TAX SUBSIDIES - ACHIEVEMENT OF ACCOUNTABILITY

Tax subsidies signify a deviation from the normal structure of taxation. The purpose of this deviation is to support a particular group of beneficiaries or a particular type of activity that is considered beneficial. Tax subsidies are estimated to total about 10 billion euros a year. Tax subsidies have a significant effect on the state's revenues, corresponding to around one-fourth of the state's annual income.

This audit investigated the Government's accountability to Parliament with regard to tax subsidies. The Constitution of Finland and the State Budget Act and Decree specify criteria concerning accountability. According to these criteria all known matters influencing appropriations and revenues must be taken into consideration in the state budget. In its report on the final central government accounts, the Government must provide correct and adequate information concerning compliance with the budget and social effectiveness. In addition to statutory criteria the achievement of accountability was evaluated on the basis of legislative development projects, the budget handling of appropriations and performance management procedures. Criteria were also borrowed from international recommendations concerning the handling of tax subsidies.

The main finding in the audit was that the handling of tax subsidies in state's financial management is not in line with their economic significance. The quantity and quality of handling has also weakened in recent years. In the 1990s tax subsidies were dealt with in an appendix to the state budget. In 2000 reporting was shifted to the Government's report on the management and state of central government finances and in 2005 to the report on the final central government accounts. At the same time the amount of information was also reduced and presently the Government covers tax subsidies in a one-page summary.

In the opinion of the National Audit Office, the Government should pay clearly more attention to tax subsidies as part of the

state's financial management. Tax subsidies have a large impact on state revenues. They also signify the allocation of resources and costs in the state economy. In the National Audit Office's view this means that tax subsidies should be dealt with in reporting on the state economy both as factors influencing revenues and in connection with appropriations that are approved for the same purpose. Performance targets should be set for tax subsidies in the same way as appropriations and their achievement should be monitored and reported.

The Finnish tax reform at the beginning of the 1990s had the aims of a broad tax base and lower tax rates. Tax subsidies were also cut back at that time. In recent years the number of tax subsidies has grown and the downward trend has been reversed. The risk is that tax subsidies will be used to circumvent the ceiling for the budget expenditures. The ceiling solution provides upper limits of appropriations for the ministries. A new tax subsidy or an increase in an existing tax subsidy does not require an increase in appropriations. In this case it is possible to stay within the budget ceiling on paper but actually exceed it. In the opinion of the National Audit Office, selecting tax subsidies as a form of aid in order to stay within the budget ceiling is not proper. The choice between tax subsidies and direct subsidies as policy tools should be made on the basis of their relative effectiveness.

The audit observed that Government bills regarding specific tax subsidies have improved in recent years. In particular advance estimates of the amount of tax subsidies and the presentation of intended benefits and impacts have clearly improved. On the other hand monitoring plans are still not made and the achievement of objectives is not monitored to any real extent. In the opinion of the National Audit Office, the social effectiveness of significant tax subsidies should be evaluated regularly. There is no reason to deviate from the handling of appropriations with similar significance in this regard.

The audit looked closer at the effectiveness of tax deductions for voluntary pension insurance premiums. This system was changed in 2006. The objectives of the subsidy were not presented even at that time. This is a shortcoming that makes it impossible to evaluate the impacts of the subsidy from the viewpoint of accountability. The grounds for subsidizing voluntary pension insurance premiums should be clearly explained. This subsidy can be presumed to have two types of objective: to increase saving generally or to supplement citizens' statutory pension coverage. The subsidy appears to increase saving, but savings are not paid out in the same way as a normal pension. Instead they can easily be taken out in a fairly short time after a person reaches retirement age. There is not much difference between this and other forms of long-term saving. The need to explain grounds is also underlined by the observation that voluntary pensions are not worth taking out without tax subsidies.