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Tax expenditures of the Swiss Confederation

Examination of the reporting of the Federal Finance Administration

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Key facts

Every year tax expenditures cause losses of at least CHF 2.5 billion of tax revenues for the Swiss Confederation. Tax incentives thus represent one of the Confederation's most important steering instruments. Tax exceptions can be found in all types of taxes, particularly in the direct federal tax, in the value added tax, stamp duty and also increasingly in the mileage-related HGV charge. The Subsidies Act obliges the Swiss government to examine its subsidy regulations at least every six years. Tax expenditures are likewise to be examined as they represent a special form of subsidy. In 1997 the Federal Finance Administration (FFA) reported for the first time in the Subsidy Report (part I) on corresponding tax expenditures.

The Swiss Federal Audit Office examined this reporting and recommends several improvements for the coming report in 2005. The FFA should describe which tax standards it applies. The definition of tax expenditures must be extended so that less tax expenditures are excluded from the report. Estimates and tables are to be integrated into the report and should be organized in such a way that comparisons with ordinary subsidies are facilitated. Further recommendations of the Swiss Federal Audit Office concern the fundamental assessment of financial and fiscal incentives, the integration of information about the impact of tax expenditures in the report and, finally, the way it is received.

The original text is in German

Steuervergünstigungen beim Bund
Prüfung der Berichterstattung der Eidgenössischen Finanzverwaltung

Das Wesentliche in Kürze

Steuervergünstigungen verursachen dem Bund Einnahmenausfälle von mindestens 2.5 Milliarden Franken pro Jahr. Steuerliche Anreize stellen damit eines der bedeutsamsten Lenkungsinstrumente der Eidgenossenschaft dar. Ausnahmeregelungen sind in allen Steuerarten des Bundes enthalten; eine besondere Häufung von Vergünstigungen befindet sich im System der Direkten Bundessteuer, bei der Mehrwertsteuer, den Stempelabgaben und zunehmend auch bei der Schwerverkehrsabgabe. Das Subventionsgesetz verpflichtet den Bundesrat, mindestens alle sechs Jahre die spezialgesetzlichen Subventionsbestimmungen zu überprüfen. Steuervergünstigungen sind ebenfalls zu untersuchen, wenn sie als geldwerte Vorteile eine spezielle Form der Subventionierung darstellen. Die Eidgenössische Finanzverwaltung (EFV) hat erstmals im Subventionsbericht Teil I von 1997 über entsprechende Steuervergünstigungen berichtet.

Die Eidgenössische Finanzkontrolle hat diese Berichterstattung überprüft und empfiehlt, dass beim kommenden Bericht 2005 verschiedene Verbesserungen vorgenommen werden. So sollte die EFV darin erläutern, von welchen Steuernormen sie ausgeht. Die Definition der Steuervergünstigungen muss offener sein, damit weniger steuerliche Regelungen aus dem Bericht herausfallen. Der Zahlenteil ist gemeinsam mit dem übrigen Bericht zu publizieren und so zu gliedern, dass Vergleiche mit den normalen Subventionen leicht fallen. Weitere Empfehlungen der Eidgenössischen Finanzkontrolle betreffen die grundsätzliche Beurteilung von finanziellen und steuerlichen Förderinstrumenten, die Vermittlung von vertieften Informationen über Steuervergünstigungen und die Rezeption der Berichterstattung.

Originaltext in Deutsch

Allègements fiscaux de la Confédération
Examen du reporting de l'Administration fédérale des finances

L’essentiel en bref

Les allègements fiscaux entraînent un manque à gagner pour la Confédération d'au moins 2,5 milliards de francs par année. Ils constituent ainsi un de ses moyens d'action les plus importants. Des dérogations sont prévues dans tous les types d'impôts. L'impôt fédéral direct, la taxe sur la valeur ajoutée, le droit de timbre et, de plus en plus, la taxe poids lourds se caractérisent par un grand nombre d'allègements fiscaux. La loi sur les subventions oblige le Conseil fédéral à examiner au minimum tous les six ans les actes normatifs régissant les subventions. Les allègements fiscaux doivent également être examinés lorsqu'ils constituent, en tant qu'avantages monnayables, une forme spéciale de subventionnement. En 1997, l'Administration fédérale des finances (AFF) a traité des allègements fiscaux dans son premier rapport sur les subventions (partie I).

Le Contrôle fédéral des finances a examiné le traitement de ces allègements fiscaux et recommande diverses améliorations pour le futur rapport de 2005. Ainsi l'AFF doit expliquer sur quelles normes elle se fonde. La définition d'allègement fiscal doit être plus large pour accroître le nombre d'actes normatifs traités dans le rapport. La partie chiffrée doit être publiée conjointement avec le reste du rapport et structurée de manière à faciliter la comparaison avec les subventions. D'autres recommandations du Contrôle fédéral des finances concernent l'appréciation générale des allègements fiscaux en tant qu'instrument d'action de l'Etat (concrétisation de l'art. 6 lit. e de la loi sur les subventions), la diffusion d'informations approfondies concernant les allègements fiscaux et la bonne communication du rapport.

Texte d'origine en allemand

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1. Introduction

1.1 Why broach this topic?

There are a number of OECD countries who regularly report on their tax expenditures. The IMF has already recommended that Switzerland does likewise in order to improve transparency in public expenditure. The Federal Finance Administration reported in 1997 for the first time on tax expenditures in the Subsidy Report. The next publication on this topic should appear as the 2005 Subsidy Report. The Swiss Federal Audit Office (SFAO) has examined the reporting on federal tax expenditures of 1997 (audit mandate dating from 19.08.04). Two main issues are of concern to the SFAO, namely:

- What changes should be made to reporting practice in the short term (within the framework of the 2005 Subsidy Report)?
- What further refinements in reporting should be targeted beyond the 2005 report?

1.2 Our Approach

In order to respond to these two questions two subject areas were looked at in detail:

- reporting on federal tax expenditures in the 1997 Subsidy Report (hereafter also referred to in short as the 1997 Report)
- international experience and problem-solving in reporting on tax expenditures

The results from this review are presented in Chapters two to nine. Chapter ten contains the conclusions drawn there from. Annex 1 contains the essential results in the form of a proposed report structure. Recommendations drawn from chapters one to nine are listed in Annex 3.

Overall responsibility for this examination lies with the Swiss Federal Audit Office. The study was conducted by its Performance Audit & Evaluation Unit. Management of the mandate was assumed by Armin Vuillemin; the project was conducted by Bruno Nideröst (project management / subjects of international experience and problem-solving) and Tobias Bauer (1997 Report) under the supervision of the Head of the Performance Audit & Evaluation Unit, Emmanuel Sangra.

The Swiss Federal Audit Office discussed this report on 22 December 2004 with the Federal Finance Administration as well as with the Federal Tax Administration on 26 January 2005. The Federal Finance Delegation treated the report in its regular meeting of 20 - 21 April 2005. The report on the examination is available on the SFAO's website (www.efk.admin.ch, publications, audit reports).

2. Legal requirements on reporting

Article 5 of the Subsidy Act of 5 October 1990 (SR 616.1) obliges the Federal Government to periodically carry out an examination of the specific legal provisions on subsidies with regard to their compliance with the principles set down in Chapter 2 of the Subsidy Act (Articles 6 - 8). Reporting must be carried out at least every six years, although a shorter interval between examinations is also permissible.

Key articles in the Subsidy Act on reporting on tax expenditures

Art. 5 Periodic examination

[1] The Federal Government carries out periodic examination, at least every six years, with regard to compliance of the provisions governing financial assistance and compensation with the fundamental principles laid down in this Chapter.

[2] The Federal Government reports the conclusions of the examination to Parliament. If necessary, it motions to amend or abolish legislation and ensures the amendment or abolition of ordinances. In so doing, it shall consider the need, in the interests of recipients of financial assistance and compensation, to provide for continuity of law.

[3] The Federal Department of Finance draws up proposals for legislation and reports in conjunction with other relevant departments as required and submits motions to the Federal Council.

Art. 6 Prerequisites

Provisions governing financial assistance may be waived if:

a. the task is in the interests of the Confederation;
b. it is not necessary for the task to be fulfilled autonomously by the cantons or supported by the cantons in the interests of an efficient division of tasks and costs, or moreover if the fulfilment or support of these tasks place particular burden on individual cantons and if adequate financial equalisation between cantons is not possible;
c. the task cannot be adequately fulfilled without financial assistance;
d. reasonable autonomous funding initiatives and other funding options are inadequate; and
e. the task cannot be fulfilled more simply, more effectively or more rationally in an alternative manner.

Art. 7 Other conditions

Provisions governing financial assistance are to be based on the following conditions:

a. The task must be able to be fulfilled effectively, economically and with a minimum of administrative outlay.
b. The level of financial assistance provided is determined by the level of interest on the part of the Confederation, as well as on the part of the recipients in seeing the task fulfilled.
c. The recipient is required to provide a contribution commensurate with his economic capacity; in the case of financial assistance to the cantons and to their regional public corporations, this should be in accordance with the economic capacity and financial strength of the canton.
d. The recipient shall within reason take full advantage of his own resources, as well as of other sources of funding at his disposal.
e. Financial assistance will be set as a broad package insofar as the desired objectives can be met in this manner and the fulfilment of the task can be achieved economically.
f. Financial assistance in the form of start-up, reorganisation or relief funding with fixed time limits is envisaged where possible.
g. The provision of financial assistance in the form of tax expenditures will generally be renounced.
h. Financial policy requirements will be taken into account wherever possible, in particular with respect to provisos on loans and maximum interest rates.

Art. 8 Financial assistance by the cantons

[1] In the interests of an efficient division of tasks and costs between the Confederation and the cantons, it is envisaged that, as a rule, financial assistance will only be given if the cantons, including their public corporations, likewise provide financial assistance in accordance with their financial strength.

[2] Cantons which supplement federal financial assistance are expected, as a rule, to participate in the execution of the same. Applications for financial assistance and the provision of the same should occur via the cantons. The activities of the authorities should be coordinated and multiplicity in administrative procedures should be avoided.

Tax expenditures therefore represent a special type of subsidy. Article 3, paragraph 1 of the Subsidy Act defines financial assistance as "monetary advantages accorded to recipients outside of the federal administration in order to encourage or support the fulfilment of tasks designated by the recipient". As concluded in the Subsidy Report of 25 June 1997 (p. 24), a monetary advantage can be accorded to an economic subject not only in the form of financial transfers (financial assistance), but also through a waiving of financial claims (i.e. tax expenditures). According to Article 5 of the Subsidy Act, tax expenditures must be reported on. Reporting on tax expenditures is all the more important as, according to Article 7g, the provision of financial assistance in the form of a tax expenditures should generally be renounced.

3. Definitions and scope of the 1997 Report

The basic definition of a tax expenditure used in the 1997 Report is that it refers to a deviation from normal taxation. In contrast, a general deduction is often incorporated as part of the benchmark tax system, as it is available to all taxpayers in order to take into account the basic needs of food, clothing and housing and thereby virtually is part of the tax system itself, just as tax rates do. Such general deductions can be built into the tariff scale without producing a significant change to the distribution of the tax burden. If a deduction is part of the benchmark tax system, then it does not represent a tax expenditure.

3.1 The benchmark tax system

The Subsidy Report concludes that an insurmountable difficulty is posed just by the very task of defining what actually represents the "tax norm" (see p. 25 of the Report 1997). However, it is not further explained in the Report as to how this methodological problem was dealt with. Tax law is complex - it contains tax deductions and rate reductions, tax exemptions, tax credits and rebates, as well as deferrals. Deciding what constitutes the tax benchmark system, and deviations from it, therefore represents a preliminary and key step for determining tax expenditures. In this respect, the following questions should be addressed for example:

- What is the tax unit used for imposition on personal income?
- How is the juxtaposition between corporation tax and income tax treated?
- How to deal with depreciation regulations?
- How is the imputed rental value of owner-occupied freehold property treated?
- How are contributions to the first, second and third pillar classified?

It should be emphasized that differentiating between the benchmark tax system and deviations from it does not represent a political, ethical or economic value judgement, but rather represents simply a first step in a process at the end of which tax expenditures are documented in the Subsidy Report.

The examination by the Swiss Federal Audit Office has revealed that there are various differing approaches for establishing the benchmark tax system:

1. A tax system can serve as a reference system which is based upon the *concept of synthetic income tax, as well as on the principle of financial capacity*, as the decisive standard of income tax law.
2. The reference system can be viewed from the *perspective of tax imposition on cash flow*.

3. The tax benchmark can be determined using the *outcome of tax optimisation theory*, based upon which tax expenditures are to be defined.[1]

4. The *revised theory on net accrual (the Haig-Simons Net Accrual Theory)* - according to which all real increases in wealth, less real losses, are treated as income.[2]

Making a choice from among these different systems for tax expenditure reporting has the following ramifications:

- Information content of the report: the narrower the definition of the tax norm and the broader the definition of the deviation from this benchmark, the greater the information content of the reporting and vice versa.

- Classification or non-classification: according to selected benchmark, certain tax exceptions will be considered to be a deviation from the norm or not (the Cash-Flow approach, for example, does not consider expenditure on pensions, nor special and accelerated depreciations, to be deviations from the norm, whilst other models do consider them to be so).

- Evaluating tax expenditures as an instrument: tax optimisation theory looks at the tax system with a view to its overall economic impact. From this perspective, tax exceptions can be useful, for example, in order to take into account differing price elasticity's of demand for certain goods and services. From the point of view of synthetic income tax and the principle of financial capacity, these points are irrelevant - for this reason, tax expenditures here tend to be assessed as unfair and incompatible with the tax system.

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[1] Boss, Alfred and Rosenschon Astrid (2004): Steuervergünstigungen in Deutschland: eine Aktualisierung [Tax Expenditures in Germany: An Update]. Kieler Working Paper 1220; provisional manuscript pp. 2 - 3. Also see Department of Finance, Canada (2000): Tax Expenditures and Evaluations 2000, pp. 40 - 45.

[2] For example the revised "Haig-Simons Net Accrual Theory" is the basis for the work of the Behnisch Committee which is investigating loopholes in the existing tax system in accordance with the Direct federal tax Act and the DTHA (Federal Act on Harmonisation of Direct Taxation at the Cantonal and Communal Levels).

Recommendation 1a
It should be explained in the methodology section to the 2005 Report, what is meant by the tax norm that constitutes the normative benchmark tax system.
Keeping the information objectives of the reporting in mind, the term *benchmark tax system* must be narrowly defined, and the term *deviation from the benchmark* must be broadly defined, so that as few special tax provisions as possible are left out of the reporting. In case of doubt, the Report 2005 should contain one case too many rather than one case too few, as this would raise its information content.

Recommendation 1b
In an *Appendix 1* to the 2005 Report*, Special Provisions considered part of the tax benchmark system*, should be outlined. This should show those deductions, measures and peculiarities of the tax system which are considered to be part of the tax benchmark.
As the federal tax system comprises several types of taxes, Appendix 1 should be further sub-divided as appropriate (with e.g. *1a Special tax provisions as part of the benchmark in direct federal tax*, *1b Special tax provisions as part of the benchmark in stamp duty*, *1c Special tax provisions as part of the benchmark in Value Added Tax* and so on).

Creating such an Appendix 1 is basically a once-off exercise. If the appendix were to be incorporated into the 2005 Report, it would only need to be republished for a following report in an updated form, providing that relevant amendments to tax legislation have occurred.

The Canadian government's Department of Finance labels the Appendices 1a, 1b etc. as *Memorandum Items*.[3] For example, it includes credits for tax on dividends as part of the tax benchmark, in order to avoid the double taxation of dividends at the corporate level as well as at the shareholder level. Thus, already from the outset, this special provision in tax law is ruled out as a tax expenditure. Furthermore, this appendix also lists elements of the tax system for which good arguments can be found for, as well as against, considering them as part of the tax benchmark (for example deduction of removal costs, carrying capital losses forward, carrying losses forward for farms and fisheries). This approach improves transparency and raises the information content of the reporting.

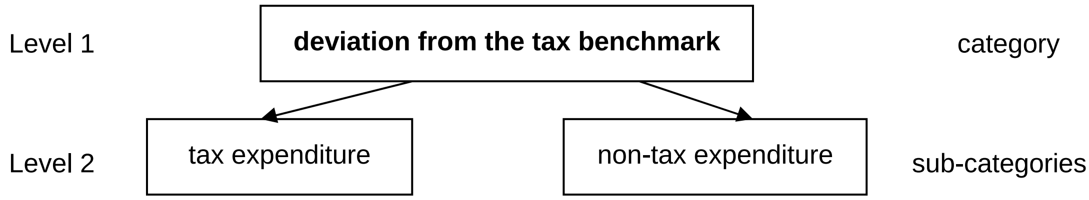
3.2 Deviations from the tax benchmark

Deviations from the tax benchmark (as consistently defined) is further sub-divided in a second stage in the 1997 Report into "tax expenditures" and "non-tax expenditures" - the latter term is not actually used in the Report, but can be deduced from the description used (i.e. "is not a tax expenditure"). This two-step approach (firstly, the defining the tax benchmark, and secondly, sub-dividing into deviations from the tax benchmark and further categories) is basically applied in a

[3] Department of Finance, Canada: Tax Expenditures: Notes to the Estimates/Projections 2004.

similar manner in Germany, the USA and in the U.K.[4] The following ***Figure 1*** should provide an overview of this approach:

Figure 1: Notions and categories



The 1997 Report goes into great detail on its approach on Level 2, but not on Level 1. For classification as a tax expenditure, an item should represent an exception to the tax benchmark (exactly as is the case with financial transfers) - i.e. *a conscious act on the part of the government in order to encourage certain behaviour* (p.24). The Report then applies eight further criteria to classify a deviation from the tax benchmark as a tax expenditure:

2. A tax expenditure contains a monetary advantage without the *delivery of a usual market service*.[5]
3. A tax expenditure supports a *voluntary activity* (from a legal point of view, the beneficiary is free to decide whether he or she carries out the activity fostered).
4. A tax expenditure is linked to the fulfilment of a specific activity or task (*a behavioural obligation*).
5. A tax expenditure can only apply to taxpayers outside of the *federal administration* (which also includes the army for example).
6. *Fiscal-based deductions*. Deductions resulting from the nature of the tax structure and principles on which the system is based, do not represent a tax expenditure in the case of direct taxes (i.e. the system of imposition on net income).
7. Special provisions that stem primarily from *reasons of imposition efficiency* do not represent tax expenditures.
8. Provisions which apply to the *majority in general* do not represent tax expenditures. Apart from this, the number of taxpayers is not important for the question of whether a tax expenditure applies or not.
9. Special tax provisions arising from *international obligations* do not represent tax expenditures (such as for example, the special tax treatment of foreign diplomatic representatives in Switzerland).

The Report does not explain whether the criteria are to be met as exceptions, or simply met for the most part, in order to be assigned the classification (i.e. that of a tax expenditure). Criteria 1 to 5

[4] Department of Finance, Canada: Tax Expenditures and Evaluations 2000, p. 39 and following pages

[5] As the requirement for a conscious involvement by the government also represents a criteria as described below, the numbering here starts already at number two and not with number one as in the 1997 Report.

can be traced back directly to the Subsidy Act, in a similar manner to financial transfers. In order to reduce the latitude that still remains after applying the first five criteria, criteria 6 to 9 were additionally formulated. However, based on the 1997 Report, there are further cases which cannot be clearly classified, due to the fact that in many cases of deviation from the tax benchmark, several reasons apply simultaneously. Furthermore, many of these objectives fall into policy conflict, such as shown by the following examples:

- *Efficiency in tax imposition, but at the same time, providing tax relief to the self-employed.* In the case of the provision whereby self-employed with an annual turnover of less than CHF 75,000 are exempt from value added tax, grounds of imposition efficiency could be a primary consideration. Nonetheless, the aim of providing relief to the small self-employed from the administrative and financial burden, can indeed also enter into it. This applies similarly in the case of the exemption applied to alcoholic spirits for one's own use, or in the reduced tax rate for small producers.
- *Imposing tax on net income, but at the same time, meeting a range of objectives of encouraging certain behaviour.* Fiscal-based deductions (i.e. deductions resulting from the nature of the tax structure and principles on which it is based) come, on the one hand, from the basic concept of imposing tax on net income. For natural persons this applies to deductions allowed for costs incurred in exercising one's profession, as well as to the majority of general deductions. The fact that donations to charities are also allowable under a general deduction is a form of encouragement of desirable behaviour and represents, therefore, as already mentioned above, a tax expenditure. The eligibility of contributions to individual pension plans as a deduction can indeed be explained by the logic of fiscal-based deductions; but nonetheless, this provision does in fact also contain a substantial tax expenditure component.
- *Imposition based on financial capacity, but at the same time favouring the family -* Fiscal-based deductions can also be traced back to the logic of tax imposition according to financial capacity. This refers for example, to family situation based tax deductions in direct federal tax for children and dependents. At the same time, these deductions take on the aspect of encouraging or facilitating certain behaviour (e.g. raising children).[6]

From the point of view of the Swiss Federal Audit Office, choosing to sub-divide on a second level, as carried out in the 1997 Report, basically makes sense, as the first five criteria resemble criteria for other subsidies. This practice makes comparisons easier and improves the compatibility of the reporting on tax expenditures with the remainder of the Subsidy Report. However, criteria eight and nine might be better applied on Level 1. One deduction for all comes very close to a generally applicable benchmark and the special treatment accorded to foreign diplomatic representation could be considered as a generally applicable benchmark between governments.

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[6] It is in this very context that family policy debate is taking place as to whether it would not be more transparent and socially fair to introduce explicit transfers (child benefits and bonuses) instead of tax deductions (see for example, parliamentary initiative 00.430, Fehr Jacqueline: Supporting the family - a change of system).

The criteria applied in the 1997 Report however, in many cases may not solve the delineation problem once and for all between tax subsidies and other deviations from the tax benchmark. In light of experience in other countries this is not surprising, since there is no internationally recognised definition of the term "tax expenditures".[7] This is first and foremost due to the fact that in many cases it cannot be clearly established what constitutes the tax benchmark and what represents a deviation from it. Secondly, there is frequently no clear-cut dividing line between a tax expenditure and other deviations from the norm. This lack of clarity is part of the nature of tax expenditures. The 1997 Report gives an unduly strong impression that, thanks to its application of the criteria, a clear cut classification of all tax expenditures has been made possible.

If we look at reporting in other countries, we must ask ourselves whether or not the division on Level 2 should not be broken down into more than two sub-categories. In any case, Level 2 requires two distinctly separate and distinguishable groups. In France, a report from the *Conseil des Impôts* from 2003[8] proposes a more thorough two part division, whereby the *dépenses fiscales* (on Level 1) should be further broken down into *allègements structurels* (structural relief) and *instruments de politique publique* (public policy instruments).[9]

In the U.K., deviations from the tax benchmark are described as *tax relief.* They are divided into three sub-categories on Level 2 - namely, *tax expenditures*, which are alternatives to normal subsidies and generate a similar impact; the second sub-category is described as *structural relief,* which is an integral part of the tax system; and between the two lies a category to which border cases are allocated, displaying features of both *tax expenditure* and *structural relief*. In this middle category are included, for example, deductions for old age allowances, child benefits, as well as special disability living allowances. The reasons for allocating deductions to the middle category vary from case to case - the deduction for married couples contributes to neutrality of the tax system with regard to civil status; the deduction of a non-realised price gain in an estate simplifies the system. All deductions in the middle category also contain objectives falling outside of the tax system.[10]
A proposal from the Canadian Department of Finance would appear to differentiate to an even greater extent, working with four sub-categories on Level 2. The main criterion to be applied for breaking down all tax exceptions (*tax concessions,* Level 1) is whether or not they can be replaced by normal subsidies.

In the Swiss Federal Audit Office's opinion, such sub-categories have both advantages and disadvantages. On one side, they permit a detailed classification of information, but on the other, they make it more difficult to overview the report and interpret its content. The U.K. solution, with its middle category, demonstrates that in some cases, classification on Level 2 is not always clear-cut. The Canadian proposal focuses rather on the replacement of tax expenditures by instruments of

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7 Department of Finance, Canada: Tax Expenditures and Evaluations 2000 p. 49.

8 Conseil des Impôts: La Fiscalité Dérogatoire. Pour un Réexamen des Dépenses Fiscales. XXIème Rapport au Président de la République, September 2003, pp. 151 - 157.

9 Conseil des Impôts: La Fiscalité Dérogatoire, p. 151.

10 Conseil des Impôts: La Fiscalité Dérogatoire, pp. 39 - 41.

direct support, as in making their classification, they apply the criterion of substitutability with a financial subsidy.

The breakdown of deviations from the tax benchmark into sub-divisions on Level 2 does not, however, represent an evaluation as such. This classification exercise too simply represents a second step in a process at the end of which tax expenditures must be established, in order that they may be reported on within the framework of the Subsidy Act.

Recommendation 2
In the opinion of the Swiss Federal Audit Office, the two part division opted for in the 1997 Report, namely of tax expenditures and "non-tax expenditures", can be retained.[11] It should, however, be explained in the 2005 Report that classifying an item as a tax expenditure is not always clear-cut, due to the fact that tax expenditures often pursue several objectives simultaneously.

The issue of how tax expenditures and "non-tax expenditures" are to be published in the Report will be dealt with in the following sections.

[11] A comprehensive term for "non-tax expenditures" is "other deviations from the tax benchmark".

4. Quantifying tax expenditures

Appendix 3 of the 1997 Subsidy Report contains a list of tax expenditures. The estimates and tables were not published in the Subsidy Report, but were available on request to the Federal Finance Administration. In the SFAO's opinion, this method of publishing does not take into adequate consideration the objectives of the reporting, namely, that of making information available to parliament and the general public.

Recommendation 3
The estimates and tables section on tax expenditures should be published in the 2005 Report directly following the body of the text.

Appendix 3 of the 1997 Report covers 46 tax expenditures. As illustrated by the following **Table 1**, tax expenditures were mostly found in the areas of stamp duty (14), direct federal tax (12) and value added tax (8).

Table 1: Tax expenditures in the 1997 Subsidy Report

	number of tax expenditures	number of which estimates are available on revenue foregone	estimated revenue foregone in CHF millions *
Stamp duty	14	13	1,424
Value added tax	8	2	270
Vehicle duty	2	2	1
Mineral oil duty	2	1	144
mileage-related Heavy Vehicle Charge	4	4	28
Direct federal tax	12	6	725
Import duties	4	3	8
Total	46	31	** 2,600

* estimates on revenue foregone (tax losses) relate to different base years (1991 - 1997). Data for a base period were converted into annual values.

** this summing was carried out by the Swiss Federal Audit Office purely for informational purposes and should be interpreted conservatively for the reason that
a) some tax expenditures listed in the first column could not be estimated,
b) tax expenditures are mutually dependent.

The 1997 Subsidy Report stresses that Appendix 3 does not claim to be complete.

In exploring the subject of tax expenditures, the Swiss Federal Audit Office undertook an examination of legal provisions in all types of taxes and from this compiled a list of potential tax expenditures. As is clear from the following **Table 2**, this produced around two and a half times more potential tax expenditures than listed in the 1997 Subsidy Report:

Table 2: Potential tax expenditures

	Tax expenditures according to the 1997 Report	Potential tax expenditures according to the SFAO's 2004 list
Stamp duty	14	14
Value added tax	8	28
Tobacco duty	0	1
Duty on spirits	0	2
Vehicle duty	2	2
Mineral oil duty	2	3
mileage-related Heavy Vehicle Charge	4	17
Direct federal tax	12	36
Gambling houses tax	0	3
Withholding tax	0	5
Military service exemption tax	0	5
Import duties	4	5
Total	46	121

The variances are particularly significant in the following areas (highlighted in the table above):

- **Value Added Tax**: the significantly higher number of tax expenditures revealed in the SFAO's revision is partly a reflection of the fact that in the new Value Added Tax Act of 2 September 1999, additional new tax expenditures were introduced. Moreover, special tax provisions were also incorporated into the SFAO list primarily on grounds of imposition efficiency or other grounds.
- **Mileage-related Heavy Vehicles Charge**: the SFAO's revision produced more than fourfold the number of tax expenditures than appeared in the Subsidy Report. This can mainly be explained by the new Federal Act of 19 December 1997 on the capacity-linked mileage-related Heavy Vehicle Charge, which makes a stronger differentiation between the components of the tax expenditure.
- **Federal Direct Tax**: the substantially higher figure contained in the Swiss Federal Audit Office revision can be explained in particular by the inclusion of special tax provisions for reasons primarily grounded in the fiscal system.

The narrower definition of the term *tax expenditures*, as used in the 1997 Report, is, in the opinion of the SFAO, justified in itself. Nonetheless, the Report also lacks an Appendix 2, in which every deviation from the tax benchmark that has not been itemised as a tax expenditure at Level 2 (i.e. the "non-tax expenditures") would be listed. Without the inclusion of such an Appendix 2 the 1997 Report is substantially missing out on information content.[12] The combination of the lack of an

[12] In the worst case, the lack of an Appendix 2 leaves scope for manipulation. In the report from the French *Conseil des Impôts* it was observed that in the majority of cases where tax expenditures were supposedly "abolished",

Appendix 2 plus the narrower definition of the term tax expenditure prevents the attainment of the information objective of reporting. Deductions for payments in pension funds would probably appear in this Appendix 2. They are not contained in the figures section for 1997. Contributions to and purchase of assets in pension institutions were not considered to be tax expenditures, probably due to the criteria of the "voluntary nature" of the contributions; however forced savings plays an important role in the Swiss pension system. Nonetheless, here too, the division between tax expenditures and other tax measures is questionable, as more than half of the capital stock of the pension system in Switzerland stems from voluntary contributions. Regardless of how one classifies deductible pension fund contributions: such an important deduction should be included to the Report - at least in an appendix.

Some countries not only publish figures on tax expenditures in the narrow sense, but also attachments containing other deviations from the tax benchmark system.[13] Valuable information on tax measures is thereby made accessible, and transparency for the benefit of parliament and the general public is improved. The criteria applied on Level 2 serve in these countries only to classify tax expenditures and other tax measures into their appropriate category, but they are not decisive for the tax measure’s being or not being in the Report. The reader can decide for himself whether or not the exception from the tax benchmark represents a tax expenditure or not. This strengthens the overall acceptability of the reporting. In borderline cases, an Appendix 2 can serve the purpose of taking up the flak on disputes about the applied definitions and demarcations, as no deviation from the tax benchmark is omitted from the reporting.

In Germany, the World Economic Institute in Kiel applies a liberal definition of tax expenditures and thus obtains around three to four times more tax expenditures than the Ministry of Finance.[14] Public debate on the topic is not helped by the existence of differing nomenclatures and demarcations. If the reporting authorities choose to adopt a liberal approach to classifying tax expenditures, they avoid fuelling unfruitful disputes. The demarcation between the various deviations from the tax benchmark will remain of political interest, as from experience, tax expenditures attract more attention than other tax deviations occurring say out of reasons grounded in the tax system itself or for the purposes of simplification and so on. It is therefore important that all deviations from the tax benchmark be shown in their appropriate form.

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they were in fact only removed from the definition, without actually having removed the exemption from legislation. In the absence of an Appendix 2, such a reclassification can go unnoticed.

13 For example Canada and Germany (see the 19th Subsidy Report of the German Ministry of Finance pp.111 - 127). The German Ministry of Finance describes this category as "other tax provisions". Also the Canadian province of Quebec and the state of Massachusetts in the USA, report in an appendix on deviations from the tax benchmark which have not been classified as tax expenditures in their reporting.

14 Ministry of Finance, Germany (2003): 19th Subsidy Report p. 15, as well as Appendix 8.

Recommendation 4
All deviations from the tax norm (i.e. the benchmark) which are further broken down at Level 2 should be shown in the 2005 Report (as *tax expenditures* in the estimates and tables section to the Report, as well as *other deviations from the tax benchmark* in an Appendix 2). [15]

On Level 2, deviations from the tax benchmark could also, in principle, be listed in their own separate category where they lead to ***higher*** tax receipts. To what extent this would be practical in the case of Swiss tax law is debatable. Currently, as far as the Swiss Federal Audit Office is aware, only the *non-deductibility of bribes deployed as an outlay in commercial activity,* would be an example which could fall into such a sub-category. Regulations in force since 2001 (Direct federal tax Act, Art. 59 c, para. 2) has ruled out deductions of such outlays. This aspect of reporting could gain significance in the future, if more so-called *disincentives* are entered into tax law. In international reporting on tax expenditures, as a rule, virtually no information is provided on surplus revenue coming from *fiscal disincentives.* The issue of *surtaxation* for example is only briefly touched upon in the report of the French *Conseil des Impôts* (see p. 25). In the case of tax reform of environmental taxes in Germany, the higher level of imposition on certain types of energy sources has been interpreted to be part of the norm and has not been identified as a disincentive in the report.[16]

Putting aside the special category of fiscal disincentives, the following schematic classification can be drawn from the above explanation ***(Figure 2):***

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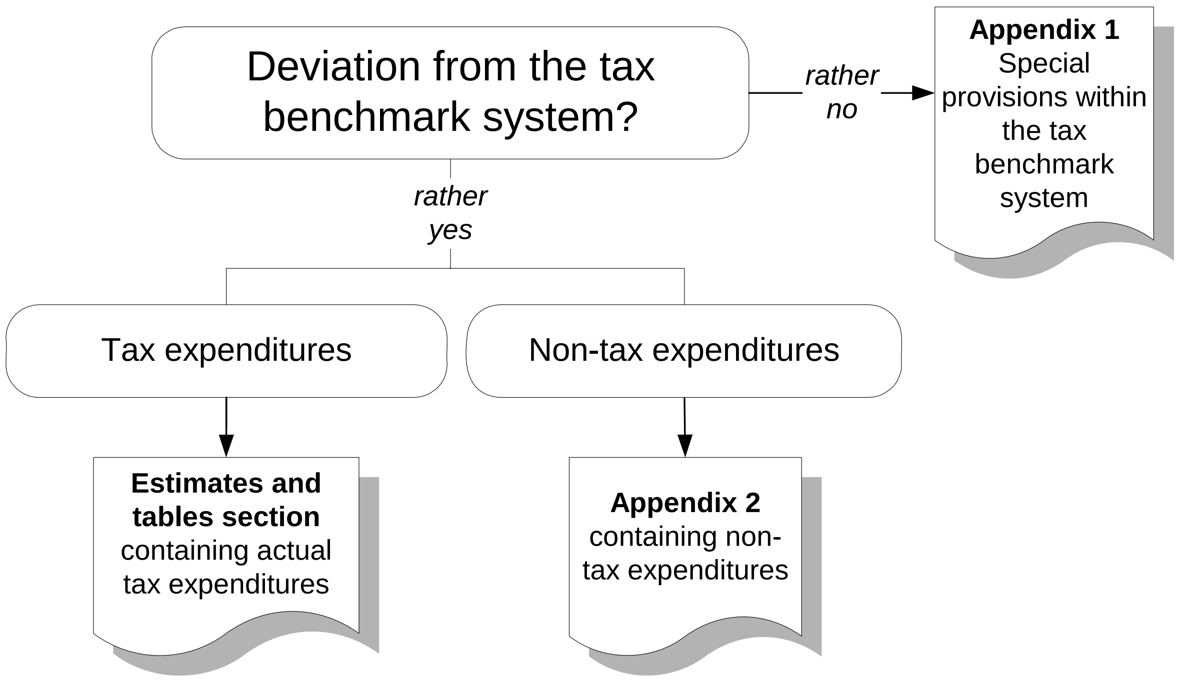
[15] Note: Appendix 1 contains those tax provisions which are considered as a component of the tax benchmark system, whilst Level 2 / Appendix 2 always deals with deviations from this benchmark.

[16] Ministry of Finance, Germany, 19th Subsidy Report, pp 30 - 31.

Figure 2: Classification and resulting parts of a tax expenditure report



5. Structuring the estimates and tables section

The estimates and tables to the 1997 Report are arranged according to the type of tax (i.e. federal direct tax, stamp duty, value added tax, mileage-related Heavy Vehicle Charge, import duties, mineral oil duty and vehicle duty). As the Report is supplementing information available on direct financial support, data contained in the Report should be arranged according to the same criteria as for other subsidies. This improves the extent to which comparisons between data can be made, even if an exact classification can only be carried out in some cases on a best-case basis.

Recommendation 5a
For ease of use of the Report, the estimates and tables section should be structured according to similar criteria as for the reporting on other subsidies.

Recommendation 5b
It should be reflected upon as to which additional criteria should be applied for structuring the data in the estimates and tables section.

Additional criteria for structuring the estimates and tables section could include:

- functional area defined based on the State Accounts[17]
- area of economic activity / sector
- general objectives (fairness, progressiveness, tax system, etc....),
- specific objectives (encouraging home ownership, health, old age pensions, education and vocational training etc...)
- primary beneficiary (individual persons, households, companies)
- secondary beneficiary
- etc.

[17] The State Accounts make a distinction between eight separate functional areas (social welfare, finance and taxation, transportation, education and basic research, foreign relations, the environment and land use, defence, agriculture and food).

6. Methodology applied to the data and estimates

In the 1997 Report, for 31 of the 46 tax expenditures, an estimated total annual amount of CHF 2.6 billion of foregone tax revenue was arrived at. The Subsidy Report does not quantify this aggregate of revenue foregone, as no estimate was possible for many of the tax expenditures. Summing is also often left out of reporting in other countries because estimates of individual tax revenue foregone are based on the assumption that all other tax expenditures remain unchanged.[18] But the more progressive the tax system and the greater the tax deductions it contains, the less this assumption holds.
Where estimates were provided in the 1997 Report, they relate to an individual base year or base period (e.g. 1992 - 94).

The methodology applied to estimates is not explained in the 1997 Report. Basically a distinction can be made between three approaches to choose from:

1. *Estimate receipts received* (based on the assumption that the behaviour of taxpayers remains unaltered). This is the most commonly applied methodology internationally.
2. *Estimate the anticipated increase in receipts from the removal of a tax expenditure - revenue gain approach* ((based on the assumption that taxpayers adapt their behaviour - this is a demanding approach).
3. Supplementary to approach 2, include additional fiscal and social effects (in practice, this is rarely possible).[19]

Based on the observations by the Swiss Federal Audit Office, the lack of data is a crucial problem encountered in reporting on tax expenditures domestically as well as abroad.[20] Tax expenditures can often only be estimated within relatively wide margins. Moreover, according to a joint study carried out by the *U.S. General Accounting Office* and the *Office of the Auditor General of Canada,* it is unavoidable that such estimates contain a degree of uncertainty as:

- it is not clear to what extent taxpayers will adapt their behaviour in seeking to minimise their tax burden in response to the removal of a tax expenditure,
- the removal of a tax expenditure can exert a negative influence on tax receipts if turnover, income or the value of assets fall in the affected sectors as a result of the higher level of taxation,

estimates cannot be aggregated for revenue received for two reasons; namely, (1) tax expenditures interact with each other, as in the case of an elimination of a tax expenditure, the

[18] Department of Finance, Canada: Tax Expenditures and Evaluations 2000, p. 9.
[19] Conseil des Impôts, p. 44.
[20] See Canada 2004, p.10 as well as France, Conseil des Impôts, p. 42.

- remaining tax expenditures take on greater weight and vice versa, and what is more, it could be that (2) not all tax expenditures have been assessed.[21]

The Confederation has only just begun with its reporting on tax expenditures. The Swiss tax system has grown out of historical reasons and is federalist in nature. Various problems must be solved for the further development of reporting in Switzerland; namely,

- The reporting should be in a position to *bridge at least its own time interval between publications.* If a report is compiled every six years, it should be possible to make an estimate for example, for tax revenue foregone for the three past years, plus a projection for the next three years, in order that the subsequent report can follow with seamless data. Various countries go beyond this - despite the fact that they publish an annual report, they also compile retrospective estimates and projections over several years. The Nineteenth Report from 2003 of the German Ministry of Finance for example, contains an attachment on tax expenditures per functional area covering the years 2001 to 2004. Thanks to the overlapping of reporting periods with the publication frequency, estimates and projections of the previous report can be corrected in the subsequent report.

- Improvements in data and in the methodology of estimates cannot be realised from one day to the next, but should be seen rather as an ongoing exercise. Reporting on tax expenditures has been developed in various OECD countries over several decades:

Table 3: First report and report frequency in some OECD-Countries

Country	**first report**	**report frequency**
Germany	1959	half yearly
USA	1968	yearly
Spain	1978	yearly
Canada	1979	irregularly
UK	1979	yearly
Sweden	1979	yearly
France	1980	yearly
The Netherlands	1987	irregularly
Switzerland	*1997*	*every 6 years*

(Source: Conseil des Impôts, p. 41.)

[21] Federal Government Reporting Study, 1986, p. 23, from the International Federation of Accountants IFAC, Public Sector Committee: Study 10 - Definition and Recognition of Expenses/Expenditures, p. 23.

7. Appraising tax expenditures as a support instrument

The Subsidy Report carries out a general assessment of tax expenditures. Basically, the Report concludes that steering behaviour through the use of tax expenditures is generally less efficient in achieving objectives than direct financial transfers. Furthermore, the 1997 Report refers to the disadvantages of tax expenditures itemised in the dispatch to the Subsidy Act:

- Tax expenditures go against the basic principle of imposing according to financial capacity and thus put the concern of tax fairness in danger, if non-fiscal objectives are given preferential tax treatment.
- According to the 1997 Report, conditions and stipulations cannot be attached to tax expenditures, which makes it difficult to exert an influence on the task or activity being encouraged.
- The financial impact of the tax expenditures granted can often not be calculated. They therefore escape review and possible removal. Over a number of years, they can turn into an undesirable bottomless bucket for subsidies.
- The lack of transparency also arises from the fact that tax expenditures are not reflected, neither directly nor visibly, in the National Accounts. In this sense, they are hidden subsidies, removed from the decisions of parliament on the budget.
- Furthermore, they present a problem with regard to the principle of gross presentation (separately itemised and comprehensive accounting on expenditures and receipts) as set down in the Budget Act. Tax expenditures are hidden, that is, as income deductions they are in reality disguised government expenditure. With every tax expenditure a deviation from the principle of gross presentation occurs, which leads to an underestimation of public spending.

The Subsidy Report furthermore concludes that in only rare cases can tax subsidies be justified, namely, when in efficiency terms, they fare better than measures on the expenditure or outlay side targeted at the same objective. Nonetheless, this is not further specified in the Report. Furthermore, the 1997 Report justifies a few existing tax expenditures with the argument of maintaining Switzerland's competitiveness. This is particularly the case in existing tax expenditures in the stamp duty - only thanks to this tax expenditure, could parts of the international and very flexible financial market be retained in Switzerland.

The Subsidy Report is very reserved on the "crucial issue" of whether or not the basic principle is lived up to, namely, as set down in the Subsidy Act, that tax expenditures are to be renounced.[22] A reduction in tax expenditures could moreover, result in a reduction of the complexity of the tax system. With respect to this, the Subsidy Report 1997 mentions that, in many cases, the Confederation cannot decide autonomously on its own tax laws, particularly not in the federal direct tax.

Tax expenditures as an instrument, are not to be rejected in all cases as they also have advantages. The administrative costs are smaller than in the case of direct financial subsidies as a

[22] SA Art. 7g: "the provision of financial assistance in the form of tax expenditures will generally be renounced".

tax deduction is checked less stringently than would be a request for a subsidy. In general, the Federal Tax Administration does not require any additional staff or infrastructure for introducing a new tax expenditure. Furthermore, a tax expenditure can be more suitable than direct financial assistance in achieving a certain objective. In the literature, subsidies that stimulate private sector activity are advocated, in order that the state is obliged to spend less. Typical examples of this are charitable organisations in the area of social services and health, as well as in culture and education, which take on quasi public duties and thereby mobilise a voluntary and financial commitment. The issue of whether a direct financial subsidy or a tax subsidy is the more appropriate instrument depends on whether it favours or threatens private initiatives and how price (tax) elastic is the response of private entities to a tax expenditure.[23]

Recommendation 6
As to the question of under which circumstances a tax expenditure or direct financial assistance is the more appropriate instrument, the fundamentals should be considered, removed from the specifics of individual cases.

Making such a distinction is in itself a prerequisite, in order that Articles 6e and 7g of the Subsidy Act can generate a tangible impact. The choice between tax instruments and instruments of financial support has been discussed scientifically in detail in the literature - the results can be appraised accordingly.[24]

Once the issue of the basic choice of the appropriate instrument has been clarified, a variety of measures would be feasible. The German Ministry of Finance for example, has developed a "flow chart for examining subsidies". It is based on a research project carried out by the Cologne Centre for Public Economics of the University of Cologne. In this approach, selecting the appropriate instrument of support is done systematically in the process of auditing subsidies.[25]
The U.K. Tax Authority can reject applications from the sectoral administration for tax expenditures if only a small number of beneficiaries are addressed, on the grounds that this would lead to a

[23] Rosen, H.S. (1999): Public Finance. Boston: Irwin. Price elasticity of taxation depends for example, on the level of awareness of tax deduction possibilities and the formal requirements such as receipts and itemised statements.

[24] See also, Feldstein, M. (1980): A Contribution to the Theory of Tax Expenditures: The Case of Charitable Giving, appearing in H.J. Aaron und M.J. Boskin (eds.), The Economics of Taxation. Washington, D.C.: Brookings Institution. // Paqué, K.-H. (1986): Philanthropie und Steuerpolitik [Philanthropy and Tax Policy] in the Kiel Studies 203. Tübingen: J.C.B. Mohr (Paul Siebeck). // Paqué, K.-H. (2003): Gute Subventionen [Good Subsidies], in the Financial Times Germany, 30 December 2003:26. // Rosen, H.S. (1999): Public Finance. Bosten: Irwin. // Weisbach, David A. and Jacob Nussim (2003): The Integration of Tax and Spending Programs. Chicago Working Paper Series, 2nd Series, Paper No. 194.

[25] The German Ministry of Finance: the 19th Subsidy Report; government report on the Development of Government Financial Assistance and Tax Expenditures 2002 - 2004, p. 13.

complication of tax law and to an increase in the costs of implementing the legislation.[26] Here, in contrast to the German approach, where existing instruments of support are checked thoroughly, in the UK approach the adoption of new and inappropriate tax expenditures into current regulations should thus be prevented. What is common to both systems is that they both establish the prerequisite of binding principles for the selection of the support instrument in order to avoid the need for each new case to be freshly assessed.

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26 See Conseil des Impôts, p. 172.

8. Exploring further topics and aspects of particular interest

With no explanation provided, the 1997 Subsidy Report does not choose to carry out an in-depth examination of tax expenditures and maintains that such a comprehensive or targeted and selective reporting can be postponed until a later date. In addition, it expresses the expectation that it will also undoubtedly be possible to analyse individual tax expenditures in greater depth within the context of the Behnisch Group of Experts.[27] The Behnisch Report established various recommendations on the reduction or elimination of certain tax expenditures.

The issues dealt with so far by the Swiss Federal Audit Office and the solutions proposed, aim primarily at a *comprehensive* reporting on all deviations from the tax benchmark, and in particular on tax expenditures. A prioritisation of specific topics or aspects is not linked to this. The quandary of whether or not, and to what extent, in-depth information should be provided in conjunction with reporting on tax expenditures is addressed in various ways internationally. The following models can be distinguished:

- The *Canadian* province of *Quebec* does not see its reporting as an evaluation of its tax policy or as a response to the question of whether or not various exceptions from the tax benchmark should be retained or otherwise. Nonetheless its readers are provided with a separate analytical framework, where data drawn from the report together with additional information can be applied for the purpose of making one's own evaluation.[28]
- The *German Ministry of Finance* refers to new research mandates on financial assistance and tax expenditures in an Appendix 10.[29] The Subsidy Report itself prepared by the German government, does not however, contain an independent in-depth analysis.
- To the consternation of the *Conseil des Impôts,* virtually no tax expenditures have been evaluated in *France*. There are exceptions here in areas where the European Commission has required an in-depth analysis.[30]
- In contrast, since 2000 the *Canadian Department of Finance* completes each of its reports on tax expenditures with three topics which are analysed in depth. In its 2000 edition for example, the following topics were treated - *Defining Tax Expenditures*, *The Alternative Minimum Tax* and *GST/HST Treatment of Export Distribution*.[31]

The solution opted for in the 1997 Report most closely resembles the German approach where it refers to a more in-depth analysis based on the Behnisch Report from 1998.

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[27] Expert Committee Report on the Examination of Loopholes in the System of Direct Taxation (Expert Committee on Tax Loopholes), Bern 1998.

[28] Ministère des Finances, de l'Economie et de la Recherche, Ministère du Revenu: Tax Expenditures. 2003 Edition (in particular the introduction, p. 9 as well as Part I, Section 3).

[29] The German Ministry of Finance (2003): the 19th Subsidy Report, p. 142.

[30] Conseil des Impôts, pp. 115 - 144.

[31] Department of Finance, Canada: Tax Expenditures and Evaluations 2000, "Part 2 - Tax Evaluations and Research Reports", pp. 37 - 96.

One conjectures that reporting on tax expenditures best generates results leading to concrete measures, if important topics are looked at in depth and appropriate proposals presented accordingly. For example, the U.S. *General Accounting Office* evaluated a tax expenditure which was aimed at encouraging direct investment in Puerto Rico.[32] From this evaluation it emerged that the tax expenditure per employee was higher on average than the average salary and even higher in certain cases. Based on this evaluation, Congress decided to abolish the relevant tax expenditure.[33]

The Subsidy Act allows the Federal Government to seek amendments or the abolishment of legislation as required and for ordinances to be amended or abolished (Subsidy Act, Art. 5 para. 2). For this purpose, the Federal Department of Finance together with the other departments of the federal administration responsible, should submit the required proposals for legislation and reports and propose a motion to the Federal Government (Subsidy Act, Art. 5 para. 3). In formulating motions for tabling in parliament on the subject of tax expenditures in particular, it is virtually a prerequisite that, apart from the comprehensive reporting, selected topics also be evaluated in depth and presented in the Report. Whether an in-depth analysis section is included or not and what shape it takes, is more an issue of setting policy priorities than an issue of classification, definition or layout.

Recommendation 7

In refining their reporting, the Federal Finance Department must clarify in what manner more in-depth information on tax expenditures, if additionally required, is to be provided in order that concrete motions can be proposed in accordance with Article 5, Paragraphs 1 and 2 of the Subsidy Act.

[32] U.S. General Accounting Office: Tax Policy; Puerto Rico and the Section 936 Tax Credit, GAO/GGD-93-109, (Washington D.C.: June 8, 1993).

[33] U.S. General Accounting Office: FEDERAL BUDGET. Opportunities for Oversight and Improved Use of Taxpayer Funds, GAO-03-1030T, p. 32.

9. The 1997 Report in parliamentary procedural requests

To give flavour to the political discussion surrounding tax expenditures, all parliamentary procedural requests submitted on this subject will now be summarised in the following section. This is based on the databank Curia Vista (http://www.parlament.ch/homepage/cv-curia-vista.htm) which collates all parliamentary procedural requests treated by the National Council or Council of States since 1996. All parliamentary procedural requests with the term "tax expenditure", "tax relief" or "tax deduction" contained in the text, have been included.

In total, this comes to 24 parliamentary procedural requests for the years 1996 to 2004 - these are summarised in **Table 4** as follows:

Table 4: Parliamentary procedural requests on tax expenditures 1996 - 2004

Under "Type" of procedural requests the following abbreviations are applied: Ip = interpellation; Mo = motion; Po = postulate; Q = simple question; PaIv = parliamentary initiative

Request No.	Type	Member of Parliament	Party faction	Title	Content	infor-mation	expan-sion	reduc-tion
04.3429	Ip.	Sommaruga Simonetta	s	Tax deductions. Who benefits?	Impact of tax deductions on FDT	X		X
03.3598	Ip.	Stähelin Philipp	c	Encouraging the use of bio fuels	Exemption of mineral oil duty		X	
03.3250	Ip.	Green faction	g	Raising the pension age to 67 years old	Removal of tax expenditures for the 3^{rd} pillar		X	
02.3545	Mo.	Leuthard Doris	c	Support for care at domicile by relatives and acquaintances	Tax deductions for care at domicile		X	
01.3452	Mo.	SVP faction	v	Tax relief for enterprises which train apprentices	Tax relief for training of apprentices		X	
01.3004	Po.	Standing Committee for Economic Affairs & Tax - National Council	-	Tax deductions for charitable work	Tax deductions for charitable work		X	
01.1120	Q	Widmer Hans	s	Impact of tax harmonisation on taxpayers with low income	Impact of removal of tax deductions	X		
00.430	Pa.Iv.	Fehr Jacqueline	s	Family support. Change of system	Tax deductions for the family	X		X
00.418	Pa.Iv.	Zysiadis	-	Recognition of charitable work	Tax deductions for charitable work		X	
00.3679	Mo.	Social Democratic faction	s	Strengthening the economic base of low and middle income parents	Tax deductions for the family	X		X
00.3664	Ip.	Berger Michèle-Irène	rl	Tax relief for families	Raising deductions for children in FDT		X	
00.3037	Mo.	Spielmann Jean	-	Extending contracts in occupational pensions	Deductions for occupational pensions		X	
99.466	Pa.Iv.	Leutenegger Oberholzer Susanne	s	Declaration obligations for recipients of state assistance	Declaration obligations for enterprises receiving tax relief	X		X
99.412	Pa.Iv.	Büttiker Rolf	rl	Savings for home building. Amendment to the Fed Act on Harmonisation of Direct Taxation at Cantonal and Communal Levels (DTHA)	Deductions for reserves for savings for home building		X	
99.3613	Ip.	Fehr Jacqueline	s	Poverty in the family should not exist	Tax deductions for the family	X		X
99.3518	Mo.	Jans Armin	s	Bribes. No tax deductions	Tax deductions for bribes			X
98.3173	Ip.	Fehr Jacqueline	s	Study "Children, Time and Money"	Tax deductions for the family	X		X
98.3061	Ip.	Strahm Rudolf	s	VAT Special rates. Priceimpact for the hospitality industry	Impact of tax expenditures on prices	X		X
98.3022	Mo.	Gysin Remo	s	Tax expenditures. Federal legal provisions	Tax agreements containing tax expenditures	X		X
97.3572	Po.	Vollmer Peter	s	Rewarding bicycle-friendly enterprises	Tax relief for enterprises		X	
97.1064	Q	Rennwald Jean-Claude	s	Promoting business. Danger of over-generosity	Tax agreements containing tax expenditures			X
97.1040	Q	Jaquet-Berger Chr.	s	Bribes. Tax deductions	Tax deductions for bribes			X
96.3047	Mo.	Hochreutener Norbert	c	Equality in pensions based on the 3a pillar	Opening up of tax expenditures in the 3a pillar		X	
96.1128	Q	Ostermann Roland	g	Tax deductions	Limiting deductions of debt interest payments			X

Source: Database Curia Vista (http://www.parlament.ch/homepage/cv-curia-vista.htm)

The various parliamentary procedural requests can be described as follows:

- There is a relatively even spread of parliamentary procedural requests for the years examined (1996: 2; 1997: 3; 1998: 3; 1999: 4; 2000: 5; 2001: 3; 2002: 1; 2003: 2; 2004: 1).
- More than half of the parliamentary procedural requests, i.e. thirteen of them, were submitted by members of the Swiss Democrats Faction (s), 3 from members of the Christian Democratic People's Party Faction (c), 2 from members of the Green Party Faction (g), 2 from the Radical Free Democratic Party Faction (rl) and 1 from a member of the Swiss People's Party Faction. 3 requests came from outside of factions (2 parliamentary procedural requests came from Worker's Party members without a faction, 1 request from the Standing Committee for Economic Affairs and Taxation - National Council).
- 11 additional parliamentary procedural requests tended towards seeking an expansion of tax expenditures, 12 went more in the direction of dismantling tax expenditures.
- Some specific tax expenditures/ tax deductions were addressed by several parliamentary procedural requests. 5 requests dealt with tax deductions for families and children in the Federal Direct Tax (FDT), 4 requests dealt with tax agreements (with natural persons or legal entities), 3 requests demanded tax deductions for charitable work or care, and 2 requests criticised the tax deductibility of bribes (in force up until the year 2000).
- 9 requests primarily demanded information for the purpose of raising transparency in certain areas of tax expenditures. Of particular significance is the interpellation by Sommaruga, a member of the Council of States (04 - 3429, see the attached excerpt):

Interpellation by Sommaruga (04.3429): Tax deductions. Who benefits?

Date of receipt: 18.06.2004, debated by the Council of States on 27.09.2004

Text received

The Federal Government is requested to answer the following questions:

1. What is the financial scope of individual deductions which can be exercised within the framework of Federal Direct Taxes?

   a. How large is the reduction of taxpayers' income created by the individual deductions (per deduction broken down according to income category)?

   b. How large is the tax loss or loss of income for the Confederation created by individual deductions (per deduction broken down according to income category)?

What is asked for is a presentation where, on the one hand, the individual deductions are shown according to their impact for each income category accordingly, as well as providing an overview of all tax deductions.

2. Could the Federal Government outline the impact of these numerous tax deductions on tax progression and how does it evaluate this impact?

3. In case the Federal Tax Administration is not able to carry out this exercise due to the lack of data, then the question applies: how could such research be managed and would the Federal Government be prepared to issue such a mandate?

Justification

The various deductions allowed under current legislation have the purpose of meeting differing objectives (these deductions cover: deductions for pillar 3a - with or without a pension fund, 2nd pillar deductions, deductions for joint earnings of couples, deductions for children, deductions for insurance premiums, deductions for dependents, donations; professional costs - transportation, meals, accommodation and meals by weekly commuters, other professional costs; supplementary employment, deductions of capital contributions to pension savings, with separate imposition at a special rate; deductions for managing share portfolios including custody of shares and so on). First and foremost, the financial capacity of the taxpayer should be ascertained. There are however, also tax deductions which pursue policy incentives.

The wide variety of deduction options does not help the current tax system to be transparent or efficient. The division of jurisdiction between the Confederation and the Cantons is often unclear and controversial. Accordingly, deductions for health fund contributions and deductions for childcare for example, are not treated as deductions based on one's family situation.

In the interests of creating a coherent and efficient tax system, the Confederation should review and explain the consequences of the deduction options available. What should be examined in particular is whether or not the current tax system actually fulfils its constitutional requirement of according the right to be imposed based on financial capacity. This interpellation should serve this purpose.

The Federal Council's response 01.09.2004

The Federal Tax Administration has accepted the mandate to respond to the questions posed in points 1 and 2 of the interpellation. In view of the large number of tax deductions to be examined and the scope of the evaluation requested, the Federal Tax Administration needs sufficient time in order to be able to safely respond to the questions with reliable statistics. It is envisaged that by the end of the year consolidated results will be made available.

It is noteworthy that none of the parliamentary procedural requests listed in **Table 4** made reference to the Subsidy Report 1997. It would appear that it is not perceived as a reference in connection with tax expenditures. The level of awareness of the 1997 Report is therefore disproportionate to the outlay invested in preparing it. Parliament's interest in preferential tax treatment for selected areas has somewhat increased since the publication of the 1997 Report.[34] In contrast, the Subsidy Report is referred to by politicians when referring to instruments of direct financial support. The Subsidy Report is mentioned in 25 parliamentary procedural requests on the subject in total (or in the responses of the Federal Council)

Recommendation 8

The mild reaction by parliament to the 1997 Report is disproportionate to the outlay invested in preparing the Report. One year after political consultation on the 2005 Report has been concluded, the Federal Finance Department must examine the response to the 2005 Report.

[34] In recent years parliament has received the following parliamentary procedural requests for special tax treatment, which could not however be located in the Curia-Vista-Databank using the key terms referred to:
- Amman Schoch Motion, 15 March 1999 on "Encouraging expansion of home ownership"
- Mörgeli Motion, 25 November 2002 for tax relief regarding "Direct Federal Taxes... a comprehensive deduction of health fund contributions"
- Teuscher Motion, 12 December 2002 in favour of "Tax relief for single parents"
- David Motion, 3 October 2003 on "Vocational training. Tax Treatment”
- Banga Motion, 19 March 2004 on tax exemption for pay of the fire brigade

Source: Report of the Federal Council in response to the postulate of 18.06.2003 from the Christian Democratic Party faction entitled: Less Bureaucracy in the Tax System, p. 18.

10. Conclusions

Reporting on tax expenditures contained in the Subsidy Report of 1997 can be evaluated as follows:

- The definitions and demarcations applied in the Subsidy Report essentially represent an appropriate foundation for reporting.
- The 1997 Report simply covers special tax provisions that display particularly strong features of tax expenditure. The list of tax expenditures compiled in the Subsidy Report would appear to be somewhat lacking as a result of the rather narrow interpretation of the term tax expenditure.
- The results of categorising into steps 1 and 2 are not described comprehensively. In particular, what is missing is an appendix containing special provisions within the tax benchmark system and deviations from the benchmark that are not classified as tax expenditures.
- The body of the text, the estimates and tables and the appendices to the Report should be published together.
- Tax expenditures were not analysed in depth in the 1997 Report. The 1997 Report rated tax expenditures rather critically in general, however it did not go beyond this general standpoint and it did not lead to any proposals. Future Reports should evaluate topics of particular interest in detail where action is required.
- The Report on Tax Expenditures from 1997 went barely noticed in political debate.

The Swiss Federal Audit Office has oriented its examination in terms of timing and content in order that the results can be applied to the 2005 Report. Further refinements to be applied to reporting post 2005 do not relate merely to the data and methodology applied to estimates, but also to the availability of information on tax expenditures in the budget cycle. In this context, procedural and organisational issues within the Federal Finance Administration must also be considered. In view of the large sums involved, improved transparency in tax expenditures is of high priority for the Swiss Federal Audit Office. The SFAO will follow further developments in reporting with interest as soon as we have gained experience from the 2005 Report.

Structure of a Tax Expenditure Report *Annex 1*

Statements regarding the structure of a Report on Tax Expenditures have been made in several chapters of this report. The presentation below should provide an overview of these comments. The order of the content of reporting on tax expenditures within the Subsidy Report can also be founded on an alternative basis to that indicated.

Description	**Contents**	**1997 Report**
Body of text	explanation (with submissions to parliament if necessary)	O. K.
Methodology Section	definitions, classification base, assumptions, procedure, methodology of estimates, reliability limits	partly lacking, particularly on Level 2
Tables & Estimates on Tax expenditures	estimates, projections, sub-divided according to various criteria	not published, only 1 division
In-depth analysis	topics of particular interest, evaluation of the effectiveness of selected tax expenditures, generally with reference to proposals formulated in the text if applicable	not available
Appendix 1	table listing special tax provisions that are classified as part of the tax benchmark system (Level 1)	missing
Appendix 2	table listing deviations from the tax benchmark system that are not classified as tax expenditures	missing

Expert Committee Report on the Examination of Loopholes in the System of Direct Taxation [Bericht der Expertenkommission zur Prüfung des Systems der direkten Steuern auf Lücken (Expertenkommission Steuerlücken)], Bern 1998.

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Department of Finance, Canada: Tax Expenditures: Notes to the Estimates/Projections 2004.

Department of Finance, Canada: Tax Expenditures and Evaluations 2000.

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Feldstein, M.: A Contribution to the Theory of Tax Expenditures: The Case of Charitable Giving. In H.J. Aaron und M.J. Boskin (eds.), The Economics of Taxation. Washington, D.C.: Brookings Institution (1980).

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Paqué, K-H.: Philanthropy and Tax Policy [Philanthropie und Steuerpolitik]. Kiel Studies 203. Tübingen (1986): J.C.B. Mohr (Paul Siebeck).

Rosen, H.S.: Public Finance. Boston: Irwin (1999).

U.S. General Accounting Office: Tax Policy; Puerto Rico and the Section 936 Tax Credit, GAO/GGD-93-109 (Washington D.C.: June 8, 1993).

U.S. General Accounting Office: Federal Budget. Opportunities for Oversight and Improved Use of Taxpayers' Funds, GAO-03-1030T.

Weisbach, David A. and Jacob Nussim: The Integration of Tax and Spending Programs. Chicago Working Paper Series, 2nd Series, Paper No. 194 (2003).

Recommendation 1a
It should be explained in the methodology section to the 2005 Report, what is meant by the tax norm that constitues the normative benchmark tax system.
Keeping the information objectives of the reporting in mind, the term *benchmark tax system* must be narrowly defined, and the term *deviation from the benchmark* must be broadly defined, so that as few special tax provisions as possible are left out of the reporting. In case of doubt, the Report 2005 should contain one case too many rather than one case too few, as this would raise its information content.

Recommendation 1b
In an *Appendix 1* to the 2005 Report, *Special Provisions considered part of the tax benchmark system*, should be outlined. This should show those deductions, measures and peculiarities of the tax system which are considered to form part of the tax benchmark.
As the federal tax system comprises several types of taxes, Appendix 1 should be further sub-divided as appropriate (with e.g. *1a Special tax provisions as part of the benchmark in direct federal tax*, *1b Special tax provisions as part of the benchmark in stamp duty*, *1c Special tax provisions as part of the benchmark in Value Added Tax* and so on).

(see Chapter 3.1)

Recommendation 2
In the opinion of the Swiss Federal Audit Office, the two part division opted for in the 1997 Report, namely of tax expenditures and "non-tax expenditures", can be retained[35]. It should, however, be explained in the 2005 Report that classifying an item as a tax expenditure is not always clear-cut, due to the fact that tax expenditures often pursue several objectives simultaneously.

(see Chapter 3.2)

Recommendation 3
The estimates and tables section on tax expenditures should be published in the 2005 Report directly following the body of the text.

(see Chapter 4)

[35] An alternative definition of "non-tax expenditures" is "other deviations from the tax benchmark system".

Recommendation 4
All deviations from the tax norm (i.e. the benchmark) which are further broken down at Level 2 should be shown in the 2005 Report (as *tax expenditures* in the estimates and tables section to the Report, as well as *other deviations from the tax benchmark* in an Appendix 2).[36]

(see Chapter 4)

Recommendation 5a
For ease of use of the Report, the estimates and tables section should be arranged according to similar criteria as for the reporting on other subsidies.

Recommendation 5b
It should be reflected upon as to which additional criteria should be applied for structuring the data in the estimates and tables section.

(see Chapter 5)

Recommendation 6
As to the question of under which circumstances a tax expenditure or direct financial assistance is the more appropriate instrument, the fundamentals should be considered, removed from the specifics of individual cases.

(see Chapter 7)

Recommendation 7
In refining their reporting, the Federal Finance Department must clarify in what manner more in-depth information on tax expenditures, if additionally required, is to be provided in order that concrete motions can be proposed in accordance with Article 5, paragraphs 1 and 2 of the Subsidy Act.

(see Chapter 8)

Recommendation 8
The mild reaction by parliament to the 1997 Report is disproportionate to the outlay invested in preparing the Report. One year after political consultation on the 2005 Report has been concluded, the Federal Finance Department must examine the response to the 2005 Report.

(see Chapter 9)

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[36] Reminder: Appendix 1 contains those tax rules that are considered as components of the benchmark, whereas Level 2 / Appendix 2 always relates to deviations from this benchmark.