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Ministry of Finance in Iceland

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Voluntary pension saving is becoming more widespread

The option to open personal pension savings accounts and deduct the contributions from income tax was introduced in 1999 when a 2% deduction was allowed. This percentage was subsequently increased to 4% in 2000 and has remained unchanged since. The number of wage earners who have taken advantage of this opportunity has steadily increased.

Deducted premiums for voluntary pension accounts

Income year	2002	2003	2004
Dedutions, million kr.	5.800	6.800	7.626
Number of taxpayers	70.566	77.107	83.400
Percentage of all contributors to general pension funds	43,4%	46,5%	50,2%

Data from the 2005 personal income tax assessment on 2004-income shows that more than half of all wage earners save for their retirement under this option in 2004. Their number had increased by 8.2 per cent from the previous year and optional pension saving rose by 12.2 per cent to 7.6 billion krónur. The average wage income of those persons who save under this option is slightly lower than for wage earners as a whole and these savers seem to be slightly younger than the overall wage-earning population, since wage income tends to rise with age. This appears to indicate that an increasing number of Icelandic wage earners deem it sensible to have greater income at their disposal upon retirement than is provided by the two other pension pillars, the general pension funds and the social security system.

Agreements on an exchange of information on tax matters

In conjunction with the work of the OECD to reduce the impact of harmful tax practices, it has been decided to commence discussions with tax havens on agreements of an information exchange regarding tax matters. This applies to instances when OECD-residents take advantage of tax havens to avoid taxation in their home countries. One aspect of this work is to conclude bilateral agreements between OECD-countries and areas that offer tax havens. Nearly all such areas have committed themselves to the OECD-countries to increase the transparency of their tax systems and tax laws and to establish realistic exchanges of information on tax matters with OECD member countries. About half of OECD-countries have commenced negotiations with tax havens for this purpose. As an example, the United States has already concluded exchange-of-information agreements with thirteen such areas.

In its deliberations, Iceland will base its negotiations on the OECD draft agreement on information exchange regarding tax matters. The draft agreement stipulates that the authorities should have access to information from banks and financial entities on specified taxpayers and could provide such information to tax authorities in the other country that is party to the agreement. The draft agreement also contains provisions with the purpose of protecting the lawful interests of taxpayers. A contracting state may, in certain instances, refuse to divulge information that could harm commercial interests. The draft agreement also stipulates that contracting authorities treat information so gathered as confidential.

Agreement negotiations will commence here in Reykjavík with the island of Guernsey in September, to be followed by Jersey later in the year. The authorities of the island of Man have expressed an interest in concluding an agreement with Iceland for the same purpose.

The interest cost of the Treasury

Following the sale of Iceland Telecom, questions have arisen regarding the use of the sales proceeds. One of the options is to reduce Treasury debt. The price for Iceland Telecom amounts to 66.7 billion krónur of which 34.5 billion is paid in Icelandic krónur and 32.2 billion in euros or dollars.

Total Treasury debt amounted to 253 billion krónur at the end of 2004 of which 112 billion is domestic debt and 141 billion foreign. The interest cost amounted to 14 billion in 2004, 9 billion for domestic debt and 5 billion for foreign debt. Interest is expected to amount to 15 billion in the 2005 budget.

As yet, no decision has been taken on the disposal of the sales proceeds. Should a portion thereof be used to repay debt, it will certainly affect the interest cost of the Treasury.

Sales profits from Iceland Telecom in Treasury and national accounts

Profits from the sale of Iceland Telecom will differ according to methods used in Treasury accounts and national accounts. Under the system of national accounts, no sales profits are recorded with the Treasury on account of the sale due to the treatment of the registration of the value of assets. According to the methodology of national accounts, the Treasury is only changing the composition of its assets, i.e. selling shares in Iceland Telecom for money. The net assets of the Treasury remain the same before and after the sale. The main reason for this conclusion is that the national accounts, which seek to register all economic events in the economy, record all assets and liabilities at market value at each point in time. At the time of the sale, the value of the shares are seen as equal to the value of the sale. Therefore, there is no sales profit or loss in the national accounting sense. The national accounts employ a quadruple-entry accounting system where the revenue of one entity is viewed as the cost of another. If the Treasury would have incurred a sales profit, it would have followed that some other entity would have incurred a corresponding loss, which can not happen under the rules of the national accounts system.

According to the methodology of the Treasury accounts, a profit can arise, based on a company-like double-entry accounting system. There, the emphasis is not on booking the market value of assets or liabilities. A sales profit can arise if the sale price of an asset differs from its book value. The book value of the Treasury's share in Iceland Telecom amounted to a little more than 9 billion at the end of 2004, whereas the sale price came to more than 67 billion. According to company accounting standards, a sizeable profit from the sale arises. It should be noted that the recorded value of Treasury-owned enterprises does not necessarily reflect their actual market value. It is quite probable that the book value of Treasury-owned enterprises has developed differently than the book value of companies in the general market. The actual sales profit according to this method – where the assets would have been booked at market value – would most likely be considerably less than the above figures would indicate.

Finally, it should be mentioned that through Iceland's participation in the European Economic Area, a basis has been created to gauge the public sector balance on the basis of the so-called Maastricht provisions, which are based on national accounting principles. Further information on a comparison between national accounts and company accounts be accessed here.

Treasury revenue. January-June

12-month changes %	2003-2004	2004-2005
Total tax revenue	14.8	18.7
Income taxes	18.2	15.5
Social security taxes	13.1	15.8
Asset taxes	18	56.8
Indirect taxes	13	18.6
Total revenue	2.3	23.9

Treasury expenditure. January-June

12-month changes %	2003-2004	2004-2005
Administration	6.1	3.6
Social affairs	13.2	6.9
Economic affairs	6.8	1.0
Interest	-15.7	64.7
Other	-2.5	14.3
Total expenditure	8.4	9.7

Treasury finances, January-June

Million krónur	2004	2005
Cash from operations	-2,243	15,536
Net financial balance	-858	25.915
Debt redemption	-28,604	-30,002
Gross borrowing requirem,	-33,212	-5,988
New borrowing	34,780	9,579
Overall cash balance	4,435	3,591

Economic indicators

12-month changes, %	2004	2005
Inflation - August	3.7	3.7
Core inflation - August	3.0	4.1
Wage index – June	5.1	6.3
Tot.turnov.Jan-April	11.3	7.1
Ret turnov.Jan-April	5.4	6.9
Unemploym.in % June	3.1	2.1

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