

English translation of the Weekly Web Release



MINISTRY OF FINANCE IN ICELAND

December 22nd, 2005

Prepayment of 2006 taxes

The decision on the prepayment of taxes assessed for the year 2006 is now at hand. The abolition of the net wealth tax means the nature and scope of the prepayment will change, both for individuals and legal entities.

For legal entities the prepayment will cover both the income tax and the special fee on industrial entities. These taxpayers must pay 8.5 per cent monthly of the 2005 assessment of these two taxes.

The abolition of the net wealth tax will have a substantial impact on the prepayment of taxes by individuals. This year, about 75,000 individuals were assessed for a net wealth tax amounting to 2.8 billion krónur. The usual notice sent out to taxpayers at the beginning of the year concerning the prepayment of this tax will therefore not be sent this year, saving paperwork and benefitting the taxpayers.

The special fee levied on industrial entities will continue to be collected on a prepayment basis. This fee will affect about 5,000 self-employed individuals in this sector in addition to around 5,500 legal entities.

The PAYE income tax

The total PAYE income tax rate covers both the central and the local government personal income tax. On January 1st 2006, the central government tax will decline by 1 percentage point, from 24.75 per cent to 23.75 per cent, whereas the average local income tax will decline by 0.01 percentage point, from 12.98 per cent to 12.97 per cent. In the year 2006, PAYE income tax rate will be 36.72 per cent, compared with 37.73 per cent this year and 38.59 per cent in 2004. In this context, it is worth noting that as the personal income tax rate declines a further 2 percentage points in 2007, to 21.75%, the share of the personal income tax is reduced by about 16% from 2004 to 2007.

In 2006, the personal tax credit will amount to 29,029 krónur a month which means that monthly tax-free income will amount to 79,055 krónur, from 71,270 krónur a month in 2004. The tax-free income has thus increased by 11 per cent in the course of two years.

Legislation presented by the Minister of Finance that have been passed into law

The Minister of Finance presented five bills in the autumn session of the Althingi that were passed into law. In addition to the 2006 budget and the 2005 supplementary budget, they were as follows:

Changes in the Income and Net Wealth Tax Act

- 1) The special income tax reduction for seamen increases from January 1st 2006. This will affect the collection of the PAYE tax in 2006 and the tax assessment in 2007. This increase is in accordance with the increase in the personal income tax credit that was passed in the autumn of 2004.
- 2) The venue of filing tax returns and rendering tax assessments will henceforth be based on the domicile of the taxpayers on December 31st. This change will come into effect in 2006 and apply to the 2007 tax assessment.
- 3) A temporary provision is appended to the Act that permits the imposition of net wealth tax on legal entities that have an accounting year different from the calendar year when their twelve-month accounting period closes in the course of 2005. This is done to avoid discrepancies in the assessment of the net wealth tax with respect to the closure of the accounting year.

Amendments to Act no. 87/2004 regarding the diesel tax and the weight-distance tax

- 1) The temporary reduction in the diesel tax will be extended by half a year to July 1st 2006. The tax will be 41 krónur per litre.
- 2) Owners of special-purpose vehicles will have the option of paying the diesel tax and the weight-distance tax or exempting themselves from the diesel tax and pay instead a weight-distance tax according to a special schedule. This amendment takes immediate effect.

Amendment to the Annual Accounts Act

The main change is related to the republication of the Act. The Act will be republished in 2006.



The hidden value of Christmas cookies

One of the crowning features of Icelandic Christmas celebrations is the traditional baking of Christmas cookies. Housewives try to outdo each other with the baking of delicious cookies prior to the holidays in stupendous quantities and a wide array of different kinds. Families have feasted on the product of their labours over the holidays and filled whatever vacant spaces that could conceivably have been found in their digestive system after the main holiday meals. There is no doubt that the traditional eating of Christmas cookies is part of the national welfare. The problem is, however, that this is never measured by economists when they gauge the nation's standard of living. Such a measurement is expected to gauge the value added that is created when a raw material is processed into consumer goods or when a services are rendered. The trouble is that in order to measure value added, it must first be traded in the market. So far, no admission fee is charged for attending family gatherings over Christmas. This impart of national life thus escapes the watchful eye of the economists responsible for the national accounts, even if the values involved are doubtlessly substantial. The same may be said for the tradition of cutting "leave-bread" and making home-made chocolates, both a common activity in the holiday season.

There are about 75,000 core-families in the country, i.e. households with more than one member. If one assumes that three different types of cookies are baked in each household *on average* (the average covering all families from those that do not bake at all to those baking scores of different cookie types), all from home-made recipes, this will imply that there are some 225 thousand recipes around, all passed from mother to daughter. In addition, it is not unlikely that some single person households will also be baking, and it should not be forgotten that some Icelanders do not celebrate Christmas at all and have therefore not adopted this important part of the national tradition. The Ministry of Finance estimates that materials going into Christmas baking will probably amount to 100 million krónur. To put this into context, Iceland's imports of household white sugar amounted to some 200 million last year. Imports of brown sugar amounted to 9 million and another 9 million worth was imported of skinned almonds. Production of baking chocolate is estimated to have amounted to some 200 million, most of which is produced locally. In addition, there is the considerable use of energy for baking ovens and, last but not least, one should not forget the labours of the bakers, in this case mostly housewives. Since this is unpaid work, even if dearly cherished, it is not included in the national accounts.

It is becoming more usual that merchants offer factory-baked cookies in stores and it is therefore possible to estimate the value of home-baked cookies (disregarding the fact that many feel that home-baked cookies are far superior to the factory kind) by assuming the same value as those sold in stores. Based on certain assumptions, the Ministry of Finance estimates that total Christmas home-baking exceeds 200 million in gross value, of which some 100 million constitute added value. This is not a large sum, considering the assessment of the Commerce Research Centre which estimates that the extra expense of households on account of Christmas amounts to 5.8 billion krónur, about 1 per cent of the annual private consumption. Tax revenue from home-baked cookies is none, save for the value added tax on the raw materials. If store-bought cookies end up eliminating home-baked cookies, the Treasury will benefit as will the country as a whole. Or what?

The editors of the Weekly Web Release wish their readers a merry Christmas and a happy new year. The next Web Release will appear on January 5th 2006.

Treasury revenue, January-October			Treasury expenditure, January-October			Treasury finances, January-October			Economic indicators		
12 month changes, %	2003-2004	2004-2005	12 month changes, %	2003-2004	2004-2005	Million krónur	2004	2005	12 month changes, %	2003-2004	2004-2005
Total tax revenue	14.9	20.8	Administration	7.2	4.9	Cash from operations	-2,848	20,294	Inflation - Dec.	3.9	4.1
Income taxes	19.8	22.6	Social affairs	8.3	7.0	Net financial balance	6,425	68,671	Core inflation - Dec.	3.5	4.6
Social security taxes	10.3	15.6	Economic affairs	7.4	-3.3	Debt redemption	-30,856	-61,557	Wage index - Nov.	5.4	7.3
Asset taxes	25.9	35.4	Interest	-8.0	41.8	Gross borr. requirement	-30,680	3,814	Total turnover - Jan. - Aug.	9.6	9.2
Indirect taxes	12.6	19.6	Other	-0.6	76.4	Net borrowing	30,408	9,048	Retail turnover - Jan. - Aug.	4.3	6.3
Total revenue	8.1	47.2	Total expenditure	6.7	10.0	Overall cash balance	-272	12,862	Unemployment, sa (%) - Nov.	2.8	1.7