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## ICELAND 2004

### 1. Overview of the system

Iceland has an insurance-based unemployment benefit system. Financial assistance is available for those without other resources. Two kinds of housing benefit programmes are in existence. There is a rent benefit for tenants with low income. Mortgage interest benefits are open to house owners. Means tested family benefits are available to parents. The social security administration provides benefits for lone parents providing for two children or more. Married people are taxed individually.

#### 1.1. *Average worker wage (AW)*

The 2004 AW level is ISK 2 892 000.

### 2. Unemployment insurance

#### 2.1 *Conditions for receipt*

To be aged between 16 and 70 years old, willing and available to work and to be able to confirm the unemployed status by means of a letter from the labour exchange. Applicants must have worked at least 10 weeks in a full time job to qualify for any benefits. The qualifying period for part-timers lengthens proportionally. They must have been registered unemployed for at least three days, but receive benefits from the first day. In order to qualify for full benefits, applicants must have worked for the last 12 months in a full time job.

##### 2.1.1 *Employment conditions*

10 weeks of insured employment to qualify for full benefits. Applicants must have worked for the last 12 months to qualify for full benefits.

##### 2.1.2 *Contribution conditions*

Coincide with the employment conditions.

#### 2.2 *Calculation of benefit amount*

##### 2.2.1 *Calculation of gross benefit*

Benefits are paid in proportion to the number of hours worked in insured employment in the previous 12 months:

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- Full benefit of ISK 4 096 per day (5 days per week) is paid to those who have worked for 2 080 hours or more (average of 40 hours per week).
- For those who have worked for between 400 and 2 080 hours, there is a scale defined with 76 steps, from 25 per cent to 100 per cent of the benefit rate, each step representing 1 per cent of the full benefit.
- And minimum benefit of ISK 1 024 per day is paid to those who have worked for 400 hours of work (25 per cent of full benefit).

There is also a family supplement of ISK 164 per day (4 per cent of full benefits) per dependent child under 18 years old.

#### *2.2.2 Income and earnings disregards*

None; there is no income test. If a recipient has occasional employment for one or two days at a time, benefit is reduced in proportion to the number of hours worked.

#### *2.3 Tax treatment of benefit*

Benefits are subject to general income taxation.

#### *2.4 Benefit duration*

Benefits are paid for a maximum of 5 years.

#### *2.5 Treatment of particular groups*

##### *2.5.1 Young persons*

None.

##### *2.5.2 Older workers*

None.

### **3. Unemployment assistance**

None.

### **4. Social assistance**

It is a last resort financial assistance, administered by local governments.

#### *4.1 Conditions for receipt*

To be aged 18 or over.

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**4.2 Calculation of benefit amount**

**4.2.1 Calculation of gross benefit**

Financial assistance is the difference between the needs (the applicable amount) and the claiming household's resources. The applicable amount for the capital, Reykjavik, is shown below. Note that rates differ regionally.

Size of household	Applicable amount: recommended minimum monthly rate (in ISK)
Single persons	77 083
Couples	123 333

There are no allowances for dependent children. The resources include all gross family income. Excluded are income of children and all benefits paid in respect of children such as child support and family benefits, and rent benefits. Unemployed youth aged 18-24 living with low-income parents are entitled to up to half assistance. In addition there are available grants/loans to receivers of assistance to meet various expenses, such as funeral costs, dental bills, etc.

**4.2.2 Income and earnings disregards**

There are no disregards; there is a one-to-one means test including all gross family income.

**4.3 Tax treatment of benefit**

Generally subject to general income taxation.

**4.4 Benefit duration**

Unlimited.

**4.5 Treatment of particular groups**

None.

**5. Housing benefits**

There are two schemes for housing benefits, one for tenants and one for home owners. A) Home owners can receive interest rebates to offset their mortgage payments. B) Rent benefits are available to households renting accommodations as long as no household member owns any other real estate. The Central government finances the rent benefits partially but local authorities administer the benefits. The cost of mortgage interest rebate is borne by central government.

**5.1 Conditions for receipt**

Rent benefits are available to tenants with a certified rental agreement of at least 6 months duration. In addition the rented accommodation must be a self-contained unit, such that e.g. rooms in

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dormitories on campus are excluded. Rent benefits are means-tested. Due to the low income disregard and steep income testing the rent benefits are targeted to low income tenants.

Mortgage interest rebate is open to all home owners with mortgage payments.

## **5.2 Calculation of benefit amount**

### **5.2.1 Calculation of gross benefit**

Rent benefit. There is a fixed amount per claiming household of ISK 8 000 per month, with additional ISK 7 000 per month if there is one dependent child, plus ISK 6 000 per month for a second child, plus ISK 5 500 per month for the third and additional children. The benefit also takes into account the rent payments, in such a way that 15 per cent of the rent above ISK 20 000 and below ISK 50 000 are added. 1 per cent of the household's previous year taxable income in excess of ISK 2 000 000 is deducted. 25 per cent of the household's net wealth exceeding ISK 3 803 748 is counted as income in this respect. The final rent benefit can never be higher than ISK 31 000 per month or half of paid rent, whichever is lower. For the purposes of this study, the persons are assumed to have been working at the same earning level, and full time, in the previous year.

Mortgage interest rebate. This programme is in effect a part of the tax system, and replaced deductibility of interest payment a long time ago. The rebate is based on paid interest, subject to a maximum of ISK 494 782 for a single person with no dependent children, ISK 649 544 for lone parents and ISK 804 304 for a couple. The interest payments are also subject to a maximum of 7 per cent of outstanding mortgage. From this amount is deducted 6 per cent of taxable income. Net wealth exceeding ISK 3 721 542 for singles and ISK 6 169 097 for a couple can further limit the rebate. The rebate depends thus basically on the size of the mortgage relative to taxable income and net wealth.

Note that the interest rebate is based on paid interest and income in the year 2004 but is not paid out until 2005.

### **5.2.2 Income and earnings disregards**

Full rent benefits are paid to families with combined annual income of up to ISK 2 million. 1 per cent of income in excess of this threshold would be deducted from benefits.

## **5.3 Tax treatment of benefit**

Rent benefit. Not taxed.

Mortgage interest rebate. Not taxed. Administered and paid through tax authorities.

## **5.4 Treatment of particular groups**

### **5.4.1 Young persons**

None.

### **5.4.2 Older workers**

None.

## 6. Family benefits

Means-tested benefit for dependent children.

### 6.1 Conditions for receipt

To have a dependent child under 16.

### 6.2 Calculation of benefit amount

#### 6.2.1 Calculation of gross benefit

The maximum per child and income limits depend on the household composition (in ISK)

Supplementary allowance (per child, per year)	Maximum	Income limit
Couple		1 487 463
First child	126 952	
Successive children	151 114	
Addition for children under 7 years	37 397	None
Single parents		743 732
First child	211 447	
Successive children	216 902	
Addition for children under 7 years	37 397	None

Note that child benefits are based on income in the year 2004 but are not paid out until 2005.

#### 6.2.2 Income and earnings disregards

The allowance for parents with one child is reduced by 3 per cent of income above the income limit, by 7 per cent for parents with 2 children and by 9 per cent for parents with 3 or more children.

### 6.3 Tax treatment of benefit

Not taxable.

### 6.4 Treatment of particular groups

See below for treatment of single parents.

## 7. Childcare for pre-school children

Pre-schools are available to all children who have not reached the age at which compulsory school begins, i.e. in autumn of the year in which the child turns six. However, very few pre-schools accept children less than one year old, and the youngest children are usually two years of age. Before that they may be cared for by daymother.

In December 2003 there were 24 per cent of all one year old children in Iceland in pre-school, 89 per cent of all two year old and 93-95 per cent of three and five year old.

### 7.1 *Out-of-pocket childcare fees paid by parents*

Local municipalities pay for the construction and the operation of pre-primary schools. Parents contribute a substantial amount towards operating costs of the pre-primary level. The share that the parents contribute varies from municipality to municipality and often depends on the circumstances of the parents like in some municipalities' single parents and students pay substantially lower fees than others and some offer reduction to parents who have two or more children attending schools at the pre-primary level. On the whole, parents contribute about a third of the operating costs of pre-primary schools.

The Tariff of Reykjavík Preschools depends on the number of hours and on the economic status of the parents. The tariff is divided into three categories:

I. General tariff, married parents and parents who live together.

II. One parent is a student or one parent is an invalid. The Icelandic Government Student Loan Fund has issued some guideline rules as to which studies are considered valid like the student should take at least 75 per cent of full time University hours and 100 per cent in cases where the student is specializing in a certain field. Students at the University of Iceland should take at least 11 credit hours each semester. This category is also for fulltime students in junior college and vocational schools. Evening classes are not valid.

III. Single parents. Both parents being students according to the definition of the Icelandic Government Student Loan Fund. Both parents being invalids. Employees of Reykjavik Preschools.

#### **The Tariff of Reykjavík Preschools (valid from January 1st 2004)**

<b>Hours</b>	<b>Category I</b>	<b>Category II</b>	<b>Category III</b>
4	12 500	10 200	10 000
5	18 900	12 200	11 300
6	21 900	14 500	12 400
8	27 900	21 100	14 400
9	30 800	22 200	15 800

In Category I lunch is not included in a four hour day. Snack is included in all categories. A discount for siblings is 33 per cent for the second child and 75 per cent for the third child. There is also a discount for siblings if children in a preschool have siblings in a family day-care or in a private preschool, see the tariff for subsidy of day-care fees.

### 7.2 *Child-care benefits*

none

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7.2.1 *Conditions for receipt*

7.2.2 *Calculation of benefit amount*

7.2.2.1 Calculation of gross benefit

7.2.2.2 Income and earnings disregards

7.2.3 *Tax treatment of benefit and interaction with other benefits*

7.2.4 *Treatment of particular groups*

## **8. Employment-conditional benefits**

None.

## **9. Lone-parent benefits**

Lone parents with two or more children are entitled to additional benefits from the Social Security Administration, the so-called mother/fatherhood allowance.

### **9.1 *Conditions for receipt***

To be living alone with at least two children under 18 years of age.

### **9.2 *Calculation of benefit amount***

#### **9.2.1 *Calculation of gross benefit***

Lone parent benefits	Yearly amounts
2 children	56 016
3 children	145 620

#### **9.2.2 *Income and earnings disregards***

The benefit is not income tested.

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**9.3 Tax treatment of benefit**

Subject to general income taxation.

**9.4 Treatment of particular groups**

None.

**10. Tax system**

Iceland has proportional tax rates on personal income for central and local government taxes. A tax is levied on net wealth. Capital income is taxed separately, at a rate of 10 per cent.

**10.1 Income tax rate schedule**

General income tax rate is 38.58 per cent. Annual income above ISK 4 191 686 for single persons and ISK 8 383 372 for couples are taxed additionally at a rate of 5 per cent.

**10.1.1 Tax allowances and credits**

- *Relief(s) for compulsory pension contributions:* Since January 2000, the compulsory payment to pension funds, which amounts to 4 per cent of wages, is deductible. In addition, an optional payment of up to 4 per cent of wages may also be deducted. As the additional 4% contribution is optional, it is considered to be a non-standard relief.
- Work related expenses: earnings related transportation costs (net of fringe benefits) are deductible up to a certain limit.
- There is a basic tax credit of ISK 329 948 per earner; married couples may utilise up to 100 per cent of spouses' unutilised portion of his/her credit. The credit is subtracted from central and local government taxes; unused portions are not refundable. Seamen enjoy an additional tax credit, calculated per diem for number of days at sea.

**10.1.2 The definition of taxable income**

*Category A* comprises wages and salaries, including presumptive employment income of the self-employed (see below), employment-related benefits, old-age pensions, social security payments, grants, payments to copyright holders, royalties, etc. *Category B* comprises income from a business and income from an independent economic activity. *Category C* comprises investment income such as dividends, interest and capital gains. Income in category C is taxed at a flat 10 per cent rate with no tax credit.

Individual gross earnings minus allowances.

**10.1.3 The tax schedule**

- Central government: 25.75 per cent of taxable income.
- Local government (average rate): 12.83 per cent of total gross income (before allowances).

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**10.2 Treatment of family income**

The tax unit is the individual. Unearned income of married couples is taxed jointly.

**10.3 Social security contribution schedule**

Employees pay a fee to the Construction Fund for the Elderly at a fixed annual amount of ISK 5 576 if annual taxable income was above ISK 835 019 in 2003. Those 70 years or older are exempt as well as old age pensioners or invalids residing in old age, nursing homes or in special care.

Pension funds: The employer's contribution is at least 5.73 per cent of the employees' wages/salaries directly to the pension fund. The employee pays a contribution of 4 per cent which is deducted from these wages. The employee deducts the 4 per cent from income prior to taxation. This is applicable for the unemployed as well as for wage earners but not for people on other welfare.

In addition, employees can contribute up to 4 per cent of their income to a voluntary private pension fund and this contribution is also tax exempt. If an employee chooses to take this option the employer will match the employees contribution by up to 2 per cent of the employee's wages. The government will also contribute up to 0.4 per cent.

**11. Part-time work**

**11.1 Special benefit rules for part-time work**

Benefits are paid proportional to the time spent in paid employment.

**11.2 Special tax and social security contribution rules for part-time work**

None.

**12. Policy developments**

**12.1 Policy changes introduced in the last year**

The PAYE tax rate remained nearly unchanged from the year before, at 38.58 per cent compared with 38.55 per cent in 2003. The annual tax-free income threshold was increased by 2.4 per cent, from 835,019 to 855,241 krónur.

All reference for child benefits and interest rebates were raised by 2.5 per cent at the beginning of the year. The ceiling on interest payments that qualify for the interest rebate is being reduced to from 7 per cent to 5.5 per cent of debt in order to reduce the incentives to increase household debt. This will take effect from the beginning of 2005. For 2004, the interest rebates will be cut by 10 per cent.

Social security and unemployment benefits increased by 3 per cent as of the beginning of the year.

In March the Government declared (in connection with the wage agreements with two groups of blue-collar labour unions) that it will increase unemployment benefits by 9,000 krónur a month, from 79,767 to

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88,767 krónur, as of March 1<sup>st</sup>. Such benefits will increase thereafter in line with the agreed increase in wage rate, i.e., 3, 2½ and 2¼ per cent as of the beginning of 2005, 2006 and 2007, respectively.

**12.2**      *Policy changes announced*