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**Redemanuskript ECCVAT**

*Turnover tax and welfare associations in Germany*

Members of the European Parliament,  
Ladies and Gentlemen,

Today you have followed the European Charities Committee on VAT's invitation to discuss a subject which at first does not sound very exciting. However, the apparently rather dry topic of turnover tax turns out to be of a quite explosive nature which, in the case of Germany, may bring about a substantial additional burden on the social systems. Let me thus first of all give you an outline of the structure of what we call the "welfare services" in Germany.

Private welfare organisations are active throughout the entire spectrum of the social security system. Within this system - which is financed either through compulsory contributions or taxes - citizens have a legal claim against the respective obligor. However, cost carriers such as social insurance frequently provide their services through private bodies which are generally organised as non-profit organisations. This system of the actual social services being provided through private organisations is nearly comprehensive and is based on the principle of subsidiarity.

Service provision by the state, which used to be common practice, has been considerably curbed in recent decades, while service provision by non-profit organisations, which are called "voluntary welfare services" in this area in Germany, have clearly come to the fore. Apart from these organisations, there are meanwhile areas in which services are also provided by commercial suppliers. In this respect, a social market is now developing in Germany as well.

Social services and institutions are generally financed either by the public sector – i.e. through taxes – or by social insurance such as health or nursing insurance.

At this point, I would like to briefly mention those welfare organisations currently joined in the Federal Association of Voluntary Welfare Services, which I represent here. These are the "Arbeiterwohlfahrt" (workers' welfare union), the „Diakonisches Werk“ (social service agency of the evangelical church of Germany), the German Caritas Association, the "Paritätische Wohlfahrtsverband" (German parity welfare association), the German Red Cross and the Central Welfare Association of Jews in Germany. In order to give you an idea of the scale of the services provided by these non-profit organisations, let me give you just a few figures based on overall statistics as of 1 January 2000: The organisations I just mentioned operate more than 1,200 hospitals with a total of about 220,000 beds.

In view of the demographic development in Germany, particularly the number of institutions in the area of old people's care has clearly increased in recent years. At present, voluntary welfare associations operate more than 6,000 stationary institutions in which more than 400,000 old people are taken care of. In addition, there are many other institutions spanning the whole spectrum of social work. In total, voluntary welfare services have more than 650,000 full-time and about 450,000 part-time employees. In fact, this sector is bigger than the entire German banking sector.

Obviously, the economic significance of the services provided within this social system is enormous.

However, I would now like to resume the initial question and come back to the tax issues.

As follows from the system I have just outlined, social services are generally provided free of charge for the person concerned since they are borne by a cost carrier.

In general, each individual case involves three parties: First of all the service provider who usually provides services free of charge for the person concerned. Then there is the cost carrier, which may be social insurance such as nursing insurance in the area of stationary old people's care or another cost carrier such as the local authorities or the respective federal *Land*. Only if the services to be provided by them are insufficient, the person concerned him- or herself may have to make additional payments. This means that in most cases the actual cash flow generally only takes place between the cost carrier and the service provider.

As a rule, turnovers achieved in this area are not subject to turnover tax due to exemption provisions under national turnover tax law. Turnovers of the carriers of social insurance, hospitals, old people's homes, nursing homes and youth welfare services are exempt from turnover tax if and as far as their services directly benefit the persons concerned. Certainly, the examples I have mentioned do not cover all exemptions.

To sum up, one could say that the main areas of social work, as far as they directly benefit the persons concerned, are exempt from turnover tax. The same applies to turnovers of voluntary welfare organisations achieved from services provided against payment - however, again only if they directly benefit the person concerned.

Ultimately, this means that the German system of social service provision is for the most part exempt from turnover tax, but also that the service-providing welfare organisations themselves are not entitled to deduct input tax.

The major part of the expenses incurred by welfare associations account for staff expenditure, which does not trigger any turnover tax liabilities, but incurs no input tax either. However, they also have to purchase services which include a turnover tax component. If they purchase a vehicle, for example, they have to pay the amount of turnover tax attributable to this without being able to deduct any input tax. Consequently, in this respect, they have the same status as an end consumer. In conclusion one can thus say that voluntary welfare organisations in Germany are not subject to turnover tax with regard to the payments they receive from the social insurance systems since these are exempt from turnover tax. They are also not subject to charge turnover tax for costs they have to charge to the persons concerned where necessary, for example in the form of additional payments. However, as far as these associations purchase services themselves, they are treated like end customers, i.e. they have to pay the taxes incurred without being able to deduct input tax.

Incidentally, this system applies to the payments from social insurance irrespective of whether a welfare or a commercial entity is concerned. This is because it is the actual turnover that is exempt from turnover tax and the legal form is irrelevant in this respect.

Let me add that turnovers from services, which these service providers do not directly provide to the persons concerned, are as a rule subject to turnover tax, however, partly at a reduced rate.

Now, what would happen if these exemption provisions no longer applied under the European regulations? The whole social insurance system, which in Germany is exclusively financed by the work factor, would be burdened by the amount of the VAT rate. This would lead to an additional burden on those liable to provide services, i.e. ultimately the social insurance systems and also public budgets. As far as public budgets are concerned, one may say that the money goes from one pocket to another. In the case of Germany, however, it has to be taken into account that this would enable the various levels - local authorities, the Federal *Länder* and the Federal Government –to shift costs. The social insurance systems would be forced to raise contributions and would thus further increase the cost of the work factor.

Of course, the social insurance carriers would attempt to pass a part of this additional burden on to the service providers through reimbursement negotiations. Given their quasi-monopoly positions, they would probably be to some extent successful. As a result, service providers, which in recent years have also experienced tough economic times, would run into further difficulties.

As regards the persons concerned, the social security benefits, part of which have to be borne by the persons concerned themselves, would be increased by the amount of the turnover tax rate without any possibility to compensate this by deducting input tax.

In addition, due to the high staff intensity in this sector there would be hardly any possibilities to claim input tax credits at all.

All in all, it is to be feared that an inclusion of the services described into the turnover tax system, i.e. ultimately limiting the exemption provisions, would result in a substantial additional burden on the social insurance systems, which certainly would also have effects on the overall economy. Service providers would have to carry additional economic burdens leading to the overall service guarantee being jeopardised, which to some extent is already the case today.

We are therefore of the opinion that the system of non-taxable turnovers, supplemented by the existing exemptions, should essentially remain untouched. Moreover, we welcome the idea of giving certain non-profit organisations the right to choose between the above-mentioned exemption and a reduced tax rate, since this approach reflects the structures of a number of EU countries and takes into account their specific conditions.

In conclusion I would like to stress again that simplifying turnover tax law in such a way that the turnovers currently exempted under Article 13 of Guideline 77/388 EEC become subject to turnover tax, would shake the German social security system to its very foundations.