way via budget allocation, it is up to the government departments concerned to decide whether the reduction will be implemented by decreasing the number of grants and/or by decreasing the amount of assistance granted in each case.

		Items with a degressive structure	Items with no degression	Total	Expired (for information)
Financial assistance	Number	19	43	62	16
	%	30.6	69.4	100	25.8
Tax benefits	Number	2	100	102	2
	%	2	98.0	100	2

Evaluation

All subsidies must be reviewed repeatedly in terms of their necessity, their expediency (taking external effects into account), and their coherence with the Federal Government's fiscal, economic, social and environmental policy objectives. Regular, effective, internal and/or external performance evaluations play a decisive role in subsidy policy, not least because they strengthen the government's ability to reduce subsidies in a way that is both targeted and economically sound. These performance evaluations review whether a certain assistance item continues to be necessary and the extent to which it actually fulfils the desired objectives. This requires the clear definition of objectives.

Reliable analysis of outcomes is very difficult, however, as it is based on assessments of how markets would have performed without state intervention. To this end, improved data can significantly improve the quality of evaluations.

Effective performance evaluation requires measurable target criteria. In addition, the evaluations themselves must be subject to cost-benefit considerations. In particular, for measures lacking a significant fiscal impact, it is often feasible only to conduct internal evaluations, because the cost of preparing and delivering data for external evaluations can be very high. Similarly, for temporary measures in their final funding phase, it is doubtful whether any potential findings from a performance evaluation will be worth the associated costs.

Evaluations are conducted both internally – by public administration authorities, the responsible federal ministries, and/or the Federal Court of Auditors – as well as externally, by independent appraisers. They can result in the production of internal reports as well as public reports that sometimes provide overviews of entire policy areas.

Evaluations of federal financial assistance and tax benefits		External	Internal	Not evaluated
Financial assistance	Number	29	15	18
	%	46.8	24.2	29.0
	Volume (€ millions, 2013)	3,461	1,170	937
	%	62.2	21.0	16.8
Tax benefits	Number	22	5	75
	%	21.6	4.9	73.5
	Volume (€ millions, 2013)	11,646	133	3,954
	%	74.0	0.9	25.1

A total of 44 of the 62 financial assistance items – or 71% – were evaluated internally or externally during the reporting period. Overall, 83.2% of total financial assistance was subject to evaluation. This represents a significant improvement of over 30 percentage points compared with the 23rd Subsidy Report. 29% of financial assistance items – all smaller programmes – were not subject to evaluation, for various reasons: Some are new measures that need to be operating for a certain amount of time before it make sense to evaluate them. Others are so short-term in nature that evaluations can be conducted – if at all – only after the programme runs out. Still others involve measures which have already expired but still hold residual funding and for which no further evaluations are planned. Non-evaluated financial assistance items account for only 16.8% of total financial assistance in 2013.

The marked shift in favour of external evaluations, which was already evident in the previous Subsidy Report, is remaining steady during the current reporting period. The share of financial assistance items evaluated externally – at 46.8% – has remained basically constant compared with the share of 47.3% recorded in the 23rd Subsidy Report. The proportion of financial assistance items evaluated internally increased just slightly from 19% to 24.2%.

The shift towards external evaluations is continuing for tax benefit measures as well. The share of tax benefit items evaluated externally – at 21.6% – has increased slightly compared with the 19.4% share posted in the 23rd Subsidy Report. The proportion of internally evaluated tax benefit items remained constant at 4.9%. As a result, the share of tax benefit items that were not subject to evaluation declined slightly from 75.7% to 73.5%.

In terms of volume, federal tax benefits subject to evaluation made up just under 75% of total federal tax subsidies.

VII. Concluding remarks

In the reporting period covered by the 24th Subsidy Report, trends in subsidies have made a positive contribution to fiscal consolidation while simultaneously enhancing the competitiveness of the German economy. These policies thus contribute to the Federal Government's pursuit of growth-friendly consolidation.

Federal subsidies have been kept at a moderate level, hitting an annual maximum of €21.8 billion during the 2011 2014 period. In this way, subsidy policy has helped the Federal Government achieve sustainable consolidation of the federal budget in just one legislative term. Over the entire reporting period, subsidies account for just 0.8% of GDP, the lowest level in almost two decades.

Temporary and degressive subsidies are a legitimate instrument of fiscal policy. In a social market economy, they can have a key impact wherever market-based approaches provide no satisfactory solutions.

However, in order to prevent unwanted effects, it is essential to regularly review all subsidies in terms of their necessity and justification and to identify possibilities for reducing them. This is particularly true given the ongoing need to achieve structural consolidation of the federal budget in light of the challenges posed by demographic change, among other things.

The decisive factors to be taken into account in evaluating subsidies are their impacts on growth, distributive policy, competition and the environment. Subsidy policy implemented along these lines not only facilitates compliance with quantitative consolidation targets but also helps to boost the effectiveness and efficiency of public spending.

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