

# English translation of the Weekly Web Release



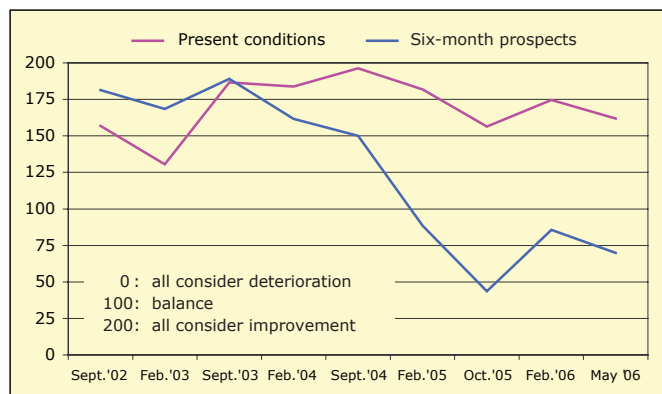
MINISTRY OF FINANCE IN ICELAND

June 15th 2006

## A new survey of business prospects

The latest IMG Gallup poll of business prospects was conducted from May 8<sup>th</sup> – 31<sup>st</sup> and covered 389 firms with a response rate of 65.3 per cent. The companies in the survey are selected on the basis of total payrolls. The survey is conducted on behalf of the Ministry of Finance, the Central Bank and the Confederation of Icelandic Employers.

The confidence index



Some 57 per cent thought that economic conditions were generally favourable and 13 per cent saw them as unfavourable. Executives of fisheries companies are generally more optimistic than in previous surveys, probably due to the development of the exchange rate in recent months. The confidence index currently stands at 161.8 points and declines from the February survey figure of 174.5 points. Business leaders are increasingly pessimistic about prospects six months from now; 18 per cent of the respondents believe that prospects will be better and 33 per cent think they will be worse. The confidence index for six months stands at 69.9 points compared to 85.7 in February. This time, twelve-month prospects were not surveyed.

In the survey, it was also inquired what impact the development of the exchange rate since the turn of the year had had upon business profits. About 32 per cent thought that the exchange rate change had a positive effect and about half an adverse effect. Firms in construction and commerce generally felt that the decline in the exchange rate would have an adverse effect on business profits, whereas nearly all in the fisheries sector saw the decline as favourable.

## Outsourcing policy for the central government

According to the proposal of the Minister of Finance, the Government has agreed upon a policy for the purchases of the central government and its agencies of services and outsourcing of various operations. Under the outsourcing policy, ministries and their agencies are requested to do analysis of the efficiency and effect of those operating tasks that the central government performs directly or has already entrusted to market entities. The policy refers to a recently introduced Regulation (no. 343/2006) concerning contracts for operational tasks of ministries and agencies for a longer term than one year. It also takes account of the central government's purchasing policy approved by the Cabinet in November 2002 and constitutes a general policy base for public purchasing.

The central government purchases goods and services for about 90 billion krónur a year. Through its purchases, the central government is therefore in a strong position to encourage competition and create new opportunities in the market. A further outsourcing of individual tasks would support such a development.

By applying an outsourcing policy, government entities acquire measurable objectives regarding the outsourcing of tasks and the benefits derived therefrom. The aim is to increase the share of purchases of goods and services in total expenditure – excluding transfers payments and interest – by 2 per cent a year. The central government should be able to save 400 million krónur a year by implementing such a policy or a total of 1,600 million krónur in the years 2007-2010. Such a saving can be used to improve government services.

This year each ministry is expected to analyse the nature and content of its public service tasks and how they can best be performed. They must formulate a policy concerning these tasks and forward it to their agencies. The intention is that such a policy will review all service and operational tasks in an organised manner and that they be assessed on the basis of how well they are suited for outsourcing. Should such an analysis conclude that such tasks are suitable for outsourcing, this should be put into offer before the end of 2008. It is also recommended that other tasks be reviewed at regular intervals, since the prerequisites for outsourcing can change over time.

The policy places particular emphasis on its implementation. The intention is to establish a consulting working party on outsourcing that will implement the policy, acquire and disseminate practical experiences on outsourcing and help in the cooperation of the central government and private companies regarding the development of individual tasks. Emphasis will be placed upon tendering to an increasing extent when decisions are made on the outsourcing of services. Tenders can be individual or grouped together for several agencies for particular sets of tasks, or frame agreement tenders can be applied for all agencies.

The policy emphasises increased education and a firm process for the formulation and implementation of service contracts. It is anticipated that attention will be drawn to tasks that already are in competition as well as to the role of outsourcing in developing innovations and greater diversity in markets. Should implementation be successful, it could provide the scope for new solutions and lead to increased competition by entrusting certain tasks to the private sector.

## Personal tax credits for the payment of the municipal income tax

The taxation of personal income is governed by the Income Tax Act and the Municipal Tax Act. The former defines income taxation for the Treasury and the latter the municipal income tax for each respective municipality. These are two separate taxes, even if they are imposed jointly. The Director of Internal Revenue levies an income tax on the income tax base of individuals. The Treasury's share is 23.75 per cent this year and the municipal share 12.98 per cent, a total of 36.73 per cent. A tax credit of 348,343 krónur is subtracted from the combined income tax, which means that the first 950,000 krónur in income bear no income tax. The municipalities, on the other hand, receive a municipal income tax as if there was no tax credit, with the Treasury paying the difference. From the standpoint of the municipalities, the municipal income tax is a flat tax, a fixed rate on all taxable personal income, regardless of the tax credit.

In a recent reply to a parliamentary question by the Minister of Finance, it was shown that payments by the Treasury to the municipalities on account of the personal tax credit amounted to just over 4 billion krónur a year in recent years. This constituted 6 per cent of the total imposed municipal income tax. The share was lower in the capital area than outside it and in a number of municipalities the share exceeded 10 per cent and in some more than 20 per cent.

Treasury revenue January-April			Treasury expenditure January-April			Treasury finances January-April			Economic indicators		
	2004- 2005	2005- 2006		2004- 2005	2005- 2006		2005	2006		2004- 2005	2005- 2006
12 month changes (%)			12 month changes (%)			Million krónur			12 month changes (%)		
Total tax revenue	21.0	15.0	General public services	122.5	-30.7	Cash from operations	13,092	24,347	Inflation (June)	2.8	8.0
Taxes on income & profit	18.0	34.0	Health	52.4	6.9	Net financial balance	19,356	21,869	Core inflation (June)	3.5	7.0
Taxes on property	64.4	-29.1	Social security & welfare	47.8	6.6	Debt redemption	-29,826	-31,685	Wage index (April)	6.7	8.4
Taxes on goods & services	19.7	6.5	Economic affairs	46.0	-6.7	Gross borr. requirement	-11,670	-11,136	Total turnover (Jan. - Feb.)	5.9	9.2
Social contributions	23.1	14.3	Education	41.0	10.4	Net borrowing	13,949	6,456	Retail turnover (Jan. - Feb.)	1.8	6.5
Total revenue	25.4	9.0	Total expenditure	58.7	-2.7	Overall cash balance	2,279	-4,680	Unemployment rate, sa (May)	2.1	1.2