



Report to the Public Accounts
Committee on transparency of tax
expenditures (tax exemptions,
allowances, etc.)

October
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Rigsrevisionen issues this report to the Public Accounts' Committee in accordance with section 17(2) of the Auditor General's Act, cf. consolidated act no. 3 of 7 January 1997 as amended by act no. 590 of 13 June 2006. The report concerns section 9 of the Fiscal Act. The Ministry of Taxation.

I. Results of examination

1. This report deals with Rigsrevisionen's examination of the transparency of Danish tax expenditures.

Tax expenditures can be defined as measures which reduce or defer taxes payable by taxpayers. Tax expenditures may take the form of tax allowances, tax exemptions or tax reliefs resulting in loss of revenue for the public sector. Tax expenditures may also take the form of delays in payment of tax which will also lead to a loss of revenue for the public sector.

Generally, tax expenditures are used as instruments to achieve certain political objectives, e.g. promotion of specific activities or exertion of influence on matters of an allocative and distributive nature.

2. The impact of tax expenditures on the government budget and the respective beneficiaries is to a considerable extent comparable to the impact of direct transfers of public resources or government subsidies.

In many instances, tax expenditures increase the need for public administration and control, and complex tax regulations often increase the burden of administrative costs to be carried by businesses and citizens. These administrative costs should therefore be added to the loss of revenue.

Other tax expenditures may ease administrative burdens, i.e. tax exemptions, triviality limits and special terms applying to small businesses.

3. In Denmark, tax expenditures are considerable. In an appendix to the budget for 2006, tax expenditures were estimated at around DKK 35.1 billion, or 4.4 % of total tax revenues in 2006. The figure represents a rough estimate and many of the exceptions made from the regulations governing taxes and duties are not included due to either insufficient data, which have made it impossible to estimate tax expenditures, or because certain tax expenditures fall below the Ministry of Taxation's triviality limit of DKK 5 million. In addition, the concept of tax expenditures has not been precisely defined which opens up for the adoption of a broader definition than the one applied by the Ministry of Taxation: for example also general tax deductions, like interest deductions, could be included and that would increase tax expenditures significantly.

4. Rigsrevisionen has decided to examine the transparency of tax expenditures because they may contribute to reducing the total tax base and thereby increase the level of other taxes and duties. If, at that, no budgetary cost limits have been set for tax expenditures, they may, like statutory benefits, lead to open-ended spending. Moreover, because these expenditures are not included in the budget and are not estimated, they may not be reflected in the budget nor in the state accounts and thereby they will be excluded from the political decision-making process. Finally, various tax expenditure programs may not be subjected to regular political scrutiny due to lack of follow-up on objectives and impact of

tax expenditures and consequently tax expenditure programs may remain in force even though they no longer promote their original objective.

5. The examination is based on international best practice guidelines worked out by, e.g. the Organisation for Economic Co-operation and Development (OECD) and the International Monetary Fund (IMF).

However, the guidelines prepared by these organisations are formulated on a somewhat general level, and Rigsrevisionen has therefore based its recommendations also on best practice in a number of other countries where the issue of tax expenditures has recently been examined by the respective supreme audit institutions. Among these countries are Sweden, Finland, Holland, Germany and the US.

6. International best practice guidelines promote transparency concerning preparatory legislative work, budgeting and reporting of tax expenditures, and recommend that tax expenditures are treated as direct expenses and subjected to the budget and appropriation control applied to direct expenses.

7. With this as a starting point, the overall purpose of Rigsrevisionen's examination is to examine and assess whether fiscal transparency concerning tax expenditures can be improved. The report will answer two questions:

- Will it be possible to increase transparency of preparatory legislative work and budgeting with respect to tax expenditures?
- Will it be possible to increase transparency of reporting of loss of revenue, costs and impact of tax expenditures?

8. Rigsrevisionen has taken the initiative to conduct this examination. The draft report has been submitted to all ministries with the exception of the Ministry of Ecclesiastical Affairs. The ministries' comments are incorporated in the report.

RESULTS OF EXAMINATION

According to Rigsrevisionen's overall assessment, the transparency of Danish tax expenditures can be improved. The examination showed that the preparation of bills on tax expenditures has improved in recent years. Transparency related to budgeting of tax expenditures and reporting of revenue losses, administrative costs and the impact of tax expenditure programs can be further improved.

The Ministry of Taxation has indicated that it attaches great importance to transparency of legislation governing taxes and duties.

Rigsrevisionen is of the opinion that the guidelines developed by OECD and IMF provide an excellent platform for the establishment of a practice in Denmark which may improve transparency of tax expenditures.

This overall assessment is based on the following:

In recent years, the quality of preparatory legislative work has improved and it generally creates transparency around tax expenditures. Still, transparency can be even further improved if the impact of tax expenditures on tax revenue is included in the budget process.

Budgeting

- Up to and including 2006, an overview of estimated tax expenditures was presented in an appendix to the budget. Since the beginning of 2007, tax expenditures do not appear from the budget and this has decreased transparency. However, Rigsrevisionen agrees with the Ministry of Taxation and the Ministry of Finance that the data upon which the overview was based were obsolete, and the appendix therefore no longer relevant.
- In 2006, the Ministry of Taxation estimated the loss of revenues at around DKK 35.1 billion. If a broader definition of tax expenditures is applied, according to which deviations from current regulations are being categorised as tax expenditures, then the amount will be considerably higher. The Ministry of Taxation has indicated that there are significant methodology difficulties related to a definition of tax expenditures. Rigsrevisionen is of the opinion that the Ministry of Taxation should make a definition of tax expenditures on the basis of international guidelines and practice in comparable countries.
- Transparency of tax expenditures will be promoted if they are included in budgeting and thereby subjected to regular political scrutiny and prioritisation. The Ministry of Taxation has indicated that the ministry on the basis of Rigsrevisionen's examination intends to investigate the opportunities of achieving greater transparency in budgeting. The Ministry intends to examine practice in comparable countries and discuss the issue under the auspices of OECD.

Preparatory legislative work

- The quality of preparatory legislative work has improved, as explanatory notes now include information on program objective, beneficiaries, impact on revenue and administrative costs.
- The transparency of tax expenditures will be enhanced if explanatory notes to bills on tax expenditures inform of significant uncertainties related to the estimation of revenue loss. Transparency will also improve if administrative costs resulting from tax expenditures are estimated more accurately.

Reporting includes only a few of the tax expenditures, previously estimated by the Ministry of Taxation. Rigsrevisionen finds that the transparency of tax expenditures can be considerably improved if revenue losses, administrative costs and the impact of the tax expenditure programs are being reported.

Reporting

- The Ministry of Taxation, the Ministry of Finance and the responsible departments present an annual status report on employee benefits/benefits in kind. This report, however, covers only 3.9 % of the tax expenditures previously estimated by the Ministry of Taxation.
- Transparency concerning tax expenditures will be enhanced if total loss of revenues and volume of administrative costs related to the programs are reported.

The Ministry of Taxation has stated that it will look into practice of reporting in comparable countries in order to establish whether transparency of reporting can be improved.

- Transparency will also be improved through an evaluation of objective achievement and scheme impact. This evaluation should be carried out on the background of an assessment of materiality and risk, and could, as indicated by the Ministry of Taxation, take place in combination with an evaluation of other legislation in the field.

II. Preface

A. Background

9. This report deals with Rigsrevisionen's examination of the transparency of Danish tax expenditures.

Tax expenditures can be defined as measures which reduce or defer taxes payable by taxpayers. Tax expenditures may take the form of tax allowances, tax exemptions or tax reliefs resulting in loss of revenue for the public sector. Tax expenditures may also take the form of delays in payment of tax which will also lead to a loss of revenue for the public sector.

Generally, tax expenditures are used as instruments to achieve certain political objectives, e.g. promotion of specific activities or exertion of influence on matters of an allocative and distributive nature.

10. The impact of tax expenditures on the government budget and the respective beneficiaries is to a considerable extent comparable to the impact of direct transfers of public resources or government subsidies.

In many instances, tax expenditures increase the need for public administration and control, and complex tax regulations often increase the burden of administrative costs to be carried by businesses and citizens. These administrative costs should therefore be added to the loss of revenue.

Other tax expenditures may ease administrative burdens, i.e. tax exemptions, triviality limits and special terms applying to small businesses.

11. In Denmark, tax expenditures are considerable. In an appendix to the budget for 2006, tax expenditures were estimated at around DKK 35.1 billion, or 4.4 % of total tax revenues in 2006. The figure represents a rough estimate and many of the exceptions made from the regulations governing taxes and duties are not included due to either insufficient data, which have made it impossible to estimate tax expenditures, or because certain tax expenditures fall below the Ministry of Taxation's triviality limit of DKK 5 million. In addition, the concept of tax expenditures has not been precisely defined which opens up for the adoption of a broader definition than the one applied by the Ministry of Taxation: for example also general tax deductions, like interest deductions, could be included and that would increase tax expenditures significantly.

12. Rigsrevisionen has decided to examine the transparency of tax expenditures because they may contribute to reducing the total tax base and thereby increase the level of other taxes and duties. If, at that, no budgetary cost limits have been set for tax expenditures, they may, like statutory benefits, lead to open-ended spending. Moreover, because these expenditures are not included in the budget and are not estimated, they may not be reflected in the budget nor in the state accounts and thereby they will be excluded from the

political decision-making process. Finally, various tax expenditure programs may not be subjected to regular political scrutiny due to lack of follow-up on objectives and impact of tax expenditures and consequently tax expenditure programs may remain in force even though they no longer promote their original objective.

13. The examination is based on international best practice guidelines worked out by, e.g. the Organisation for Economic Co-operation and Development (OECD) and the International Monetary Fund (IMF).

However, the guidelines prepared by these organisations are formulated on a somewhat general level, and Rigsrevisionen has therefore based its recommendations also on best practice in a number of other countries where the issue of tax expenditures has recently been examined by the respective supreme audit institutions. Among these countries are Sweden, Finland, Holland, Germany and the US.

B. Objective and delimitation

14. International best practice guidelines promote transparency concerning preparatory legislative work, budgeting and reporting of tax expenditures, and recommend that tax expenditures are treated as direct expenses and subjected to the budget and appropriation control applied to direct expenses.

15. With this as a starting point, the overall purpose of Rigsrevisionen's examination is to examine and assess whether fiscal transparency concerning tax expenditures can be improved. The report will answer two questions:

- Will it be possible to increase transparency of preparatory legislative work and budgeting with respect to tax expenditures?
- Will it be possible to increase transparency of reporting of loss of revenue, costs and impact of tax expenditures?

C. Method

16. The examination is based on international best practice guidelines. In addition, Rigsrevisionen has based its recommendations on best practice in a number of countries where the issue of tax expenditures has been raised by the respective supreme audit institutions. Among these countries are: Sweden, Finland, Holland, Germany and the US.

17. Rigsrevisionen has examined 12 representative tax expenditures, including both financially significant and less significant types of expenditure.

The 12 tax expenditure programs account for DKK 7.2 billion or well over 20 % of the tax expenditures estimated by the Ministry of Taxation in the past. In terms of time, the examination covers tax expenditure programs adopted in the period 1962-2004. Finally, the examination addresses reporting of tax expenditures up to 2007.

18. The review of the 12 tax expenditure programs includes mainly preparatory legislative work, e.g. draft legislation and explanatory notes, working papers and materials related to the bill, and consultation responses to the bill. Rigsrevisionen has participated in a working group under the European Organisation of Supreme Audit Institutions (EUROSAI) and in that connection issued a questionnaire on tax expenditures. The Ministry of Taxation's responses provided to this questionnaire are also included in the examination. Rigsrevisionen also had meetings with managers and staff from the department of the Ministry of Taxation and SKAT (Danish tax authorities) regarding Danish tax expenditures.

Finally, Rigsrevisionen has reviewed national budgets for the period 1998-2006 and other reporting to the Folketing (Danish parliament) on tax expenditures

19. Rigsrevisionen has taken the initiative to conduct this examination. The draft report has been submitted to all ministries with the exception of the Ministry of Ecclesiastical Affairs. The ministries' comments are incorporated in the report.

Definitions

20. OECD defines tax expenditures as *"a transfer of public resources that is achieved by reducing tax obligations with respect to a benchmark tax, rather than by a direct expenditure"*. Exceptions from the general tax regulations of this nature result in loss of tax revenues. Furthermore, these exceptions may increase the administrative costs borne by citizens, businesses and public authorities.

BOX 1. TAX EXPENDITURES

Tax expenditures may take the form of:

- **Exemptions from tax, VAT and duties** like for instance the duty exemption regarding particulate filters for diesel vehicles. It becomes a tax expenditure because new diesel vehicles, which are having particulate filters installed in the period 2006-2009, are exempt from paying full registration fee, as the fee is reduced by up to DKK 10,700 per vehicle.
- **Allowances**, for instance the transport allowance. The tax expenditure is the loss of tax revenue resulting from the indirect tax-subsidy granted to commuters.
- **Reduced tax, VAT and duty rates**. For example, the excise duty on diesel is lower than on petrol. Diesel vehicles are charged with a compensatory fee, but this does not offset in full the difference in fee and therefore the reduced excise duty becomes a tax expenditure.
- **Tax deferral** means a delay in paying tax. The particularly long credit time for payment of VAT granted to small businesses is an example of a tax deferral. The tax expenditure is the value of the interest-rate advantage after tax which the businesses achieve due to the extension of credit time.

21. The IMF defines fiscal transparency as *"openness toward the public at large about government structure and functions, fiscal policy intentions, public sector accounts, and projections"*. However, according to the IMF, transparency is only one aspect of good practices within fiscal policy. Two other important aspects are effectiveness, i.e. political achievement of objectives, and balance between government revenue and expenditure. This examination is focused on transparency of tax expenditures, and therefore the two above-mentioned aspects of good fiscal practices are not addressed in this report.

International recommendations

22. According to OECD's recommendation, tax expenditures should generally be treated as direct expenses. This means that tax expenditures should be subjected to the same budgetary control as direct expenses. The motivation is amongst other that if less strict budgetary control is applied, then the scope of tax expenditures cannot be controlled and subjected to political scrutiny. The IMF recommends the inclusion of tax expenditures in the budget as a basic requirement of transparency.

BOX 2. INTERNATIONAL RECOMMENDATIONS

The OECD proposes the following recommendations concerning tax expenditures:

- All tax expenditures should be estimated and integrated in the expenditure documentation that is presented to the budgetary authorities for all significant taxes. Regular expenditures and tax expenditures should be shown in this documentation side-by-side for the same number of years.
- Tax expenditures should either be included in the total expenditure cap that is set every year during budget preparation or in a special tax expenditure cap. Overspending on tax expenditures should be fully compensated, at least in so far as it originates in policy change.
- Tax expenditures should be reviewed in the same way as regular expenditures in the annual budget process. They should be reviewed by the financial staff of spending ministers and the Ministry of Finance in the same way as regular expenditures. Tax expenditures should be subjected to special evaluation procedures, including law review.
- Tax expenditures should be estimated by the revenue forgone method, indicating government's net loss of revenue resulting from tax expenditures.
- Finally, the OECD recommends the application of a broad definition of tax expenditures, according to which all deviations from a benchmark tax are defined as tax expenditures.

And the IMF's recommendations:

- Tax expenditures should be included in the government budget as they are a basic requirement of fiscal transparency. The budget should describe the objective, duration and intended beneficiaries of tax expenditure policies.
- The cost of tax expenditures should be estimated. Methods of estimation and assumptions underlying the statement of costs should be provided in the budget.

23. Rigsrevisionen's examination deals with tax expenditures in two phases: 1. budgeting and preparatory legislative work and 2. reporting and evaluation.

In relation to the preparatory legislative work, Rigsrevisionen considers it important that tax expenditures are authorised by law. Moreover the financial implications of tax expenditure programs should be estimated and their objective, beneficiaries and/or the activities governed by the program should be clearly indicated. Rigsrevisionen has also attached importance to the fact that tax expenditures should be included in the budgetary process.

Finally, Rigsrevisionen has emphasized that reporting should provide the members of the Folketing with a reliable basis for assessing the impact of a certain tax expenditure program. Reporting should therefore include information on both cost and impact of program.

III. Budget process and preparatory legislative work

RIGSREVISIONEN'S COMMENTS

In recent years, the quality of preparatory legislative work has improved and it generally creates transparency around tax expenditures. Still, transparency can be even further improved if the impact of tax expenditures on tax revenue is included in the budget process.

Budgeting

- Up to and including 2006, an overview of estimated tax expenditures was presented in an appendix to the budget. Since 2007, tax expenditures do not appear from the budget and this has decreased transparency. However, Rigsrevisionen agrees with the Ministry of Taxation and the Ministry of Finance that the data upon which the overview was based were obsolete, and the appendix therefore no longer relevant.
- In 2006, the Ministry of Taxation estimated the loss of revenues at around DKK 35.1 billion. If a broader definition of tax expenditures is applied, according to which deviations from current regulations are being categorised as tax expenditures, then the amount will be considerably higher. The Ministry of Taxation has indicated that there are significant methodology difficulties related to a definition of tax expenditures. Rigsrevisionen is of the opinion that the Ministry of Taxation should make a definition of tax expenditures on the basis of international guidelines and practice in comparable countries.
- Transparency of tax expenditures will be promoted if they are included in budgeting and thereby subjected to regular political scrutiny and prioritisation. The Ministry of Taxation has indicated that the ministry on the basis of Rigsrevisionen's examination intends to investigate the opportunities of achieving greater transparency in budgeting. The Ministry intends to examine practice in comparable countries and discuss the issue under the auspices of OECD.

Preparatory legislative work

- The quality of preparatory legislative work has improved, as explanatory notes now include information on program objective, beneficiaries, impact on revenue and administrative costs.

- The transparency of tax expenditures will be enhanced if explanatory notes to bills on tax expenditures inform of significant uncertainties related to the estimation of revenue loss. Transparency will also improve if administrative costs resulting from tax expenditures are estimated more accurately.

A. Budget process

24. With international guidelines as point of departure, Rigsrevisionen has examined whether tax expenditures are included in the budget process and appear from the government budget like other expenditure. It has also been the intent of Rigsrevisionen to determine whether the transparency of the budget process can be increased.

25. Textbooks mention three methods for the estimation of tax expenditures' impact on revenue: 1. revenue forgone, 2. outlay equivalence and 3. revenue gain. All three methods are described in more detail in box 3 below.

BOX 3. METHODS FOR THE ESTIMATION OF TAX EXPENDITURES' IMPACT ON REVENUE

The revenue foregone approach estimates tax expenditures according to a net principle. It estimates tax expenditures to be the tax revenue which government would have gained, had the tax program not been implemented. This means that the revenue foregone approach calculates the net impact of tax expenditures on the government budget and implications for the beneficiaries. This method shows how much it will cost government to provide a direct tax exempt grant equivalent to the indirect grant which is the result of the tax expenditure. However, this approach does not take into consideration the change in behaviour which will occur as a result of the tax expenditure and which will affect revenues.

The outlay equivalence approach estimates tax revenues according to a gross principle. The tax expenditure related to each individual tax concession is estimated as the expenditure which the public sector would incur had the tax expenditure been replaced by a direct, but taxable grant.

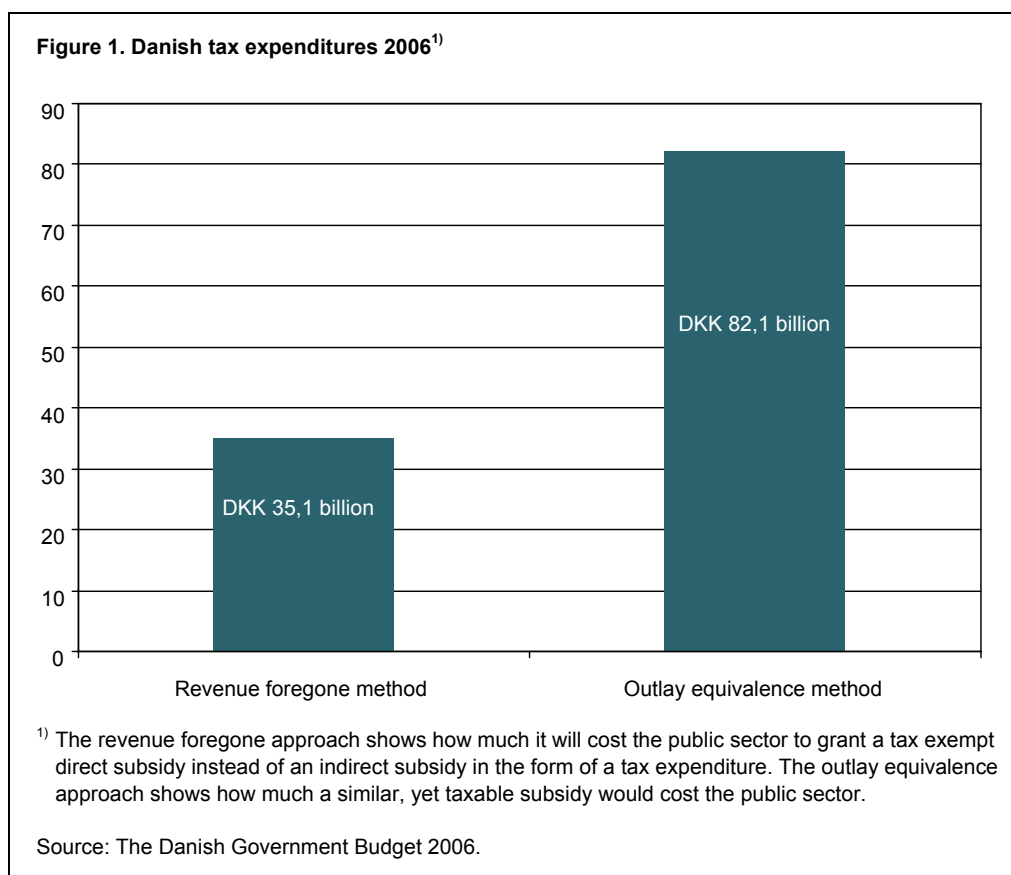
The revenue gain approach attempts to estimate the incremental tax revenue which the public sector would gain if a tax expenditure were to be abolished. In other words, this approach takes into account the change of behaviour caused by a tax expenditure. This method is rarely applied.

26. In the budget report "Tax expenditures in Denmark" from 1996, the Ministry of Taxation and other ministries estimated Danish tax expenditures for the first time ever. The impact of tax expenditures on tax revenues was estimated on the basis of the revenue foregone approach and the outlay equivalence approach. On the background of a subsequent report from 1997, the Ministry of Taxation worked out an appendix to the budget on tax expenditures in the period 1998-2006. However, as from 2007, this appendix is no longer part of the budget.

The Ministry of Finance has stated that the estimation of tax expenditures was removed from the budget because the data used were obsolete.

The Ministry of Taxation has pointed out that the usefulness of the overview did not measure up to the resources invested in producing the overview.

27. Figure 1 shows Danish tax expenditures in 2006 estimated according to the revenue foregone and outlay equivalence approach, respectively.



28. It appears from figure 1 that Danish tax expenditures in the appendix to the budget for 2006 are estimated at around DKK 35.1 billion according to the revenue foregone approach. This figure equals 4.4 % of total Danish tax revenues. If based on the equivalent outlay approach, it amounts to DKK 82.1 billion in 2006, or 10.2 % of tax revenues.

OECD recommends that revenue losses related to tax expenditures are estimated by the revenue forgone method. The difference between the revenue forgone method and the outlay equivalence method is that the revenue forgone approach estimates the net effect of tax expenditure on the government budget, whereas the outlay equivalence method estimates the pre-tax effect on the budget. Therefore, tax expenditures estimated by the outlay equivalence method will be higher because tax expenditures are converted into direct taxable subsidies.

29. The estimate in figure 1 is based on the definition of tax expenditures which was recommended by OECD at that time and was used in the budget analysis report issued by the Ministry of Taxation in 1996: *"Deviations from the generally accepted or normal tax system which favour certain activities or classes of taxpayers through a reduction of the tax basis"*.

30. However, OECD's definition of tax expenditures is very general and does not indicate precisely the nature of the exemptions, allowances, etc. that should be included when estimating tax expenditures. The question is whether for example a tax allowance represents a deviation from the benchmark tax – and thereby a tax expenditure – or is considered a general feature of the tax system in that particular country.

If instead, any deviation from the tax norm is defined as a tax expenditure, then tax expenditures in Denmark would be considerably higher than indicated in the most recent estimate from 2006.

31. What should be perceived as deviations from the general tax norm is a matter of opinion. And during the examination, Rigsrevisionen has come across several examples which were difficult to categorize as either tax expenditures or general regulations in the tax system. As an example, neither the transport allowance, differentiated registration fee for cars used for private transportation (cars with yellow license plates) nor interest deductions are included in the Ministry of Taxation's statement from 2006.

Moreover, the examination showed that interest deductions in some countries, for example the US and Finland, are treated as tax expenditures, and the transport allowance is treated as a tax expenditure in for example Sweden and Finland. It cannot, due to differences in the countries' tax systems, be concluded that what is considered a tax expenditure in one country is also treated as such in the next country.

32. The Ministry of Taxation's report on tax expenditures from 1996 (item 26) also points to other factors of uncertainty concerning estimation of tax expenditures. According to the report, data on the utilisation of the various tax expenditure programs are insufficient and therefore Danish tax expenditures may be underestimated.

As an example, the report mentions that employees' are allowed a deduction of trade union membership fees and businesses are allowed a similar deduction of membership fees paid to an employers' association. These deductions are in the 1996 report referred to as tax programs for which it is not possible to estimate tax expenditures because data on the employers' use of the deduction are insufficient. For the same reason, this tax expenditure is not included in the Ministry of Taxation's latest estimate of Danish tax expenditures.

Finally, when estimating tax expenditures, the Ministry of Taxation employs a triviality limit according to which minor tax expenditures (under DKK 5 million) are not included.

33. Rigsrevisionen is of the opinion that transparency of Danish tax expenditures can be improved if tax expenditures are included in annual budget reviews and thereby subjected to political scrutiny and prioritisation. The estimate of Danish tax expenditures should be based on the most recent international recommendations and estimates prepared in countries comparable to Denmark.

34. The Ministry of Taxation has stated that it agrees with the objective of increasing the transparency of tax legislation and this is reflected in the explanatory notes to tax bills which have become more specific and detailed. The Ministry also states that it will continuously strive to develop and improve the methods applied to analyse and describe the impact of the tax system.

The Ministry of Taxation has also stated that there are significant methodology issues related to defining tax expenditures. According to the Ministry of Taxation, not every tax exemption, tax allowance, rate relief or tax deferral can be considered a tax expenditure. As examples, the Ministry mentions interest deductions or deductible expenses, like for instance the transport allowance, which the Ministry considers to be part of the general tax system in accordance with OECD's definition.

The Ministry also mentions that the estimation of tax expenditures is subject to considerable uncertainty and therefore it will not make any sense to present the estimated tax expenditures along with the direct expenses in the budget. The statement of most tax expenditures is based on rough estimates due to uncertainty related to identification criteria and reliability of data. Furthermore, the estimation of tax expenditures does not take into account the side effects of tax expenditure on tax revenues and taxpayers' changed behaviour if a tax expenditure program is repealed.

Finally, the Ministry of Taxation has indicated that the inclusion of tax expenditures in the budget is not crucial to ensure ongoing political scrutiny and prioritisation of tax expendi-

tures. Still, the ministry has stated that it will look into the possibilities of improving transparency in the budget process. The ministry intends to examine best practise in countries comparable to Denmark and discuss the issue under the auspices of OECD.

35. The Ministry of Finance has pointed out that it generally agrees with the Ministry of Taxation's views, cf. item 34.

36. Rigsrevisionen finds that Danish tax expenditures, as opposed to now, should be included in the budget process, as improved transparency would bring Denmark on level with comparable countries and improve the basis for political scrutiny and prioritisation.

Rigsrevisionen has not aimed to establish an operational definition which could be used to estimate Danish tax expenditures. Rigsrevisionen is aware of the difficulties of defining and estimating tax expenditures. OECD highlights the interest deductions as an explicit example of the disagreement concerning the definition of tax expenditures. The Ministry of Taxation does not include interest deductions under tax expenditures, but other countries do. Due to national differences in tax systems – mentioned in item 32 – a tax program which is being treated as a tax expenditure in one country is not necessarily considered a tax expenditure in the next country.

Rigsrevisionen also agrees that calculation of tax expenditures is subject to some uncertainty. However, Rigsrevisionen does not consider this uncertainty to be any larger than the uncertainty related to the estimation of other types of tax revenues. This uncertainty of calculation manifests itself also in connection with the very rough estimates of statutory expenditure.

Rigsrevisionen is of the opinion that a more specific definition of tax expenditures should be based on international recommendations, cf. box 2, and best practice in comparable countries. And tax exemptions and rate reliefs which should not be included under tax expenditures should be clearly identified.

B. Preparatory legislative work

37. Rigsrevisionen has reviewed the Ministry of Taxation's preparation of bills, involving tax expenditures. The examination of the preparatory legislative work is based on a review of 12 of the 104 programs for which the Ministry of Taxation has estimated tax expenditures. The 12 tax expenditure programs will appear from appendix 1, and appendix 2 presents an overview of the 104 programs.

To assess whether transparency of tax expenditures is improved through the preparatory legislative work, Rigsrevisionen has examined the following:

- Are tax expenditures authorised by law, is the objective and beneficiaries of each individual tax expenditure program specified in the explanatory notes.
- Is the financial impact of the programs described in the explanatory notes.
- Does the preparatory legislative work take into account also the issue of control.

Legal base, objective and beneficiaries

38. Rigsrevisionen has examined the legal base of tax expenditures and whether the objective of each individual tax expenditure program is clearly described in the explanatory notes. Rigsrevisionen has also reviewed whether the beneficiaries of the tax expenditure programs are described in detail.

39. The review showed that all 12 programs are authorised by law. 8 of the tax expenditure programs are managed under the Tax Assessment Act and 4 are managed under one or several special acts and in some instances under the Tax Control Act.

40. The examination also showed that the objective of 10 of the 12 programs is specified in the explanatory notes. The objectives of the individual programs are described on an overall, general level in the explanatory notes and do not translate into concrete performance targets which would facilitate a follow-up process. The objectives of 2 of the older programs are not specified, i.e. the diesel and assessment expenditure program from 1962 (bill on vehicle excise duty, introduced to parliament on 7 December 1961) and research and development expenditure program from 1977 (L44).

BOX 4. INDICATION OF THE OBJECTIVE OF TAX EXPENDITURES

For most of the tax programs, the objectives and beneficiaries are clearly specified. One example is the tax program concerning businesses' right to deduct costs concerning health-related treatments. The objective of these programs is to improve the general welfare and make it more attractive for businesses to assume social responsibility. According to the bill, an employee who falls sick will receive treatment earlier which will again improve the chances of an optimum result of the treatment. Reducing the waiting time for medical or other treatment will minimise also the physical and psychological inconvenience experienced by the employee and his/her family.

41. Rigsrevisionen finds that the authorities will be in a better position to follow-up on the impact of the various tax expenditure programs, if their objectives are transformed into concrete performance targets.

However, it is not always relevant to set performance targets for tax expenditures. For example, the objective of the special VAT reliefs for nursing homes and day-care centres is solely to VAT-exempt the activities pursued.

Performance targets should, however, be set whenever relevant to ensure proper follow-up on achievement of the objectives of tax expenditure programs. Performance targets represent goals set for impact and expenditure and they are intended to create a platform for control and decision-making with regard to implementation of adjustments or improvements of tax expenditure programs. Performance targets may be reconsidered as required in connection with the annual budget estimates.

42. Rigsrevisionen's review also showed that 11 of 12 tax expenditure programs included a clear definition of tax expenditure program beneficiaries.

Economic implications

43. Rigsrevisionen has examined whether the economic implications of tax expenditures are estimated and referred to in connection with the introduction of new bills. The economic implications may be divided into costs and benefits of tax expenditure programs.

Costs

44. Costs are mainly the public loss of revenue which is a consequence of the tax and duties reliefs. To these should be added the administrative costs resulting from the tax expenditure programs which are borne by the public sector, businesses and/or citizens. These costs may be running administrative costs caused by new requirements to reporting, self-assessment, etc. and costs related to the adjustment of various systems, e.g. new accounting or control systems.

45. Rigsrevisionen's review showed that revenue losses are estimated in the explanatory notes to 7 of 8 more recent tax expenditure programs. Loss of revenue has, however, not been estimated in connection with 3 older tax expenditure programs (diesel and compensatory fee, employee share ownership program, and research and development activities) and 1 more recent tax expenditure program (relief from effluent charges).

All estimates of revenue losses are made with explicit reservations, as the data required to estimate revenue losses accurately are missing. Thus the explanatory notes repeatedly emphasize that it is only possible to make conservative estimates of the impact on revenues, as tax expenditures often serve as incentives for the taxpayers to change their behaviour, which has a bearing on revenue losses.

The Ministry of Taxation has noted that the uncertainty related to the consequences for revenues applies not only to tax expenditures, but is characteristic of most tax bills, because tax legislation tends to change taxpayers' behaviour.

BOX 5. IMPACT ASSESSMENTS

The impact on revenues has been estimated for the majority of tax programs. As an example, the tax program concerning lower particle emissions from new diesel vehicles reduces tax revenues by a total of DKK 90 million net in the period 2006-2009. The impact of the exemption from car tax for low-emitting vehicles (A) and abolition of the car tax allowance for rear screen wipers (B) is stated as follows for the period 2006-2009:

(DKK millions)

| | 2006 | 2007 | 2008 | 2009 | Net 2006-2009 |
|------------|------|------|------|-------|------------------|
| A | (25) | (60) | (95) | (120) | (300) |
| B | 0 | 70 | 70 | 70 | 210 |
| Net impact | (25) | 10 | (25) | (50) | (90) |

Source: Bill on amendment of various tax regulations (L 80 B).

The impact of tax reliefs depends upon a number of factors, amongst these the actual additional costs of the particle filters and the actual number of people choosing particle filters including or excluding the tax relief. It is estimated that the bill will reduce public sector revenues generated by taxes related to passenger cars and commercial vehicles by DKK 25-120 million annually (cf. A). The abolition of the car tax allowance for rear screen wipers is expected to increase total revenues by DKK 70 million annually (cf. B). The negative net impact is on the basis hereof estimated at a total of (DKK 90 million) in the period 2006 through to 2009, at which time the tax program will be repealed.

46. The administrative consequences for the public sector have been estimated for 7 of the 12 tax expenditure programs. However, the explanatory notes are focused mainly on the costs for system adjustments to be implemented by the customs and tax authorities. Current administrative costs (operating costs) are considered moderate with the exception of the Effluent Act, for which operating costs for control measures have been estimated in man-years.

47. Administrative consequences for businesses and/or citizens have been estimated for 7 tax expenditure programs. However, the administrative costs for system adjustments to be implemented by the businesses are not being estimated separately, as the explanatory notes only refer to the current "operating costs" caused by the tax expenditure programs. According to the explanatory notes to all 7 tax expenditure programs, the resulting cost burden for citizens and businesses is considered moderate. In general, the tax expenditure programs are not considered to increase costs for citizens and businesses to any appreciable extent.

BOX 6. ADMINISTRATIVE COSTS

The administrative costs related to the programs have been estimated for several of the tax programs. One example is the program concerning the act on effluent charges. Public sector one-off expenses for information campaign and it are estimated at DKK 1.1 million. To this should be added annual operating costs of DKK 0.5 million and 4 man-years for control procedures. The program is not expected to increase administrative costs for neither businesses (fish farms) nor citizens.

Benefits

48. Among the benefits of tax expenditure programs are the effect they have directly on business economics and their side-effect on citizens and businesses. In addition, tax expenditures also have allocative and income distribution effects.

Rigsrevisionen's review shows that the direct business economic benefits are mentioned in the explanatory notes, whereas the side-effects of the tax expenditure programs under review only to a very limited extent are being estimated. The examination has not either in any of the bills found evidence that the distributive effect of tax expenditures has been estimated.

In this connection, the Ministry of Taxation has stated that calculations of allocative and distributive effects of tax expenditure programs are generally subject to uncertainty, because they do not take into consideration behavioural responses by the beneficiaries. Still, the Ministry of Taxation is continuously seeking to improve its methods of calculation and analysis in order to include the effect of behavioural changes and other side-effects.

BOX 7. DIRECT BUSINESS ECONOMIC BENEFITS

The business economic benefits appear from the tax programs. As an example, the tax relief concerning particle reducing filters on new diesel vehicles is estimated to represent a value of around DKK 35 million to the trades involved over a three-year period (2006-2009).

49. The preparatory legislative work generally also includes estimation of the tax expenditure's impact on revenue along with its administrative and business economic consequences.

However, Rigsrevisionen finds that transparency of tax expenditures can be further improved if in future also significant prerequisites and uncertainties of calculations are described in detail in the explanatory notes.

Rigsrevisionen is also of the opinion that transparency will increase if administrative costs resulting from tax expenditures are estimated more accurately in the explanatory notes.

Considerations concerning control provisions

50. Rigsrevisionen has examined whether the risk of abuse of tax expenditures is being assessed, for example when tax expenditure programs are difficult to control and monitor.

51. The review showed that control provisions are included in the explanatory notes to 6 of the tax expenditure programs under review. In some instances, the taxpayer must report to SKAT before an allowance or deduction is allowed.

The Ministry of Taxation has also stated that the nature of the control provisions to be implemented is being considered in relation to the risk of abuse. According to the Ministry of Taxation there is continuous focus on potential abuse.

The examination showed that the preparatory legislative work generally includes assessments of risk of abuse.

BOX 8. CONTROL PROVISIONS

Several of the tax programs include control measures. As an example, it appears from the professional athletes' pension scheme that premiums and contributions to the pension scheme as well as payments made from the pension scheme must be reported in accordance with the the Tax Control Act.

52. Overall, the review of tax programs resulting in tax expenditures shows that the preparatory legislative work concerning tax expenditures has improved. The explanatory notes include information on objective of tax program, beneficiaries, revenue impact and scope of administrative costs.

Still, Rigsrevisionen finds that transparency of tax expenditures can be improved if the basis of calculations and uncertainties related to the statement of revenue losses are included in the explanatory notes. Furthermore, the administrative costs resulting from tax expenditures can be more accurately estimated.

IV. Reporting and impact assessment

RIGSREVISIONEN'S COMMENTS

Reporting includes a few of the tax expenditures, previously estimated by the Ministry of Taxation. Rigsrevisionen finds that the transparency of tax expenditures can be considerably improved if revenue losses, administrative costs and the impact of the tax expenditure programs are being reported.

Reporting

- The Ministry of Taxation, the Ministry of Finance and the responsible departments present an annual status report on employee benefits/benefits in kind. This report, however, covers only 3.9 % of the tax expenditures previously estimated by the Ministry of Taxation.
- Transparency concerning tax expenditures will be enhanced if total loss of revenues and volume of administrative costs related to the programs are reported. The Ministry of Taxation has stated that it will look into practice of reporting in comparable countries in order to establish whether transparency of reporting can be improved.
- Transparency will also be improved through an evaluation of objective achievement and scheme impact. This evaluation should be carried out on the background of an assessment of materiality and risk, and could, as indicated by the Ministry of Taxation, take place in combination with an evaluation of other legislation in the field.

A. Reporting

53. Rigsrevisionen's considers it essential for fiscal transparency that tax expenditures and the impact of tax expenditures are reported regularly. Rigsrevisionen has therefore examined whether reporting to the Folketing includes information on extent and cost of tax expenditures and basis of calculation. It is essential that the Folketing is provided with sufficient information to assess the financial implications of the tax expenditure programs, including revenue losses.

54. Tax-privileged employee benefits represent a special type of tax expenditures. Employee benefits are provided to employees in addition to their normal wages or salaries. Compared to cash payments, the financial advantage of employee benefits to employer and employee is the tax rate which is lower than for normal wages and salaries. At the same time, the tax relief related to tax-privileged employee benefits results in a public

revenue loss. Employee stock option schemes, employer-paid health insurances, home PC workstations, and transport between home and workplace paid by the employer are all examples of tax-privileged employee benefits.

55. Since 2003, the Ministry of Taxation and other ministries have worked out an annual status report to the Folketing on the prevalence of employee benefits. Amongst other, the report includes a financial overview of the impact of employee benefits on public revenue and an estimation of the distributive and allocative effect of employee benefits.

In the most recent report from 2006, it is estimated that tax expenditures/revenue losses related to employee benefits make up around DKK 1,35 billion. This figure represents an increase of DKK 275 million over the figure reported in 2005. Compared to the 2003 report, the increase is around DKK 350 million.

56. However, the Ministry of Taxation emphasizes that calculations are based on rough estimates, as data on payment of employee benefits are often not available. Data sources are the tax returns submitted by businesses and employees and data provided by the suppliers of the employee benefits. The estimation of the prevalence of employee benefits that do not appear from the tax returns is still subject to considerable uncertainty.

57. Of all the tax expenditures, only employee benefits are being reported to the Folketing. Employee benefits only make up 3.9 % of the tax expenditures included in the budget for 2006.

Rigsrevisionen's examination also showed that estimation of tax expenditures is subject to considerable uncertainty, amongst other because data concerning some of the major tax expenditure programs are not included in the tax returns. Estimation of tax expenditures would become much more accurate, if it was based on concrete reports submitted to the tax authorities.

58. Rigsrevisionen is of the opinion that systematic reporting on tax expenditures and resulting revenue losses for the public sector would highlight the financial consequences of tax expenditure programs and thereby increase fiscal transparency. Reporting should include all relaxations in tax regulations and the resulting public revenue loss. Also the administrative costs imposed on the public sector, citizens and businesses should be estimated. The reports should also address the uncertainty related to calculations and thereby clearly indicate the nature of the assumptions underlying the estimation.

59. The Ministry of Taxation is of the opinion that tax expenditures should not be subjected to other reporting requirements than those applying to the tax system in general. The ministry finds that focusing on a small section of the tax system consisting of various types of tax expenditures would bias the overall efforts made by the ministry. The ministry points to the fact that total resources in the ministry are best utilised by focusing on the overall collection of taxes and duties rather than on targeted assessment and control of tax expenditures which make up less than 5 % of total government revenues. In that connection, the ministry has emphasized the ongoing efforts to develop tools to analyse the impact of the tax system, e.g. the distortions created by the tax system. The cost of distortions is considered to be two times higher than the cost of tax expenditures and as opposed to tax expenditures, the distortions inevitably lead to socioeconomic losses.

The Ministry of Taxation is therefore of the opinion that tax expenditures should be assessed and controlled in conjunction with the legislation which they are a part of. The assessment of tax expenditures should therefore be made along with the ongoing assessment of the various parts of the general tax system. However, the Ministry of Taxation has indicated that the ministry will look into best practice concerning reporting of tax expenditures in comparable countries in order to establish whether transparency of reporting can be improved.

60. The Ministry of Finance has pointed out that it agrees in general with the views put forward by the Ministry of Taxation, cf. item 59.

61. Rigsrevisionen finds that tax expenditures make up such a large part of public spending that separate budgeting and reporting of said expenditures are required to improve transparency.

Tax expenditures make up around DKK 35.1 billion annually, cf. item 28, or 4.4 % of total tax revenues. Depending on the method of calculation, the total amount may be significantly larger.

The point of departure for Rigsrevisionen's examination has been the international recommendations according to which tax expenditures in terms of budgeting and reporting should be treated like regular expenditures, cf. box 2.

Finally, Rigsrevisionen has based its recommendations on the fact that tax expenditure reporting in a number of comparable countries, including Sweden, Canada, Finland and the US, is considerably more comprehensive than in Denmark.

B. Impact assessment

62. Rigsrevisionen has also examined whether the impact of tax expenditures is being assessed. This is important because impact assessments will show whether the intended objective of a tax expenditure program is achieved. Appropriations are subjected to the same ongoing procedure of assessment.

63. The examination showed that generally the impact of tax expenditures is not being assessed. The consequence is that neither the Ministry of Taxation nor the responsible government departments have a clear picture of the actual effects of tax expenditures.

64. The Ministry of Taxation has stated that two of the tax expenditure programs under review are subjected to the government's program for monitoring of legislation. Thus the home PC workstation tax expenditure program was assessed in December 2005 and the tax allowance for donations made to cultural institutions is up for assessment in 2008.

The Ministry of Taxation has moreover stated that it monitors and assesses the various sections of the tax system, including tax expenditures, on a current basis. The Ministry of Taxation has also said that it is of course ready to comply with a political request to monitor specific parts of the tax system more closely, and the annual report on employee benefits is an excellent example hereof. But according to the Ministry of Taxation such a request should be the result of a concrete evaluation, balancing the cost of ongoing assessment with the cost of the additional resources required to perform the monitoring.

The Ministry of Taxation has also stated that an assessment of tax expenditure impact will require active involvement of the responsible ministries. The Ministry of Taxation cannot assess the impact of tax expenditures on other ministries' remits, i.e. the impact of tax exempted employer-paid health insurances, etc.

65. With regard to the home PC workstation program, Rigsrevisionen has established that a brief report has been prepared on the legislative basis, prevalence and financial implications of the program, but the report does not include any actual assessment of the impact of the program. In the opinion of Rigsrevisionen, assessment of selected tax expenditure programs would increase transparency related to the impact of tax programs. As a result, decisions regarding the spending of public funds would be facilitated and politicians would be provided with a basis for assessment and discussion of adjustment, repeal or continuation of tax expenditure programs. This would improve transparency of tax expenditures.

66. Rigsrevisionen agrees with the Ministry of Taxation that assessment of tax expenditure programs should be based on a concrete evaluation of, e.g. resources required to perform the assessment. Furthermore, materiality and risk should be included in the assessment which, as indicated by the Ministry of Taxation, could take place in combination with the conduct of impact assessments of other legislation in the field.

Rigsrevisionen, 3rd October 2007

Henrik Otbo

/Henrik Berg Rasmussen

Appendix 1. Overview of tax expenditure programs under review

Rigsrevisionen has reviewed 12 of the more than 100 tax programs included in the statement of tax expenditures in the budget for 2006. The 12 tax expenditure programs are presented in the schedule below. The first column indicates the year in which the tax expenditure program took effect. The bill introducing the tax expenditure program and a brief summary of the contents of the program will appear from column two. Estimated annual revenue loss generated by the tax expenditure programs according to the explanatory notes will appear from column three. The fourth column states the estimated revenue loss in 2006 according to either the statement prepared by the Ministry of Taxation or the status report on employee benefits/benefits in kind submitted to the Folketing in 2006.

(DKK millions)

| Year | Description of tax expenditure program and reference to bill | Estimated annual revenue loss according to bill | Estimated annual revenue loss in 2006 |
|--------------------|--|---|---------------------------------------|
| 1962 ¹⁾ | Diesel duty and compensatory tax fee Act no. 99 (28 March 1962) and bill no. 95 (introduced 9 November 1972). The compensatory tax fee for diesel vehicles is not fully balanced by the higher duty on gasoline. | N/A | 3,409* |
| 1971 | Employee stock option program (1) Bill no. 161 (introduced 17 March 1971). Employee share options are exempt from tax. | N/A | 51* |
| 1977/ 1988 | Deduction of research and development expenditures Bill no. 44 (introduced 14 October 1977) and bill no. 6 (introduced 7 October 1987). Expenditure for research and development activities may be deducted as other operating costs or depreciated over several years. | N/A | 2,858* |
| 1987 | Improvement of employee stock option program (2) Bill no. 179 (introduced 21 January 1987). The employee share options are tax exempted and employee share allotments at a value of up to DKK 6,000 per share are also tax exempted. | 175 | 45* |
| 1996 | Tax relief for effluent charges Bill no. 249 (introduced 17 April 1996). Certain trades will be exempted from paying effluent charges and others will be charged a reduced rate. | N/A | 120* |
| 1999 | Tax exempt alcohol rehab program Bill no. 149 (introduced 17 December 1998). Employer-paid alcohol rehab programs are tax exempt for the employee. | 40 | 40* |
| 2002 | Home PC workstation and employer-paid data communication Bill no. 55 (introduced 17 January 2002). Home PC workstation and internet connection paid by the employer are tax exempted for the employee. If the home PC workstation is only partially paid by the employer, then the tax expenditure will consist in an additional tax allowance of up to DKK 3,500 per year. | 162.5 ²⁾ | 175** |

(DKK millions)

| Year | Description of tax expenditure program and reference to bill | Estimated annual revenue loss according to bill | Estimated annual revenue loss in 2006 |
|---|---|---|---------------------------------------|
| 2002 | Health insurance for employees Bill no. 97 (introduced 6 February 2002). The value of the employer-paid health-care treatments and health insurances are tax exempt for employees | 35 | 405** |
| 2002 | Health insurance for self-employed individuals Bill no. 77 (introduced 7 November 2002). Self-employed individuals and their spouse are granted a tax allowance for the health insurance programs that are tax exempt for employees. | 15 | 15* |
| 2004 | Special pension program for professional athletes Bill no. 111 (introduced 10 December 2003). Reduced tax rate paid by professional athletes when they set up an instalment pension program with pension payments starting before the age of 40. | 5 | 5* |
| 2005 | Tax allowance for donations made to cultural institutions and improved depreciation possibilities in connection with art purchases. Bill no. 39 (introduced 20 October 2004). The business may depreciate art purchases made in accordance with the regulations applying to purchases of operating equipment. In addition, businesses and private individuals may deduct their contributions to cultural institutions. | 35 | 51* |
| 2006 | Duty exemption for diesel particulate filters for new diesel cars Bill no. 80 B (introduced 16 November 2005). Duty exemption worth DKK 4,000 for particulate filters for new diesel cars in the period 2006-2009. | 75 ³⁾ | N/A |
| Total estimated tax expenditures | | 542.5 | 7,174 |

¹⁾ Differentiated excise duties on vehicles used for transportation of passengers and goods was provided by Statute in 1931 as compensation for the petrol duty.

²⁾ In the bill, revenue losses are estimated at between DKK 160 and DKK 165 million per year. The figure indicated in column three represents an average of the two.

³⁾ The DKK 75 million represent the annual average of DKK 300 million distributed over four years (DKK 25 million in 2006, DKK 60 million in 2007, DKK 95 million in 2008, and DKK 120 million in 2009).

* Source: Ministry of Taxation 2007.

** Source: Status report to the Folketing on employee benefits/benefits in kind (December 2006).

Appendix 2. The Ministry of Taxation's overview of tax expenditures in 2006

According to the Ministry of Taxation not all tax expenditures are included in the statements, amongst other due to inadequate data. It should be noted also that calculation of most of the indicated revenue losses resulting from tax expenditures is based on estimates. Amounts related to the following factors have been estimated: uncertainty concerning identification criteria and data on tax expenditures. Also the side effects on revenue and the effect of behavioural changes if a tax expenditure did not exist have been estimated.

| Tax expenditure programs – personal income taxation | Description of tax expenditure | DKK millions. ¹⁾ |
|--|--|-----------------------------|
| Urban redevelopment | Tax exempt subsidy according to the Act on Urban Redevelopment etc. cf. the Tax Assessment Act, section 7 F. | 349 |
| Tax relief/protected buildings | Full or partial exemption for payment of municipal land tax for protected buildings, cf. Act on Municipal Real Property Tax, sections 7-9. | 47 |
| Home improvements, repair and insulation | State subsidy to home improvements according to the provisions of a special act. The program was repealed in late 1994, but subsidies allocated but not yet disbursed were paid out subsequently. | - |
| DIS tax relief | Tax relief on wages earned onboard a Danish vessel registered in the Danish International register of Shipping (DIS) and applied for purposes under the Tonnage Taxation Act, cf. the Taxation of Seafarer's Act, section 5. | 614 |
| Sea tax relief | Persons who earn wages onboard vessels which are not in regular ferry service to ports abroad may deduct DKK 56,900 from their personal income, cf. the Taxation of Seafarer's Act, section 3. | 1 |
| Government officials in the service of the Ministry of Foreign Affairs | Allowances granted for living abroad, moving allowance, etc. are free of tax cf. the Tax Assessment Act, section 7, no. 15. | 100 |
| Draftees tax exempt subsistence allowance | Payments in kind to draftees and draftee subsistence allowances are free of tax, etc. cf. the Tax Assessment Act, section 7, no. 16. | 46 |
| Employer-paid health related treatments | Tax exemption for employer-paid health related treatments, cf. the Tax Assessment Act, section 30. | 240 |
| Deduction for self-employed individuals' health related treatments | Self-employed individuals' deduction of health related treatments, cf. the Tax Assessment Act, section 30 A. | 15 |
| Gifts, bonus payments and severance pay | Tax exemption for gifts, bonus payments and severance pays of DKK 8,000 in total paid by the employer in connection with retirement or anniversary, cf. the Tax Assessment Act, section 7 U. | 178 |
| Lump sum in accordance with the Industrial Injury Insurance Act, etc. | Tax exemption for certain lump sums payable in accordance with the Industrial Injury Insurance Act, etc., cf. the Tax Assessment Act, section 7, no. 20. | 151 |
| Taxation of employee benefits | Triviality limit of DKK 5,200 (2007) regarding taxation of benefits which the employer has primarily provided to ensure the employee's work performance, cf. the Tax Assessment Act, section 16, (3). | 52 |
| Cancellation of study debt | Tax exemption for study debt remission, cf. the Tax Assessment Act, section 7.no. 23. | 57 |
| Tax exempt rewards, etc. | Tax exemption for rewards, cf. the Tax Assessment Act, section 7, no. 28. | 10 |
| Alcohol rehab | Tax exemption for payments made to alcohol rehab programmes by the employer, trade union, pension fund, etc., cf. the Tax Assessment Act section 30. | 40 |

| Tax expenditure programs – personal income taxation | Description of tax expenditure | DKK millions. ¹⁾ |
|--|---|-----------------------------|
| Land value, farmhouse | The land value of farmhouse sites and gardens is estimated at farmland value which is not indicative of the open market value, cf. the Land Assessment Act, section 33 (4). In consequence, the municipal tax charged is lower than stipulated in the Real Property Tax Act. | 16 |
| Tax relief for room letting costs | Basic allowance of DKK 7,000 related to the letting of a weekend cottage and an additional allowance of 40 % of the reduced rental income, cf. the Tax Assessment Act, section 15 O. | 124 |
| Taxable value of property (maximum increase) | If real property taxes have increased by more than DKK 500 compared to the preceding year, or by an amount representing minimum a 20 % increase over the preceding year less DKK 900, then the property value tax will be reduced by the excess amount, cf. the Property Value Tax Act, section 9. The rules applying to citizens who are not receiving retirement pension are slightly different: Real property taxes may increase by maximum DK 2,400, yet equalling minimum 20% compared to the preceding year, cf. the Property Value Tax Act, section 9 a. . | 240 |
| Taxable value of property (tax relief for senior citizens) | A 4 per mille, maximum DKK 6,000, reduction of property tax rate applying to senior citizens, cf. the Property Value Tax Act, section 8. | 505 |
| Taxable value of property (old owners) | Estimated real property tax to be reduced by 2 per mille of the basis of calculation, if the taxpayer has acquired the property no later than 1 July 1998, cf. the Property Value Tax Act, section 6. | 1,785 |
| Taxable value of property (old owners of detached houses and weekend cottages) | Estimated real property tax to be reduced by 4 per mille of the basis of calculation, maximum DKK 1,200, if the taxpayer has acquired the house or weekend cottage no later than 1 July 1998, cf. the Property Value Tax Act, section 7. | 1,095 |
| Letting rooms | Basic allowance of two third's of the rent which the letter is charged or 1.33 % of the homeowner's real property value, yet maximum DKK 24,000, cf. the Tax Assessment Act, section 15 P. | 20 |
| Savings program for professional athletes | Special pension program for professional athletes, allowing them to reclaim pension payments at an earlier age than is generally accepted, cf. the Taxation of Pension Programs Act, section 15 B. | 5 |
| Lower paid employees' transport allowance | An additional allowance for lower-paid employees of 25 % of the transport allowance, maximum DKK 6,000, cf. the Tax Assessment Act, section 9 C (4). | 175 |
| Home PC and data connection | Tax exempt home PC and internet connection to workplace network for employees. If the home PC is partially employer-paid, the tax expenditure is made up of an additional deduction of up to DKK 3,500 annually, cf. the Tax Assessment Act, section 16. | 465 |
| Increased transport allowance to pendlers residing in fringe municipalities. | The allowance for transportation over 100 kilometres per day, is estimated at a rate determined by the National Tax Board, and not the general 50 % rate, cf. the Tax Assessment Act, section 9 C. | 24 |
| Tax allowance for researchers' travel expenses, etc. | Researchers working on research grants, which are taxed at source, are allowed to apply the employee regulations governing travel expenses, cf. the Tax Assessment Act, section 27 B. | 2 |
| Researchers and key personnel | 25 % gross taxation of foreign residents' salaries for three years, if a number of requirements are fulfilled, cf. the Tax at Source Act, section 48 E. | 382 |
| Subsistence allowance and travelling allowance | Tax exemption for the part of the allowance which exceeds the actual travelling expenses, cf. the Tax Assessment Act, section 9 A. | 15 |
| Value of own work exempted from VAT and tax | Tax exemption for the value of own work, cf. the Tax Assessment Act, section 27 (26). | 25 |

| Tax expenditure programs – personal income taxation | Description of tax expenditure | DKK millions. ¹⁾ |
|--|---|-----------------------------|
| Improvement of employee share programs | Taxation of granted shares, etc. is postponed to the time when the employee is selling the shares, which are then taxed as capital gain, not salary. In consequence, the company granting the shares is not allowed to deduct the equivalent expenses. cf. the Tax Assessment Act, section 7 H. | 45 |
| Employee share options | Taxation of share options and subscription rights which are granted by a company to its employees is postponed to the time of exercise or surrender, cf. the Tax Assessment Act, section 28. | 51 |
| Free shares | Tax exemption for employee shares worth up to DKK 21,500 (2007) and tax exemption for the employer in connection with the grant of employee shares worth up to DKK 4,900 (2007), cf. the Tax Assessment Act, section 7 A. | 90 |
| Total personal income taxation | | 6,965 |
| Tax expenditure programs - VAT and duties | Description of tax expenditure | DKK millions ¹⁾ |
| Adjustment of the CO ₂ Excise Duty Act to the CO ₂ Quota Act | Fuels used in production processes which are covered by the EU's legislation on CO ₂ -quota are exempted from Danish CO ₂ -duty, cf. act no. 464 of 9 June 2004, section 3 (1) (tax treatment of CO ₂ -quota and herring quota and adjustments of the CO ₂ -duty on quota-restricted fuel consumption). | 31 |
| Entertainment – VAT | VAT exemption for cultural activities, including libraries, museums, zoological gardens etc. and supply of goods and services in relation hereto, cf. the VAT Act, section 13 (1), no. 6. | 1,763 |
| Newspapers and magazines – VAT | Zero-VAT rate for delivery of newspapers with a frequency of minimum one issue per month, cf. the VAT Act, section 34 (1) no. 14. | 974 |
| Cabs | Tax-free mileage allowance for taxi-cabs, cf. the Vehicle Registration Fee Act, section 6 (4). | 297 |
| Finance sector – VAT | VAT exemption for a number of financial activities and insurance operations etc., cf. the VAT Act, section 13 (1), no. 10 and 11). | 2,535 |
| Education – VAT | VAT exemption for teaching and supply of goods and services closely connected herewith. The VAT exemption does not apply to commercial course activities directed mainly to businesses, institutions, etc., cf. the VAT Act, section 13 (2), no. 3. | 841 |
| GP, dentist – VAT | VAT exemption for treatment provided by general practitioners and general-dentists, cf. the VAT Act, section 13. | 2,541 |
| Daycare – VAT | VAT exemption for public assistance, etc., cf. the VAT Act, section 13 (1), no. 2. Act no. 517 of 7 June 2006 made certain optional choice services subject to VAT as per 1 July 2006 which increased annual VAT income in 2006 by around DKK 56 million. | 391 |
| Nursing home – VAT | VAT exemption for public assistance, cf. the VAT Act, section 13 (1), no. 2. | 56 |
| Day-care institutions – VAT | M VAT exemption for social security and assistance, cf. the VAT Act, section 13 (1), no. 2. | 2,284 |

| Tax expenditure programs – VAT and duties | Description of tax expenditure | DKK millions ¹⁾ |
|---|---|----------------------------|
| Letting – VAT | VAT exemption for administration and letting, etc. of real-estate, cf. the VAT Act, section 13 (1), no. 8. | 197 |
| Heat and power | District heating customers are charged a reduced fee for energy delivered in connection with the combined generation of electricity and district heating. The tax expenditure thus represents a direct subsidy to district heating in preference to fuel based heating, like for example oil. | 2,051 |
| Electricity duty on renewable energy. | According to the Act on Electricity, section 2, the following types of electricity are not subject to electricity duty: electricity generated on plants smaller than 150 kW, electricity produced and consumed by trains, vessels, aircraft, etc., electricity produced by means of renewable energy and consumed by the producer, back-up power units used in connection with power failure and private solar cell plants of maximum 6 kW. | 1,646 |
| Electricity heating duty | For allocative reasons, the electricity duty on power consumption in excess of 4,000 kWh for heating of permanent residences is reduced compared to other power consumption. | 45 |
| Light beer, etc. | Light beer and root beer are duty exempted when the contents of ethyl alcohol is below 1.2 %. | 6 |
| Passenger transport – VAT | VAT exemption for passenger transport, cf. the VAT Act, section 13 (1), no. 15. | 416 |
| Mail and postage – VAT | VAT exemption for Post Danmark A/S's collection and delivery of letters and packages, cf. the VAT Act, section 13 (1), no. 13 and VAT exemption for stamps, cf. the VAT Act, section 13 (1), no. 14. | 221 |
| Package holidays – VAT | VAT exemption for travelling agencies and the services provided by tourist offices, cf. the VAT Act, Section 13 (1), no. 16. | 148 |
| Energy consumption by aircraft | Various sectors are exempted from paying energy duties on their fuel consumption, including domestic and foreign air traffic. | 139 |
| Energy consumption by ferries | Various sectors are exempted from paying energy duties on their fuel consumption, including domestic and foreign ferry service. | 315 |
| Security equipment in cars | The basis of calculation of the registration fee for security equipment is reduced by a tax allowance, cf. the Car Registration Act, section 8 (7) and so is the calculated car registration fee., cf. the Car Registration Act, section 3 (2). | 225 |
| Fuel efficient cars | Reduction of registration fee for fuel efficient cars, cf. the Car Registration Act, section 4 (2). | 5 |
| Registration fee – total loss cars | If the costs of reconstructing a car damaged in traffic does not exceed 75 % of its market value prior to the accident, then the car registration fee will not be re-calculated, cf. the Car Registration Act, section 7. | 400 |
| Services – VAT | VAT exemption for a number of expenses incurred in connection with burials, services provided by real-estate agents and membership fees for charitable associations, cf. the VAT Act, section 13 (1). | 721 |
| Diesel and compensatory fee | Diesel used as motor fuel – also taking into consideration differences in energy contents – is subject to a lower fee than petrol. The diesel fee is to some extent balanced by the compensatory fee. | 3,409 |
| Total VAT and duties | | 21,600 |

| Tax expenditure programs – business taxation | Description of tax expenditure | DKK millions ¹⁾ |
|---|--|----------------------------|
| Immediate tax deduction of certain grant financed costs related to acquisition of property. | In accordance with the Act on Taxation of Income and Property, section 4, the various government grants which businesses receive are subject to taxation. The businesses may choose to write off immediately expenses for acquisition of depreciable property paid for by government grants, cf. the Depreciation Act, section 44. The tax expenditure is caused by the fact that expenses are written off immediately rather than being depreciated over a longer period of time. | 10 |
| Additional tax deduction | Activities/projects concerning basic research and applied research which are authorised before the end of 1995 will be entitled to an additional tax deduction of 25 %, cf. the Tax Assessment Act, section 8 F. The company will be allowed to deduct additionally 25 % from the deductible expenses. The activity in question should be authorised by the Minister for IT and Research in advance. Similarly, businesses and foundations are allowed to deduct additionally 25 % of the expenses related to participation in certain EU research projects, cf. the Tax Assessment Act, section 8 G. This additional deduction is only granted if the research project has been authorised in advance and before the end of 1995. | - |
| Cooperative societies - cooperative taxation | Income subject to cooperative taxation is calculated as 14.3 % of the property owned by the cooperative. The tax falls due whether the cooperative has generated a profit or loss in that particular year. It becomes a tax expenditure because the cooperative can save up for future investments at a tax rate close to nil compared to the 25 % company tax rate on profits which ordinary companies are subjected to. | 41 |
| Foundations' basic allowance | All foundations have a tax-free basic allowance of DKK 25,000 applying to their non-commercial income, cf. the Foundation Tax Act, section 3 (2). | 32 |
| Basic allowance for cooperatives subject to foundation income tax | All associations subject to foundation tax, i.e. trade unions, trade association and employers' associations, are allowed a tax-free basic allowance of DKK 200,000 to be deducted from their non-commercial revenues, cf. the Foundation Tax Act, section 3 (2) and section 8 (3). | 30 |
| Promotion of private rental housing construction | Grants provided and applied in accordance with the Act on Private Rental Housing Construction or Act on Subsidised Housing Construction are not included in the taxable income, cf. the Tax Assessment Act, section 7 X. | 190 |
| Depreciation of works of art | According to a provision in the Depreciation Act, section 44 A, which is no longer in force, it was possible to depreciate artistic decorations made in connection with reconstruction activities or extensions made to a commercial building. However, the basis of depreciation can maximum represent 1 % of the purchase sum and the total purchase sum related to the construction, reconstruction or extension must exceed DKK 1 million. | 16 |
| Deduction on purchase of works of art | The Depreciation Act, sections 44A and 44 B. Compared to the previous act on depreciation of artwork, the provisions in this act provide expanded opportunities to depreciate artistic decoration of buildings. The requirements concerning timing of decoration and purchase sums have been abolished. Moreover, artwork purchased for placing or hanging in commercial buildings may now also be depreciated. | 15 |
| Tax allowance on donations to cultural institutions | The Tax Assessment Act, section 8 S provides companies with a tax allowance for cash donations made to cultural institutions. The provisions of the act also provide companies and private individuals with tax allowances for the value of donations made to cultural institutions in the form of artworks or cultural or natural history objects. | 35 |
| Tax allowance on gifts to foundations, etc. | Tax allowance for donations of DKK 500 to 6,800 made to charitable foundations, etc., cf. the Tax Assessment Act, section 8 A. | 114 |

| Tax expenditure programs – business taxation | Description of tax expenditure | DKK millions ¹⁾ |
|---|---|----------------------------|
| Windmills | Fuels like straw, wood chips, biogas, etc. are not covered by the energy tax and therefore represent a tax expenditure. | 86 |
| Depreciation of live stock | Live stock are eligible for depreciation. A fixed annual deduction in the taxable income is allowed. As from 2003, the tax allowance is 15 % of total live stock value which should be recognised as revenue the following year. | 55 |
| Environmental investments in farming | Provisions repealed by statute no. 433 of 26 June 1998. | - |
| Fishermen | Deduction for commercial fisheries of DKK 190 per day at sea, maximum DKK 41,800 per year, in connection with catching expeditions of minimum 12 hours duration, cf. the Tax Assessment Act, section 9 G. | 3 |
| Land value, farmland | The land value of farmland is fixed at a lower level than market value, cf. the farm provision in the Land Assessment Act, section 14 (1-3). In consequence, municipal taxes charged are lower than stipulated in the Real Property Tax Act. | 1,306 |
| Inflation guarantee, vessels | In connection with the Ship Credit Fund of Denmark's issue of index-linked bonds to finance construction or reconstruction of vessels, the state disbursed tax free amounts for the inflation guarantee. The recipients are not required to pay taxes on these amounts, cf. the Tax Assessment Act, section 7 I. | 3 |
| Small breweries | Reduced duty on beer brewed in small breweries. | 3 |
| Vapour recovery systems | Tax relief of DKK 3 øre per litre on respectively leaded and lead-free petrol supplied by petrol stations with vapour recovery systems, cf. the Act on Excise Duty on Mineral Oil, section 1 (1) no. 12 and 13. | 75 |
| Research of new markets | With effect from 1992, expenses for research of new markets for the purpose of establishing a commercial business or expand a current business will be deducted from the taxable income, cf. the Tax Assessment Act, section 8 I (2). The tax expenditure consists of a tax deduction on otherwise non-deductible establishing costs. | 100 |
| IT software | IT software and operating equipment for tests and research can be written off immediately in accordance with the Depreciation Act, section 6. | 306 |
| Establishment Account Act | Tax allowance for deposits made into establishment accounts (special savings account for individuals planning to set up their own business). After the new business has been established, this allowance is combined with a reduction of the basis for depreciation (allowance brought forward), cf. the Establishment Account Act. | 9 |
| Special rules governing establishment on Bornholm | The Establishment Account Act stipulates certain requirements to the sum spent to purchase the company's total property. In addition, the Establishment Account Act and the Investment Fund Act require active participation in the running of the company. The county of Bornholm was exempted from these requirements in 1994. | - |
| Test and research activities | According to the Tax Assessment Act, section 8 B (1), expenses for test and research activities may either be deducted immediately or depreciated over 4 years. | 2,858 |
| 150 % deduction for certain research expenses | Pilot program which has now been extended. The Tax Assessment Act, section 8 Q. This program allows an increased tax deduction for expenses incurred in connection with research projects financed partly by a commercial company and partly by a public research institution. Only amounts paid directly from the company to the research institution are deductible. In addition small to medium-sized companies may deduct salary expenses related to the project. Only co-financed research projects established up to and inclusive of the income year 2006 are covered by the program. The program will fade out after expiry of year 2006. | 23 |

| Tax expenditure programs – business taxation | Description of tax expenditure | DKK millions ¹⁾ |
|--|---|----------------------------|
| Effluent charge | Tax exemption and reimbursement of the effluent charge in connection with discharges under special conditions, cf. the Effluent Charges Act, sections 9 and 10. In addition, specific heavily polluting industries may under certain specified conditions be reimbursed for the effluent charges paid, cf. the Effluent Charges Act, section 11. . | 120 |
| VAT credit time, farming and small urban trades | Differences in credit times, depending on company turnover, cf. the VAT Act, section 57. Current regulations do not distinguish between farming and urban trades. | 241 |
| Extension of the time for payment of tax on goodwill in connection with payment of current instalments | The Depreciation and Amortization Act, section 40 (7). The deferral of payment of tax on goodwill is included in the regulations governing taxation of current instalments in mutually binding agreements. As a result of the deferral of taxation on goodwill, the vendor is not required to settle taxes till he/she receives payment for and assigns the goodwill and other immaterial rights to the vendee. | 20 |
| Banks and mortgage banks' provisions. | The Gains on Securities and Foreign Currencies Act, section 25, (6-9). The provisions allow banks and mortgage banks and other credit institutions to deduct their bad debt provisions. Generally, bad-debt losses may not be deducted before the loss has actually been suffered. The requirements to the accounts are not that strict. As a result of the provisions, the tax deduction is brought forward. | 190 |
| Provisional tax allowance for institutional investors | Tax allowance for trading on alternative markets, cf. the Pension Returns Tax Act, cf. section 5 a. Not yet in force, awaiting approval by the EU Commission. | 15 |
| energy-intensive processes - tax relief | In relation to the CO ₂ tax, companies with energy-intensive processes are granted a tax relief. | 615 |
| Capital expenditure and initial costs | Generally, companies are not allowed to deduct initial costs. With effect from 1992, lawyers and auditors fees incurred in connection with the establishment or expansion of a commercial business may be deducted, cf. the Tax Assessment Act, section 8 J. Also fees to the Danish Commerce and Companies Agency may be deducted. | 42 |
| Payment of social security contributions made by banks | Credit time for banks' payment of social security contributions, cf. the Act on Labour Market Contributions, section 13. | 20 |
| Total business income tax | | 6,575 |
| Total tax expenditures | | 35,140 |

¹⁾ The amounts in the table do not sum up to the indicated total due to rounding-off.