Tax Expenditures in the Nordic Countries

A report from a Nordic working group, presented at the Nordic Tax Economist meeting in Oslo, June 2009

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Disclaimer:

At the Nordic Tax Economist meeting, held annually, civil servants from the Ministries of Finance and Taxation of the Nordic countries meet to exchange experiences, discuss taxation trends and issues, and to build and maintain networks. To each meeting a report is prepared on a topic decided upon at the previous meeting. The report is written by a group of civil servants from all the countries and does not necessarily reflect the views of the Governments or the Ministries of Finance and Taxation.

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1 Introduction

The background for this work is partly the increased interest in tax expenditures from parties outside the ministries, for instance the National Audit Offices, but also a realisation that there is a need to produce more reliable, transparent and maybe also comparable tax expenditure analyses in the Nordic Countries. It is our ambition that this report can shed some light on some issues related to tax expenditures and maybe also serve as an "easy entry" to the tax expenditure concept. We also present a comprehensive overview of how tax expenditures are treated in the Nordic countries.

The main objective of tax expenditure analysis is increased expenditure control by identifying tax provisions that escape the scrutiny applied to regular subsidies and transfers on the expenditure side of the budget. Originally tax expenditure analyses ambitiously were regarded as tools for revealing the inferior nature of tax expenditures as a way to appropriate public resources. It was believed that a thorough tax expenditure analysis would unveil that a lot of tax expenditures violated the objectives of efficiency, fairness and simplicity in the tax system. Since the first tax expenditure analysis was presented in the US more than forty years ago, the concept of tax expenditures has spread worldwide and today virtually all OECD-countries make tax expenditure analysis in one form or another.

Using tax expenditure analysis in the tax policy work to pursue such idealistic principles of the tax system as mentioned above is highly ambitious and demands a definition of a normative tax system which reflects the principles of efficiency, fairness and simplicity. This has proven to be a difficult task, and have brought about extensive discussions and also substantial criticism of the definitions and methodologies used in tax expenditure analyses, not the least in the US.

The examination of tax expenditure analyses of the Nordic countries in this report shows that the levels of ambitions are fairly moderate compared to those mentioned above, and the methodologies are to a larger extent based on pragmatic choices and prevailing tax rules. These analyses are therefore less vulnerable to the general criticism regarding the normative assessments of the benchmark, but have on the other hand to some extent been criticised for the lack of transparency.

The working group does not work out detailed recommendations for a reform of tax expenditure analyses in the Nordic countries. However, we make some suggestions for possible future improvements. One suggestion is that the Nordic countries endeavour to clarify the tax expenditure analysis. Another is that more emphasis could be placed on *evaluating* tax expenditures. We believe that this could help to increase both transparency and the accuracy of tax expenditure analysis.

The report is structured in a theory part (chapter 2 and 3) and a practical part (chapter 4). Chapter 2 presents the theoretical background of defining a benchmark. In chapter 3 we discuss some important elements of tax expenditure analyses, with a specific emphasis on reporting and evaluation. In chapter 4 the treatment of tax expenditures in Denmark, Finland, Norway and Sweden is described and discussed. Each country has been responsible for its own description. The chapter starts with a summary of common features and points towards some differences. The challenges concerning the treatment of tax expenditures, which are

common in these countries, are also discussed. In chapter 5 the group concludes and points at some possible areas for future work and improvements.

2 Benchmark

2.1 Theory

2.1.1 The concept

The term *tax expenditure* refers to provisions in the tax code that give favourable tax treatment for an activity or a group of taxpayers. Tax expenditures may take a number of forms like exemptions, allowances, credits, preferential rates, deferral rules etc. They are, in effect, policy instruments of government to promote specific social or economic policies and thus are closely related to direct spending programs. Negative tax expenditures are tax sanctions. A tax sanction is the result of levying tax at a higher rate than the norm.

The identification of tax expenditures is a difficult task for many reasons. The tax code may include a number of provisions that lead to revenue losses but nonetheless promote the standard goals of a good tax system. They are integral parts of the tax system and are not judged as tax expenditures. Neither can the tax expenditure analysis rely entirely on legislative documents, since the objectives of tax provisions are not always expressed clearly and openly there. So, there is a need for a systematic method for identifying tax expenditures.

Such an approach was developed in the US in the late 1960s, well captured in the following (Surrey & McDaniel (1985)):

> "The tax expenditure concept posits that an income tax is composed of two distinct elements. The first element consists of structural provisions necessary to implement a normal income tax, such as the definition of net income, the specification of accounting rules, the determination of the entities subject to tax, the determination of the rate schedule and exemption levels, and the application of the tax to international transactions. The second element consists of the special preferences found in every income tax. These provisions, often called tax incentives or tax subsidies, are departures from the normal tax structure and are designed to favour a particular industry, activity, or class or persons. … Whatever their form, these departures from the normative tax structure represent government spending for favoured activities or groups, effected through the tax system rather than through direct grants, loans, or other forms of government assistance."

Under this approach tax expenditures are defined as deviations from a normal tax structure, also called a benchmark or a reference tax system. With this concept we may understand a 'pure' tax system as a system that focuses on raising revenue, while also fulfilling the principles of a good tax system, neutrality, equality and the requirement to be implementable.

According to the quotation, other criteria for tax rules to be judged as tax expenditure are that they favour some narrow activities or tax payer groups and that they serve some specific

policy goals.[1] The overall idea that tax expenditures can be identified by comparing the actual tax system against a normative one has been very influential in practice. Most developed countries have adopted it as the basis of their tax expenditure analysis.

2.1.2 Normative tax system

Tax expenditure analysis is based on the concept of a normative tax system. This concept is the measuring rod to identify and to measure the amount of tax expenditures. The normative tax system captures the generally accepted elements of the tax system that are necessary to achieve the fiscal goals and to fulfil the objectives of equity, efficiency and simplicity.

Tax expenditure analysis requires good understanding of the objectives and functions of the elements of a particular tax. Based on such understanding the normative structure can be defined and the tax expenditures identified as deviations from the norm. This understanding can be drawn from some idealized tax structures developed in tax research. Income tax and VAT are good cases in point. The so called Schanz-Haig-Simons economic income concept (SHS income) has been an influential tool when specifying the norm for the income tax base in the US and elsewhere. It defines one period's income as consumption plus the change in net wealth during the period. The concept is of course abstract and leaves several important aspects of a normative tax system open. Therefore the benchmark tax system usually is a combination of elements from the theoretical abstract and the actual tax system. Similarly, a general non-cascading sales tax could be a useful abstract concept behind the benchmark tax system of VAT or, even more broadly, behind all taxes on private consumption.

Examples of elements of the actual tax system usually accepted in the benchmark are the tax rate schedule, the unit of taxation, the time frame of taxation, accounting principles, realization principle[2] as the basis of taxation and the potential non-elimination of inflation gains. Some allowances motivated by redistribution of income may be part of the benchmark. Similarly deductions or relieves that are grounded on simplification of tax administration or the tax code may be defined as parts of the benchmark.

That the benchmark tax is a compromise between the theoretical ideal and the actual tax system has rendered tax expenditure analysis subject to much criticism in recent years, especially in the US. The concern is that under this approach the norm cannot be defined rigorously enough to ensure that the identification of tax expenditures leads to an objective and reliable outcome. This criticism has led to at least two new ideas in tax expenditure analysis. One is that the connections to the theoretical ideals (SHS income) are not useful since the choice of the norm is mainly a pragmatic exercise. The other is that classifying relevant provisions into subgroups could relieve the problems from branding all items as provisions.

2.1.3 Measurement

Tax expenditure literature usually list three different approaches to estimate the cost of tax expenditures: revenue forgone, revenue gain and outlay equivalence method. There are two

1 OECD (1996) gives also other supplementing criteria for a provision to be considered as a tax expenditure. They include that the objective of the tax expenditure could be achieved by a direct subsidy, that the tax in question is sufficiently broad in range such that a norm can be established and also that there is no offsetting provision elsewhere in the tax system. However it is not clear whether those requirements have been applied systematically.

2 Usually only realized income is subject to individual income tax.

distinguishing features in this classification: whether the method takes behavioural responses into account or not and whether the measure describes the size of the subsidy net or gross of taxes.

- Revenue foregone: a static estimate of the loss of tax revenue. Hence the method does not take account of behavioural responses. The cost of a tax allowance is then the product of tax rate and the observed amount of the allowance.

- Revenue gain: the amount by which tax revenue is reduced as a consequence of the introduction of a tax expenditure, taking into account behavioural changes and the effects on revenues from other taxes as a consequence of the introduction.

- Outlay equivalence: the direct expenditure that would be required in pre-tax terms, to grant the same after-tax gain for the taxpayers as the tax expenditure.

The revenue foregone method is based on the assumption that the introduction of tax expenditures does not affect the behaviour of taxpayers or the revenues from other taxes. It is therefore the easiest estimation method. In general, there are good reasons to believe that taxpayers change their behaviour in response to the tax expenditure (increase their demand for the tax-subsidised good or increase/decrease their demand for income). Therefore the revenue forgone method gives a narrow picture of the revenue effects of a tax provision. However, if the tax expenditure is re-estimated the behavioural effects will indirectly be accounted for if the tax base changes due to the tax expenditure.

The method of revenue gain takes the behavioural change and the change in tax interaction into account. Of course this makes the method much more complicated to apply in practice. Although the method is superior in principle, many governments seem to assume that the accuracy that may be gained is not worth the efforts required to apply the method.

Outlay equivalence is a measure that leaves the net budget impact (on the surplus or deficit) and the after-tax incomes of taxpayers the same in the situation with tax expenditure and in the situation with equivalent outlay but without tax expenditure. Outlay equivalence takes into account the fact that regular transfers are sometimes estimated gross of the tax paid by the recipient, whereas tax transfers are by definition net of tax. In order to estimate these tax expenditures on the same basis as regular expenditures, it is necessary to add the tax that is typically levied upon the regular transfer. Otherwise, it appears as if the tax expenditure is a cheaper way to get the same amount of cash into the hands of the recipient than the regular expenditure.

Methods of measurements are a much broader matter, however.. There are at least the following additional aspects:

- Which methods are used? E.g. present value calculations or implementation of micro simulation models.
- Is the calculation one periodic or does it take into account counterbalancing effects in later years. One example here is the so called EET model of voluntary pension savings which deviates from a SHS income based norm in several respects. The essential feature is that those deviations spread over years. Another example but with some different features are the depreciation rules. Even if the main approach would be

one periodic, the tax expenditure reporting could also give multi-periodic present value estimates.

- Usually tax expenditures are estimated provision by provision, one at a time. Since the tax provisions may interact, for example through the progressive tax schedule, the total amount of tax expenditure cannot simply be calculated by summing up all the parts.

2.2 Criticism of tax expenditure analysis

The aim of tax expenditure analysis is widely shared, i.e. to improve the control of the use of government resources on the revenue side of the budget. The usefulness of the concept of tax expenditure has, however, been questioned for years, almost since its introduction in the late 1960s (JCT 2008).

The most important part of the criticism is focused on the concept of a benchmark tax system. The main objection is that the concept does not have a sufficiently rigorous formal basis and is more or less a result of a series of subjective, pragmatic choices. As an example, it is common that the tax expenditure analysis officially refers to SHS income as a starting point when the normal structure for income tax is defined. Here it follows the approach introduced by Surrey. In principle comprehensive income can be defined quite precisely. However, SHS income is not an operational concept that could be measured exactly and easily enough to be used either as a basis for taxation or as a tool in tax expenditure analysis. Therefore the benchmark applied is usually a compromise between SHS income and the actual tax system or, put differently, an extension of the actual tax system towards the theoretical concept.

Due to the vagueness of the benchmark, the classification of at least some tax expenditures has weak grounds and their status will easily become subject to discussions. If there is no hard theory behind the benchmark it is very hard to defend the identification decisions. There is much experience from such a debate from the US.

One line of criticism targets the transparency of the benchmark. It can be traced back to Bittker (1969) who questioned Surrey's way of officially connecting the normal tax system to the SHS-concept but at the same time include several other elements into it without implicating the theoretical grounds. Bittker considered these additions as subjective choices.

According to Burman (2003) the US tax expenditure debate has had an ideological stance. Those who have favoured an income tax have supported the current way to identify and measure tax expenditures. On the other hand, those who have preferred consumption tax features in the tax system have proposed changes towards savings relieves in the benchmark system.

The criticism also includes the hidden reform agenda on the background of tax expenditure reporting and also that tax expenditure analysis implies an idea of a clean and apolitical tax policy that does not fit well with social decision making. It seems that this kind of debate and the resulting credibility problem are, to some extent, a result of unclear theoretical grounds of the identification process.

Another main subject of criticism has been the measurement methods (Burman 2003). The tax expenditure estimates usually give a static first year revenue loss due to a particular tax provision. They do not include any behavioural responses which may be incorporated in

more serious revenue estimates. Neither do they reveal the long term costs of tax expenditures. Here tax expenditure estimates may deviate a great deal from estimates made in other instances in tax policy analysis.

The tax expenditure analysis is currently facing a challenge to improve its theoretical grounds and measurement processes. One obvious response to the criticism is to improve transparency of the reporting by communicating the definitions and foundation of the analysis more openly and clearly. The US Joint Committee on Taxation aims to solve the credibility problem by introducing a new pragmatic framework to identify and report tax expenditures.[3] The core idea of the approach is to refuse theoretical ideals in the light of the benchmark tax and instead to build the reference base on the general principles of the current system. Parallel discussions on alternative ways to improve the methods are going on in several countries and in the OECD.[4]

3 Analysing tax expenditures

Beyond the broad conceptual description of tax expenditures in section 2, there are numerous specific issues that analysts have to deal with when making tax expenditure analyses. Due to practical reasons most tax expenditure analyses necessarily have to be based on a compromise between the theoretical concepts described above and pragmatic and feasible solutions. Finding a reasonable balance between theoretical orthodoxy and pragmatic adjustments seems to be the key to make an appropriate and useful tax expenditure analysis. Below we describe some practical matters related to tax expenditure analysis, and we try to shed some light on how tax expenditures are reported (including different ways of classifying tax expenditures) and the need for evaluating the effectiveness and efficiency of tax expenditures.

3.1 Practical issues of tax expenditure analyses

Making tax expenditure analyses raises a lot of practical issues on how to define and operationalise the appropriate benchmark, and there is no universal recipe on how to solve them. The crucial task is to define a suitable tax code and a feasible and adequate tax base that serves as a reference. Calculating tax expenditures requires a distinction of the normative components of a particular tax from its tax expenditure component, and deciding what should be part of the benchmark structure and income and what should constitute a tax expenditure. Such considerations have to be made for each individual tax, which hampers the direct application of a general theory or methodology.

Tax expenditure analyses around the world differ widely both when it comes to definitions and applied methodology. This can make tax expenditure analyses from different countries virtually incomparable, and a comparison of the number and amount of tax expenditures can be rather misleading. A general definition tends to generate a lot of tax expenditures, while a more narrow definition can lead to less or almost no tax expenditures at all. In between there are systems based on various concepts that differ along several dimensions. Some are loosely based on a "norm" where the norm can change over time (as in France) and others are very restrictive and detailed but not necessarily strictly based on principles (as in Canada and to

3 See Joint Committee on Taxation (2008).

4 See e.g. OECD (2008/1) and OECD (2008/2).

some extent the US and UK). However, since most countries are claiming more or less the same methodology and definitions at the overall level (e.g. revenue foregone method, income tax benchmark etc.), these variations are probably more due to how the methodology and the definitions are applied in practice, and maybe due to the lack of practical guidelines founded on undisputed theory.

The most difficult task seems to be related to choosing the right tax base. Many countries use the Schanz-Haig-Simmons (SHS) income definition for tax expenditure purposes. The main reason for this is probably that the SHS definition constitutes a tax base that neutralise the tax treatment of consumptions and savings (while a conventional comprehensive income definition gives a preferential treatment of consumption). However, it is by no means straightforward to apply this income definition in practice. A lot of income and expenditure components have to be treated separately. How do you treat governmental transfers and grants, consumption of public goods or what kind of expenses constitutes a cost of earned income and so forth? There are also difficult issues related to the appropriate taxable period to be used. How do you treat unrealised gains or other tax credits or the missing opportunity to get negative deferred taxes? Which unit of taxation do you choose, families, couples or individual taxpayers, and should you use equivalent scales to adjust for family size? How do you measure imputed income when there is no "physical" profit or payout? The SHS definition of income is too rigid and demanding to be applied comprehensively in a national income tax and a range of pragmatic choices has to be made.

Choosing the right rate structure can also lead to practical challenges. The lack of a clearly defined set of tax laws implies a vast amount of subjective judgement in the analyses, which increase the level of arbitrariness. This is especially true when it comes to choosing the tax rates that applies to deductible expenses and losses.

3.2 Reporting and evaluation of tax expenditures

Although tax expenditures, like direct expenditures, affect the government's budget by reducing the resources available, tax expenditures typically are not included in the budget (especially after the year of enactment), are normally not limited to a maximum cost set, and often continue permanently without regular evaluation or reauthorization. Furthermore, the level of tax expenditures can increase when new taxes are introduced or existing taxes are altered. Direct expenditures do not necessarily have maximum cost set, but the level of expenditures appear more transparent in the budget. While direct expenditure programs are more or less routinely reviewed and funded through the normal course of the annual state budget process, such a process is often lacking for tax expenditures. As a result, tax expenditures can become expensive subsidies that lead to considerable amounts of forgone revenues without legislative action or even awareness.

Apart from the fiscal deficit dimension, tax expenditures can also increase tax systems complexity and distort both its neutrality and the allocation of resources. Furthermore, tax expenditures themselves are often non-transparent (e.g. concerning financial volume, target attainment, and beneficiaries). For all these reasons, it is important that tax expenditures – as well as the tax system itself and spending programs – receive (periodic) review to ensure that they are effective and are justified continued support from the public.

In addition, a more comprehensive assessment of government activity leads to a better understanding of the effects of providing tax expenditures, and helps to make tax policy more transparent. Tax expenditure reporting is thus a contribution to the design of the whole tax

system because it improves transparency by promoting and informing public debate on all elements of the tax system.

All in all, the key functions of reporting and evaluating tax expenditures can be summarised as follows:

- Increasing cost control and transparency,
- Aid for efficiency, effectiveness, and accountability,
- A more comprehensive assessment of government activity, and
- Contribution to the design of the tax system.[5]

When reporting tax expenditures it might be helpful to distinguish between existing and new tax expenditures. In general, when new tax expenditures are introduced, or existing ones expanded, it receives special attention. The legislative process will often be the natural starting place to determine whether the initiative can be defined as a tax expenditure or not. Depending on the institutional framework it might be difficult to classify changes as tax expenditures later on. This focus on tax expenditures in the legislation process will make the revenue effects, distribution etc. more transparent as is the case with other changes in the tax system.

In general, there is little discussion about the need of tax expenditure reporting and evaluation, but in reality this is often lacking.

3.2.1 Classification

Tax expenditures differ in many ways (e.g. target, tax base, volume, recipients and type of tax measure). For the purpose of analysing and reporting, tax expenditures can be structured in an appropriate manner. Tax expenditures can be classified and structured according to different methods and purposes. Theoretically, there is not one correct way to classify tax expenditures, and the choice of classification method is subjective. The most common methods are to classify them according to their taxable base, their purpose and/or objective or the type of measure (see table 3.1).

It should be noticed that tax expenditures can be classified on the basis of more than one method. When reported, however, tax expenditures ought to be structured according to one main classification method, as the reporting would otherwise be difficult to follow. Sticking to the same classification will also make it possible to follow any trends in the tax expenditures.

5 See Australian Treasury (2009), p. 2.

Table 3.1: Types of classification

Classification according to	**Example**	**Pros and cons**
Taxable base	Deviations from the benchmark tax on labour is divided into one category, deviations from the benchmark tax on capital into another category etc.	Simple, but does not give any extra information. Important for tax revenue forecasts.
	Used in: Norway and Sweden.	
Purpose and/or objective	- Budget function - Recipients - Related type of direct spending	Additional information, but approach does not always allow objective (comparable) judgments.
	Used in: Denmark, Finland, Norway, and Sweden.	
Type of tax measure	Allowances, exemptions, deductions, rate relieves, and tax deferrals	A direct and simple approach with few categories which is widely used for research purposes.
	Used in: Finland.	

As table 3.1 shows, one method of classifying tax expenditures is to categorise them according to their taxable base. For example, deviations from the benchmark tax on labour are defined as one category, deviations from the benchmark tax on capital as another category, and so on. This simple classification system gives an overview of the tax expenditures within each tax category and to some extent it gives an idea of who the direct recipients of the tax expenditures are, but gives limited additional information. In general, this method is used to demonstrate how different kinds of tax revenues are affected by tax expenditures. It is particularly important in the context of tax revenue forecasts.

Classifying tax expenditures according to their purpose and/or objective (that is budget function, recipients, and related type of direct spending) is another widely used method. The German Government, for instance, differentiates between tax expenditures which are directly aimed at companies (business sector level) and others which are aimed at private households (but nevertheless indirectly to companies). Besides, for further categorisation the objective targets preservation, economic adjustment, and productivity are used.[6]

However, the Joint Committee on Taxation in USA classifies according to tax transfers (e.g. refundable portion of the earned income credit and child tax credit), social spending (e.g. IRAs, fringe benefits, mortgage interest deduction) and business synthetic spending (e.g. energy subsidies and R&E credit).[7] Another approach to classify according to technical reasons can be found by the OECD's classification: "technical" tax expenditures, other income exemptions, tax expenditures which could not be repealed without being replaced by a spending program, and other tax expenditures.[8]

Classifying tax expenditures in this manner gives additional information. For example, it can be shown, which tax expenditures belong in a special context (e.g. make work pay,

6 See German Government (2007), p. 8 f. and 112.

7 See Joint Committee (2008), p. 17.

8 See OECD (2008/2), p. 6.

retirement, employees benefits or education[9]) or who are the recipients of tax expenditures. However, one should bear in mind that the different kinds of classification not necessarily give the full picture of incidence, i.e. the persons who benefit from the tax expenditure in the end. Furthermore, the fact that it is often unclear to which category a tax expenditure belongs and why the categories are chosen as they are, represents an important disadvantage of this categorising method. Besides, the volume of additional information generally increases with the number of categories, while the clarity of the categorization decreases. All in all, objective judgements and comparisons are often difficult.

Furthermore, tax expenditures can be classified according to what type of tax measure they represent. That means, how the tax expenditure is designed from a regulatory point of view: allowances, exemptions, deductions, rate relieves, and tax deferrals.[10] This relatively direct and simple approach which is widely used for research purposes contains only few categories and allows objective (comparable) judgements.

All in all, the Nordic countries classify, as many other countries, first of all according to purpose and/or objective on the one hand and tax base on the other. For example, Norway uses tax base and budget function. Denmark divides the tax expenditures into categories between purposes (e.g. education, health, business development etc.). In Sweden, tax expenditures are divided into two broad categories: expenditures which would affect the budget balance if they where abolished and expenditures which do not. In addition to this division, the tax expenditures that affect budget balance are classified according to their tax base and presented in subgroups. Moreover, the expenditures are also classified with respect to their general purpose. However, Finland is the only Nordic country which classifies in addition to the budget function also to the type of tax measure.

3.2.2 Important elements of reporting

Reporting tax expenditures in one form or the other, helps keeping focus on this part of the tax system. When reporting, the following should be considered: what to report; how often and where to report.

In the ideal world tax expenditure reports should be as comprehensive as possible. Depending on benchmark, reporting should include tax incentives, tax credits, tax breaks, exemptions and other measures. Therefore the report should include a complete list of all explicit and implicit exemptions in all taxes (including personal income, corporate income and sales taxes), regardless of the fiscal impact. When present, tax expenditures in local government taxation should also be included. In practice, there is often used a minimum level for a tax expenditure to be reported/calculated.

The ambitious report include detailed information about all tax expenditures (see for instance German "*Datenblätter*" – tabular summary of each tax expenditure containing original and actual objectives, legal citation, possible time limitation and/or digressional design, fiscal volume, and – if available – results from former evaluations).[11]
The following information is valuable when reporting tax expenditures:

9 See for example OECD (2008/1), p. 36 with target to compare tax expenditures and spending programs.

10 See for example OECD (1996), p. 9, OECD (2003), p. 2, Kran (2004), p. 130, Thöne (2005), p. 55 f., Boss and Rosenschon (2008), p. 5.

11 German Government (2007), p. 186 ff.

First of all it is important to describe the applied benchmark used to identify tax expenditures. If the definition is not transparent, it is not clear what kind of information you get from the reporting.

As the main focus probably will be on the estimates of the annual revenue loss, in the sense of costs which the expenditures create, it should be clear which method is used when calculating the tax expenditures (revenue foregone, revenue gain or outlay equivalence). Including cost in recent years and cost estimates for the future will give an indication of any trends in the single tax expenditure. It might not be necessary to re-calculate all tax expenditures every year. Instead, different parts/categories of the tax expenditures could be re-calculated e.g. every 2-4 year, or when the (groups of) tax expenditures are evaluated in connection with other parts of the tax- or spending system.

When reporting existing tax expenditures and re-estimating tax expenditures, one has to be aware that behavioural responses have an impact, even though the revenue foregone method is applied. In the longer term the level of tax expenditures will reflect behavioural responses due to the tax expenditure itself. Change in economic fluctuations, market conditions etc. will also effect the level of the existing tax expenditures. Changes in the general tax rates can also have an impact on tax expenditures, even though the specific legislation regarding the tax expenditure has not changed.

Besides listing all tax expenditures one by one, they can be listed according to tax base, purpose, who benefits from the tax expenditures etc. (see 3.2.1). Furthermore the reporting could include legal citation, reasons for enactment (intended objectives), and year of enactment for each tax expenditure. If there is a time limitation and/or degression this will be useful information as well. In addition, information from (former) evaluations could be summarized in the report.

Last but not least, tax expenditure reports should be timely and accessible. One target of tax expenditure reporting is to give policymakers and voters the information which they need to evaluate spending through the tax code. This allows them to weigh tax preferences against other spending and decide what really deserves funding. Tax expenditure reporting could, for instance, be incorporated into budget process or in a permanent list on the internet. Wherever tax expenditures are reported, the reports should be up-to-date and easily (online) available.

3.2.3 Challenges in evaluating tax expenditures: Effectiveness and efficiency

Evaluating tax expenditures is a key component of providing data on the effectiveness of the measures and the achievement of intended objectives (if explicitly specified). Furthermore, evaluation improves legislation since it provides evidence of what is working and what is not. However, evaluating tax expenditures is not at all an easy task. Especially, the extent to which resources could be rationalized or better allocated to strengthen government finances and to support progress towards broader economic and social objectives is not obvious. But also many other challenges arise and have to be tackled (e.g. benchmark system, evaluation criteria, data problems, interactions, and behavioural effects).[12]

Not only to identify and measure tax expenditures but also to evaluate them there is a need for reliable benchmark system. Merely changing this system at frequent intervals can render

12 See for example LAO (2003), p. 5.

analysis of tax expenditures less useful and therefore discredit and weaken them. In addition, evaluation criteria are needed. Designing principles as generally as possible can be seen as applications of the substantive goals of equity, efficiency, and ease of administration. Due to completely different types of tax expenditures with nearly incomparable targets and effects, evaluating tax expenditures systematically is problematic. Nevertheless comparable results are necessary to give fruitful advice to the public and politicians. If methods necessarily differ, one possibility to ensure comparable results is to use a common evaluation framework.

Apart from these evaluation scheme problems, there are a lot of practical difficulties in evaluating tax expenditures (e.g. data problems, interactions and behavioural effects) which can strongly affect the value of evaluations. One major challenge is that significant empirical data is required to evaluate the theoretical background of tax expenditures. Whereas data for collected taxes typically are registered, data for tax expenditures which are taxes not collected are not always recorded. The introduction of tax expenditures can even directly lead to a lack of information. All in all, widely data collecting and providing of data (by taxpayers benefiting from tax expenditures) is necessary in order to evaluate the effectiveness of tax expenditures. For purpose of comparison, tax expenditure data has to have the same standing and be of the same level of quality as spending data in the budget. An increased use of mandatory reports from businesses and households can establish an improved dataset for evaluating tax expenditures. This extra information must be weighted against the cost, both monetary and in terms of integrity, of obtaining this information and possible political objectives of administrative burdens.

Further challenges result from interactions between different tax expenditures and/or between different political subdivisions when tax expenditures exist at both federal and state level. In these cases changing one tax expenditure can affect costs and effectiveness of another and thereby make it difficult to isolate the effects of individual tax expenditures. When analyzing the distributional effect of a certain tax expenditure it is therefore important to analyze the tax system as a whole. Analyzing one tax expenditure in isolation might give a false impression of the real distributional effect of all elements of the tax and expenditure system. This could be true in the case where the same group of persons or firms receive a tax deduction in one area but have to pay an extra tax or fee in another area.

In addition, there is often limited information regarding how taxpayers' behaviour are affected by the existence of tax expenditures. Therefore, the overall effect often differs significantly from the first stage effect. Furthermore, looking at tax expenditures next to direct spending is not always an apples-and-apples comparison. Direct spending does e.g. not necessarily take account of taxes, whereas tax expenditures mostly are stated after taxes.

All in all, evaluating costs, efficiency, and equity impact of tax expenditures requires a high level of ambition. Comprehensive assessments will potentially require a lot of resources, which are not allocated today. Therefore, depending on the amount of resources allocated for assessments a more targeted approach, which focuses on individual tax expenditures of special interest, could be considered. Evaluations of tax expenditures along with other evaluations of the tax system in general or when specific areas are evaluated will could also be considered. Such an approach should include studies both by the administration itself as well as by other institutions. A sunset provision is another possibility to ensure that (newly) created tax expenditures do not continue indefinitely unless merited.

3.3 Reporting and evaluation in other countries

3.3.1 In general

In general, international comparisons of tax expenditures are difficult.[13] Definitions of tax expenditures share a common core across countries. Every country defines tax expenditures as exceptions from some baseline standard for the entire tax. Although the benchmark is almost identical, the countries differ in the purpose of the exercise of the identification of tax expenditures and this cause differences in what is considered as tax expenditures in the specific country. Japan, for instance, defines its benchmark in terms of its basic principles of taxation: equity, neutrality and simplicity. This benchmark is expected to give a large number of tax expenditures. In the other end of the spectre, the Netherlands considers its benchmark to be the "primary structure" of the actual tax system in place, which is expected to induce relatively few tax expenditures. Thus, with the choice of definition the number of identified tax expenditures can vary considerable. Few countries identify tax sanctions.

Some countries have made it a legal requirement to report tax expenditures, and others have not. Some report outside the budget and some in annexes to the budget. Reporting of tax expenditures alongside similar outlay programs is seldom done. In general most countries report annually, but some countries report every two years or less frequent. Most countries generally cover only a few years when reporting, but some countries like Canada, the Netherlands, and USA covers a period for 7-8 years.

Most countries acknowledge the importance of evaluation, but no countries have systematic programs to evaluate tax expenditure. Even in the few countries where evaluating programs are required by law, the evaluations only comprise of an estimation of the cost of tax expenditure.[14]

3.3.2 The German evaluation of tax expenditures

In 2007, the German Federal Ministry of Finance commissioned – based on the Federal Government's report on subsidies – a systematic evaluation of the Federal Government's most important tax expenditures.[15] The current research project, undertaken by the Cologne Centre of Public Economies (FiFo), the Mannheim-based Centre for European Economic Research and Copenhagen Economics, determines if there are rational goals for these tax expenditures, as well as effectiveness and efficiency in achieving objective targets.

The tax expenditures in question reach from VAT reductions to income tax measures and instruments with environmental objectives. These tax expenditures belong to completely different categories with both incomparable targets and effects, and this makes it impossible to evaluate them according to one method. Nevertheless a systematic evaluation is ensured by asking the same questions in a common evaluation framework for each of the tax expenditures. The following structure is used:

13 This section draws on OECD (2008).

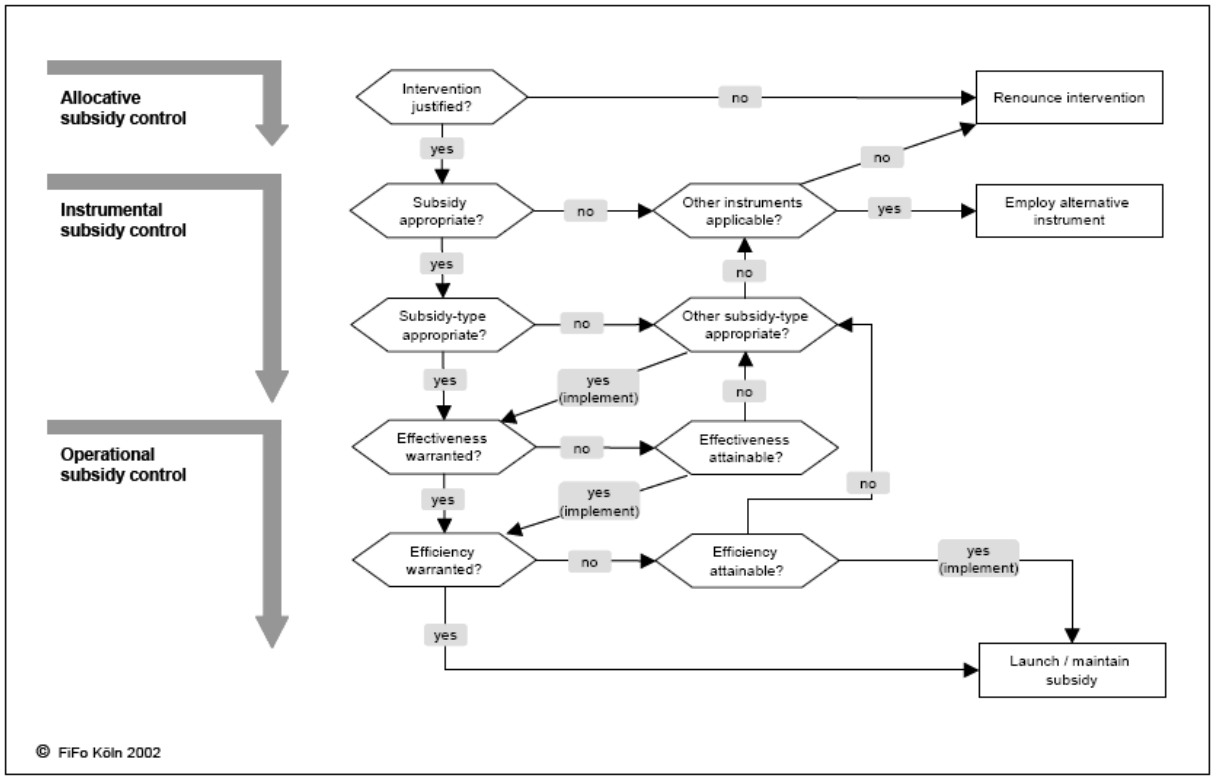
14 For detailed information see Annex 7.1. Further overviews on this topic are especially provided by Bratić (2006), p. 117, Australian Treasury (2009), p. 3, OECD (2008/1), p. 79 ff., and OECD (2008/2), p. 2 f.

15 See for example German Government (2007), p. 5 and GSI (2007), 1 f. To clarify the importance of this research project, it has to be considered that the 20 most important German tax expenditures nearly amount to 90 % of the fiscal resources that are spent in the context of tax expenditures by the Federal Government (see German Government (2007), p. 18).

1. Short description of the tax subsidy and its history
2. Measurement of the actual volume of the tax expenditures
3. Record of past evaluations and their results
    a. Past evaluations of the tax measure in question
    b. Past evaluations of comparable tax expenditures home and abroad
4. Core evaluation:
    a. Rationale of the subsidy
    b. Relevance of the subsidy and instrumental subsidy-control
    c. Testing for effectiveness
    d. Testing for efficiency
5. Conclusions and proposals for actions to be taken

While steps 1-3 compile the information necessary to build a well balanced evaluation on, step 4 is the core evaluation part. This structure is modelled after the scheme for an optimal subsidy control developed by FiFo on the basis of international benchmarking endeavour and common best practise (see figure 3.1).

Figure 3.1: Simplified scheme of optimal subsidy control



Source: Thöne (2003), p. 41.

This three-steps-approach (allocative subsidy control, instrumental subsidy control and operational subsidy control) contains all the basic questions that have to be asked to justify or to renounce tax expenditures. That means: Is the subsidy justified? Is it relevant? Is it well-designed? Is it effective? And last but not least: Is it efficient? If one of these 5-level-questions has to be denied, the decision process of the respective subsidy is immediately

terminated. In this case a renouncement or at least an employment of an alternative measure is recommended.

For example, if a certain tax expenditure cannot (or no longer) be justified on principal reasons, the necessary and sufficient conditions for its abolishment are fulfilled.[16] In general, there is no more need to analyse the further questions. Nevertheless the forthcoming German evaluation report will contain full evaluations of all German tax expenditures in question.

16 See Thöne (2003), p. 38 f.

4 Country overviews

4.1 Introduction

In this chapter we discuss the treatment of tax expenditures in Denmark, Finland, Norway and Sweden. Section 4.2 starts with a summary of common features and points towards differences. The common challenges are also discussed. Then more detailed descriptions of tax expenditures in each country follow.

4.2 Main features

Tax expenditures are calculated in all of the Nordic countries. The general principles in defining and calculating tax expenditures are quite similar, but there are differences. Differences can be found for example in the reporting practices and the reasoning behind tax expenditure calculations, and in the political objectives concerning the use of tax expenditures.

4.2.1 Definition of tax expenditures and the benchmark system

Tax expenditures are generally defined as deviations from a benchmark tax system. In all of the countries discussed here, the underlying idea behind the definition of the benchmark system is the concept of comprehensive income taxation, a broad based system where all income is largely taxable. For pragmatic reasons, the benchmark system is in all countries more or less based on the prevailing tax system. Sweden applies a more ambitious approach in defining the benchmark, as the benchmark is based on the idea of uniform taxation, i.e. each type of tax should be levied uniformly and without exemptions. The benchmark nevertheless allows for exemptions and can thus also be perceived as pragmatic. Besides tax expenditures, all countries also calculate tax sanctions in cases of unfavourable tax treatment of specific groups or activities. Denmark, however, only calculates tax sanctions when there is a close link to the tax expenditures, like when a tax sanction reduces a tax expenditure. The general features of the benchmark systems are fairly stable, although as they are to a large extent based on the prevailing tax systems, they do change when the general tax systems change.[17]

Defining the benchmark system can be complicated in practice, even though the benchmark is based on the current tax system. Deciding which tax rules should be included in the benchmark and which constitute tax expenditures is not always straightforward. Examples of these questions are the treatment of interest deductibility, earned income tax deductions, deductibility of pension income contributions, VAT exemptions and excise duties.

All the Nordic countries use the dual income tax system where labour income and capital income are taxed separately, although with great individual variations. This system is generally included in the benchmark. Progressive taxation, including standard deductions, is part of the benchmark in all countries. In Denmark and Sweden in-work tax deductions are also considered part of the benchmark. Denmark includes deductions for many, but not all expenses in the benchmark, whereas the other countries only allow for deductions of costs

17 An example of these changes is the adoption of the shareholder model in taxation and in the benchmark in Norway in 2006.

directly linked to generation of income. Generally the deductions that are allowed for in the benchmark are of general nature and do not favour specific groups or activities.

All countries except Finland include interest rate deductions in their benchmarks. Imputed rent from owner occupied housing is considered as real income in all countries but the tax expenditure is not calculated in Denmark due to difficulties in defining the benchmark. In Norway a wealth tax is included in the benchmark. Deviations from the standard rate or lower assessment values than real values are regarded as tax expenditures.

All countries have a standard rate for corporate taxation and deviations are defined as tax expenditures. In Norway real profit is taxed as ordinary income, with the same rate as other income sources.

In value added taxation, the standard VAT rate (25 per cent in Denmark, Norway, and Sweden, while 22 per cent in Finland) defines the benchmark in all of the countries, and deviations from the standard rate create tax expenditures. In Finland all, and in Sweden some, VAT exemptions are also considered part of the benchmark, in Denmark and Norway exemptions are considered to create tax expenditures.

The countries define the benchmark with respect to excise duties in different ways and the scope of excise duties included varies as well. Finland has no special benchmark for excise duties, but defines tax expenditures as deviations from the standard rate. The same applies for Denmark and Sweden, but included in the benchmark for energy is a split between where and to what the energy is being used. Denmark considers a new benchmark for environmental excise duties that reflect externalities. Norway on the other hand applies a benchmark that is based on the theory of optimal taxation and thus a normative benchmark. The benchmark is divided between fiscal and environmental excise duties. For fiscal excise duties the exemption of taxes on factors on production is part of benchmark and the environmental taxes are in line with external costs. Sweden and Finland only considers excise duties that involve tax expenditures with a certain magnitude, whereas Norway and Denmark include all, or most of the excise duties.

4.2.2 The volume of tax expenditure

Comparing tax expenditures between countries and over time is not straightforward. The coverage of the tax expenditure calculations varies, as does the definition of tax expenditures in the first place. A more orthodox definition of the benchmark usually leads to a higher number of tax expenditures. It should also be kept in mind that tax systems, and thus the benchmarks, within each country change, and this will affect the evolvement of tax expenditures over time.

Moreover, the data used may be of varying quality. This, among other things, calls for caution when interpreting tax expenditures. Nevertheless, the number of tax expenditures ranges from 60 in Norway to 115 in Sweden. The total estimated volume of tax expenditures is by far the largest in Sweden, 25 billion euros, and smallest in Denmark, 5 billion euros. In Finland the estimated value of tax expenditures was 13 billion euros, and in Norway 16 billion euros. The share of tax expenditures as per cent of GDP is largest in Sweden, 8 per cent, and smallest in Denmark, 2.2 per cent. In Finland the share is slightly lower than in Sweden, 7 per cent, and in Norway the share of tax expenditures is 5.4 per cent of GDP. As

per cent of total tax revenue, the tax expenditures amount to 4.4 in Denmark, 17 in Sweden, 16 in Finland and 13 in Norway.[18]

As method of calculation, all countries apply the revenue-foregone method. Tax expenditures are calculated as the direct revenue effect of abolishing a specific tax rule that is not part of the benchmark system. Denmark and Sweden also use the outlay equivalent method. This method calculates the corresponding amount needed on the expenditure side of the government budget to reach the same effect. Norway calculates some tax expenditures as present value. This method is used when there is a time horizon, by estimating today's value of a future gain. The tax expenditures related to depreciation rates higher than actual depreciation and tax expenditures related to employee premiums and contributions to occupational pension schemes are calculated using this method. A common feature among the countries is that behavioural responses are not taken into account when calculating tax expenditures. Moreover, interactions between different taxes are not taken into account. The tax expenditure calculations rely on tax administration data and other statistical data. In addition, Finland and Norway utilise microsimulation models in calculating tax expenditures in personal income taxation. In Denmark and Sweden the Ministry of Taxation and Ministry of Finance, respectively, performs the calculations, and in Norway the work is divided between the Ministry of Finance and Statistics Norway. In Finland the Government Institute for Economic Research makes the calculations.

Since the late 1990's, the share of tax expenditures to GDP has declined in Denmark. This is mainly due to abolition of tax expenditures related to taxation on energyconsumption. There have also been some changes in the composition of the tax expenditures. The Danish Tax reform (Forårspakke 2.0) will reduce the tax expenditures with app. 0.2 billion euros. In Finland the share of tax expenditures to GDP has remained relatively stable during this period, but it has come down remarkably since the mid-eighties, which is the start of the reporting period. Lately there has been an increasing tendency towards introducing new tax expenditures in Finland, so generally the volume of tax expenditures can be expected to increase rather than decrease in the years to come. Since the late nineties in Norway, an increasing number of deductions and allowances have been defined as tax expenditures. This has contributed to an increasing volume of tax expenditures. One of the objectives of the 2006 tax reform in Norway was to abolish several exemptions and allowances that were poorly justified, but the reform was only partly successful in this matter. The general trend in Norway is that the reported tax expenditures are growing. A substantial part of this growth can be attributed to growing tax bases, but some tax policy changes have also contributed to this development. In Sweden the level of tax expenditures has been fairly constant over the last few years. Although there has been some year-to-year variation it is hard to point in any direction.

In all of the countries, the composition of tax expenditures evolves over time when new tax expenditures are introduced and old ones abolished. The distribution of tax expenditures to different policy areas is different in the Nordic countries, but currently tax expenditure on housing seems to be among the most important tax expenditures in all of these countries. The most important tax expenditures in Denmark are in the area of business development, corresponding to 30 per cent of total tax expenditures. Besides from business development, traffic and communication, housing and energy supply represent areas with a relatively high level of tax expenditures. Tax expenditures directed to business development and housing has

18 The figures in this paragraph refer to 2008 or 2009.

increased substantially since the late 1990's in Denmark, and at the same time tax expenditures for energy supply has decreased. In Finland, the most important tax expenditures are in the area of social security, housing and labour income taxation. The share of tax expenditures directed to manufacturing has decreased since the late 1980's, and since late nineties, the share of tax expenditures on labour income has increased. In Norway, the most important tax expenditures relate to lack of taxation of imputed income from, and low assessment values on, housing. The regionally differentiated employers' social security contribution and employee premiums and contributions to occupational pension schemes also give rise to major tax expenditures. In Sweden, the largest tax expenditure in 2009 is associated with returns to housing as it is not taxed as other capital income. Three other large tax expenditures involve VAT, indirect taxation of labour income and energy taxes.

4.2.3 Reporting, classification and evaluation of tax expenditures

Tax expenditures reflect political priorities, and by reporting tax expenditures, these priorities are made visible. Tax expenditures have been reported since late 1990's in all of the countries except for Finland, where they have been reported since 1988. All countries except Denmark report tax expenditures yearly to the Parliament. In Denmark tax expenditures were reported in an appendix to the Budget Proposal until 2006, when the Danish Government decided to exclude them. The Danish Ministry of Taxation publishes a list of changes to tax expenditures due to legislation on its homepage. In Sweden tax expenditures are reported in a Government Communication in conjunction with the Spring Fiscal Policy Bill, and they are re-reported in the autumn as supplement to the Budget Bill. In addition to the actual numbers, Sweden also publishes the methodology of the calculations. In Norway tax expenditures are reported in the National Budget, and in Finland the main categories of tax expenditures are presented in Report on the Central Government Final Accounts. Although there is no systematic tax expenditure reporting in Denmark, new tax expenditures are explicitly mentioned when a bill includes tax expenditure. Revenue and distributional effects and the purpose of the new tax expenditure are then presented. In Sweden, when a new tax expenditure measure is introduced, this is explicitly pointed out in the tax expenditure report. In Finland, the status of the tax expenditure reporting is relatively low at the moment, and no special attention is given to new tax expenditures in tax expenditure reporting. Norway has no systematic approach to new tax expenditures in the tax expenditure report, but in the latest report (2008) new tax expenditures were pointed out.

There are differences between the countries not only in how the tax expenditures are reported, but also in what is left out of the tax expenditure reports or not calculated. The main reason for leaving something out is methodological difficulties. In Finland, real estate taxation, inheritance tax or social security contributions are not covered in the tax expenditure reports. Also most of the excise duties are not covered, as is also the case in Sweden. In Norway all existing tax expenditures are included in the report, but not all are calculated. This for example applies to the inheritance tax and several tax expenditures related to payments in kind. In Denmark tax expenditures are not calculated where a benchmark is difficult to establish, as for example in private pensions systems, where the time horizon and correlation to public transfers complicates the matter.

There are different ways of classifying tax expenditures (see chapter 3.2), and the information given by the tax expenditure reports also depends on the classification. In Denmark and Finland, tax expenditures are classified according to operational categories. In Finland this classification was originally based on budgetary categories, but in that sense the classification is no longer valid, since the budget categories have changed. Tax expenditures are also

classified according to types of tax (income tax, indirect taxation etc.) in Finland. In Norway tax expenditures in direct taxation are classified according to taxable base. In indirect taxation, tax expenditures are classified according to both the type of tax (VAT, excises) and objectives (fiscal, environmental, health). In Sweden, tax expenditures are divided into two broad categories: expenditures which would affect the budget balance if they where abolished and expenditures which do not. For the former category, which includes most tax expenditures, both the revenue forgone and the outlay equivalent are calculated. For tax expenditures not affecting the budget balance, i.e. tax exempted transfers, only the outlay equivalent is calculated. The revenue foregone is readily available on the expenditure side of the government budget. In addition to this division the budget balance affecting expenditures are classified according to their tax base and presented in subgroups. Moreover, the expenditures are also classified with respect to their general purpose. In this respect, a distinction is made between technically or administratively motivated tax expenditures and politically motivated tax expenditures.

Despite of the reporting, tax expenditures are not an integrated part of the budget process in any of the countries. In most cases tax expenditures are not reported in connection with direct expenditure targeted to the same activities or recipient groups, so it seems that when discussing the distribution of public finance to different policy areas, tax expenditures are not systematically included. One exception is found in Norway, where direct and tax transfers to different industries are reported under the heading "Industrial support" in the National Budget.

Some have pointed to the lack of yearly evaluation and assessment of whether the public support given trough tax expenditures is increasing or decreasing, and how well the targets of the tax expenditures are achieved.There is no systematic evaluation of the effectiveness of tax expenditures in any of the countries discussed here. But there are good examples of evaluation though. For example in Norway, tax allowance for R&D expenses has been thoroughly evaluated by Statistic Norway. Prior to the Norwegian tax reform in 2006, a government appointed Tax Committee also evaluated several tax expenditures. In Denmark taxation and other regulation of emissions of CO_2 have been evaluated in 2007. The double regulation of CO_2 can be regarded as a form for tax sanction. In Finland, the tax credit for household services introduced in 2001, has been evaluated for employment effects. More comprehensive evaluations of tax expenditures are often done in connection with tax reforms. This has been the case in Finland when a comprehensive tax reform was introduced in the late 1980's**.** A distinction can be seen between the treatment of new tax expenditures and existing ones – new tax expenditures tend to be better evaluated, (in terms of for example of employment effects), than existing ones. There is often an ex ante evaluation of the effects of new tax expenditures when they are introduced. It should be noted that not all direct expenditures are evaluated on a yearly basis.

4.2.4 Critique from National Audit Offices

Denmark, Finland and Sweden have all received critique from the National Audit Offices (NAO) concerning tax expenditures. The common main point stressed in all of the countries is lack of transparency in the treatment of tax expenditures. The Swedish NAO has emphasised, that the principles behind reporting and calculating tax expenditures are not suited for continuous evaluation of different tax expenditures, and that the reporting of tax expenditures is not well suited to fulfil its purpose. The Swedish NAO has advised the Swedish Government to consider how tax expenditures should be treated in the fiscal process. The Danish NAO has recommended annual publishing of the tax expenditures in

connection with the budget process. It also recommended that each tax expenditure should be revised and evaluated every year. In Finland the central question raised by the NAO is whether the legislation process and evaluation of tax expenditures is on an adequate level. The Finnish NAO also stressed that the rationale behind the tax expenditures should be clear, especially if there are other reasons besides the suitability of the tax expenditures, such as the budgetary spending limits, that might encourage the policy makers to use tax expenditures instead of direct budgetary expenditures.

4.2.5 Tax expenditure and fiscal policy

It is not easy to draw conclusions about the general atmosphere and discussion concerning tax expenditures in the Nordic countries. There clearly are different tendencies in the primary objectives behind tax expenditure reporting, the political interest in using tax expenditures and in the political and general discussion about the reporting of tax expenditures, and the treatment of them in the budget process.

Tax expenditures can be justified for various reasons, but there can also be less satisfactory reasons behind the use of tax expenditures instead of direct expenditures. For the latter, the principle policy instrument, there are routines and systems designed for efficiency, control and fiscal discipline. In general such systems are missing for tax expenditures. For example, while a cap can be applied to direct expenditures, there is no direct limitation on tax expenditures. Finland and Sweden apply budget caps to direct expenditures and it may be argued that such caps give incentives to give support through the budget income side, i.e. through tax expenditures. Denmark does not have a budget cap, but there is a long run balanced budget goal. Due to the tax freeze since 2001, tax expenditures cannot be reduced. New tax expenditures can be introduced, which will reduce the room for direct expenditures. This is also the case in Norway, where the government operates with a balanced budget rule, i.e. a structural non-oil central government budget deficit corresponding to the expected real return (estimated at 4 per cent) on the Government Pension Fund – Global (the former Petroleum Fund). Even though this implies that the government has a choice between tax expenditures and direct transfers, it often seems like tax expenditures are regarded as easier to implement than direct expenditures and also appears to be less costly. This probably stems from a fact that applies to all the countries in question, namely that tax expenditures are not subject the same scrutiny as direct expenditures. Although in Denmark changes in tax expenditures are subject to the same scrutiny as other changes in the tax code. A full integration of tax expenditures into the budget process is hardly feasible. Lack of data, computational methods, benchmark choice and other methodological issues complicates this matter.

The Danish Government has decided to end tax expenditure reporting in the Budget Proposal. This does not mean that the tax expenditures are totally neglected though. The exclusion of tax expenditures is justified by that the fundamental objective with the Budget Proposal is to establish the basis for next year's direct expenditures and revenue. Distortions due to the tax system and direct regulation are not listed in the Budget Proposal, even though these costs exceed the costs due to tax expenditures. Even though collecting more information about tax expenditures would improve transparency, it would also involve increasing costs and administrative burden. The Danish Government has committed to decreasing administrative burden, and so these costs should be carefully weighted against the gains from more information. Yet the Danish Government agrees that the use of tax expenditures should not lead to open ended public spending.

In Finland the interest in using tax expenditures has been increasing recently, after being relatively limited for almost 20 years. There has been an increasing amount of requests for new tax expenditures, and as a consequence, new tax expenditures have been introduced. It can be argued that this is due to budgetary spending limits on direct expenditures. At the same time, the distance between tax expenditure reporting and the budget process has grown. The rationale behind each tax expenditure is discussed in a working group report published in 1988, but they are not presented along the yearly reporting of tax expenditures. Following the critique from the National Audit Office and the Parliamentary Audit Committee, the Finnish Ministry of Finance has appointed a working group with a mandate to evaluate, and suggest improvements to, the treatment of tax expenditures.

In Norway the stated purpose of reporting the tax expenditures is to obtain a greater degree of transparency regarding political priorities and financial support to different groups or activities. However, the pragmatic approach to the reference system used to identify tax expenditures, limits the informational value of reporting tax expenditures. On the other hand, this approach implies that the issue of tax expenditures attracts only moderate attention in Norway, and the estimates are more or less undisputed.

Despite of the differences, in can still be argued that the importance of discussing tax expenditures in the Nordic countries is increasing rather than decreasing. In all of the countries, the problems in defining the benchmark tax systems, and also in documentation of the calculation methodologies applied, limit the informational value of the tax expenditure reports. The lack of evaluation of tax expenditures also makes the matter more important.

4.3 Tax expenditures in Denmark

4.3.1 Introduction

The first comprehensive survey of tax expenditures in the Danish tax system dates back to 1996. After 1997, tax expenditures were included in an appendix to the Budget Proposal (Finansloven). The tax expenditures were not reported in connection with direct transfers or subsidies. The tax expenditures were published in the Budget Proposal until 2006 and covered the period up to 2009. The tax expenditures have not been updated with revisions in the benchmark system the last couple of years, but were more or less a mere mechanical projection with the annual change in the GDP or consumption growth when relevant and taking into account changes in the legislation with respect to tax expenditures. In 2006 the Government decided to stop publishing tax expenditures in the Budget Proposal. Instead, when a Bill implies tax expenditures, this must be accounted for explicitly. The revenue effects, distribution, purpose etc. will thereby be transparent as is the case with other changes in the tax system.

A list of changes in tax expenditures due to legislation is published on the Ministry of Taxation homepage.[19] This reporting started in the financial year 2007/2008. The list will not update all tax expenditures every year, but will include new tax expenditures and changes in existing tax expenditures.

The benchmark for tax expenditures in Denmark is, in general, based on a pragmatic approach. The tax expenditure is calculated as direct revenue when abolishing a special rule

19 See www.skm.dk.

that is not considered part of the benchmark. Both the revenue foregone method and the outlay equivalent method have been used, although the revenue foregone method is the most widely used method when reporting tax expenditures.

4.3.2 Definition of tax expenditures

All types of taxes are included when calculating tax expenditures; also differences in the timing of tax payment are covered. Tax expenditures are not calculated where a benchmark is difficult to establish as for example owner-occupied accommodation or in private pensions systems, where the time horizon and correlation to public transfers complicates the matter. The benchmark for tax expenditures is, in general, based on a pragmatic approach, where the tax expenditure is calculated as direct revenue when abolishing a special rule that is not considered part of the benchmark system.

The applied benchmark tax base can be characterised as a Comprehensive Tax Base, including capital income and gains, labour income, fringe benefits and public transfers. The benchmark has some modifications. For instance, the dual income tax system, which has been in place since 1987 is considered part of the benchmark. In addition, the progressive tax rates are part of the benchmark system for income taxation.

Furthermore, deductions for expenses to acquire and maintain income are part of the benchmark system. But differentiation between private expenses and expenses to acquire and maintain income are not always simple in the real world. As a practical solution all expenses (some specified by law) are regarded as part of the benchmark system, while only deductions targeted to specific groups are calculated as tax expenditures. For example, deductions of interest payments are part of the benchmark. If not, the level of tax expenditures would increase substantially. Moreover, the in-work tax credit is regarded as part of the benchmark, even though it only concerns income from employment and not income from transfers. The credit has a max and is given to all employed. For higher incomes it doesn't reduce the marginal tax rate, but only reduce the average tax rate.. All in all, this benchmark is in practice relatively close to the overall structure of the Danish tax system.

For VAT purposes the standard VAT rate (25 per cent) is the benchmark. Therefore lower VAT rates and exemptions are considered tax expenditures. This includes exemptions that follow the EU VAT directive. For excise duties however there is no general benchmark. Instead, tax expenditures are defined as deviations from the benchmark for each excise duty.

The Danish corporate tax rate amounts to 25 per cent, which is the general benchmark rate for corporate taxation. There are some difficulties in defining which exceptions to the general system have to be treated as tax expenditures. In the list below there are some considerations regarding selected topics in the corporate taxation area:

R&D tax incentives are treated as tax expenditures in Denmark. The legislation puts up different rules of preferential treatment regarding R&D expenditures, which makes it possible to deduct expenditures to R&D right away and not following the normal rules of depreciation.

Imputation systems for taxation of dividends are a part of the benchmark system in Denmark and are therefore not treated as tax expenditures. Dividend incomes are taxed at preferential rates (compared to interest income) at the shareholder level. The rate is set so that the overall

CIT + dividends equal the nominal tax on wages. Therefore the real tax rate on capital income might exceed the wage income tax. This could lead to a discussion about what the benchmark system should be if the tax expenditure had to be calculated.

Reduced tax rates for certain forms of capital income. Capital incomes are taxed differently whether it is positive or negative capital income. Negative capital income is taxed with a flat rate whereas positive capital income is taxed with varying rates depending on the type of capital income. The different tax rates on different types of capital incomes are not regarded as tax expenditures in the Danish system. Neither is taxation on an accrual basis (as opposed to taxation upon realisation) calculated or regarded as a tax expenditure.

Tax expenditures are not defined by an independent organization, so the government has some leverage when deciding whether changes in the tax system give birth to change or new tax expenditures. There has not been much debate over what to define as tax expenditures. The National Audit Office of Denmark has recommended a broader definition of tax expenditures in line with recommendations from OECD. As the tax expenditures are defined as deviations from a norm this benchmark will change if the tax system undergoes reforms or changes.

Finally, tax sanctions are only calculated if there is a close link to tax expenditures. That is typically a tax sanction reducing a tax expenditure. Moreover, tax expenditures include general and local taxation but tax expenditures are not split into different levels for purposes of reporting. Almost all tax expenditures are permanent.

4.3.3 Methods of calculation

In Denmark both the *revenue foregone method* and the *outlay equivalent method* have been used, even though the revenue foregone method has been most widely used. The *revenue gain method* has not been applied, although the estimated behavioural responses are included in proposals for changes within the tax system. Even though behavioural responses are not directly taken into account when calculating tax expenditures, the level of tax expenditures in the longer term, when recalculated, will reflect behavioural responses due to the tax expenditure, market conditions etc. But this behavioural response is of course the reason why the tax expenditure often will be different to the revenue if the tax expenditure were to be abolished.

The individual tax expenditure is estimated under the condition that all other tax expenditures are unaltered. The possible interaction of different tax expenditures is thus neglected, as the theory does not point to correct order of adding up.

The Ministry of Taxation that manages the calculations does not use any special models to derive the tax expenditures. Tax expenditures are not calculated where a benchmark is difficult to establish as for example in private pensions systems, where the time horizon and correlation to public transfers complicates the matter.

4.3.4 Reporting and evaluation

The first comprehensive survey of tax expenditures in the Danish tax system dates back to 1996.[20] The survey was presented by the Danish central administration and covered the

20 "Skatteudgifter i Danmark, 1996", by the Danish central administration.

period from 1993 to 1998. The 1996 report was followed by an update in 1997.[21] This update included new tax expenditures, and minor revisions in the reference system and changes due to revised data sources. The 1997 report covered the period 1997 to 2001.

After the 1997-update, tax expenditures was included in an appendix to the Budget Proposal (Finansloven). The tax expenditures were not reported in connection with direct transfers or subsidies. The tax expenditures were published in the Budget Proposal until 2006 and covered the period up to 2009. The tax expenditures have not been updated with revisions in the reference system the last couple of years, but were more or less a mere mechanical projection with the annual change in the GDP or consumption growth when relevant.

The Government decided not to publish tax expenditures in the Budget Proposal after 2006. Although tax expenditures are no longer reported in the Budget Proposal, this does not imply that tax expenditures are neglected. There is a greater focus on tax expenditures in the legislation process. When a Bill implies tax expenditures, this must be accounted for explicitly. Thereby the revenue effects, distribution, purpose etc. will be transparent as it is the case with other changes in the tax system.

There is a list of changes in tax expenditures due to legislation on the Ministry of Taxation homepage.[22] This reporting started in the financial year 2007/2008. The list will not be updated completely every year, but will include new tax expenditures and also revisions of existing tax expenditures. In addition, parts of the tax expenditures are reported separately in different contexts.

In 2007 the National Audit Office of Denmark (NAO) evaluated the use of tax expenditures in Denmark.[23] The NAO main critique was a lack of transparency in the use of tax expenditures. The NAO recommended proceeding with a yearly publishing of tax expenditures in connection with the Budget Proposal. Every single tax expenditure should be revised and evaluated every year.

The Danish Government agrees that the use of tax expenditures should not lead to open ended public spending. The fundamental objective with the Budget Proposal though is to establish the basis for next year's direct expenditures and revenue. Distortions due to the tax system and direct regulation are not listed in the Budget Proposal as well, even though these costs exceed the costs due to tax expenditures.

The NAO also noted that an increased collection of data would improve the quality of tax expenditure estimates in certain areas. An increase in the collection of data will involve extra costs. Whereas data for collected taxes are registered, data for tax expenditures which are taxes not collected, are not always recorded. An increased use of mandatory reports from

21 "Skatteudgifter i Danmark, 1997", by the Danish central administration.

22 http://www.skm.dk/tal_statistik/provenuoversigter/6731.html.

23 Beretning til Statsrevisorerne om gennemsigtighed vedrørende skatteudgifter (fradrag mv.), 2007:

http://www.rigsrevisionen.dk/media(419,1030)/Beretning_om_gennemsigtighed_vedr per centC3 per centB8rende_skatteudgifter_(fradrag_mv.).pdf.

The National Audit Office (NAO) is an office of parliament. Parliament has no other investigative or audit body. The NAO is not a constitutionally mandated body but is rather set up by a regular legislative act. The audit plan is drawn up by the NAO itself, although up to one-third of audits come from parliamentary requests or agreements. The parliamentary public accounts committee receives audit reports and ministers are held to account for the contents.

businesses and households can establish an improved dataset for evaluating tax expenditures. This extra information must be weighted against the cost to get this information. The Government has committed itself to reducing the administrative burdens on businesses with up to 25 per cent by 2010. An extended duty to report data will impose administrative burdens on businesses and households, which conflicts government objective.

Transparency of tax expenditures, and evaluation of the tax system and expenditures in general, can be established outside of the Budget Proposal. This might not imply an evaluation of all aspects of the tax system etc. every single year, but directs resources to specific parts of the system. In time the majority of direct as well of indirect spending will be evaluated.

The tax burden was technically increased between 1993 and 1994 as a consequence of restructuring a number of social pensions from being fully or partially tax free to fully taxable. Contributions before tax rose accordingly. This technical reform raises the tax burden and lowers tax expenditures (if the reference system claims that all income must be taxed) but has no real economic effects.

4.3.5 Overview of the most important tax expenditures

In this subsection there is a description of size, distribution and trends of tax expenditures in Denmark. It should be noted, that there are considerable uncertainties when estimating and calculating tax expenditures. The estimates are, as described above, sensitive to changes in the choice of benchmark and different benchmarks would generate different levels of tax expenditures. There are also tax expenditures in a number of areas where the statistical and analytical basis for a survey are not sufficient. Therefore the estimates of the total tax expenditures are not complete and must be taken as such.

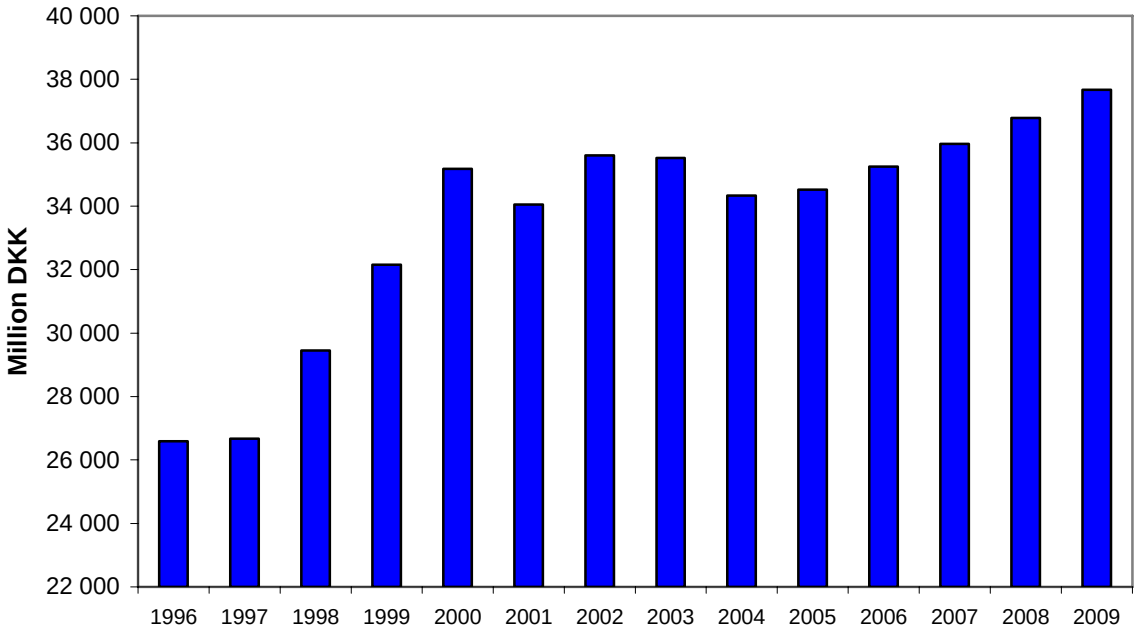
Total tax expenditures

The number of tax expenditures in Denmark is approximately 90. Total tax expenditures can with considerable uncertainty be estimated to around 37.8 billion DKK or 5 billion euros[24] in 2009 using the revenue forgone method. This corresponds to around 2.2 per cent of GDP, and around 4.4 per cent of total tax revenue.

As figure 4.1 shows, tax expenditures have fluctuated between 26 and 38 billion DKK in current prices in the period from 1996 to 2009. From 1996 to 2000 there was a relatively high increase in tax expenditures, which was mainly due to new legislation regarding health and business development expenditures. The increase in tax expenditures from 2003 and forward was mainly due to economic growth and inflation.

24 1 euro is app. 7,45 Danish kroner, April 2009.

Figure 4.1. Total Tax Expenditures (current prices) 1996-2009 - Revenue foregone method



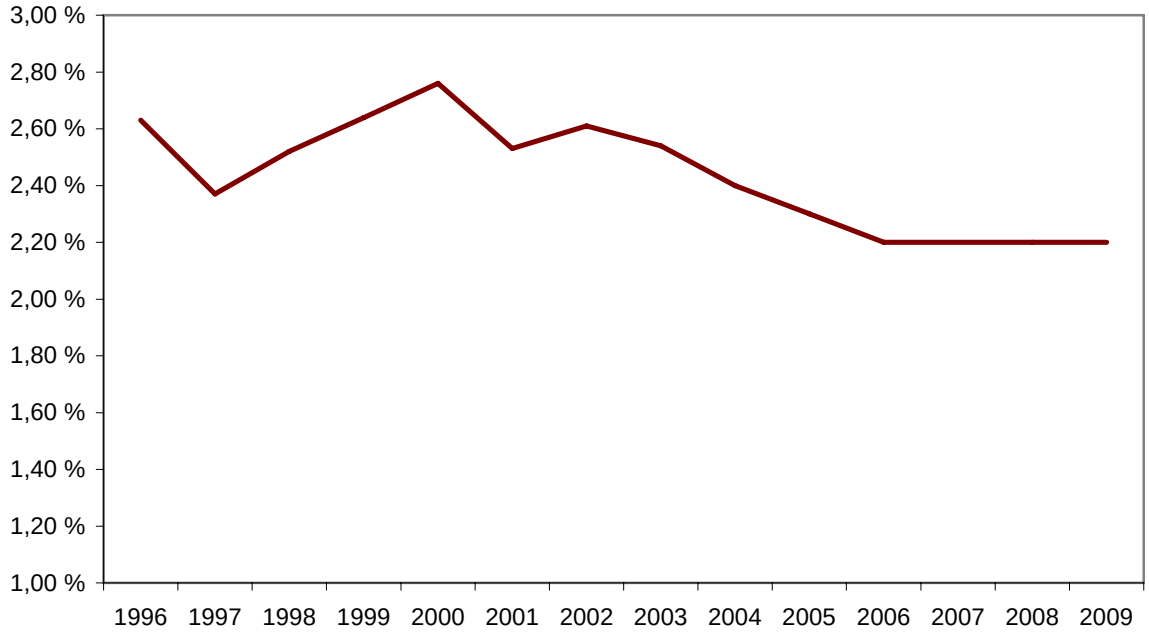
Source: Danish Budget Proposal 1998-2006. Note: 2007 to 2009 are estimated figures.

As figure 4.2 shows, tax expenditures constitute between 2.2 per cent and 2.8 per cent of GDP in the period from 1996 to 2009.

There has been a decline in tax expenditures as a share of GDP from 1999 and forward. This is primarily due to relatively small increases in overall tax expenditures in the period. Tax expenditures to housing conditions have decreased from 2000 and forward. This is due to the reductions in the taxable value of properties, which was given to owners of houses bought before 1 July 1998, in connection with the introduction of a new base for calculation of property taxes at that time.

Not all tax expenditures have been reduced though, and there are still some tax expenditures that are continuing to increase. An example is fringe benefits, which have increased rapidly during the past 2-3 years.

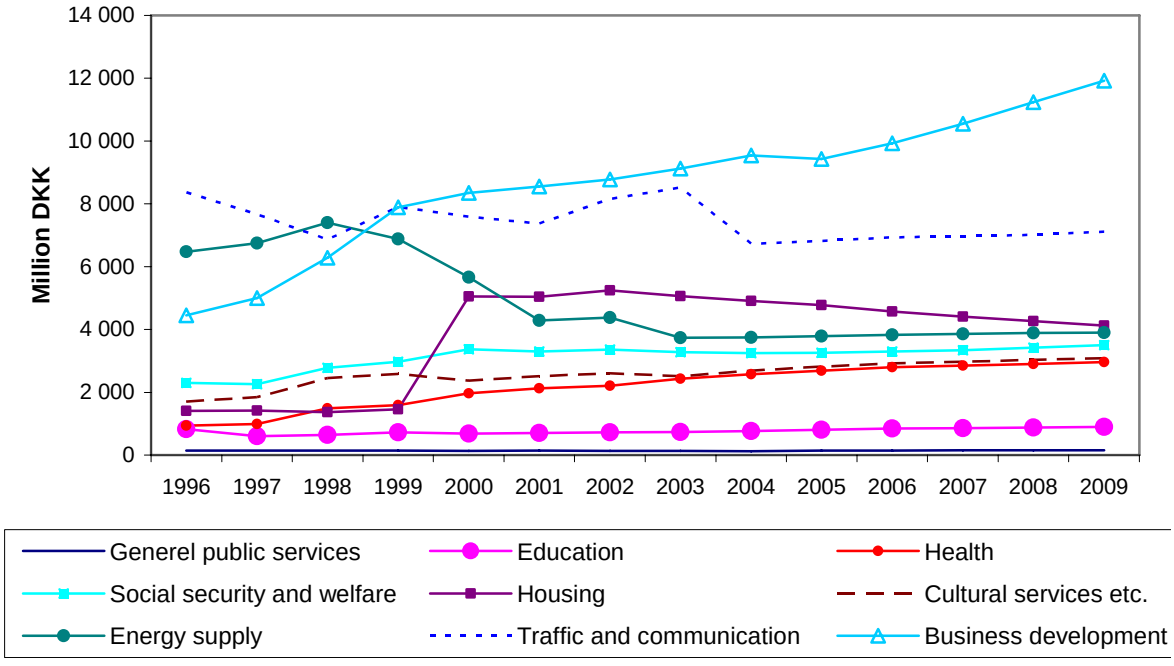
Figure 4.2. Tax Expenditures as a share of GDP – Revenue foregone method



Source: Danish Budget Proposal 1998-2006.
Note: 2007, 2008 and 2009 are estimated figures.

Distribution of Tax Expenditures
When analyzing tax expenditures it is relevant to split the total into categories and show how tax expenditures are distributed between the different purposes. This is done in figure 4.3 and 4.4 where the development from 1996 to 2009 is shown split into purposes.

Figure 4.3. Distribution of Tax Expenditures 1996-2009

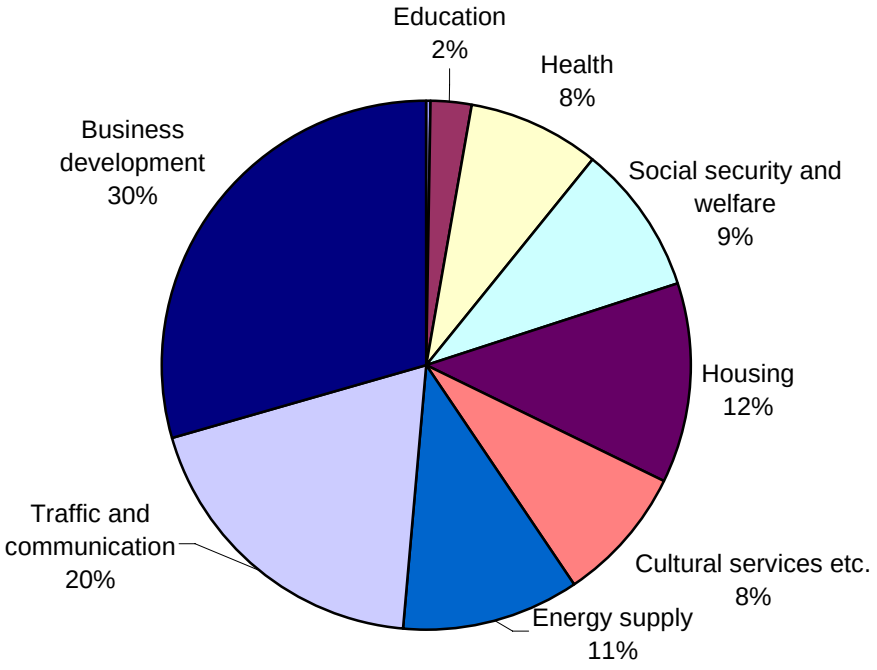


Source: Danish Budget Proposal 1998-2006. 2007, 2008 and 2009 are estimated figures
Note: Defence tax expenditures are added to the category "General public services". Revenue foregone method.

Since 1999 business development has represented the highest level of tax expenditures. In 2007 tax expenditures to business development corresponded to a share of 30 per cent of total tax expenditures.

There has been a relatively rapid growth of tax expenditures in the business development area since 2005. This is partly due to a political priority aimed at stimulating businesses, especially the research and development sector and small and medium seized business. Also tax-deductions for researchers and key-workers represent some of the growth in tax expenditures. Researchers and key-workers recruited from another country are under certain circumstances taxed at a lower tax rate.

Figure 4.4. The distribution of Tax Expenditures 2007



Source: Danish Budget Proposal 2007.
Note: General public services + defence expenditures are left out in the figure because of a share of total tax expenditures in 2007 corresponding to between 0 and 1 pct. Revenue foregone method.

Besides from business development, traffic and communication, housing and energy supply represent areas with a relatively high level of tax expenditures. In 2007 traffic and communication represented 20 per cent of the total tax expenditures.

The developments in the total number of tax expenditures have not been computed.

4.3.6 Challenges and future development

An important element of the Government platform is the tax freeze, which impose restrictions on the tax policy in general and thereby also on tax expenditures. The Danish Liberal-Conservative Government has upon its election in the autumn of 2001 implemented a tax freeze, which means that no tax can be increased. The tax freeze applies for both direct and indirect taxes. For a tax stated in a percentage rate, the rate cannot be increased and for a

tax stated as a nominal amount, the amount in DKK cannot be increased. Reductions in tax expenditures are not within the restrictions of the tax freeze. The tax freeze is not established directly by law, but it commits the Government to abstain from raising any tax.

However, the tax freeze does not completely exclude a necessary restructuring of the tax system. If there are compelling reasons to introduce a new tax or raise an existing one, the revenue resulting from this rise in taxation will have to be used fully to reduce another tax. The same principle will be applied if it becomes desirable, for environmental reasons, to introduce a new environmental tax or raise an existing one.

If Denmark is forced to lower a tax as a result of EU decisions or international agreements, there may be compensated for this reduction by increasing other direct or indirect taxes. Such changes will be required to leave the net revenue from taxes unchanged.

The Government set up a tax commission in 2008 to draw up models for a total tax reform. The resulting tax reform has led to changes in some tax expenditures, especially base broadening in the VAT system and general reductions of the marginal tax rates. The tax freeze will be maintained after the tax reform.

New Benchmark system due to quota system
1 January 2005 marked the start of the EU greenhouse gas emissions trading scheme, which introduced a quota system for CO_2-emissions across the 25 Member States of the European Union. The quota system gives rise to reconsider the benchmark system with respect to the CO_2 tax.

The way the ETS functions there will be no global reduction in CO_2 emissions if you on top of the price of emission rights is burdening emissions directly with a CO_2 tax on fuels or indirectly with a tax on products produced inside the ETS sector (e.g. electricity). However if you on top of the price of emissions rights is burdening emissions with different CO_2 taxes in different countries the consequence is, that the cost of reducing CO_2 emissions inside the ETS sector will be higher than necessary.

A binding quota system will set the level of CO_2 emissions from within the emission scheme. Therefore the Danish policy is to abolish CO_2 taxes on emissions, which already on the margin is burdened with the price of emissions right. It has already been proposed to remove the CO_2 tax on fuels used for industrial process inside the ETS sector.

The quota system gives an opportunity to change the benchmark for CO_2 taxes as well as for taxes on other externalities. This implies that the benchmark is moved towards an optimal taxation scheme. For practical matters the quota price is assumed to be equal to the correct estimate of the environmental cost of CO_2 emissions.

Externalities and tax expenditures when no tax or regulations are applied?
A new tax on emissions of nitrogen oxides (NO_x) will be implemented in 2010. The harmful effects of NO_x emissions have been acknowledged for decades. This gives rise to whether identified externalities should be regarded as tax expenditures when no tax is implemented at all. If "Pigou taxing all externalities" were the benchmark, then - theoretically - this would imply tax expenditures even when no taxes are in place. This approach has not been applied in Denmark, though.

4.4 Tax expenditures in Finland

4.4.1 Introduction

Tax expenditures have been reported in Finland since 1988, when the first report covered the period from 1984 to 1987. In recent years, the connection between the reporting of tax expenditures and the budget process has been loosened. At the same time, the interest in using tax expenditures for distribution of public financial support has increased. This has been seen problematic, and thus the Ministry of Finance has appointed a working group with a mandate to evaluate and improve the treatment of tax expenditure. The term of the working group is 1.5.2008-31.12.2009.

The share of tax expenditures as per cent of GDP has decreased from 14 per cent in 1985 to 7 per cent in 2007. The most significant tax expenditures are in the area of social security, housing and labour income taxation.

Tax expenditures are defined as deviations from the benchmark tax system, which is largely based on the prevailing tax system. The underlying principle is the concept of comprehensive income, where all income is taxable and the tax base is thus as wide as possible. The benchmark tax system is defined in personal income taxation, taxation of corporate income and other enterprise income, value added taxation and excise duties. In calculating tax expenditure, the revenue foregone method is used.

4.4.2 Definition of tax expenditures

The definition of tax expenditures in Finland is based on a working group report published by the Ministry of Finance in 1988. Tax expenditure refers to indirect support, which is incorporated in the tax system, i.e. when a tax provision departs from the basic structure of taxation for support purposes. On the other hand, if a tax provision leads to a form of taxation more strict than normal, this is considered a tax sanction. Tax expenditures are defined as deviations from the benchmark tax system. The benchmark system is in principle based on comprehensive income, so that all types of income should be taxed and the tax base should be as broad as possible. For practical reasons the benchmark system is nevertheless quite near the prevailing tax system. When the prevailing tax system undergoes changes, the benchmark system also changes.

The benchmark tax system is defined in personal income taxation, taxation of corporate income and other enterprise income and value added taxation. For excise duties there is no general benchmark. Instead it is defined individually for each excise duty, for which tax expenditures are calculated (currently there are only tax expenditures in motor car taxation and in no other excise duties). There is no benchmark tax system for real estate tax, inheritance tax or social security contributions. Tax expenditure calculations include general government taxation, municipal taxation, church taxation and contributions paid by individuals to the Social Insurance Institution[25].

In personal income taxation, income is in principle largely taxable and tax liability is thus as comprehensive as possible. The deductions are only related to actual costs. The benchmark

25 Although there is no reference system for social security contributions, the contributions paid to the Social Insurance Institution can be included in the tax expenditure calculations, since they are included in the income taxation.

tax system also includes imputed income and income transfers. All exemptions from the income tax are considered tax expenditures. Since 1993 Finland applies dual income taxation of capital and earned income. Dual income taxation is considered part of the benchmark system, including the splitting of income of the self-employed, partnerships and agricultural income. Progressive taxation of earned income, including a standard deduction for low income earners, is also considered part of the benchmark. The tax rate schedules are incorporated in the structure of the benchmark in such a form as they have been laid down at any one time.

In income taxation, the prevailing tax rates define the benchmark. In capital income taxation, the prevailing tax rate is 28 per cent. The deduction of interest in personal income taxation is not considered part of the benchmark system and thus creates tax expenditure. Capital gains taxation in realisation without taking inflation into account is considered part of the benchmark. Neither the capital gains taxation nor the treatment of losses create tax expenditures or tax sanctions.

The definition of tax expenditures in the taxation of business profits and income from professional activities is based on the principle that income is largely subject to tax. Furthermore, the allocation of income and expenses is closely linked to the accounting principles. Losses can be carried forward 10 years and this is taken as part of the benchmark. Regarding to the depreciation of buildings and machinery over their technical economic life, currently the tax expenditure is calculated based on the depreciation of machinery. In Finland, the norm depreciation is 15 per cent whereas the prevailing provisions allow for 25 per cent depreciation.

In corporate income taxation the benchmark is the prevailing tax rate, 26 per cent. The tax exemption on public companies is considered part of the benchmark tax system. The situation is the same when it is question of communities that complete the operations of public organisations (e.g. national unemployment fund). The prevailing system of partial double taxation of dividends is considered part of the benchmark system. (That is 70 per cent of the dividends from listed companies are taxed as capital income. In unlisted companies the yield of 9 per cent to the mathematical value of the share is tax exempt up to 90 000 euro, 70 per cent of the rest being taxed as capital income. From the 9 per cent exceeding yield, 70 per cent is taxed as earned income according to the progressive taxation.)

In value added taxation the benchmark tax system is a broadly based, multi-stage (with input VAT deduction) value-added tax, collected according to the destination principle (that is with exports exempted and taxation of imports). The standard VAT (22 per cent) rate is part of the benchmark, and deviations from the standard VAT tax rate create tax expenditures. Exemption from VAT is considered part of the benchmark system (e.g. financing, education, public or publicly supervised social and health care). Tax exemption for enterprises with turnover below 8 500 euro, and without voluntary registration, as liable for VAT is not considered as tax expenditure. The graduated tax relief for enterprises with turnover between 8 500-22 500 euros creates tax expenditure.

Tax expenditures from excise duties arise only in departures from the standard level of excise duties (only in motor car taxation; e.g. support directed to disabled people or taxi drivers). There is no special benchmark taxation system in the excise taxation. In energy taxation there are certain provisions that could be considered tax expenditures, but they are not currently included in the tax expenditure calculations.

4.4.3 Methods of calculation

The Government Institute for Economic Research performs the tax expenditure calculations annually. Tax expenditure calculations in personal income taxation are based on a microsimulation model TUJA. In enterprise taxation tax expenditure calculations are based on tax forms data from tax authorities. In value added taxation calculations are based on data from Statistics Finland.

Tax expenditures are measured by the revenue foregone method. The method is applied by leaving each tax expenditure out in turn, and calculating the tax expenditure by keeping the prevailing provisions unchanged. No behavioural effects are taken into account. Calculations are one periodic and any counterbalancing effects in later years are not taken into account. Present value calculation is not applied. The interactions between different taxes and/or tax expenditures are not taken into account.

4.4.4 Reporting and evaluation

Tax expenditures have been reported in Finland since 1988. The first report covered the period from 1984 to 1987. Since then, the report has been published annually. In 1989-1999, the tax expenditure report was published as an appendix to the budget proposal. In 2000, it was moved to the Parliament's Report on the administration of government finances and further in 2005, to the Report on the Central Government Final Accounts, where a summary of the tax expenditures in different categories is presented under the topic Fiscal Policy. The latest report (published in May 2008) covers tax expenditures in 2005 and 2006. At the web page of the Government Institute for Economic Research, a more detailed report on tax expenditures is presented, including estimates for 2008 and 2009. The Report of government's financial statements is presented to the Parliament, but tax expenditures are not systematically discussed as part of the budget process.

The reports on tax expenditures have been utilised for tax reform planning (i.e. the comprehensive income tax reform between 1989 and 1991). It enhanced transparency in public finances; created prerequisites for describing better the public subsidies received by different sectors and facilitated the comparison among alternative forms of subsidies.

There is no comprehensive reporting of public assistance for specific causes, where both tax expenditures and direct budgetary expenditure would be included. The tax expenditures are not reported in connection with subsidies or income transfers that serve the same purpose. It has not been thoroughly evaluated, whether the existing tax expenditures would better reach their objective if replaced by direct expenditure.

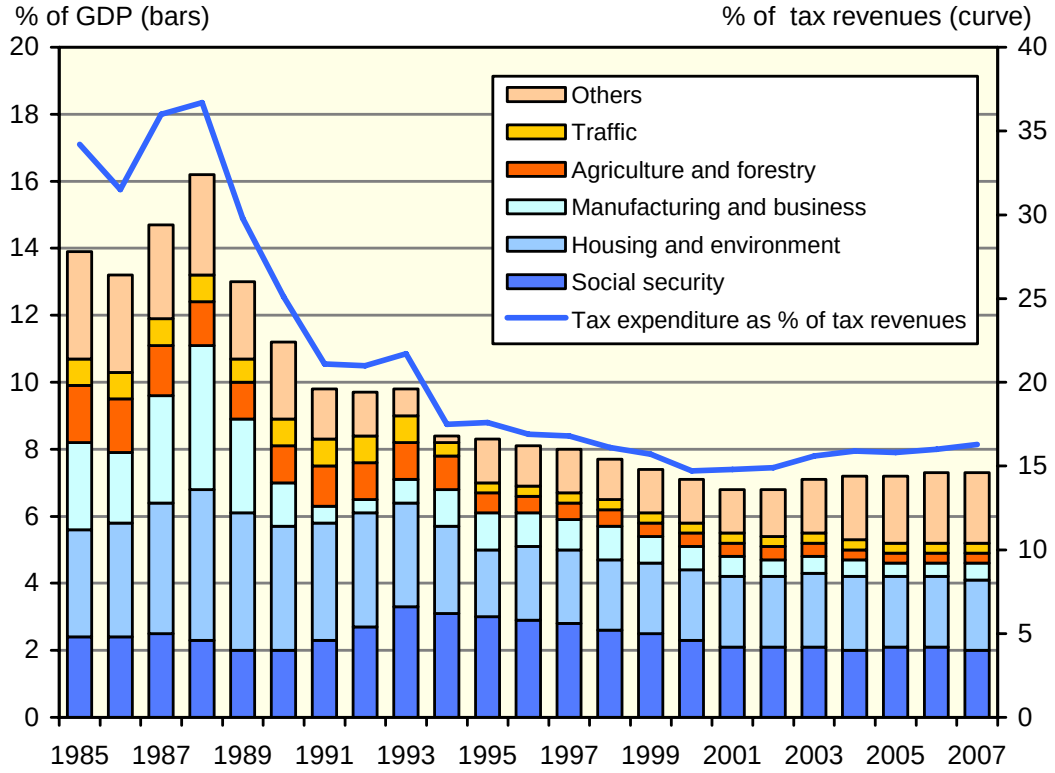
The motivation of each tax expenditure is based on the tax expenditure report, which was published in 1988 (or 1989). The motivation for each individual tax expenditure is presented in the tax law proposal when the tax expenditure in question is first introduced. There is no mention in the legislation about the treatment of tax expenditures in general.

4.4.5 Overview of the most important tax expenditures

Figure 4.5 below presents tax expenditures in Finland in 1985-2007, as per cent of both the GDP and total tax revenue. In 1985 the total sum of tax expenditures was nearly 14 per cent of GDP, and in 2007 only 7 per cent of GDP. The percentage of total tax revenue was 34 and 16, respectively. In nominal terms the amount of tax expenditures has increased 63 per cent,

from 8 billion euros to 13 billion euros. In real prices the amount has, however, decreased from 8 billion euros in 1985 to 7 billion euros in 2007.

Figure 4.5 Tax expenditures in Finland 1985-2007



The number of tax expenditures has remained almost the same in the past 10 years. There were 66 tax expenditures in 1998 and 60 in 2008. Some tax expenditures have been abolished and new ones have been introduced. In the comprehensive tax reform 1986-1992 and the capital income tax reform in 1993, a large number of tax expenditures was abolished and replaced with direct income transfers. The majority of tax expenditures are permanent, but there are a couple of temporary tax expenditures also (i.e. the reduced rates of value-added tax for certain labour-intensive services 2007-2010).

The tax expenditures are classified under 11 operational categories: General Administration (0.1 % of tax expenditures in 2008), Defence (0.0 %), Education, Science and Culture (1.3 %), Social Security (29.4 %), Health Care (1.0 %), Housing and Environment (30.0 %), Agriculture and Forestry (3.8 %), Transport and Communication (3.7 %), Industry (4.4 %), Other Expenses (0.0 %), and Miscellaneous Items[26] (26.5 %). The tax expenditures are also categorised according to the type of tax (Income Tax, Business Taxation, Indirect Taxation). The sum of tax expenditures in each operational category is also reported for the General Government separately.

The most significant tax expenditures in 2008 are the exemptions in the area of

26 This category includes tax expenditures with non-identifiable allocation or distributions into several categories. The largest tax expenditures in this category are the earned income tax allowance and earned income tax credit.

- social security: deduction of employees' statutory pension insurance contributions (1 310 mill. €)
- housing: tax exempt imputed rent of owner-occupied housing (1 900 mill. €) and tax exempt capital gains from selling own housing (900 mill. €), interest deduction of mortgage etc. (900 mill. €)
- taxation of labour income: the earned income deduction in municipal taxation (1 400 mill. €) and earned income tax credit in state taxation (800 mill. €).

The basis for calculating the tax expenditure of tax exempt capital gains from selling own housing is the nominal value of selling prises of houses and estimated holding time of houses. The capital income tax rate (28 per cent) is used. The tax expenditure from the imputed rent of owner-occupied housing is calculated on the basis of the net income from housing, as estimated by Statistic Finland.

There are some problems with the calculation of some specific tax expenditures. In calculating the tax expenditure on deduction of voluntary pension savings contributions, only the deduction (and not the future pension income) is taken into account because of lacking data. This does not give the correct estimate of the total amount of the tax expenditure. The same problem concerns the deduction of employers' statutory pension insurance premiums. The calculation of tax expenditure of depreciation gives also the wrong amount on the true subsidy effect to the enterprises. It only tells us how much the public sector looses tax revenues in a specific year.

4.4.6 Challenges and future development

In the past 20 years the attitude towards tax expenditures has been quite reserved. In recent years the opinion on directing public expenditure as tax expenditure has however changed somewhat. There has been an increasing amount of requests for new tax expenditures, and as a consequence, new tax expenditures have been introduced. At the same time, the distance between tax expenditure reporting and the budget process has grown.

As the role of budgetary spending limits in controlling public expenditure has increased, using tax expenditures seems to have grown more attractive in recent years. This is, of course, not the meaning of the spending limits since as well as direct budgetary expenditure, also tax expenditures are used in allocating public means for different targets, and thus should be under public scrutiny. The National Audit Office and the Parliamentary Audit Committee have both taken notice on the reporting tax expenditure, and there clearly is a need for a more extensive discussion of tax expenditure. The Finnish Ministry of Finance has on the 1st May 2008 appointed a working group with a mandate to evaluate, and suggest improvements to, the treatment of tax expenditures. The work is due by the 31st of December 2009. The working group is expected to propose major changes in the way some central tax expenditures (e.g. dividend taxation, fringe benefits) are defined nowadays. Totally new tax expenditures will be introduced in the areas of excise duties, real estate tax, transfer tax, social security contributions and inheritance tax.

4.5 Tax expenditures in Norway

4.5.1 Introduction

Norway has reported tax expenditures annually since 1999 in the national budget (St. meld. nr.1 (Nasjonalbudsjettet)). The purpose of reporting tax expenditures is to obtain a greater degree of transparency regarding political priorities and financial support to different groups or activities. Tax expenditures (tax sanctions) are defined as exemptions from the general rules in the tax system that imply lower (higher) tax revenue due to a more gentle (stricter) taxation of certain groups or activities. Norway has chosen a pragmatic approach by using the general rules in the tax system as the reference system, instead of a more idealistic or theoretical norm. This approach is probably one of the reasons that the issue of tax expenditures attracts only moderate attention in Norway. On the other hand the informational value of tax expenditures calculated in this manner is limited to a rough estimate of the revenue loss of the tax provision in question. Most tax expenditures can be considered as tax provisions with a clear element of subsidy, and many of these could easily be replaced by spending programs. There are also a few examples of tax incentives (e.g. R&D expenses and savings schemes).

4.5.2 Definition of tax expenditures

The definition of the reference tax system that constitutes the benchmark in the annual tax expenditure analysis in Norway is rather vague and is based on the general tax system. Hence Norway does not operate with a normative tax system in order to identify tax expenditures. The general tax system is heavily influenced by the low rate/broad base approach and the fundamental principles of equality, neutrality and symmetry. This implies that all types of income and all assets should be taxed, and the tax base should be as close to real values as possible. This approach has made tax expenditures a subject of very little controversy in Norway, because the definition of tax rules and tax bases that constitutes the reference system is based on clearly identifiable tax rules and a straight forward definition of (otherwise taxable) income. On the other hand it has probably also led to a minimal consciousness about tax expenditures in the tax policy work.

The reference system is defined in an appendix to the National Budget 2001(St.meld. nr. 1 (2000-2001) vedlegg 1). The definition states that *"..equal persons, equal activities, equal goods etc., should be taxed according to the same principles. Exemptions from these general rules are regarded as tax expenditures or tax sanctions, unless the deviation can be justified for practical or other superior reasons."*

This implies that the benchmark for personal income is that all advantages from working, including benefits in kind, and all other types of income should be taxed. The personal income tax has two tax bases: personal income and ordinary income. Personal income is defined as income from labour and pensions. Personal income is a gross income base from which no deductions are made, and are subject to a progressive rate schedule. Ordinary income is subject to a flat rate of 28 per cent and includes all types of taxable income from labour, pensions, business and capital exempt any deductions or allowances. This is in line with the principles of the dual income taxation.

Personal income is subject to a social security contribution of 3 per cent and 7.8 per cent of pension and wage income respectively. Contributions from self-employed are 11 per cent of personal income from labour. Personal income for self-employed is a net income where costs

directly related to generation of income are deducted. Deviations from these rates are regarded as tax expenditures. For example is the lower rate for agricultural income considered as a tax expenditure. An employer's social security contribution of 14.1 per cent of wage costs is also included in the benchmark. The contribution is geographically differentiated with lower rates outside the central parts of southern Norway. These lower rates are considered as tax expenditures. Personal income above a threshold (NOK 441 000 in 2009) is subject to surtax. The progressive tax structure, which includes the surtax, is considered as part of the benchmark

Ordinary income is taxed according to a rate of 28 per cent, and this is the benchmark for personal income, capital income, dividends and corporations. There are several accessible deductions and allowances in the computation of tax on ordinary income. Except for costs directly linked to the generation of income, these deductions and allowances are generally regarded as tax expenditures. The basic allowances in income, which contribute to a progressive tax structure, are considered as part of the benchmark.

The benchmark for corporate and capital income taxation is that the real profit of an investment is taxed as ordinary income. "Real profit" is however not defined, at least not on an overall level. In the corporate income taxation all deviations from the ordinary tax rate of 28 per cent are regarded as tax expenditures. Dividends and capital gains to persons are taxed according to the shareholder model, where dividends or capital gains exceeding a risk free opportunity rate of interest is taxed as ordinary income. The tax allowance equal the opportunity rate of interest is part of the benchmark, and so are interest rate deductions as they ensure neutrality in capital taxation.

Wealth above a threshold (NOK 470 000 per person in 2009) is taxed at a rate of 1.1 per cent. In the computation of the wealth tax base, assessment values should be as close to real values as possible. Deviations from this principle are regarded as tax expenditures. The low assessment value on housing, for example, is one of the largest tax expenditures in Norway. Inheritance tax with lower rates for close relatives is included in the benchmark. The tax base is the assumed sales values of the inherited assets. Lower assessment values are regarded as tax expenditures. However, due to technical difficulty this tax expenditure is not calculated.

The benchmark for indirect taxes is split in two; excise duties for fiscal purposes and environmental taxes. The benchmark does not take into account differences in efficiency losses, but treats each tax separately.

Excise duties are treated individually which means that a reference rate is made for each tax. Deviations from the standard rate are either regarded as sanctions (if it is higher than the standard rate) or expenditures (if it is lower). Produced factors of production should in accordance with theory of optimal taxation not be taxed. These factors are not taxed in the benchmark for fiscal taxes. Excise duties on production factors will hence normally be treated as sanctions.

The benchmark for the VAT is the standard rate of 25 per cent, and any deviation (reductions) from standard rate is calculated as tax expenditures. Also zero rated sectors and sectors outside the VAT system are normally treated and calculated as tax expenditures. The calculation of tax expenditures from zero-rated areas and sectors outside the VAT system, is based on the difference between levying zero rates and exemptions instead of the reference system with the standard rate.

The general features of the benchmark system for direct taxes have been fairly stable since the 1992 tax reform, as has the general features of the tax system itself. One major change is that the shareholder model is included in the benchmark since the 2006 tax reform. Another change is that the definition of income and the benchmark is stricter, so that more exemptions and allowances are regarded as tax expenditures. As the benchmark is based on the general rules in the tax system, the benchmark changes when the general rates change and when the tax system undergoes reforms.

4.5.3 Methods of calculation

Norway uses the revenue foregone[27] method when calculating tax expenditures. Only tax expenditures in general government taxation are calculated, although the revenue loss will also affect local government income as tax revenue from tax on ordinary income is divided between central and local government.

The actual calculation of tax expenditures in direct taxation is for the most part performed by Statistics Norway, but some tax expenditures are calculated by the Ministry of Finance. Statistics Norway uses a microsimulation model called LOTTE-Skatt when calculating revenue effects from changes in direct taxation and tax expenditures. This model is based on tax returns from a selection of households. Tax expenditures are calculated by calculating tax revenue when one deduction or allowance is removed compared to a reference system where all existing tax expenditures are included.

LOTTE-Skatt calculates most of the tax expenditures in personal income taxation and in capital and wealth taxation. Tax expenditures that cannot be calculated by LOTTE-Skatt are calculated by the Ministry of Finance (although a limited number of tax expenditures are not calculated at all). The Ministry also calculates some tax expenditures with a time horizon. The tax expenditure related to employee premiums and contributions to occupational pension schemes are calculated as a present value. The same method is used for tax expenditures related to depreciation rates higher than what is assumed to be the real depreciation rate.

Tax expenditures related to indirect taxes are not calculated by models, but by ad hoc methods based on sectoral statistical information and information from tax administration systems. Tax expenditures related to environmental taxes are calculated by deviations from the reference rate that normally is set in accordance with the estimated external costs. Areas that are exempted from taxes but subject to other significant measures, for example quotas, are not normally treated as tax expenditures.

Challenges in calculating indirect tax expenditures are, among others, to decide to what degree goods are consumer goods and/or production factors and how to treat taxes that combine fiscal and environmental objectives.

4.5.4 Reporting and evaluation

The tax expenditures are reported annually to the Parliament in the National budget (St.meld. nr. 1). They have been reported since 1999, when tax expenditures for 1998 were presented. The first report did not contain a complete list of tax expenditures, and only a few were

27 See definition in 1.2.1.

calculated. In the following year more tax expenditures were reported and calculated, and several deductions and allowances that previously were not regarded as tax expenditures were included. In the first report the tax expenditures were classified according to purpose. Since 2000 the tax expenditures in direct taxation have been classified according to taxable base. Expenditures in indirect taxation are classified according to both the tax type (VAT, excises) and objectives (fiscal, environmental/health). Today the report contains a short description of all exceptions and deviations from the benchmark system, and the revenue effect is calculated when possible. The description is neutral and the tax expenditures are not justified in any way.

Norway operates with a balanced budget rule, which is formulated as a structural non-oil central government budget deficit. This deficit shall over time correspond to the expected real return, estimated at 4 per cent, on the Government Pension Fund – Global (the former Petroleum Fund). However, the guidelines also allow fiscal policy to be used actively to counter fluctuations in economic activity. This budgeting method implies that the government has a choice between tax expenditures and direct expenditures as policy instruments. It also implies that reduced taxes and tax expenditures imply less revenue to be distributed on the spending side of the budget.

The decision making process on new tax expenditures is the same as direct transfers, which requires a majority in the Parliament. But once the tax expenditures are in place they are not subject to the same scrutiny. All the tax expenditures are permanent, and as opposed to direct transfers, where block grants are common, tax expenditures are always open-ended, which make them more difficult to project and control. Tax expenditures reflect political priorities, just as direct transfers do. By publishing the tax expenditures the amount of governmental support to different groups becomes more evident. But the tax expenditures are for the most part not published side-by side with direct expenditures in the budget, and they are less likely to undergo rigorous review and repeal. The exception is a chapter in the National Budget where direct transfer and tax transfers to different industries are reported together under the heading “industrial support”.

Even though the purpose of reporting the tax expenditures is to obtain a greater degree of transparency regarding political priorities and financial support to different groups or activities, there are no attempts to assess whether the targeted groups of the tax subsidies really are the beneficiary, or if the tax incentives alter behaviour in the desired direction. There are still some examples of more thorough evaluation of some tax expenditures. The tax allowance for R&D expenses, for instance, has been thoroughly evaluated by Statistics Norway. The Tax Committee, appointed by the Government in order to evaluate the objectives and principles applicable to the tax system prior the tax reform of 2006, also looked into several tax expenditures. The committee’s recommendation was to abolish a wide range of tax expenditures in order to secure a broad tax base and horizontal equality of taxation (with equal taxation of persons with the same tax liability).

In general the politicians are hesitant to use tax incentives and most tax incentives in corporate and business taxation where abolished in 1992. Although there are several relieves and allowances that can be regarded as tax expenditures, few of them can rightly be defined as tax incentives. None the less, some saving schemes (BSU, retirement saving) and the allowance for R&D expenses are examples of the opposite.

4.5.5 Overview of the most important tax expenditures

In 2008 Norway had 60 calculated tax expenditures and 5 calculated tax sanctions. The actual number was higher, as there are several tax expenditures that are not calculated due to technical difficulty. When calculated by the revenue foregone method, the tax expenditures for 2008 add up to almost 16 billion Euros. This corresponds to 12.6 per cent of total tax revenue and 5.4 per cent of GDP. It should be stressed that these numbers must be interpreted with care as neither behavioural effects nor interaction effects are taken into account.

During the last 10 years an increasing number of deductions and allowances have been defined as tax expenditures. This, of course, has contributed to an increased number of tax expenditures, although the actual revenue effect is the same regardless of whether they are regarded as tax expenditures or not. Some examples of such allowances are the childcare expense deduction and the tax allowance for commuters' daily work travel and visits to main residence, which were not regarded as tax expenditures until 1999. The same applies to the tax expenditure related to the geographically differentiated employer's social security contribution. These tax expenditures are now some of the most significant tax expenditures in Norway.

The tax expenditures are also growing in size, at least on a general basis. A substantial part of this growth can be attributed to growing tax basis and growing tax revenue, but some changes in tax policy have also contributed to this development. This particularly applies to tax expenditures in capital income tax. The taxation of imputed income of owner occupied housing was removed in 2005. This policy change led to more than a doubling of the tax expenditure related to income taxation on own housing and vacation property. The tax expenditure related to the wealth tax on housing and vacation property also has grown significantly. Much of this is due to exceptional growth in marked values on properties, without an equal growth in assessment values. There has also been considerable growth in the tax expenditure linked to the tax relief on employee premiums and contributions to occupational pension schemes. Increasing employment is the cause of a substantial part of this growth, but the introduction of compulsory occupational pension in 2006 has also been of importance. The tax rules for shipping companies were changed in 2008, with effect from 2007. The shipping companies are now exempted from ordinary capital income tax, whereas they earlier had a tax deferral arrangement. The tax expenditure in personal income has been more stable, although some tax expenditures have grown and some have been reduced. Also, some tax expenditures have been abolished and new ones have been introduced.

The Norwegian VAT-reform from July 2001 broadened the VAT-base substantially by including services in the VAT base on a general basis. Since the establishment of the Norwegian VAT-system in 1970, services in general were not inside the scope unless if specifically listed in the VAT-law. A low VAT-rate on food was also introduced as a result of the reform in 2001. The tax expenditures in the VAT system in 2002 were estimated to about NOK 11 515 mill. (1 300 mill. €). Several sectors have been included in the VAT-base since 2002, e.g. accommodation, travel agencies, broadcasting and cinemas. These sectors have been included in the system with a reduced rate of 8 per cent, and are therefore still a source to tax expenditures. Recent increases of the VAT rate, latest from 24 to 25 per cent from 1. January 2001, has also contributed to increased tax expenditures.

The main tax expenditures in the VAT arise because some sectors are (i) outside the VAT-system, (ii) inside the system with a lower rate, or (iii) inside the system with a rate equal to

zero (zero-rate). The tax expenditures calculated for sectors outside the VAT-system are estimated to about NOK 1 410 mill. (160 mill. €) in 2008. The tax expenditures calculated for sectors with a lower rate are estimated to about NOK 12 225 mill. (1 380 mill. €) the same year. The bulk of this expenditure is due to the reduced rate on food (14 per cent vs. the general rate of 25 per cent). The tax expenditures due to zero-rated areas are estimated to about NOK 3 250 mill. (370 mill. €). This is mainly related to zero rating of newspapers, books and periodicals.

The main tax expenditures in the personal income tax include additional personal allowance for one-income families and sole parents, childcare expense deduction and tax allowance for commuters' daily work travels and visits to main residence. All these tax expenditures are calculated by LOTTE-Skatt and are estimated to about NOK 1 755 mill. (200 mill. €), NOK 1 960 mill. (220 mill. €) and NOK 1 510 mill. (170 mill. €) respectively in 2008. The main tax expenditures in capital income tax include deductions for employee premiums and contributions to occupational pension schemes, lacking income taxation on own housing and vacation property, lower assessment value than real value on housing and vacation property and tax exemption for ordinary capital income tax for shipping companies. The tax expenditure related to pension premiums is calculated as if the deposit had been paid out as wage income and saved in a bank. The disbursement will be taxed as pension income, and this is taken into consideration when calculating the present value of the tax savings. This tax expenditure is an example of a tax incentive and was estimated to NOK 18.2 billion (2 billion €) in 2008. The calculation of the tax expenditure related to lacking income taxation on own housing is based on marked values on marketed houses over a five year period. Market values on vacation property are estimated by assuming that market values are four times higher than assessment values. The tax expenditure is calculated by assuming a real return of 5 per cent rate on the investment and was estimated to NOK 58 billion (7 billion €) in 2008. These calculated marked values are also used when calculating the tax expenditure related to lower assessment value than real value on housing and vacation property, which were estimated to NOK 26 billion (3 billion €) in 2008. The favourable tax rules for shipping companies are estimated to constitute a tax expenditure of NOK 2.4 billion (270 mill. €) in 2008. This estimate is based on annual accounts over a four year period. The regionally differentiated employers' national insurance contribution also represents considerable tax expenditures in Norway, estimated to almost NOK 10 billion (1.1 billion €) in 2008. The calculation is based on reported wage payments by employers.

Tax expenditures from excise duties sum up to about NOK 16.5 billions (1.9 billion €) with approximately NOK 10.5 billions (1.2 billion €) linked to environmentally and health related excise taxes. The main sources are the excise tax on energy consumption, taxes on alcohol and tobacco, and a lower tax rate on diesel fuel than petrol.

There are also calculated tax sanctions related to excise taxes on totally NOK 4.4 billions. The largest sanction is the CO_2-tax on petroleum related activities which partly is committed to a quota-regime. In addition to taking account of alternative measures, corrections are done for other reasons, for instance for activities that can be deducted from the special tax on petroleum activities, and that part of the CO_2-tax is paid by the governmental institution that manages the ownership of the Norwegian state. This illustrates the complexity of calculations and the numbers of consideration linked to tax expenditures/sanctions.

4.5.6 Challenges and future development

The conceptual idea of producing tax expenditures is to provide a framework from which to evaluate the equity, efficiency and administrative issues raised by new or existing tax rules. However, as previously described in this report, practical, and to some extent theoretical, difficulties related to defining the "normal" tax system from which the definition of tax expenditures arises, weakens this ambitious objective. The purpose of producing and reporting tax expenditure estimates in Norway is not very clear, and the list of tax expenditures is presented each year in the annual budget for informational purposes. The normal tax system (the benchmark) is vaguely defined in general and is more or less based on what constitutes the general tax law. The methodology is somewhat unclear and lacks the necessary stringency when applied to different tax expenditures. The absence of behavioural effects and accounting periods makes the magnitudes of the estimates unreliable. Hence the annual tax expenditure analysis in Norway must be considered as inadequate to fulfil such ambitious goals mention above. At best the reporting of tax expenditures in Norway gives a rough overview of the relative importance of the main deviations from what can be considered as the "general" tax legislation. A tax expenditure estimate is only adequate for efficiency and distributional analysis if the reference system constitutes an efficient or fairly redistributive tax system. So the informational value of tax expenditures in the sense of equity or efficiency costs is only as good as the reference system. On the other hand, the general corporate and capital income tax law in Norway is fairly neutral, and the taxation of labour income and wealth is quite progressive compared to the majority of OECD-countries. This increases the informational value of the estimated tax expenditures. However, the link between the methodology used for producing tax expenditures and the informational value of the tax expenditures needs to be clarified.

4.6 Tax expenditures in Sweden

4.6.1 Introduction

The Swedish Government has since 1996 reported tax expenditures (and tax sanctions) to the Parliament annually in conjunction to the Spring Fiscal Policy Bill. The main objective with the reports is to illuminate the implicit support given on the budget revenue side. The tax expenditure reports may hence serve as a basis for prioritising among different policy areas. In the autumn, as supplements to the Budget Bill, the tax expenditures are re-reported within each policy area. There is also an expressed desire to describe the degree of uniformity among the tax rules. Such a description, as well as the illumination of implicit support, requires that a benchmark is specified. The Swedish benchmark for tax expenditures aims to build on the principal of uniform taxation. Deviations from the benchmark are considered tax expenditures and tax sanctions, which are estimated and presented. In general both revenue forgone and equivalent outlay are estimated and presented.

The current benchmark is relatively simple to apply and communicate. A strict application of the benchmark is rather inflexible, however. It does not consider the motives behind tax expenditures. From an economic efficiency viewpoint it may, however, be warranted with taxes deviating from the benchmark. The Swedish Government intends to initiate further development of the benchmark in a direction where economic efficiency and optimal taxation receive greater attention.

4.6.2 Definition of tax expenditures

The Swedish benchmark builds on the principal of uniform taxation, which was one of the cornerstones of the tax reform in 1990-91. The principle implies that each type of tax should be levied uniformly and without exemptions. Deviations from the principle constitute tax expenditures (or tax sanctions). The benchmark evolves with the tax system and is constantly under revision. For example, in 2003 there was a major overhaul of the excise duty benchmark. The Swedish tax expenditures can be divided into four tax areas; income taxation, indirect taxation of labour income, VAT and excise duties. The benchmark differs between the tax areas.[28]

There is no single benchmark tax rate for income taxation. Labour income, capital income and income from businesses may be taxed at different rates. The benchmark does however stipulate that the taxable income should correspond to the SHS income concept, i.e. income equals all consumption expenditures and the change in net wealth. Empirically, the Haig-Simons income is hard to measure and in order to make it operational further clarifications have been made. These include among others;

- Savings should be done with taxed incomes.
- Capital gains/losses should be taxed on accrual and not at realisation.
- The value of non-wage household work and leisure shall not be part of the tax base.
- Public payments are part of taxable income.
- The implicit return to owners of homes and condominiums is part of taxable income.
- Depreciation allowances in businesses should be based on true depreciation.
- Only interest payments made for loans where the investment return is taxable should be deductable.

In addition, the benchmark stipulates horizontal uniformity rather than vertical as different degrees of progressivity in the tax schedule are considered consistent with the benchmark. Moreover, tax credits are included in the benchmark if they are general and do not favour specific groups of tax payers. Tax reductions due to interest payments and the in-work tax credit are, for example, part of the benchmark.

The benchmark for indirect taxation of labour income is that Social Security Contributions (SSC) or SSC paid by the self-employed and the general pension contribution paid by the employee[29] should be levied on all remunerations which give eligibility in the social security system. Remunerations not giving eligibility are subject to a 'special tax on certain earned income and pension costs'.[30] For each type of contribution/tax there is only a single rate in the benchmark.

The VAT benchmark consists of a single rate, the standard VAT rate 25 per cent. All commercial good and service transactions should be taxed at this rate. There are, however, a few exceptions to this benchmark. The VAT exemption on letting property is considered as a part of the benchmark since such taxation would imply unequal treatment of rented and owned housing. The VAT exemption of financial and insurance services is considered to be part of the benchmark. Goods and services which are subsidised by public funds are not

28 The Swedish Government Official Report "Förmåner och sanktioner" (SOU 1995:36) and the Spring Fiscal Policy Bill of 1997 discuss the benchmark more thoroughly.

29 Allmän pensionsavgift.

30 Särskild löneskatt.

taxable when the net VAT is negative and not considered as tax expenditure. Finally, for international transactions the principle of destination is considered the benchmark. VAT should hence be levied in the country where the good or service is consumed.

For excise duties, only energy and CO_2 taxes including the tax on thermal effect levied on nuclear reactors (a tax sanction) are considered when tax expenditures are calculated. Prior to the 2003 overhaul of the benchmark more duties were included. It was decided that only duties with large tax bases were to be included in the tax expenditure reports. If an excise duty would, under a uniform rate, give rise to at least one per cent of the total tax revenue its base is considered large.

The benchmark for energy tax is that all energy consumption should be levied the same tax per kWh. Electricity and other sources of energy may however be taxed at different rates. Moreover, it is consistent with the benchmark to differentiate between heating and fuel consumption.[31] The rationale being that the tax on fuel also, besides serving fiscal purposes, captures some of the societies' cost of road traffic, e.g. wear and tear on roads, noise and accidents. The benchmark for electricity consumption is the normal tax rate on electricity. For other energy sources used for heating purposes the benchmark is the heating oil tax rate. For energy resources used as fuel, the tax rate of petrol constitutes the benchmark.

The CO_2 tax should according to the benchmark be levied proportional to emissions. The benchmark tax rate is the normal CO_2 tax rate regardless the source of energy and usage. There are, however, exemptions to the benchmark tax rates. Fuel used as an input in the industry is exempted from tax and this exemption is not considered tax expenditure. The energy tax on electricity is only applied to the usage of electricity and a tax exemption of fuel used in the production of electricity is therefore not considered tax expenditure.

4.6.3 Methods of calculation

In Sweden, the Ministry of Finance calculates, or rather estimates, the tax expenditures yearly. The calculations are based on accrual accounting. Levy shifting is thus not considered. Moreover, the calculations are static and disregard any behavioural effects that the tax system may have on economic agents. Possible interactions between taxes are disregarded as well. The tax expenditures are divided into two broad categories: expenditures which would affect the budget balance if they where abolished and expenditures which do not. For the former category, which includes most tax expenditures, both the revenue forgone and the outlay equivalent are calculated. For tax expenditures not affecting the budget balance, i.e. tax exempted transfers, only the outlay equivalent is calculated. The revenue foregone is readily available on the expenditure side of the government budget.

4.6.4 Reporting and evaluation

Since 1996 the Swedish Government reports the tax expenditures (and sanctions) to the Parliament once a year. From 2008 the tax expenditures are reported in a Government Communication in conjunction with the Spring Fiscal Policy Bill. Earlier the report was a supplement to the Bill. In the autumn, as supplements to the Budget Bill, the tax expenditures are re-reported within each policy area. The primary objective for reporting the tax expenditures is to make the implicit support to different policy areas visible. As such it may

31 Fuel refers here to the use of energy resources for the propulsion of vehicles.

serve as a basis for prioritising among different policy areas. The tax expenditures are, however, not an integrated part of the budget process.

As mentioned above the tax expenditures are divided into two broad categories. In addition to this division the budget balance affecting expenditures are classified according to their tax base and presented in subgroups. Moreover, the expenditures are also classified with respect to their general purpose. In this respect, a distinction is made between technically or administratively motivated tax expenditures and politically motivated tax expenditures.

4.6.5 Overview of the most important tax expenditures

In 2009 some 115 tax expenditures and tax sanctions were reported. The estimated tax expenditures were around 25 billion euros. This corresponds to around 8 per cent of GDP and 17 per cent of total tax revenues. These figures, as well as later figures, should be interpreted with care, especially if different years are compared. For several reasons the reports of tax expenditures are not complete. For example, data used for some calculations may be insufficient. In addition, there may be tax expenditures not included in the reports. Typically, a couple of new expenditures are added each year due to changes in the tax system whereas some tax expenditures will cease to exist or simply expire. In 2008 the estimated tax expenditures were 16 per cent of the total tax revenue, but the three preceding years the shares were only 11 to 13 per cent.

Two of the largest tax expenditures in 2009 are associated with tax on capital income and owner occupied housing. First, the implicit real return to owners of homes is not taxed as capital. Instead a municipal fee, designed as a tax, is paid. The revenue forgone due to this differential treatment is estimated to around 2 billion euros. In order to estimate the tax expenditure, real returns are calculated based on the market value of the properties and the real government interest rate. The difference between the capital income tax on these returns (if they were to be taxed) and the fees paid under the current system amounts to the tax expenditure. Second, capital gains from housing are taxed upon realisation. Under certain circumstances the gains, and hence the tax, may be deferred even further. At the present, 1.67 per cent of the deferred amount is taxed as capital income. The difference between these rules and the rules for taxation of deferred capital incomes is considered tax expenditure. The deviation from the benchmark is estimated to 1.7 billion euros in foregone revenue.

Three other large tax expenditures involve VAT, indirect taxation of labour income and energy taxes. For food items there is a reduced VAT. Instead of the normal tax rate of 25 per cent there is a 12 per cent VAT levied on food items. The difference between the tax rates is considered tax expenditures, estimated to about 2 billion euros. For persons under the age of 26 (at the beginning of the year) there is a reduction in social security payments. There is also a reduced energy tax on electricity used in industry production. These latter tax expenditures have an estimated forgone revenue of 1.4 billion euros each.

4.6.6 Challenges and future development

The Swedish National Audit Office (NAO) has pointed out some shortcomings in the treatment of tax expenditures.[32] There is a lack of transparency and it is not well suited for its purpose. Moreover, the principles behind reporting and calculating the tax expenditures are

32 Riksrevisionens RiR 2007:3 ”Regeringens beredning och redovisning av skatteutgifter”.

not suited for continuous evaluation of different tax expenditures. According to NAO the Government ought to consider how tax expenditures should be treated in the fiscal process. These issues are considered in the continuous development of the treatment of tax expenditures in order to make them more visible and an effective tool in the fiscal process. Besides this continuous developmental work a more fundamental methodological issue is on the rise.

The current benchmark is relatively simple to apply and communicate. A strict application of the benchmark is rather inflexible, however. It does not consider the motives behind tax expenditures. From an economic efficiency viewpoint it may, however, be warranted with taxes deviating from the present benchmark. For example, taxes that correct for market failure by internalising external effects. Moreover, certain tax expenditures may expand the tax base and in the end increase welfare. A lower – than the benchmark – tax may be motivated if the deviation increases, directly or indirectly, hours worked. This would increase the labour income tax base. Deviations like these, based on a principle of optimal taxation, could contribute to higher welfare. Under the current benchmark such deviations are considered tax expenditures. It could be questioned if such a rigid interpretation of the benchmark and tax expenditures is appropriate. The Swedish Government intends to initiate further development of the benchmark in a direction where economic efficiency and optimal taxation receive greater attention.

5 Conclusions and suggestions for future work

In section 2 we present the concept of tax expenditures, originally defined by Stanley Surrey in the late sixties. Surreys' main objective was increased expenditure control by identifying a range of tax provisions that escaped the scrutiny applied to regular subsidies and transfers on the expenditure side of the budget. This objective is still the core of any tax expenditure analysis. An extensive review of all kinds of deviations from the general tax system is crucial in order to get a full picture of public provisions that consists of both direct public transfers and favourable tax treatments. Since the first tax expenditure analysis was presented in the US more than forty years ago, the concept of tax expenditures has spread worldwide and today virtually all OECD-countries make tax expenditure analysis in one form or another.

Using tax expenditure analysis in the tax policy work to pursue these idealistic principles of the tax system is highly ambitious, and would require a benchmark developed from these principles. In other words ideally you need to define a normative tax system which reflects the principles of efficiency, fairness and simplicity, both in the rate structure and in the definition of income, and then be able to operationalise it in an estimation procedure. Of course this is not an easy task, and in practice the ideal principles have been proven difficult to accomplish. As discussed in section 2, tax expenditures have been vividly discussed and criticised among other things for the difficulties to establish a commonly accepted benchmark.

The examination of tax expenditure analysis of the Nordic countries above shows that the levels of ambitions are fairly similar. Norway aims at "obtaining a greater degree of transparency regarding political priorities and financial support to different groups or activities". Sweden has the most ambitious goal, namely to "to illuminate the implicit support given on the budget revenue side", but also "an expressed desire of describing the degree of uniformity among the tax rules". Finland and Denmark do not express the goal explicitly, but Denmark seems to have a fairly pragmatic reference system, and Finland use a methodology which to a large extent seems to be comparable to the Norwegian methodology. The National Audit Offices in Finland, Denmark and Sweden have to some extent criticised the tax expenditure analyses for not being sufficiently transparent.

The working group thinks it is crucial to ask; what do the tax expenditure analyses in the Nordic countries really tell us? Originally the ambitious goals of making tax expenditure analyses formulated by Surrey were among other things to draw reliable conclusions about effectiveness, equity or other desirable features in the tax system. Conventional methods of calculating tax expenditures presented in this report are insufficient in fulfilling these ambitious goals, and in practice the goals with tax expenditures are much more modest as indicated above. The Nordic tax expenditure analyses have so far more or less been based on identifying deviations from the basic principles of uniform taxation or the tax system in place. These analyses are therefore less vulnerable to the general criticism regarding the normative assessments of the benchmark. A uniform taxation implies a broad tax base but there could still be problems if real income or real expenses are unobservable. What is the correct depreciation of (different kinds of) real capital? How do you divide business income for self employed in capital income and labour income? What is the correct imputed income from owner occupied housing? Hence there are many examples of tax expenditure calculations that must rely on data that are not always appropriate and relevant.

Potential areas for future development

It has been beyond the capacity of this working group to work out detailed recommendations for a reform of tax expenditure analyses in the Nordic countries. However, the group would like to point at some potential areas where future development efforts may be placed. Based on the findings in this report and also with a reference to the National Audit Offices criticism that the tax expenditure reports to some extent lack transparency, the working group has pointed out some areas for further development, in order to achieve a higher degree of transparency and probably increase the informational value of the tax expenditure analyses. One suggestion is that the Nordic countries could endeavour to clarify the tax expenditure analysis in future reforms. Another is that more emphasis could be placed on *evaluating* tax expenditures.

A part of a clarification process could be to review the benchmark**.** As stated above we find the benchmarks that constitute the foundations of the tax expenditure analyses to be somewhat vaguely defined in some cases. One way forward could be to base the benchmark on easy identifiable general tax rules, and let the income definition be consistent with either Schanz-Haig-Simons or what would (otherwise) be the taxable income. This would reduce the ambition of making tax expenditure analysis to *identify deviations from the general tax system that generates less tax revenues than it would otherwise have done if the general tax legislation were applied*. This simple benchmark could be combined with efficiency promoting measures in order to create a benchmark that better reflects an economically efficient tax system. A simplified tax expenditure analysis like this could be accompanied by separate efficiency and equity analyses of tax provisions that escape the definition of tax expenditures. This could be done first and foremost in a qualitative manner, and secondly in a quantitative manner if there is a feasible and credible way to measure the welfare loss generated by the tax provision.

The group also suggests having more extensive and more frequent *evaluations* of tax expenditures, in form of periodical reviews of the effectiveness of the measures and the achievements of the intended goals. Both the actual tax provisions and the tax expenditure analyses should be investigated. A comprehensive evaluation of all tax expenditures would of course demand a vast amount of resources (as described in section 3), and is therefore unrealistic. Evaluations should therefore be carried out on a smaller scale, but be specific and targeted and make sure that all tax expenditures are subject to a proper evaluation at some point or another. It could for example be a good idea to introduce a "fixed evaluation date" for all new tax expenditure, say three years after introduction, to make sure that they are subject to proper evaluation at least once, and maybe to increase the consciousness of the politicians about the specific tax expenditure when passing the budget.

Finally the group will encourage properly and open discussions about tax expenditures. A part of this could be to invite academics, tax experts, politicians etc. to comment or analyse the tax expenditures publicly and on a frequent basis. This could help to increase transparency, make the politicians more aware of the tax expenditures and help the civil servants and technicians to improve the tax expenditures analyses.

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7 Appendix - What do other countries report?

See in detail the following overview which is based on OECD (2008/1), p. 39 ff.:

Country	Reporting		Evaluation
	Location of Estimates	**Frequency**	
CANADA	Estimates are displayed in a document separate from the budget, and therefore separate from the amounts of spending outlays for comparable purposes.	Reporting of tax expenditures is not required by law, but Canada reports its tax expenditures each year – since 1997, reports have covered the report year, the five preceding years, and two succeeding years (thus eight years in total). Each cycle's tax expenditures for the three earliest years for the individual income tax, and the four earliest years for the corporate income tax, are developed using final administrative data; the later years' figures are estimates or projections. Tax expenditure figures are produced for calendar years rather than fiscal years. Every four years, Canada produces a detailed enumeration and description of all tax expenditures.	There is no formal mechanism for tax expenditure review by parliament or Cabinet after provisions have been approved in a budget. However, tax measures are reviewed on an ongoing basis within the Department of Finance (and the Canada Revenue Agency, with respect to administrative matters), with technical input as appropriate from line departments. Some measures are evaluated more formally on a discretionary basis, and the results are published.
FRANCE	Tax expenditures are reported each year in the budget act, as an annex, "Ways and Means Evaluation," of the finance bill; and in the finance bill of social security. The presentation in the finance bill of the budget act includes a legal reference for the provision; the number of beneficiaries (when available); the method of evaluation (when available); the reliability of the evaluation; the year of the creation of the tax expenditure, and of the last important modification of it; and the cost for the budget year and two preceding years. In the finance bill for social security, there is a presentation of the provision, a legal reference, the number of beneficiaries, the year of creation, the cost, and whether there is a compensation for social	As noted above, tax expenditures are reported each year in the budget act and in the finance bill of social security. Both the budget act and the budget for social security act report the cost of tax expenditures for the budget year and the two prior years.	The organic law requires that the ways and means annex of the finance bill of the budget present an evaluation of each tax expenditure, but to date such evaluation has been limited to an estimate of cost. A new process of evaluation of tax expenditures began in 2006. However, at this stage of the process, there is concern that there is not yet a working set of performance criteria for those evaluations. The criteria used at present may be too numerous and not fully relevant. Any sunset dates for tax expenditures would be specified in the wording of each individual provision; there is no comprehensive list of measures expiring and the dates of their expirations.

	security for the provision.		
GERMANY	Tax expenditure estimates are submitted within the Federal Government's subsidy report (which covers both tax expenditures and outlay subsidies, although tax expenditures are not presented side-by-side with equivalent outlay programs) every two years, together with the draft budget. (A list of the 20 largest tax expenditures of the central government is attached to the draft budget every year.) These estimates are not integrated with the information on spending programs.	The subsidy report is submitted every other year, and includes tax expenditure figures for the current year, the two preceding years, and one future year.	Germany has begun a process of formal reviews of tax expenditures. The 20 largest tax expenditures – accounting for 92 percent of the total cost of all tax expenditures – are to be evaluated. The evaluations are charged to define the objective of the tax expenditure, including macroeconomic motivations or perceived market failures; determine whether the tax expenditures are effective and efficient, and whether the tax expenditure is the best public-policy instrument to pursue the objective; and to find any side effects for the tax system broadly. Several respected outside research institutes perform the reviews, with the use of multiple reviewers seen as an important guarantee of unbiased analysis. The Ministry of Finance will comment on the reviews, and report the findings to the Parliament.
JAPAN	Officially, the revised estimates for the Special Tax Measures are reported to the Diet annually in the "Summary of Tax Revision" and "Explanation of Tax Revenue and Stamp Duties Budget," which are submitted along with the other budget documents. The aggregate estimates of all Special Tax Measures are also reported to the Budget Committee of the Diet annually, though this is not the official report.	Only the current fiscal year data of the annual changes and aggregate estimates are reported to the Diet. The restriction to reporting of changes leads to some concern that ongoing provisions are "secret subsidies."	Special Tax Measures are reviewed annually by tax officials of Ministry of Finance, mainly focusing on those that expire in the next year due to sunset clauses. Usually, the majority of the Special Tax Measures at the national level are stipulated in the Special Tax Measures Laws to have two- or three-year sunset clauses. These sunset clauses have functioned effectively, because they force tax officials and other related parties to review the contents of the Special Tax Measures regularly. Negotiations between tax officials and the requesting ministries over the Special Tax Measures expiring in the next spring (usually the end of March) begin in September, at the same time as with the budget expenditure negotiations. In many cases, each ministry requests the creation of new Special Tax Measures for their policy objectives. The necessity, effectiveness and efficiency of the measures are scrutinized in the

			negotiations. At the same time, the government Tax Commission, which is an advisory council to the prime minister, deliberates tax policy for the coming fiscal years. From late November to early December, the tax commissions of the ruling parties begin their decisions on tax policies for next fiscal year, including the Special Tax Measures. In this deliberation, the tax officials explain the discussions among the related ministries. In December, Ministry of Finance decides the contents of the tax proposals based on the report submitted by both the government and the ruling parties' tax commissions. The tax bill is usually submitted to the Diet in the next January or February.
KOREA	At present, Korea provides its tax expenditure estimates in a document, the Tax Expenditure Report, which is separate from, and released after, the budget. The Tax Expenditure Report is produced by the Ministry of Finance and the Economy, not by the Ministry of Planning and Budget, which is the agency that produces the budget itself. Thus, tax expenditures are not now presented, and are not likely in 2010 to be presented, side by side with corresponding outlay figures in the budget.	The Tax Expenditure Report is released annually, in keeping with the language of the National Fiscal Act. The National Fiscal Act also mandates that estimates be provided for the year prior to the budget year, the budget year itself, and the year after; however, the requirement is not considered binding until 2010, and projections for the succeeding year have not to date been provided. The retrospective year is based on final data; the current year is a projection. Tax expenditures hitherto have been reported according to functional areas that have not aligned with the functions for the reporting of spending. Recategorizing the tax expenditures, and providing estimates for the succeeding year, are among the leading tasks for the 2010 reporting and process reform.	In addition to the current effort to upgrade reporting on tax expenditures by 2011, the MOFE began in 1999 to report on tax expenditures to the National Assembly, based on a procedure prescribed by the Special Tax Treatment Control Act of 1965.
THE NETHER-LANDS	Tax expenditure estimates are presented in the Tax Plan and Budget Memorandum, which is a part of the budget, but which is separate from estimates of outlay programs with the same purpose as the tax expenditures.	The Tax Plan and Budget Memorandum is presented every year. It provides tax expenditure figures for the budget year, one prior year, and the five succeeding years. The tax expenditures reported for the year prior to the budget year are the final figures for that year. Changes in individual tax expenditures – repeals, new provisions, increases and decreases – are presented.	In 2004, the Netherlands began a program of evaluations of tax expenditures, with the goal of reviewing each tax expenditure approximately every five years. Responsibility is held jointly between the Ministry of Finance and the pertinent spending department. The purpose of the evaluation is to estimate

			the effectiveness and efficiency of the tax expenditure. Questions that are specified for the evaluations to answer include: Does the tax expenditure accomplish its objective? Can the same goals be achieved with lower costs through a different policy instrument? Is the tax expenditure the logical instrument to achieve these objectives? And is the tax expenditure really the cause of any perceived effect, or would the same outcomes have occurred without the tax expenditure? This evaluation program is fully underway, and evaluations already have been produced.
UNITED KINGDOM	The data are reported in Chapter A: Budget Policy Decisions within the government's Financial Statement and Budget Report (United Kingdom, HM Treasury, Financial Statement and Budget Report, 2007).88 More details on individual tax allowances and reliefs can be found in the HM Treasury publication, Tax Ready Reckoner And Tax Reliefs, published alongside the pre-budget report. Estimates are not presented directly alongside outlays for comparable purposes.	Although there is no statutory requirement to produce a report on tax expenditures, the Government still estimates and reports all major tax expenditures in the Tax Ready Reckoner every autumn. And Chapter A of the annual Budget, Budget and Policy Decisions of Financial Statement and Budget Report, contains a list of proposed tax expenditures. No comprehensive historical report exists, but the Financial Statement and Budget Report was first reported following approval of Parliament (for the purposes of Section 5 of the European Communities Amendments Act) in 1993. The "Financial Statement and Budget Report" has been published online only since 1997.	Tax expenditures are reviewed twice a year by H.M. Treasury as part of the Budget and Pre-Budget Report process. This, however, is not a legal requirement.
UNITED STATES	Tax expenditures are presented in the annual budget, but in a section of a budget annex volume (called Analytical Perspectives) that is devoted to revenue issues. Prior to the FY 1990 Budget, they were issued separately in a volume accompanying the budget called Special Analyses. The estimates for particular tax expenditures are thus separate from the figures for spending programs directed toward similar purposes.	Tax expenditures were presented for the first time in the FY 1976 Budget issued in 1975. Since the late 1970s, the tax expenditure tables show seven years of estimates: the two years prior to the year of the budget, the year of the budget, and the four years following the year of the budget. The estimates are currently based on the economic forecast used for the mid-year estimates of the budget and they are not retrospectively revised or updated. Each year's Budget includes listings of all new tax provisions enacted in the preceding year, but no separate listing of new tax expenditures. When	There is no required review of existing tax expenditures. However, many tax provisions (including tax expenditures and structural provisions) – many more than was the case eight years ago – now have sunset dates, and will expire in the next few years (many at the end of 2010). This will require some measure of "reconsideration", if not "review." There has been a once-every-two-years volume of analyses of tax expenditures produced by the governmental but non-partisan

		new tax expenditures are enacted, they are included in the annual presentation, but only a close comparison of the current presentation with that in previous budgets would reveal which of the listed provisions are new. The tables do not identify the new tax expenditures. In the past, the Budget chapter that presents all of the revenue proposals also listed the new tax expenditures, but that practice has been discontinued, because it was difficult to include the proposed tax expenditures in a timely manner. These proposals were often determined at the end of the budget process making it difficult to prepare estimates for them before the budget was scheduled to print.	Congressional Research Service of the Library of Congress; that review does not reflect the views of either Executive or Legislative policymakers. Also, the governmental but non-partisan Congressional Budget Office produces a once-every-two-years volume of potential policy changes to reduce the deficit; the ideas considered inevitably included some reductions or repeals of existing tax expenditures. Tax expenditures receive considerable attention whenever tax reform is on the political agenda. In 2005, the President's Advisory Panel on Federal Tax Reform issued a report calling for the comprehensive overhaul of the tax system, which would have altered drastically many of the largest tax expenditures. This effort at tax reform did not lead to legislation, but the central place of tax expenditures in the reform options is typical of what a general tax reform would produce. In the FY 2008 Budget, and again in the FY 2009 Budget, the President proposed major changes in the tax expenditure for private health insurance.