

The reduced VAT rate in Europe - Opportunities for Effective Support for Families

Results of the expert meeting on 08 September 2011
Venue: European Commission Representation in Germany

The German Association of Family Organisations (AGF) and the European Confederation of Family Organisations in the European Union (COFACE) invited to an expert discussion concerning the future of the reduced rate of VAT on products and services for children. The discussion was mainly directed at representatives of German and European associations, the European Commission and members of parliament from Germany and Europe.

The results of the Green Paper on VAT and the VAT Consultation

*Input by **Werner Blockmans** from the unit on VAT and other turnover taxes in the European Commission. Werner Blockmans heads the sector in the VAT Unit of the European Commission responsible for the follow up to the Green Paper on VAT project.*

Werner Blockmans composed a brief summary of the legal foundations of the European VAT system, and pointed out that many value-added tax reductions for children's products in the Member States are based on exceptions. This was guaranteed at the time of the entry into force of the European VAT Directive (1993).

Included among these cases is the zero rate on children's clothing in the UK. In 2006, the EU has commissioned a study of the economic impact of reduced VAT, which proved that a uniform rate of VAT in the Member States would, in economic terms, be the most effective solution. Social, cultural, environmental or other policy objectives should therefore no longer be pursued via VAT regulations, but rather through the means of direct support services, that would be more effective.

The position of discussions at the European Council and the European Commission

In spring of 2009 the European Council came to the decision on the scope of reduced VAT rates. This agreement did notably rejected the Commission's proposal to include baby's diapers in annex III of the VAT Directive. As a consequence, the reduced rate applied in some Member States is not allowed under the VAT Directive and they would find itself, up until now in pending breach of contract proceedings.

Blockmans set out that economic studies demonstrated that there are more effective methods to support certain political goals or social groups, which should take precedence over a reduction of the VAT rate. Therefore the European Council views the issue of VAT reductions on the whole as being concluded.

Werner Blockmans was asked to give further information as to whether the Commission is of the view, that a uniform VAT rate is better than a reduced rate and thus



how, instead, the Commission would like to contribute to support environmental or social concerns. According to Werner Blockmans, from a purely economic perspective, it is probably actually better to abolish the reduced rates in favor of a uniform rate. He noted, however, that there are more policy areas alongside the economic sector and that it is very unlikely that the UK, for example, abolishes the zero VAT rate for children's clothing. Considerably more flexibility in the regulations on reduced VAT would allow a complete change of the taxation system in the country of origin. However, this development is very controversial with the Member States.

Blockmans hinted that the tension is also reflected in the European Commission, between a purely economic view of the value added tax and the support of certain political goals. Therefore, it is difficult to predict the further development.

The Green Paper on VAT and the Way Forward

Unfortunately, not too much detail could be given on the current EU Green Paper on the future of the VAT and the associated consultation, because the analysis of the responses thereto is currently ongoing. Altogether, approximately 1,700 responses have been received, of which however, approximately 1,100 responses were concerned with country-specific problems with VAT. The remaining 600 valid responses composed altogether between 8000-9000 pages. Werner Blockmans announced however, that the summary of responses would be viewable online around mid October and by the end of November a communication by the European Commission on the debate to the future development of the VAT, should also follow. An evaluation of the value added tax, which also considers and evaluates the value added tax from the various angles, is also to be expected at that time. Furthermore, this evaluation shall also be accessible to the public. In 2012 and 2013 new legislative proposals on the further handling of VAT in general, are expected. Concerning the special issue of reduced VAT rates, a decision has yet to be made and on top of this, it has still to be discussed within the Commission as to how to proceed.

Alternatives

Werner Blockmans primarily sees the alternative as understanding Europe as a single market and then raising the VAT in the country of origin. Thus, each state could decide itself which rates would apply to certain products and no more negotiations on exemptions would need to be conducted.

He declared that in order to implement a single VAT rate in member states, a strong harmonization of the tax rates would be sensible and only slight differences of two to three percentage points, could be tolerated. In order to achieve accordingly necessary social balance measures, the national political system would have jurisdiction here, the EU could make no specifications. He estimated however, that the probability of such a European VAT regime is very low. Finally, he pointed out that VAT in some countries constitutes the main source of state income and thus is essential for the public finances.



Also, from an economic perspective, where the family well-being is concerned, it is better to introduce uniform rates and to then redistribute the revenue.

The European Citizens' Initiative (ECI) – a possibility for the reduced VAT rate?

*Input by **Gerald Häfner**, MEP and member of the Committee on Constitutional Affairs and the Committee on Petitions. Gerald Häfner was a co-author of the report on the European Citizens' Initiative (ECI) and contributed over several years towards the realization of the project. He is also co-founder and longtime CEO of the "Mehr Demokratie e.V. (more democracy)" association.*

Development, legal and operational requirements of the European Citizens' Initiative (ECI)

An officially recognized ECI is only possible from the 1st of April 2012, because the regulation implementing the citizens' initiative will be officially adopted on the 31st of March 2012. A start of a European citizen's initiative before the first April of 2012 would also not be recommended, even if all preparations were completed, since it is not clear what is going to happen to those not yet formally approved petitions. Signatures which have been collected in advance would, therefore not have unequivocal validity.



Häfner firstly explained the conditions and proceedings of the ECI. The prerequisite for a European Citizens' Initiative is that 7 people from 7 EU Member States jointly speak out for their common concern. This is followed by a preliminary examination of the admissibility of this

concern. A rejection of the initiative is only permitted if there is flagrant abuse of the instrument, violation of existing rights and principles and non-competence of the EU Commission. This examination shall not last more than two months. After examination the initiators have one year of time in order to collect a million signatures. Both online and offline collected votes are valid, however with online collection of signatures, there is a duty to nationally certify the website used. In Germany, this certification is free of charge and is given by the Federal Office for Information Security (BSI). The collected signatures must come from at least a quarter of the European Member States, i.e. currently at least seven states.

Each country has a fixed number of votes that must be achieved. The number is degressively proportional and bases on the number of delegates in the European Parliament. For Germany the figure is approximately 74,000 signatures. The subsequent examination of the signatures collected is carried out randomly by the authorities in each Member State. In addition, varying data is required, according to the Member states, for valid signatures..

Concerning the topic, Mr Häfner stresses that he would approve a stronger recognition of children and parents in the legal and tax system. He offered to advise the initiative for a reduced VAT on children's products, where appropriate, on the implementation of ECI, but stated, however that members of parliament are not allowed to be a member of a group of initiators, as the European Citizens' Initiative wants to specifically promote the participation of citizens.

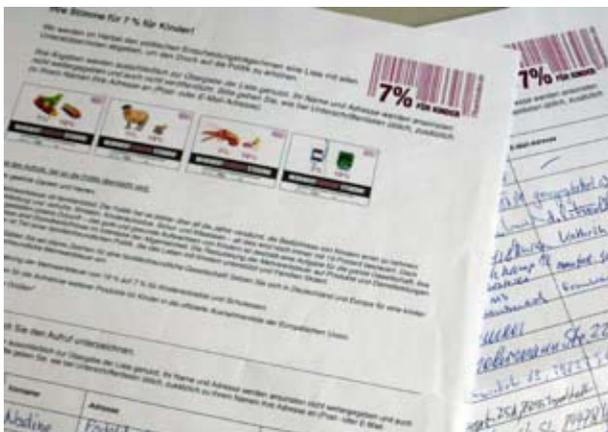
Gerald Häfner mentioned that it was advisable to collect about ten percent more signatures than what is absolutely necessary, in order to compensate for any incorrect or illegible entries.

He sees it as a major objective of the European Citizens' Initiative to give rise to political debates, which are stimulated by EU citizens. Therefore, he could achieve that, after successful implementation of the ECI, a mandatory

public hearing is held before the European Parliament and the European Commission.

In detail the following process is planned: The signatures are presented to the national authorities of the individual member states in which they were collected. Here within three months the signatures are initially examined and certified. After this step the initiative can be presented to the European Commission which holds a public hearing within another three months. Subsequently, the Commission shall decide whether or not to submit a legislative proposal.

The question whether companies would also use the instrument to further their own interests, was also raised. Häfner explained that the attempted use of the ECI by companies in order to obtain influence could, of course not be excluded. But one should not overestimate their influence, because the citizens themselves often see through these maneuvers. Furthermore within the framework of the European Citizens' Initiative there is also a transparency clause that requires full disclosure of funding. In this way, according to Häfner, the actual origins of the initiative can be completely understood.



European Citizens' Initiative (ECI) as a tool for the reduced rate of VAT

Whether or not the ECI shall be a tool, which will bring the reduced rate of VAT for children's products into discussion depends, primarily, on whether or not it falls within the jurisdiction of the European Commission or the EU, in general. Furthermore, the initiative must deal with a subject which is already present in the EU



Treaty. It will be difficult where topics aimed at a change or developments of contractual items are concerned. The subject of tax law, more specifically VAT, definitely belongs to one of the core competencies of the EU Commission. A European Citizens' Initiative for inclusion of children's products in the annex III of the VAT Directive would therefore be absolutely possible from the basic requirements. Häfner emphasised that in this way, a Europe-wide issue could be made, which would stimulate the public debate concerning the reduced rate of VAT on Children's products. Moreover, this approach might be useful to influence the upcoming decision of the European Commission regarding VAT.

A look at other Countries: Poland as an example

Input by: **Dr. Izabella Cech**, Editor of Economic Newsletter „Poland News,” former diplomat, journalist, Polish tax consultant and university lecturer.

A reduced rate on clothing for infants and toddlers and children’s shoes is still valid in Poland until the end of 2012. As of the 1st of January 2012 the VAT on these products will be increased by the Polish government, to the regular VAT rate of 23%, following a ruling by the European Court as the reduction violates applicable European law (Act No. C 49/09).



Izabella Cech reported that the Polish government had deliberately decided to leave the existing arrangements in place until 2012, so that domestic production would remain protected from cheaper imports of goods, and families would be relieved longer: Since the increase in the standard rate actually does not lie in the family policy intentions of the government.

Calculations of family associations and the Polish Adam Smith Institute have shown that with the increased VAT on children’s clothing, families will be burdened with approximately 2.5 billion zloty (about 650 million), additional spending.

Since 1972, children’s clothes had been exempt from tax in Poland. There was no official definition of the child given, so every person up until the age of 18 was considered a child for tax purposes. With the introduction of

a classical VAT system in 1993, these products received a clear definition: clothing for children up to a size of 1.40 and a maximum age of 11 years was subject to the reduced VAT rate of seven percent. Also, in the new value-added tax reform of the 1st of March 2004, during Poland’s accession to the EU, it had been established that the reduced rate would continue to apply to infant clothing, children’s shoes and clothing accessories. Due to the fact that no clear definition of a child for tax purposes existed, the reduced rate of tax applied only to baby clothing and children’s shoes. Izabella Cech pointed out that this definition has been achieved with the help of the statistical offices in Poland. The now imminent increase in VAT creates an extra burden of about 8,000 zloty (2,000 Euros) for families, per year. This shall be an enormous sum, considering the low wages in Poland.

Cech informed the participants at the event that the VAT increase was not met without protests from the public and politicians. As early as 2008, a major campaign against the tax increase for children’s footwear and apparel under the title „Say No to the sales tax increase” and the slogan „let us live” began. In addition to the association of shoe and leather industry, other groups and institutions as well as accountants, lawyers and media joined in. Together they were successful and thus, the Polish government are now trying to creatively circumvent the rules, by introducing a bill, which provides for reimbursement of the difference from the reduced to the regular VAT rate (ie about 70% of the amount of VAT) when purchasing children’s clothing up to a maxi-



imum of 3,000 zloty (about 750 Euro). This should apply to all children up to the age of 13 years. The bill is in the editing phase and is to be in force as of the 1st of January 2012. However, it is questionable whether this is temporally possible, due to the fact that there shall be October elections in Poland, before which the decision would have to be made. In addition, this bill is also being examined by lawyers to ensure compliance with EU law. She made it clear that the Polish family organizations did not support this proposal because they feared the subsequent high, bureaucratic costs. The Polish families have

in the mean time, now solved the problem quite pragmatically by purchasing at those places, where the clothes are already cheaper: in Great Britain and on ebay.

In Poland, the push for a reduced VAT rate on children's products is at the same time, a push for supporting the birth rate, stated Izabella Cech. Therefore, the Polish government and Polish MEPs have great interest in cutting the value-added-tax. Basically, the expenditure for children in Poland is a heavy burden on parents.

A look at other countries: Spain as an example

Input by: Jean Bernard Audureau from the consumer organisation ASGECO.

In Spain, there is currently a proposal to reduce the rate of VAT on certain products and services for children, particularly in education. His association, however, asks the question whether or not that really is an effective way to promote families.



Confusion reigned in his opinion, especially regarding the products that the reduced VAT rate should apply to and how a reasonable classification of children's products could be achieved. There was a considerable variety of questions to be answered concerning what products are necessary for children at various ages. For example today, a computer or the Internet could very likely be a

necessary part of education facilities, but could just as easily be used by adults. Audureau raised the question as to whether, in fact, the goal of a reduced VAT rate would be sensible, or whether it would be even better to have other support services introduced, regardless of the value added tax. He pointed out the regulations in the city of Madrid, where families are reimbursed up to a family income of 30,000 Euro for the cost of school clothing, transport to school and similar expenses.

However, there was again a great range in the money being spent on school supplies and books; you could buy similar products at very different prices. Hence, this poses at least the question as to who would benefit from a VAT reduction on children's products. In Spain there are calculations that families could reduce their spending in the area of education by about five to six per cent. It remains however unclear whether the tax reduction would really have impact on prices. According to Jean Bernard Audureau, the question that essentially arises from these considerations is whether a reduced rate of VAT could actually operate social policy, or if there would be more effective forms of relief for families, such as the ability to deduct expenses for children from the tax burden.

The initiative „7% für Kinder“ from Germany

Input: **Sven Iversen**, Arbeitsgemeinschaft der Deutschen Familienorganisationen e.V. (AGF)

„7 % für Kinder“ was developed by the AGF and the mail order company for children’s products JAKO-O, as well as being initiated in cooperation with Deutsches Kinderhilfswerk. A strong coalition of children, families and social organizations support the campaign, which started in May of 2011 in Berlin.



The aim of the initiative is that the seven percent reduced rate of VAT, valid in Germany, shall be levied on children’s products and services. This is necessary to relieve the burden on families, who traditionally spend a disproportionate amount of their income on the care and upbringing of their children. Moreover, this is an important symbolic act by which society can express its appreciation towards families. Sven Iversen pointed out that the reduced VAT rate had once been introduced for sociopolitical reasons, to ensure that the basic needs of life would be affordable for everyone.

The list of discounted products has seen significant growth over the decades and has, to a certain extent, become far removed from that earlier principle. The needs of children, however, clearly belong to the basic needs of society and lie within the interest of society. The Alliance „7% für Kinder“ have therefore compiled a catalog of products to which the reduced VAT rate should be applied. These include strollers, diapers, clothing, shoes, toiletries, toys, school supplies and much, much more. According to calculations by the AGF a reduced rate of

VAT would offer huge savings for families. Overall, the savings would approximately reach just under a billion Euros a year. Coincidentally, this happens to be almost the exact amount, that the federal government waives, by its own free will, via the lower tax on hotel stays.

Sven Iversen explained the various components of the campaign, noting that over 20,000 votes in support of this campaign had already been gathered. He pointed out that there are two steps towards implementation: the German government could immediately reduce the VAT on school lunches and child car seats, in a second step, the project should be brought to the fore at the European level, in order to alter the existing regulation, so that the VAT rate on other children’s products could be reduced. He made it clear that the reduced rate of VAT would primarily be a signal to families, to also assume a social responsibility for children, but that it also is an important component of family-friendly policy, which, in addition, makes life with children more attractive.

An advertisement for the "7% für Kinder" initiative. It features a white background with a small barcode in the top right corner containing the text "7% für Kinder". Below the barcode, there are two images: a cooked crayfish on the left and a baby's pacifier on the right. Underneath the crayfish is the text "7%" and under the pacifier is "19%". At the bottom, a black banner contains the text "MEHRWERT GERECHT STEUERN!" in white, bold, uppercase letters. Below the banner, there is a line of text: "Reduzierte Mehrwertsteuer auf Produkte und Dienstleistungen für Kinder". At the very bottom, there are logos for AGF, JAKO-O, and Deutsches Kinderhilfswerk.

The activities and positions of COFACE

*Input: **Nicolas Revenu**, President of COFACE working group 3*

Nicolas Revenu explained that within COFACE, there had been no intensive study on this topic. He could however say that there exists more of a culturally conditioned distrust of government intervention in France. The French family organization UNAF calculate the monthly cost of essential products using product lists, which could possibly be used for the discussion on VAT reduction. COFACE has primarily expressed itself in connection with the recent Green Paper on VAT.



There the issue as to whether VAT is a purposeful family and social policy tool, is being debated. At this point even in COFACE, there was no concrete answer, as the progression of the event shows. It is however clear, that COFACE calls for the preservation of a reduced VAT rate. Nicolas Revenu pointed out that it would also be possible where the reduced VAT on children's products is concerned, not to define individual products but rather the people, whom this discount should be applied to.

In either case, adequate control and enforcement tools are required. He made it clear that it would not be acceptable for COFACE to play family policy off against

other social or environmental objectives. It is more important to clarify what resources are available to support the families in the member states and the ways in which they could be most sensibly used in the particular country.

At the conclusion of the event, resulting from these remarks, the participants called for the path to be opened up for a reduced rate of VAT on children's products in Europe. On such a European legal fundament, each country could decide for itself, whether or not to go in such a direction.

Furthermore, a stimulating discussion was held on the definition of suitable products and services for children, the possible effects on prices and on possible effects of such a reduction on other social or family-policy benefits and possible unintended windfall gains.



Annex: Background information on the reduced rate of VAT for children's products

The current discussion in Germany

In Germany there are two different rates of VAT: the so-called standard rate, which stands currently at 19 percent, and the reduced rate of VAT currently at 7 percent, for products that are considered necessary basic needs of a person, such as food, newspapers or public transport services. Over the decades, the number of products and services necessary, and thus at the lower rate, has been expanded again and again - often with the aim of promoting individual economic sectors.

The federal government announced in 2009 to implement this „tax relief particularly for those in the low and middle income brackets and for families with children“ until the year 2013. Furthermore, it is „ (...) the aim of this coalition to further strengthen the economic and social capacity of families,“ and „to directly place funding instruments (...) into the reality of life for families“.

Concerning the reduced VAT rate, the federal government decided in 2009 to set up a government commission to work out a proposal in the course of 2011. Up until now, October 2011, a meeting of the Commission has yet to take place.

The reduced rate of VAT in Europe

The framework for the VAT are largely be determined by the European Union. A list determines for which products and services the reduced VAT rate can be applied. The states decide the precise application models themselves.

In some European countries, the VAT on products and services for children is reduced or zero rated (e.g. Portugal, France, Czech Republic, Poland, Great Britain, Ireland and Luxembourg). This is partly due to the existing exceptions to regulations, and partly due to the fact that many countries implement regulations, which the EU makes possible.

The Objective and core message of the campaign „7% für Kinder“: A sign for a family-friendly society and an effective relief for families.

„7% für Kinder“ requires the application of a reduced VAT rate on products and services for children. Families make a significant contribution to the development of our society and children are the designers of our future. The good and healthy growth of children is therefore a task for society as a whole. Their needs count as the basic needs in the interests of the general public.

The reduced VAT rate on products and services for children

- signifies a resounding yes! towards a social responsibility for children
- is part of a family-friendly policy that supports life with children and promotes families.
- contributes to reducing child poverty and to relieving families.

The campaign „7% für Kinder“

Those, who came together for the initiative are: the Association of German Family Organisations e.V. (AGF), the retailer company JAKO-O and above approximately 15 family-, children and social associations and other organizations and institutions in society and economy: AWO-Bundesverband e. V., Deutsche Sportjugend im Deutschen Olympischen Sportbund e. V., Deutsche Liga für das Kind, Deutscher Frauenrat e. V., Deutscher Kinderschutzbund e. V. (DKSB), Deutscher LandFrauenverband e. V. (dlv), Deutsches Netzwerk Schulverpflegung e.V., DHB-Netzwerk Haushalt Berufsverband der Haushaltsführenden e. V., FIT-Z, Home Instruction for Parents of Preschool Youngers – HIPPY Deutschland e. V., Katholischer Deutscher Frauenbund e.V., Kolpingwerk Deutschland (KWD), Bundesverband der Selbsthilfeinitiativen Alleinerziehender SHIA e. V., Sozialverband Deutschland e. V. (SoVD) und das Zukunftsforum Familie e. V. (ZFF).

Problems with the definition of „products and services for children“

The distinction is of course not easy and should be discussed. The initiative „7% für Kinder“ makes the following proposal:

- prams and buggies
- Complete baby care and nutrition needs (creams, oils, wipes, soothers, baby bottles, tippy cups etc., as well as infant care, child toothpaste, toothbrushes, kids shampoo, etc.)
- Baby diapers. (including swim diapers)
- Baby and children’s clothing up to size 176
- Baby and children’s shoes up to size 35
- school satchels
- Exercise books, pens and other customary school supplies (rulers, protractor, pencils portfolios, drawing pads)
- modeling clay, crayons, markers, paints, such as simple color boxes, finger paints, crayons plus accessories such as Aprons, brushes, scissors for children
- Child car seats
- School and nursery food
- Baby walkers/ wheels, kids scooters, tricycles and bicycles for children, including protective helmets
- Children’s toys and board games for children under 12 years
- Services for children including, for example, care services, educational programs, music lessons or gymnastics for children. Some of these services are already in the reduced tax bracket or exempted from VAT.

The passing along of reductions through companies

The companies surveyed by the AGF confirmed that they would pass on the discounts. The companies participating in the campaign commit themselves to passing on the reductions. In comparison to other areas of retail, the price pressure is so great that no company can afford not to reduce prices, especially since in this, children’s area, the consumers are very critical. As it is, no company can afford to give the impression that it is not child friendly.

The Savings potential for families

As a rule of thumb: Through the reduction in VAT from 19 to 7 percent, the current prices for products and services for children fall by about 10 percent.

Parents could save approximately 200 Euro on the initial kitting out for their babies and approximately 40 Euro on their school entry. Spending on clothing and footwear, could fall by up to 60 Euro per year, while spending on the school lunch could fall by up to 15 to 30 cents per meal.

Appropriate measures for families and children are not to be played off against each other

Families need good childcare with sufficient places and high quality. Such offers in Germany are still far too rare. We find, however, that where the support of families is concerned, it is not allowed to be a question of either-or but, should instead be one of both-and.

The needs of families are varied and spread out into many different areas: financial relief and support, infrastructural services, time. In all these areas, adequate support is needed to promote families and to relieve them. Anyone who sets off one support method for families against another ignores the real needs of families. A stringent family policy is a question of political priorities; it should not be formed around the current cash position.

Further Information can be found under:
<http://7fuerkinder.de>

November 2011

Edited by:
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Photo Credits:
Page 2, 3, 4, 5, 6, 9: Björn Hensel
Other: AGF

Typesetting:
manuka.p.r

Deutscher Familienverband (DFV) · Evangelische Aktionsgemeinschaft für Familienfragen (eaf) · Familienbund der Katholiken (FDK)
Verband alleinerziehender Mütter und Väter (VAMV) · Verband binationaler Familien und Partnerschaften (iaf)

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AGF is funded by

