

Government Institute for Economic Research

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Tax Expenditures in Finland

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TAX EXPENDITURES IN FINLAND

¹ Appendix has not been acted upon by the Government; intended as background material for budget proposal.

Translated by John Rogers and Andrew Lightfoot

FOREWORD

This report, which is a reprint of Appendix 2 to the Government proposal for the 2000 State Budget, contains a description of public support given through the tax system, i.e. tax expenditures. The calculations were performed using VATT's TUJA and YRI models and MATURE database for personal taxation and company taxation and agricultural taxation respectively, and other information sources. The tax expenditure calculations were performed by the following senior researchers: Heikki Viitamäki and Esko Mustonen (personal taxation), Timo Rauhanen (indirect taxation), Tuomo Heikkilä (agriculture and forestry) and Outi Kröger (company taxation). The report was prepared for publication by research assistant Sari Virtanen.

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GOVERNMENT INSTITUTE FOR ECONOMIC RESEARCH

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TAX EXPENDITURES IN FINLAND

Support rendered by means of the tax system results from tax concessions granted in the normal tax system. The purpose of tax expenditures is to support the taxpayer or, indirectly, other actors in the economy. The principle applied in the tax expenditure calculations presented here are described in the Ministry of Finance's publication "Verotuet Suomessa" (1988)². The calculations are published annually as an appendix to the State Budget Proposal. In the present publication, the most recent year covering all the forms of taxation is 1997.

The legislative changes in taxation enacted in 1997 did not significantly affect the overall level of tax expenditures. It was approximately FIM 46 billion.

Analysed by spending category, most tax expenditure was directed at social security. Total expenditure in this category was FIM 17 billion. The largest individual tax expenditures - the pension income deduction in municipal taxation, the deduction of employees' statutory pension contributions and the tax exemption of child benefits - accounted for over 70 per cent of tax expenditure in this category.

Housing and environment accounted for slightly over FIM 10 billion of tax expenditure, which is approximately FIM 800 million more than in the year 1996. It consisted of the deduction of interest expenses on housing loans, the tax exemptions of housing support and both capital gains and imputed rent for owner-occupied dwellings.

Tax expenditure in respect of agriculture and forestry in 1997 was FIM 3.7 billion.

Value added tax was almost solely responsible for tax expenditure in respect of transport and communication. Total tax expenditure was FIM 2.2 billion.

Tax expenditure for industry and business was totalling FIM 5.3 billion. The majority of tax expenditures, totalling FIM 3.2 billion, were granted on the basis of the provisions governing company depreciations.

Tables 1-4 summarize tax expenditures and transfer payments by spending category. Table 5 itemizes individual tax expenditures.

When considering the significance of the figures, it must be borne in mind that the discontinuance of tax expenditures does not necessarily increase tax revenues by a corresponding amount since tax expenditures affect prices and the behaviour of taxpayers.

² Available only in Finnish, English summary.

*Table 1. Economically significant tax expenditures by spending and tax category
1996 - 1997, FIM million **

	Income, wealth and related taxation		Taxation of business and agriculture		Indirect taxation	
	1996	1997	1996	1997	1996	1997
General administration	100	100	-	-	-	-
Public order	-	-	-	-	-	-
Defence	-	-	-	-	-	-
Education, science and culture	800	800	-	-	-	-
Social security	17100	17000	-	-	40	40
Health care	-	-	-	-	600	700
Housing and environment	9700	10500	-	-	-	-
Labour force	-	-	-	-	-	-
Agriculture and forestry	200	200	1200	1200	2100	2300
Transport and communication	200	200	-	-	1900	2000
Industry and business	1600	1600	3200	3300	400	400
Other expenditures	800	500	-	-	-	-
Miscellaneous items	3700	4800	-	-	900	1100

* Figures generally rounded to nearest 100 million. Tax penalties subtracted from tax expenditures.

*Table 2. Economically significant tax expenditures by spending category and taxing body
1996 - 1997, FIM million **

	Central government		Other taxing bodies		Total	
	1996	1997	1996	1997	1996	1997
General administration	40	45	40	45	80	90
Public order	-	-	-	-	-	-
Defence	-	-	-	-	-	-
Education, science and culture	300	300	500	500	800	800
Social security	6100	6100	11000	10900	17100	17000
Health care	600	700	-	-	600	700
Housing and environment	8400	9200	1400	1300	9700	10500
Labour force	-	-	-	-	-	-
Agriculture and forestry	2800	3000	700	700	3500	3700
Transport and communication	2000	2100	100	100	2100	2200
Industry and business	3500	3600	1600	1700	5200	5300
Other expenditures	800	500	-	-	800	500
Miscellaneous items	2500	2700	2100	3200	4600	5900

* Figures generally rounded to nearest 100 million. Tax penalties subtracted from tax expenditures.

Table 3. Economically significant tax expenditures in central government taxation and government transfer payments by spending category 1996 - 1997, FIM million *

	Tax expenditures		Transfer payment		Change 97/96, %	
	1996	1997	1996	1997	Tax expenditures	Transfer payments
General administration	40	45	7600	8100	13	7
Public order						
Defence	300	300	18800	18900	0	1
Education, science and culture						
Social security	6700	6800	47500	44800	1	-6
Health care						
Housing and environment	8400	9200	3200	2900	10	-9
Labour force	-	-	10600	9800	-	-8
Agriculture and forestry	2800	3000	11300	11300	7	0
Transport and communication	2000	2100	800	800	5	0
Industry and business	3500	3600	5500	3000	3	-45
Other expenditures	800	500	2900	2800	-38	-3
Miscellaneous items	2500	2700	-	-	8	-

* Figures generally rounded to nearest 100 million. Tax penalties subtracted from tax expenditures.

Table 4. Economically significant tax expenditures by spending and tax category 1994 - 1997, FIM million *

	1994	1995	1996	1997
General administration	100	100	100	100
Public order	-	-	-	-
Defence	200	-	-	-
Education, science and culture	800	800	800	800
Social security	16400	17300	17100	17000
Health care	400	600	600	700
Housing and environment	10500	9200	9700	10500
Labour force	-	-	-	-
Agriculture and forestry	5100	3500	3500	3700
Transport and communication	2300	2000	2100	2200
Industry and business	5700	5700	5200	5300
Other expenditures	1100	1000	800	500
Miscellaneous items	-1200	4400	4600	5900

* Figures generally rounded to nearest 100 million.
Tax penalties subtracted from tax expenditures.

Table 5. Itemized breakdown of economically significant tax expenditures by spending and tax category 1994 - 1999

Explanation: * = preliminary calculation, ** = forecast, - = nothing to report, .. = not estimable

Spending category Item	Tax expenditures, est. FIM million						Notes
	1994	1995	1996	1997	1998*	1999**	
1. Gener I administration							
<i>Income, wealth and related taxation</i>							
1. Tax exemption of certain benefits received by foreign service and other employees	70	70	80	90	90	90	Order of magnitude.
2. Tax exemption of foreign-stationed specialists' salaries from UN organizations	..	..	..	..	..	..	Can not be estimated.
2. Defence							
<i>Indirect taxation</i>							
1. Exemption from turnover of certain foreign acquisitions for national defence	230	-	-	-	-	-	- Exemption from turnover tax based on exemption from customs duties. Eliminated 1994.
3. Education, science and culture							
<i>Income, wealth and related taxation</i>							
1. Tax exemption of non-profit organizations (excluding Evangelical Lutheran and Orthodox churches)	500	500	550	550	..	..	Order of magnitude.

Spending category	Tax expenditures, est. FIM million						Notes
Item	1994	1995	1996	1997	1998*	1999**	
2. Tax exemption of scholarships, etc.	160	100	100	100	100	100	Support in the form of tax exemptions for student aid and university scholarships. The student aid for university students became liable to taxation on July 1, 1992 and student aid for intermediate level students since July 1, 1994.
3. Student grant deduction in municipal taxation	140	190	190	190	180	180	
4. Social security							
<i>Income, wealth and related taxation</i>							
1. Tax exemption of national pension supplements, etc.	680	670	640	620	590	590	
2. Tax exemption of war injury compensation	450	440	370	360	340	320	
3. Tax exemption of social assistance payments	800	800	850	900	750	800	
4. Tax exemption of maintenance support	590	580	600	570	570	560	
5. Tax exemption of child benefits	3850	3600	3400	3150	3150	3100	
6. Tax exemption of redundancy payments	160	100	90	80	70	70	
7. Pension income deduction in central government taxation	70	70	50	20	20	10	
8. Disability deduction in municipal taxation	200	190	160	130	130	130	

Spending category Item	Tax expenditures, est. FIM million						Notes
	1994	1995	1996	1997	1998*	1999**	
9. Pension income deduction in municipal taxation	4300	4500	4200	4100	4100	4000	
10. Disability deduction in central government taxation	260	270	250	260	270	270	
11. Maintenance obligation deduction in central government taxation	20	30	30	30	30	30	
12. Deduction of employees' statutory pension contributions	3000	3950	4700	5000	5300	5350	In calculations taken account only tax expenditure caused by deductible insurance contribution.
13. Deduction of employees' unemployment insurance contributions and unemployment fund contributions	2000	2050	1750	1750	1800	1850	
<i>Indirect taxation</i>							
1. Refund of motor-vehicle tax to disabled persons	30	30	40	40	40	..	
5. Health care							
<i>Indirect taxation</i>							
1. Reduced VAT rate for medicines (12 %, since 1998 8 %)	400	620	640	670	1000	..	Order of magnitude. Before 1995 tax expenditure resulted from tax exemption of medicines.

Spending category Item	Tax expenditures, est. FIM million						Notes
	1994	1995	1996	1997	1998*	1999**	
6. Housing and environment							
<i>Income, wealth and related taxation</i>							
1. Tax exemption of capital gains on owner-occupied dwellings	1900	1700	2300	2800	3000	3100	Order of magnitude. Calculation based on nominal sales proceeds of dwellings and estimated time of ownership of houses. The capital income tax rate has been applied.
2. Tax exemption of housing support	1200	1200	1050	1000	1150	1250	
3. Deduction for interest expense and for index and exchange rate losses (housing loans)	3500	3200	2400	2200	2300	2300	Includes additional interest deduction.
4. Partial tax exemption of imputed rent for owner-occupied dwellings	3000	3100	4000	4500	4500	4600	Order of magnitude. Calculation based on State Housing Board dwelling valuations and assumed 3 % return. The real estate tax has not been deducted from the tax expenditure.
<i>Indirect taxation</i>							
1. Tax exemption of tap water	120	-	-	-	-	-	Eliminated 1994.
2. Tax exemption of housing construction	800	-	-	-	-	-	Order of magnitude. Eliminated 1994.
7. Agriculture and forestry							
<i>Income, wealth and related taxation</i>							
1. Tax exemption of sales revenue from wild berries, mushrooms, etc.	20	20	20	20	..	..	Order of magnitude.

Spending category	Tax expenditures, est. FIM million						Notes
Item	1994	1995	1996	1997	1998*	1999**	
2. Agricultural adjustment deduction	-	150	150	140	140	80	Applies to 1995 - 1999.
<i>Farm income taxation</i>							
1. Tax exemption of own-use farm products	250	250	250	260	..	..	Order of magnitude.
2. Depreciation on machinery and equipment	-	10	10	-	..	..
3. Depreciation on building acquisition expenses	60	40	30	60	..	..	Order of magnitude.
4. Tax exemption of values of logging	240	240	240	240	..	..	Order of magnitude.
5. Forestry fee deduction	50	50	50	50	..	..	Order of magnitude.
6. Tax exemption of damaged forest area	40	40	40	40	..	..	Order of magnitude.
7. Tax expenditure due to valuation of forestry on a net income basis	600	500	500	500	..	..	Order of magnitude.
8. Tax exemption of forestry subsidies	80	80	80	80	..	..	Order of magnitude.
9. Equalization reserve	..	..	..	..	..	..
1.-9. Total tax expenditure	1320	1210	1200	1230	..	..
<i>Indirect taxation</i>							
1. Turnover tax deductions for primary products							
- domestic consumption	4200	-	-	-	-	-	Gross reduction in food-stuff prices due to primary product deduction. Eliminated 1995.

Spending category Item	Tax expenditures, est. FIM million						Notes
	1994	1995	1996	1997	1998*	1999**	
- exports	710	-	-	-	-	-	- Export subsidies for agricultural products paid through turnover tax system. Eliminated 1995.
2. Hidden turnover tax (tax penalty) on agricultural production inputs							
- investments	-440	-	-	-	-	-	- Non-deductible turnover
- other production inputs	-900	-	-	-	-	-	- taxes on machinery, equipment and building investment, and other production inputs. Eliminated 1995.
3. Turnover tax exemption of compensation for price reduction	80	-	-	-	-	-	- Reduces compensation for price reduction in Budget by amount of tax expenditure. Eliminated 1994.
4. Reduced VAT rate for foodstuffs (17 %)	-	2100	2100	2300	2400	..	.. Deductible since 1995. Order of magnitude.
Total turnover tax expenditure for foodstuffs (items 1 - 4)	3650	2100	2100	2300	2400	..	..
5. Turnover tax exemption of cattle feed							
- agriculture	(600)	-	-	-	-	-	- Part due to tax exemption
- other	90	-	-	-	-	-	- of cattle feed for agriculture in item 1. Eliminated 1995.
6. Turnover tax exemption of fertilizers							
- agriculture	(370)	-	-	-	-	-	- Figures for agriculture
- other	30	-	-	-	-	-	- included in item 1. Eliminated 1995.

Spending category Item	Tax expenditures, est. FIM million						Notes
	1994	1995	1996	1997	1998*	1999**	
8. Transport and communication							
<i>Income, wealth and related taxation</i>							
1. Deduction for seamen's wages	180	170	160	160	160	180	
<i>Indirect taxation</i>							
1. Reduced VAT rate for conveyance of passengers (6 %, since 1998 8 %)	1000	880	900	950	890	..	Order of magnitude. Before 1995 tax expenditure resulted from tax exemption of conveyance of passengers.
2. Reduced VAT rate for TV licences (6 %, since 1998 8 %)	-	200	210	220	200	..	Applies in respect of the compensation received from the State Radio Fund of Oy Yleisradio Ab.
3. Zero VAT rate for subscribed newspapers and other periodicals	650	640	670	700	750	..	Order of magnitude. Before 1995 tax expenditure resulted from tax exemption of newspapers and periodicals.
4. Tax exemption of land and water construction	400	-	-	-	-	-	Order of magnitude. Includes some work not related to transport and communication. Eliminated 1994.
5. Taxi owners' motor vehicle tax relief	120	130	140	140	140	..	Includes also estimated turnover tax relief.
9. Industry and business							
<i>Income, wealth and related taxation</i>							
1. Tax exemption of Kera Corporation, FINNFUND, Finnish Export Credit plc and Ekokem	40	40	70	40	..	..

Spending category Item	Tax expenditures, est. FIM million						Notes
	1994	1995	1996	1997	1998*	1999**	
2. Tax exemption of interest income from bonds, etc. for taxpayers with limited tax liability	1500	1300	1300	1400	1400	..	Order of magnitude.
3. Tax exemption of income earned abroad	150	150	150	150	150	..	
4. Partner deduction	150	100	70	30	20	..	
<i>Taxation of business income</i>							
1. Extraordinary investment deduction for development regions	10	5	2	3	..	-	Deduction applies to investments made in 1989 at the latest.
2. Ice fee classification deduction	40	20	5	2	..	..
3. Operating reserve	10	40	-20	30	..	..
4. Machinery and equipment depreciation	2400	2800	3000	3200	..	..
5. Temporarily accelerated depreciation of productive investments	350	40	-	-	-	-	
6. Unrestricted development area depreciation	300	820	200	30	..	..	Order of magnitude.
7. Interim subsidy of industrial investments	7	5	-	-	-	-	
1.-7. Total tax expenditure	3117	3730	3187	3265	..	..
<i>Indirect taxation</i>							
1. Turnover tax exemption for services (accommodations, beauty and health care, recreation, culture, etc.)	1600	-	-	-	-	-	Order of magnitude. Eliminated 1994.

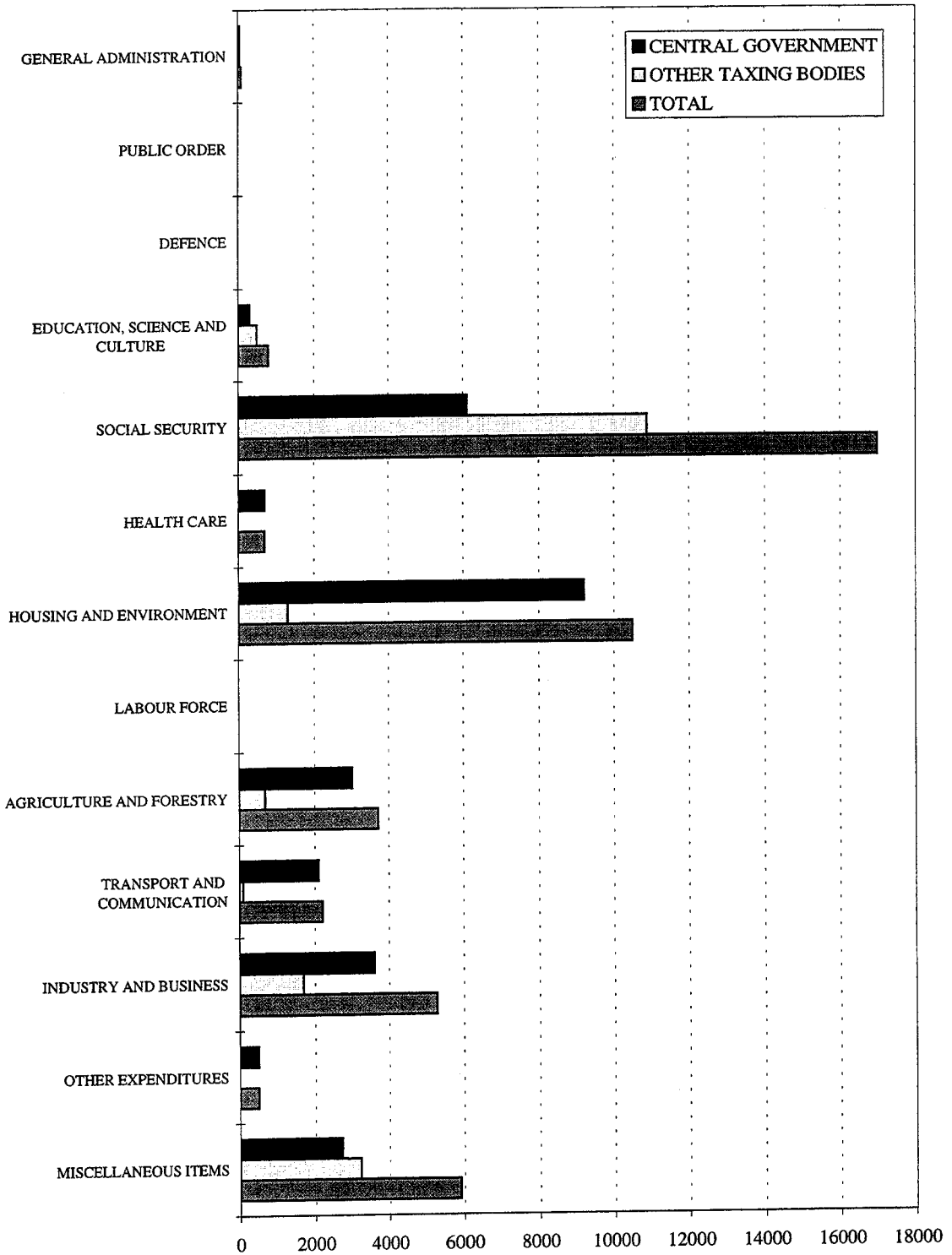
Spending category Item	Tax expenditures, est. FIM million						Notes
	1994	1995	1996	1997	1998*	1999**	
2. Turnover tax exemption of workplace canteens	200	-	-	-	-	-	- Canteen and restaurant activities generally subject to turnover tax. Eliminated 1995.
3. Reduced VAT rate for film performances (12 %, since 1998 8 %)	-	50	50	50	70	..	.. Deductible since 1995. Order of magnitude.
4. Reduced VAT rate for entertainment events etc. (6 %, since 1998 8 %)	-	30	30	30	30	..	..
5. Reduced VAT rate for physical training services (12 %, since 1998 8 %)	-	..	..	..	..	..	.. Can not be estimated.
6. Reduced VAT rate for books (12 %, since 1998 8 %)	-	120	130	140	200	..	.. Deductible since 1995. Order of magnitude.
7. Reduced VAT rate for accomodation services (6 %, since 1998 8 %)	-	200	210	220	210	..	.. Deductible since 1995. Order of magnitude.
8. Turnover tax exemption of domestic fuels and certain waste materials	350	-	-	-	-	-	- Eliminated 1995.
9. Turnover tax exemption of natural gas imports	280	-	-	-	-	-	- Eliminated 1995.
10. Hidden turnover tax (penalty) on exports	-1700	-	-	-	-	-	- Order of magnitude. Eliminated 1994.
10. Other expenditures							
<i>Income, wealth and related taxation</i>							
1. Tax exemption of bonds and interest thereon	200	150	100	50	50	50	50 Tax exemption of interest income. Calculated using the final withholding tax rate on interest income.

Spending category Item	Tax expenditures, est. FIM million						Notes
	1994	1995	1996	1997	1998*	1999**	
2. Tax exemption of deposits and interest thereon	900	900	700	500	500	500	Tax exemption of interest income. Calculated using the final withholding tax rate on interest income.
11. Miscellaneous items							
<i>Income, wealth and related taxation</i>							
1. Tax exemption of personnel benefits	1000	1000	1100	1200	1300	1300	Order of magnitude.
2. Deduction of labour organization membership fees	1050	1150	1200	1200	1150	1150	
3. Deduction for interest payments, and index and foreign exchange losses (other than housing loans)	400	-	-	-	-	-	
4. Temporary earned income deduction for individuals with a small income in municipal taxation 1991-95	560	500	480	1600	1600	2650	The rules of deduction changed 1997 and 1999.
5. Partial tax exemption of emoluments in kind	900	800	700	600	600	620	
6. Tax exemption of travel cost reimbursements in certain sectors	60	60	50	50	50	140	
7. Partial tax exemption of travel allowances	220	170	150	120	110	120	
<i>Indirect taxation</i>							
1. Turnover tax exemption of certain buildings	200	-	-	-	-	-	Order of magnitude. Covers public and other activity not subject to turnover tax, such as bank and insurance offices. Eliminated 1994.

Spending category	Tax expenditures, est. FIM million						Notes
	Item	1994	1995	1996	1997	1998*		1999**
2. Lower average VAT rate for intermediate product inputs in public sector	-	410	480	580	600	..	Deductible since 1995. Order of magnitude.
3. Lower average VAT rate for intermediate product inputs in private sector	-	100	120	190	190	..	Deductible since 1995. Order of magnitude.
4. Turnover tax exemption of sales and import of trotting horses and pets	10	-	-	-	-	-	- Order of magnitude. Eliminated 1994.
5. Non-deductibility of turnover tax included in prices of transport and services (penalty)	-3700	-	-	-	-	-	- Order of magnitude. Eliminated 1994.
6. Non-deductibility of purchase price of telecommunications services (penalty)	-900	-	-	-	-	-	- Order of magnitude. Eliminated 1994.
7. Limitation in deductibility of turnover tax inherent in investments, excluding agricultural investments (penalty)	-1800	-	-	-	-	-	- Order of magnitude. Only production-related investments and energy investments are deductible. Eliminated 1994.
8. Other types of non-deductibility of turnover tax (penalty)	-1200	-	-	-	-	-	- Order of magnitude. Eliminated 1994.
Total hidden turnover tax (items 5-8)	-7600	-	-	-	-	-	-
of which							
- share related to domestic consumption	-5900	-	-	-	-	-	-
- share related to exports	(-1700)	-	-	-	-	-	- Included in industry and other business tax expenditures.

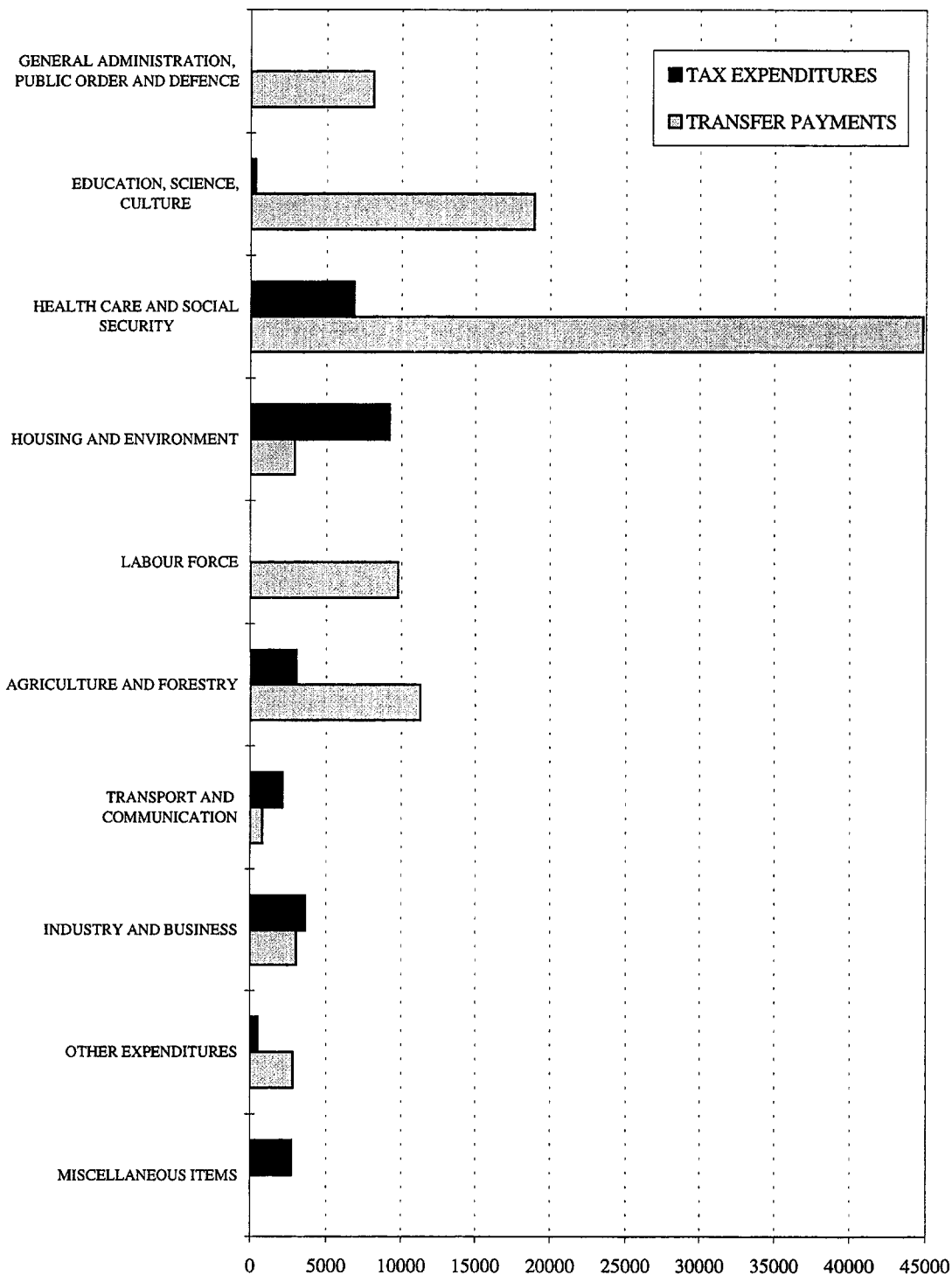
Spending category	Tax expenditures, est. FIM million						Notes
Item	1994	1995	1996	1997	1998*	1999**	
9. Tax exemption on motor vehicles imported as personal effects when moving into Finland	250	250	350	350	410		.. Order of magnitude. Includes loss of tax revenue due to exemption of motor vehicles and motorcycles and loss of VAT.

TAX EXPENDITURES BY SPENDING CATEGORY AND TAXING BODY IN 1997, FIM MILL.



IN THE CALCULATION TAX PENALTIES HAVE BEEN DEDUCTED FROM TAX EXPENDITURES.

CENTRAL GOVERNMENT TAX EXPENDITURES AND TRANSFER PAYMENTS BY SPENDING CATEGORY IN 1997, FIM MILL.



IN THE CALCULATION TAX PENALTIES HAVE BEEN DEDUCTED FROM TAX EXPENDITURES.

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