

Conclusions and recommendations of the National Audit Office

Clarity of tax legislation

Amendments of Income Tax Act 2006–2017

The goal of the Tax Administration has been to increase the degree of automation in taxation and to appropriately organise duties in order to have all taxation duties done with less employee resources than before. This goal was set during a reform of the Tax Administration organisation in 2008. At that time, one of the prerequisites set for the achievement of the effectiveness target was simplification of the tax legislation as far as possible, or at least refraining from making the legislation even more complex.

This goal was also supported by a reform of the taxation procedure. Since 2006, the tax authorities have been expected to examine the information and reports that they receive in a manner that is justified, considering the nature and scope of the matter, uniform treatment of taxpayers and the requirements of tax control. This procedure can be considered a prerequisite for the automation of taxation, as all tax returns are no longer examined on case-by-case basis, but the processing of some of them has been automated.

The National Audit Office's compliance audit covered the clarity of tax legislation. The audit covered amendments of the Income Tax Act that entered into force between 2006 and 2017.

The audit investigated whether attention was paid, in accordance with the principle of the effectiveness of taxation, to the clarity and simplicity of regulations when amending the Income Tax Act and whether the amended regulations of the Income Tax Act support the automation of taxation and thus boost performance of the Tax Administration.

During the period under review, the Income Tax Act was amended 89 times. 63 of the amendments can be classified as amendments concerning the content of the legislation, while 26 of the amendments were mostly technical in nature. The content of a total of 229 sections was changed. The changes can be divided into changes of the taxation policy and changes of single regulations. As a general rule, taxation policy changes took place once a year in connection with the preparation of the budget. 80% of the changes concerning the content of the legislation involved the taxability of income and deductions from income or tax deductions.

The National Audit Office is of the opinion that the structure and systematics of the Income Tax Act remain functional and enable the development of clearer tax legislation. However, the changes made in single regulations only clarified the tax legislation in some exceptional cases. Amendments that are partial, valid for a fixed period of time or temporary, or that involve a long transition period or special provisions, can be considered especially problematic for the effectiveness of taxation.

One goal with the audit was to assess the clarity and transparency of amendments made in the Income Tax Act from the perspective of the state budget. Tax policy changes made in the Income Tax Act have a fixed, formal connection with the annual state budget proposal. The income tax scale proposal and proposed Income Tax Act amendment regarding a fiscal year create a tax policy entity the key goal of which is, depending on the current economic situation, to lower taxes or to prevent increasing of

the taxation of employment or taxation as a whole. Income taxation has only yielded towards the lowering of taxes. Therefore, the goals have not had a direct contact with the need for financing of the state budget expenses as the budget proposal shows a deficit.

Both goals concerning the level of taxation and social policy goals, such as the promotion of employment, have a major impact on tax solutions. Income taxation is closely connected to social policy decision-making, which poses a challenge to the clarity of the Income Tax Act. As decisions on taxes are made largely based on other grounds, the taxation effectiveness principle and the clarity and simplicity of related regulations receive less attention. The National Audit Office points out that the opportunity to take the clarity and simplicity of regulations into account to a sufficient extent in the preparation of tax legislation should be taken into account.

Getting a clear overall idea of the Income Tax Act as a whole is made more difficult by the large number of tax subsidies, complexity, amendments, single exceptions and the variation of justification. Welfare benefits are granted as both taxable and tax-free income. For example, 13 of the benefits granted by the Social Insurance Institution (Kela) are taxable and 16 are tax-free. The justifications for exemption from taxation are not clear and consistent.

The Income Tax Act is subject to a great deal of interpretation, which is why it does not support efficient automation of taxation. The large number of judgements on the taxation of personal income published by the Supreme Administrative Court make the Income Tax Act even more open to various interpretations. In every other case, the Supreme Administrative Court came up with a conclusion that was not the same as the decision made by the Administrative Court that resolved the case or by the Central Tax Board. Furthermore, the Supreme Administrative Court was not unanimous in almost a quarter of the cases.

It is the National Audit Office's opinion that the implementation method of tax deductions has a key role in the assessment of decisions on taxes from the viewpoint of effectiveness. As administration becomes more automated, the implementation methods of tax deductions will be even more significant for the opportunity of the Tax Administration to further boost the effectiveness of its operations while simultaneously promoting correct and standardised taxation. At worst, single tax deductions may give rise to major additional expenses in administration.

On the basis of the audit, attention should be paid to the fact that even though additional duties could be handled with the existing resources at the time when a regulation is amended, achieving administrative savings in the long term will be even more difficult if there is a large number of duties caused by a variety of exceptions and amendments.

On the basis of the audit, the National Audit Office issues the following recommendations:

- In addition to the regulations as a whole, the clarity of single regulations and the possibility to automate taxation should be taken into account when preparing amendments to the Income Tax Act. The effectiveness of taxation should be a key viewpoint when considering the implementation of tax deductions that are based on information provided by the taxpayer, because such deductions cannot be effectively automated and monitored.
- The justification for tax subsidies given in connection with the preparation of the budget and amendments to the Income Tax Act should be more systematic and whenever possible, the estimated administrative impact of alternative direct aid should be offered.

- The Ministry of Finance should create clear and uniform criteria for the taxation of welfare benefits to standardise their taxation and clarify the drafting of laws.