The Notion of Net Income: Drawing the Line Between Professional and Personal Expenses

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1 Introduction

The purpose of this article is to discuss the distinction between personal expenses and professional expenses from a Swedish income tax perspective. On the basis of Swedish tax law I will outline a theory of how the line can be drawn between the two types of expenses. I will also present some of the results of an inventory and analysis of Swedish case law in this field.[1] The provocative heading of the article suggests that it may not be possible to assess net income in a way that is both fair and rational. On the basis of my study I will conclude with some views on how to compromise between these two interests. The article is limited to discussing income from employment and an active business.[2]

The concept of income has been a source of many theoretical as well as practical analyses and discussions since the days of Adam Smith. Many writers involved in defining and interpreting the notion have focused upon the receipts, i.e. the "input"-side of income. Especially important issues in Sweden, as well as in many other countries, have been the question of to what extent capital gains and other capital income should be considered as taxable income. This is certainly still a relevant question.

In Sweden however, there is also a need for investigations into the other side of the concept of income, that is the question of defining those relations between

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1 The article is a summary of my book *Levnadskostnader - gränsdragningsproblem vid beskattning av förvärvsinkomster*, Uppsala 1997. A version of the article was published in Intertax 1999, Jan. edition.

2 This limitation is due to limited space. Drawing the line beetween relevant expenses and expenses that do not show enough relevance, when assessing net capital income, certainly presents interesting problems. However, the analysis is complicated by the fact that many types of expenses are personal from an employment or business perspective, but may be fully relevant when it comes to estimating income from, for example, the sale of real estate.

expenses and receipts that are, or should be, relevant when computing net income, thus separating professional expenses from consumption, which is really part of the tax base.[3]

The principles and rules that draw the line between professional expenses (normally deductible) and personal expenses (normally not deductible) are as important to the bearing of the notion of net income, as is defining what should be relevant receipts and what should not. In fact, this is a somewhat eternal problem as long as net income is forming a tax base. This has led me to believe, that some of the results of my study may give readers outside Sweden additional perspective on the discussions going on in their own countries.[4] I must emphasize however, that I am discussing Swedish tax law.

Why then, is it so important that net income and not gross income is used as an income tax base? The answer is of course that it is more just to tax only that income which is at the taxpayer's disposal for consumption. A person with a high gross income is less able to pay tax than a person who has a lower gross income, but who manages to keep his net income higher due to lower costs. Therefore, the tax base should only consist of the amount that is left when such expenses have been paid, that are relevant to the taxpayer's professional activity.[5] The question is on what criterion, or which criteria, this relevance should be decided.

The Swedish tax statutes in this field are vague. The system lacks a consistent and coherent theory. As a result case law is difficult to interpret, and sometimes even contradictory. The literature of Swedish tax jurisprudence has to date not produced the required theory.

2 Relevant Swedish Statutory Law

Like the tax law of most other Western countries, the Swedish system has reached an unprecedented grade of complexity. The number of detailed statutes has increased rapidly as have their comprehensiveness. Unfortunately the Swedish tax reform of 1991 only managed to slow down this evolution for a very short time. The legislature has now regained its speed, and the flow of new legislation once again resembles a Northern river in spring.

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3 There are of course several and important works in which the distinction is thoroughly dealt with, *see*, *for example*, Eggert Møller, Mogens, *Afgrænsningen driftsomkostninger - privatforbrug*, Revision og Regnskabsvæsen 1958 at 445 and 505, Söhn, Hartmut (ed.) *Die Abgrenzung der Betriebs- oder Berufssphäre von der Privatsphäre im Einkommen-steuerrecht*, Köln 1980, Zimmer, Frederik, *Inntektsbegrep og rettsutvikling. Hovedtrek i utviklingen av begrepet inntekt i nordisk skatterett*, Nordiska skattevettenskapliga forskningsrådets skriftserie nr. 11, Oslo 1982, Tipke, Klaus, *The Demarcation beetween Professional Expenses and Personal Expenses in Income Tax Law*, Skatterett nr. 2 1984 at 144., *and* Hohaus, Benedikt, *Notwendige Erwerbsaufwendungen im britischen, US-amerikanischen und deutschen Steuerrecht*, Berlin 1998.

4 Of course this does not mean that I believe that my solutions must fit other countries.

5 On the same grounds it can be argued, that the tax base also should be reduced with private expenditure absolutely necessary for the taxpayer to maintain himself and his household, *see* Tipke at 145. I will return to this question below.

From this perspective the general statutes containing the formulas for the demarcation between professional expenses and personal expenses, seem almost paradoxical. The statutes are still short, quite vague, and based on the wordings that were used when modern income taxation was introduced about a hundred years ago.[6] The new Income Tax Act, chapter 12, section 1 (regarding employment income) and chapter 16, section 1 (regarding business income) read (approximately): "Expenses for earning and maintaining the receipts shall be deducted."[7] The formula is completed with an explicit prohibition of deductions for "cost of living". Furthermore, it applies to income from employment as well as income from a business run by the taxpayer.[8]

The Municipal Tax Act, which was in force until 2001 contained some special statutes in which the relation between relevant expenses and receipts were specified. The age of these statutes varied as did their wordings. Because of this, and due to the statutes only explicitly applying to some expenses, they gave a somewhat fragmentary impression. It was even suggested that some of the expenses in question were picked at random by the legislature, and that the primary purpose of these statutes was to stress the importance of not allowing deductions for personal expenses. However, the wording of the statutes implied that the expenses concerned, for example expenses for entertainment and literature, should be strongly connected to the taxpayer's work and thereby to his receipts.[9] Different terms were used. Some statutes contained an old form for "necessity", in others the demand for a close relation between expenditure and receipts was stressed with other words. In the bill of legislation that presented the Income Tax Act it was made clear however, that no change was intended in the field, in spite of the fact that some of these older statutes were not transferred to the new Income Tax Act.

The Supreme Administrative Court has produced many rulings on the subject through the years. Interestingly, it can easily be established that the court has interpreted the statutes with varying methods and results. This is especially obvious when mixed expenses, i.e. expenses with both personal and professional purpose, are dealt with.[10] Partial deductions sometimes have been allowed, and sometimes denied. The motivations given by the court seldom hold any reference to dogmatic theories or concepts. It is therefore difficult to draw general conclusions from case law.

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6 This also seems to be the case in some of our neighbouring taxation systems, for example Germany, *see* Tipke at 146.

7 The Municipal Tax Act of 1928, which was in force until 2001 had similar wording.

8 Hence there is not like in Germany different kinds of general clauses applicable to income from different types of sources, *see* § 9 (1) (werbungskosten) *and* § 4 (4) (betriebsausgaben) of the Einkommensteuergesetz.

9 The statute regarding entertainment has in fact been transferred to the Income Tax Act. Consequently, it is still in force.

10 *See* at sec. 5 below.

3 Methodological Approach

The demarcation between professional expenses and personal expenses may be analyzed from different points of view. One method is finding the cases in which the subject-matter are dealt with, analyzing them, and then concluding what is law for various types of expenses and situations. As mentioned above the relevant case law does not permit the use of this traditional method. Consequently, another way of investigating the field must be found.

An alternative method would be to formulate a theory, and subsequently testing the case law on it. This would mean finding and discussing general criteria, for example the notion of necessity, that could be used for separating professional and personal expenses. A study of this latter kind would have the advantage of not being limited by the existing case law. It would produce the theoretical base that is lacking in the subject-matter of the Swedish tax law. It would also allow a critical analysis of the Supreme Administrative Court as a source of law.

4 Criteria of Professional Expenses

4.1 Constitutional Limitations of Interpretation

The following outline of a theory for identifying relevant, in principle deductible expenses, is based on arguments found in court rulings as well as in literature of tax jurisprudence, and elsewhere. My aim is to find arguments that can be used generally. The perspective however, is *de lege lata*. From a Swedish constitutional perspective, this means that support for my interpretations must be found in the fiscal legislation (the principle of legality). Furthermore, the interpretations must be objectively justified. They must not favour any individual or group of individuals, unless there is explicit support in legislation (the principle of objectivity).

4.2 On Causality

The use of the notions of cause and effect has been the source of much philosophical thought for thousands of years. This is not the place for continuing the philosophical analysis. However, I would like to remind the reader that the depth and comprehensiveness of these conceptions are relevant even in a practical legal essay such as this one.

A concrete question must therefore be asked here: On what grounds should one presuppose that certain expenses are causative to receipts or vice versa?[11] The question is inevitable and must be answered, since the whole concept of net income seems to rest on an idea of causality.

11 *See* below, at section 4.5, for further discussion on the subject of whether the expense should be regarded as the cause or the effect.

Aristotle used the creation of a marble statue as a metaphor, and distinguished four different kinds of causes. The marble is the material cause (*causa materialis*), while the idea of a statue is the formal cause (*causa formalis*). The work of the sculptor is the direct cause (*causa efficiens*), while his purpose with the statue is the final cause (*causa finalis*). This classical view on causality was further developed by the scholastics, who identified chains of causes, primary and secondary causes, etc.. When generally speaking of cause and effect, one may use a less comprehensive notion. In the field of tax law, however, the conception of causality must be given a wide implication. Expenses can sometimes be considered a direct or material cause or effect, in relation to the taxpayer's profession. But on the other hand some expenses are considered relevant when the taxpayer's purpose with them is to generate receipts. They are in this context final causes.

With this perspective the analysis is not limited by a narrow and mechanical theory of causality. It is instead rational to take into account direct causality as well as other factors, such as values. Hereby the notion of causality is given a wide implication, thus rendering the formulating of alternative criteria possible.[12]

4.3 Necessity

The wording of the statutes in Swedish tax law on the subject-matter implies a demand for deductible expenses to be necessary.[13] It must therefore be put to question what bearing the word necessity should be given.[14] The answer must involve values. The term necessity can be used in different ways. An expense may of course be considered necessary, if the receipt would not have occurred, had it not been for the action that brought on the expense, for example a carpenter's aquiring of a screwdriver. But necessity may also be given a somewhat more relative bearing. For practical reasons necessity may be presupposed, where the actual connection with receipts cannot be determined. This seems to be the case with, for example, entertainment expenses.

It would lead to unreasonable consequences if a taxpayer with business income, as a rule, after the end of the fiscal year would have to identify those expenses, that showed to be direct causes of receipts. A general demand of this kind would result in enormous practical problems, and it would quite rightly be considered unjust. Entertainment expenses are again a good example, since they rarely can be identified as direct causes of the closing of deals, etc. Therefore, it

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12 *See* below, at sections 4.3 - 4.7.

13 The Municipal Tax Act explicitly stated a demand for necessity (applicable only to income from employment) regarding some specifically mentioned costs. However, as mentioned above no change is intended in the Income Tax Act, in spite of the fact that the word necessity has been left out.

14 An interesting comparative investigation into the use of necessity for identifying deductible costs, has recently been published in Germany, *see* Hohaus, Benedikt, *Notwendige Erwerbsaufwendungen im britischen, US-amerikanischen und deutschen Steuerrecht*, Berlin 1998. Hohaus advises the German legislator not to use the word necessary in the definitions of Werbungskosten and Betriebsausgaben, *see* at 314.

may be concluded that necessity cannot be used as a *general* criterion of the relation between expenses and receipts.

However, as mentioned above it must be emphasized that the term necessity can be given a variety of implications. This has also been the case in several rulings by the Supreme Administrative Court and in Swedish literature of tax jurisprudence. Some writers seem to understand the word as a description of direct cause, in the sense that it must be clear that receipts would not have occurred, had it not been for the expenses in question. Others have stated the opinion that not even the presence of the word necessary in legislation, should be understood as a demand for a more restrictive treatment of the expenses in question. The prevailing opinion is, however, that a demand for necessity cannot be deduced from the general formulas stated in chapters 12 and 16 section 1 of the Income Tax Act (where the word necessary does not occur, see above under sec. 2.) As will be shown below, the attitude of Supreme Administrative Court towards the question of necessity is not altogether satisfactory.

My own opinion is that necessity certainly can be used for interpreting the statutes in such a way, that deduction for personal expenses for living is denied. On the other hand it must not be considered a general criterion, not a general demand. The vagueness and the openness of the notion of necessity must be remembered. Since it is often impossible to objectively conclude that certain expenses are direct causes of receipts, etc., the final motive of the taxpayer must be taken into consideration.[15] Another factor that should be considered when giving bearing to the notion of necessity, is the nature of the expense involved. It is for instance less difficult to objectively estimate the necessity of expenses for the taxpayer's use of a home office in his house, than it is to make the corresponding estimation of his expenses for acquiring additional education within his trade.

The fact that necessity can be understood in a variety of ways by different individuals, and the view-point that necessity should not be used as a general criterion, leads to the conclusion that other, additional, criteria must be identified, in order to reach a useful theory for the demarcation between professional expenses and personal expenses.

4.4 Usefulness

Even if the notion of necessity is given the wide implication that I have suggested above, it cannot be extended to any point desired. It would then lose its precision and become meaningless. Assume for instance, that a writer or a journalist acquires a computer, as a substitution for his old mechanical typewriter. The acquisition perhaps saves him some time, but cannot on the basis thereof be labelled necessary. It might still be reasonable however, to regard the acquisition cost as a deductible expense.

This point of view can be made more clear and precise, by comparing necessary expenses with other costs. Assume that a taxpayer earns his living as a

15 The important question of whether the taxpayer's own view of what is necessary should be decisive, is discussed below, *see* in section 4.6.

carpenter.[16] It is not possible for him to use his finger-nails when fastening screws. A screwdriver is therefore a *necessary* acquisition. If the carpenter wants to keep up with modern technology he will probably get an electric screwdriver. This tool is not absolutely necessary for him to carry out his work. However, he may consider it necessary in the long run, if he is to be able to hold on to his job, get better salaries, or if he is self-employed, find new customers. If these are his motives, his purpose behind the acquisition, the expense can be regarded as a final cause of receipts.

But assume that the carpenter can carry out his work, and get along within his trade with just an ordinary screwdriver, but that his work takes more time and demands more strain. If this is the case, the acquisition of the electric tool may certainly be considered so *useful* for his activity, that the expense ought to be deductible. But the acquisition is still not necessary. The example can obviously be applied to a variety of activities.

In addition, there are expenses which due to their character very rarely can be considered necessary, such as entertainment expenses. However, expenditure of this kind can be regarded as professional and therefore deductible, on the ground of their being in principle useful for the taxpayer's activity.

My conclusion is that one should not try to force a completely objective bearing onto the notion of necessity. Instead, this criterion should be used both objectively and subjectively, depending on what is possible. Furthermore, the concept of necessity must be supported with the criterion usefulness. Necessity and usefulness cannot, and should not, be given a completely precise meaning when it comes to determining what is deductible and what is not. When taking into consideration the vagueness of the two notions, as well as the openness of language itself, it seems more accurate to speak of stronger and weaker necessity or usefulness.[17]

4.5 Exclusiveness

It can be called in question, if deduction should be allowed for an expense that shows necessity or usefulness, if the expense also would have occurred if the taxpayer had not had his professional activity.[18] A good Swedish example is the fee that everyone who owns a TV set, must pay to the state. Now, assume that the taxpayer earns his living as a TV producer. In order to carry out this kind of work, I believe one must also spend some time watching TV. The TV fee may therefore appear quite necessary for the producer, for individual receipts as well as for maintaining his source of income in the long run. From this perspective the expense appears to be professional. But on the other hand, there is a TV in

16 The significance of the taxpayer's status as a business person or as employed, is discussed below, in sec. 5.

17 The idea of placing these notions on a scale, where they can be “strong” and “weak” is not mine. I found it in the article by Mogens Eggert Møller, that I have referred to in note 3 above. Eggert Møller speaks of higher and lower *intensity* of necessity etc.

18 The question of how so-called mixed expenses should be treated is discussed below, at section 6.

most Swedish homes. This suggests that the taxpayer probably would pay a TV fee, regardless of his source of income. The expense is therefore characteristically not *exclusive* in relation to his taxable income. Under these circumstances the expense can be regarded as basically a cost of living, something that according to statute legislation is not deductible in Sweden.

In the example with the TV producer I used the exclusiveness criterion as an argument against deduction. However, the criterion can also appear as a reason in favour of allowing deduction. Assume that a taxpayer has expenses for acquiring some special competence within his trade, for example for attending a course. Assume also that this special education is of no personal value for him. The exclusivity of the expense leads to the conclusion that it should not be considered a cost of living. This estimation should be as objective as possible. Since no cost of living is present it is reasonable that the taxpayer's own view of the necessity or usefulness is decisive.

The exclusiveness criterion render flexibility and consideration of individual circumstances possible. It also raises some principally important questions. This criterion is different from necessity and usefulness, in the sense that it identifies certain expenses as consequences of the taxpayer's professional activity. The necessity and usefulness criteria on the other hand, are based on the assumption that expenses cause receipts.[19]

Furthermore, the two criteria necessity and usefulness are primarily relevant, when estimating the relevance of costs in relation to the carrying out of various tasks, such as carpentry in the example above. The exclusiveness criterion on the other hand, tells us which expenses are relevant, for the taxpayer's ability of carrying out *any* activity that may result in income. Provided expenses of this kind are not to be left out completely, the exclusiveness criterion can prove to be very useful.

The exclusiveness criterion may lead to the conclusion that expenses with a somewhat personal character, but with a high grade of exclusivity, can be regarded as relevant when assessing income. This could actually result in a more just computation of net income. The reason for this is that the criterion render it possible to take into consideration the taxpayer's ability to pay, *his taxable capacity*. Take for instance expenses for travelling between work and home, or expenses for child care. Both these types of expenses have an undeniable personal character. Yet they may be completely exclusive in relation to the taxpayer’s professional activity. This argument certainly speaks for the right to deduct the expense.[20]

The problem here, as I see it, is that deduction solely on the ground of exclusivity may not always be appropriate. Child-care expenses may for instance, as is the case in Sweden, have been considered by the state, within the welfare system. It may also prove impractical for the tax administration if deductions where to be allowed on these grounds. On the other hand it must be

19 *See* the *veranlassungsprinzip* in German tax law, Tipke, Klaus & Lang, Joachim, *Steuerrecht*, 14. völlig überarbeitede Auflage, Köln 1994 at 266 f.

20 In Swedish tax law such costs for travelling are deductible according to special statutes, while case law dating back to 1940s is generally thought to make deduction impossible for child-care costs.

stressed, that justice is a stronger interest than practicality. Taking into consideration the taxpayer's ability to pay is certainly necessary if the income taxation system is to maintain its credibility.

4.6 Reasonableness

I now turn back to the example with the carpenter. So far I have found his acquiring of a screwdriver objectively necessary, and his acquiring of an electric screwdriver useful, perhaps also subjectively necessary. Assume now, that he makes an acquisition that obviously lacks any objective connection with his activity and the receipts of it: he has the handle of his screwdriver plated with gold, in order to show off in front of his colleagues.

The treatment of his deduction claim will now involve the important question of whether the taxpayer's view of what is necessary, useful etc. and what is not, should be allowed to be decisive. My opinion on this issue is that the taxpayer's discretion in principle ought to be decisive, when it comes to choosing between high and low *but deductible, that is professional,* expenses. In this context it is one's factual income that is to be taxed, not the income one could have had if one had acted more economically. As pointed out above the deductibility cannot be governed solely by the objective necessity, etc.[21]

However, the risk of tax evasion leads to the conclusion that it should not be generally assumed that the taxpayer always acts from economically rational motives. The taxpayer must therefore not be freely allowed to form his own concept of income. As far as the demarcation between professional and personal expenses is concerned, there is cause for an objective estimation. The reasonableness criterion provides the ability for the fiscus to reject the taxpayer's treatment of his own expenses, and deny deduction for the cost of gold plating the carpenter's screwdriver.[22]

4.7 Customariness

I have already argued that there sometimes may be grounds for demanding a somewhat weaker connection between expenses and receipts. Take, as examples, entertainment expenses or a medical specialist's costs of attending a conference. It is usually not possible to determine if these expenses are necessary. It may be difficult even, to assess their usefulness *in casu*.

One line of argument that can be used here, is the customariness of the expense in question. If it can be said to be customary, and thus normal, for a taxpayer in approximately the same situation, we have an argument that speaks for deduction. This is for two reasons. First, the customariness of the expense shows that it is generally regarded as relevant for the professional activity by professionals. This circumstance should be taken into consideration. Secondly, this general opinion may in its turn lead to the assumption that many other

21 *See* Tipke in Skatterett 1994 at 150.

22 *See* Hohaus at 252.

taxpayers, who are in the same situation as 'our' taxpayer, in fact are allowed to deduct the expense. The demand for equal treatment, which is stated in the Swedish constitution, in my opinion makes it necessary to take into account this assumption as an argument for deduction. The customariness of a doctor's expenses for attending professional congresses may on these grounds be considered sufficiently connected to his receipts and to his activity.

However, estimations of this kind must be carried out with caution. The customariness may also be such an expression of tradition or fashion, that ought not to be considered relevant in a legal context. Customariness must therefore be estimated in a way that is as objective as possible. Consideration of customariness on grounds that are not well motivated may otherwise lead to illegitimate advantages for some taxpayers.

5 Weighing Criteria Against Each Other

It is obvious that the arguments outlined above cannot be applied and used without methods of weighing them against each other. In which situations and for which expenses is it appropriate or convenient to demand necessity? When should exclusiveness allow a weaker causative connection between expense and activity? Since the scope of this article does not permit a complete analysis of the problems involved, I will give a short outline of my views on the subject.

First, the character of the expense in question must be considered. As stated above, it is sometimes not possible to estimate the necessity of an expense, such as the doctor's costs of attending a congress. We must simply accept, that it can be impossible to conclude necessity for various reasons, such as individual circumstances, but also on account of the very character of certain types of expenses, such as entertainment and education.

Secondly, in Sweden the constitutional principles of legality and objectivity must be considered. Any interpretation must find support in fiscal legislation. However, this does not prevent the use of legal principles, such as the principle of taxable capacity or the principle of neutrality. I shall give two examples in which the estimation may involve these principles.

It is customary, as well as necessary, for many taxpayers to leave their small children in kindergartens, or to use other child-care facilities, while they are at work. The expense is often completely exclusive in relation to the taxable receipts, in the sense that the expense would not have occurred, had it not been for the taxpayer having to earn his or her living. Yet, according to the prevailing opinion in Sweden, the expense is personal and therefore cannot be deducted.[23] This opinion is based on a few cases dating back to the 1940s, where deductions were denied for servants. In those days it was quite customary for wealthy families to have servants, also when the wife did not go to work. Today this is a most unusual situation in Sweden.

In addition today's society holds many single parents, for whom child care expenses cannot be avoided at all. My opinion is that this expense ought to be considered professional, if it is exclusive and unavoidable for the taxpayer. This

23 At present there are no rules allowing deductions for "family costs" etc. in Swedish tax law.

strong emphasis on the exclusiveness criterion is of course based on the principle of taxable capacity. It must be noted that this is my own opinion. As mentioned, the prevailing opinion in Sweden is different.

My next example involves the use of the principle of neutrality when interpreting the general formula for deductibility. The Swedish legislature, as well as the Supreme Administrative Court, often refers to this principle in motivations. Unlike the principle of tax capacity the principle of neutrality can be considered a general instrument for interpreting the Swedish tax law.

The different situations of an employed taxpayer and someone who is running his own business can sometimes result in different estimations of expenses, whose characteristics are quite similar. Take again, as examples, entertainment expenses or expenses for attending courses, etc.. In Sweden these costs are generally considered to have a sufficient connection with the business of private individuals. Employed taxpayers, however, are not often expected to have expenses like these. The reason for the difference in attitude seems to be that the economic situation, and thus the receipts, of the employed person is thought to be more secure, than that of the business person. If this really is the case I agree that there may be reason to demand less necessity, or less usefulness, when estimating the deductibility of the business owner's expenses.

If, however, the labour market in the field of trade in question is not so secure, the argument does not stick. The unemployment situation of today's Sweden has, I regret to say, generally resulted in a labour market where many employees find themselves in as insecure situations, as do taxpayers who run their own business. This means, for instance, that many computer consultants cannot be guaranteed employment for more than short periods, and that they have to attend necessary courses, etc., at their own expense. The principle of neutrality then calls for similar treatment when assessing the income of employed persons and those who run their own business.

6 Mixed Expenses

The observant reader may by now have become slightly irritated over the fact that I have not yet discussed the most important practical problem of the subject: how shall the so-called mixed expenses be treated? I have deliberately saved this question until now, because I believe it requires special solutions. A general theory of the somewhat vague kind that I have outlined above, is not sufficient for solving these problems. More precise instruments are called for. I choose to make a distinction between two kinds of mixed expenses.

First, there are mixed expenses that clearly can be divided into professional and private parts. Assume that a computer consultant has to install a special ventilation system in one of the rooms of his house, in order to keep his working tool, a computer, cool during hot summer days. His electricity bill will now become a mixed expense. However, the bill is burdened with an additional cost that is quite easy to establish. As I see it, there is no reason for why this easily identifiable professional expense should not be deductible.

Secondly, there are expenses related to both professional and private activities. If a writer, for instance, aquires a computer and uses it both in the line

of business, writing books etc., and for pleasure, playing games, the aquisition cost is partly professional and partly private. Here a choice must be made. It is of course possible to dissect the expenses and allow deduction for the professional part. Since it is normally impossible to establish the portions exactly, it becomes necessary to make an estimation. In my opinion practicality calls for a restrictive approach here. The principle of legality however, calls for statutory support if deduction is to be denied for professional expenses. This problem is solved if the law explicitly states that the mixed expenses of this kind can be deducted only if the professional part is the essential one. Of course a stronger, more restrictive expression can be used. This would of course be practical but perhaps less fair. At present there is no such general rule in Swedish tax law.

7 Abstract of my Analysis of Swedish Case Law

My investigation of the Swedish case law on the subject-matter involves nearly 150 cases, dating from 1932 to 1993. By studying primarily the motivations, I have managed to identify the criteria for deductibility that the Supreme Administrative Court has been using. For practical reasons I only studied cases, where certain types of expenses were involved. These were

a) expenses related to participation in congresses and similar,

b) expenses related to the keeping of an office, etc., in the taxpayers home,

c) expenses for professional literature,

d) expenses for tools and instruments,

e) entertainment expenses, and

f) expenses related to health care.

For the expenses listed under c, d and e special provisions applied according to the Municipal Tax Act. These stated a demand for expenses for literature, tools and instruments to be necessary (an older form was used). In spite of these special provisions not having been transferred to the new Income Tax Act, the tax law is intended to remain unchanged.[24] For entertainment expenses both the Municipal Tax Act and the new Income Tax Act provides for a close connection (appr.) to the taxpayer's professional activity.

Due to the scope of this article I limit the following remarks to a few especially interesting questions. I concentrate on critical remarks since I find these more important. My analysis clearly shows that the criteria that I had formulated (see above in sections 4.3-4.7), also were the ones that dominated the

24 It may be put to question however, if this will really be the case once the wording of the corresponding rules in the Income Tax Act is subjected to a test in court. This has not yet happened. *See* Påhlsson Robert, *Några termer och begrepp* in IL. Skattenytt 2000 at 478.

motivations of the Supreme Administrative Court during the whole of the investigated period of time. I was surprised to discover the extent of this domination. However, the criteria were used in very different ways, depending on the type of expense. There were also other important variations, such as differences between old and new cases.

The notion of necessity is given very different bearing in the motivations of the court. It is used primarily when estimating the character of expenses for home offices and literature. Sometimes hypothetical tests are made, but quite often the necessity is presumed. The presumption often appears to have been made on the basis of customariness. Unfortunately there are signs of a more generous treatment of taxpayers whose professions have high status in society. This is certainly a very dangerous pattern, even though the results of my investigation are not altogether clear on this point. I get the general impression that the court has used the notion of necessity without making any theoretical effort to explain or define it. As a result the bearing of the notion has come to lack coherence to the extent that it is sometimes openly contradictory.

In addition, the court has added some criteria that have no explicit support in legislation, and thus are in conflict with the constitutional principle of legality. The most obvious example is the demand for home offices to be separated from the taxpayer's home. The treatment of this type of expense is also one of many examples of the changes in time. Since 1976 deductions are not allowed for home offices situated in the home of the taxpayer. This is a sign of a general evolution towards a more restrictive treatment of almost all types of expenses.

There are several signs of the growing restrictiveness. As for the criteria that I have described in this article, the Supreme Administrative Court almost seems to have given up the use of exclusiveness. From having been an important line of argument when estimating expenses for travel and home offices, it is hardly used anymore. This is in line with the treatment of mixed expenses, which up to some 30 years ago as a rule were dissected by the court in a professional and a personal part. Nowadays deductions are hardly ever allowed at all for mixed expenses, regardless of their character.[25] I put it that this change of practice is unconstitutional, since deduction is hereby denied for professional expenses. A change of system, from net to gross taxation, which is indeed subject to current debate, is something for the legislature and not the courts to achieve.

8 Final Remarks

So, is there nothing good to say about case law? Well, certainly. It is clear that the written motivations of the Supreme Administrative Court have improved enormously. However, the quality varies somewhat, but that problem can easily be solved. Unfortunately, there are structural contrasts that the court cannot solve on its own. It is the responsibility of the legislature to weigh the demand for a fair, just taxation, against practicability. The courts need better tools in the shape of precise legislation, especially when it comes to the estimation of mixed

25 *See* above, at section 6.

expenses. But it is still the responsibility of the courts to reason with the depth and theoretical base necessary for arriving at a fair result.

I believe that it is possible to achieve a system where the demarcation between professional and personal expenses is made in a way that is relatively fair and relatively practical. Practicability cannot be allowed to dominate the assessing of net income. Neither is it always possible to reach a result that is altogether fair.