

## **Ecopreneur.eu: Adequate amendment of the EU VAT directive important to boost the circular economy**

**Ecopreneur.eu, the European Sustainable Business Federation, calls for amendment of the EU VAT Directive 2006/112/EC to allow a low VAT rate for circular goods and services.**

To boost the circular economy, Ecopreneur.eu calls for economy-wide tax measures including a tax shift from labour to resources and differentiated value-added tax (VAT) rates to boost the circular economy. In view of the ongoing Open Consultation on amending the VAT Directive, this position paper focuses on the VAT. If adequately used, value added tax can strengthen the circular economy by transferring clear prices signals to consumers and producers throughout the supply chain.

A lack of demand for circular goods and services is the main bottleneck for leading companies to accelerate and mainstream their introduction. The best way to overcome this hurdle is for the EU and member state governments to create framework conditions using economic incentives for companies to implement circular business models, as well as for users and consumers to purchase circular goods and services.

This involves an integrated package of systemic incentives for companies and consumers to promote circular behaviour throughout the chain: design, materials choice and sourcing, marketing, maintenance, repair, reuse, sharing and refurbishment of goods, remanufacturing of parts, collection of waste products, increasing the share of sustainable cascaded biomass and recycled raw materials in the goods, and extraction and composting of sustainable biomass.

While these activities are formally included in the European Waste Hierarchy through prevention and preparation for reuse, we recommend taking them into account in more detail as to stimulate them through economic incentives including a tax shift, the VAT and Extended Producer Responsibility (EPR). Without these, the goal to create a circular economy seems unattainable. They serve to improve the basic “rules of the game” of our economy by “mechanism design”.

Thus, concerning the VAT, Ecopreneur.eu **recommends the European Union to provide room, guidance and encouragement to all member states for a zero (or low) VAT rate for circular goods and services.** The EU VAT Directive 2006/112/EC on the common system of value added tax forbids (permanent) low VAT rates based on circularity or sustainability. The EU Circular Economy Package currently lacks economic incentives for consumers. “Eco” labels are mentioned, but can only inform. Boosting demand requires price incentives along the full circle, and the VAT is the only price incentive aiming at consumers.

The VAT is a powerful economic instrument. Sustainable businesses all over Europe ask for low VAT rates for circular goods and services to overcome the barrier of lacking demand. Given the choice between two otherwise equal goods or services, even a moderate VAT difference can effectively nudge consumers to purchase the circular option rather than the linear one. Existing evidence concerning limited impact of VAT differentiation of an entire product group (e.g. all hair dryers) are therefore not applicable to differentiation based on circularity.

VAT differentiation can be devised to avoid “leakage” of industrial activities by covering all imports from outside the EU. Split incentives between chain partners are avoided by covering business activities along the full cycle. Materials-specific fiscal tariffs may be used where needed.

With respect to the Open Consultation on the VAT Directive (2006/112/EC), **Ecopreneur.eu therefore recommends amendment of the Directive to allow a low VAT rate for circular goods and services.** To accomplish this Ecopreneur.eu favours Option 1: Extension and regular review of the list of goods and services eligible for reduced rates in Annex III of the VAT Directive. The major disadvantage of option 2 (abolition of the existing list) is that it may very well lead to prevention of reduced rates for high-value goods and services, in particular for those that are easily transportable. The latter would severely hit current circular goods and services: they are particularly found in high-value goods and services, including printers, carpet tiles, furniture and textiles. Therefore Option 1 seems more favourable. Concerning specific economic activities, Ecopreneur.eu supports the proposal of the Swedish government to boost their repair sector by a combination of low VAT and income tax as of 1 January 2017. The Netherlands already have a similar provision which was found beneficial for employment in the repair sector. Extending the current list to include more and more circular goods and services seems the *only* way to really boost consumer demand for them. Starting with the obvious cases of repair and maintenance services, the list could be annually extended to also cover digital services powered by renewable energy and replacing a material product (e.g. an online newspaper), product-based services (services connected to a physical product), pay per use services (one-time payment for each use), Cradle-to-cradle products, next-life (2nd hand) goods, goods made from recyclable 100% recycled materials, and the Best Available Solution for each product group. All subject to a simple sustainability check to avoid greenwashing – to be discussed further. The VAT Directive should at the same time prohibit governments to introduce low VAT rates for economic activities that are clearly non-circular and environmentally detrimental, such as a low VAT rate for coal-fired plants. Also, the low VAT rate should apply for a limited number of years and expire if the application has become mainstream or if more circular solutions have been developed. At the same time, for certain product groups, low VAT rates may be needed even in a circular economy to prevent the return of linear products and services.

Based on this amendment of the VAT Directive, the VAT rates for circular goods and services could be differentiated. Such differentiation is greatest if the EU legal framework allows a zero-rate based on the circularity criterion. A zero VAT would most certainly give a strong boost to mainstreaming circular business models, directly for consumers, and indirectly for producers as well. The circular goods and services added to Annex III of the VAT Directive can follow the definition of circular goods and services planned for 2017.

**Next to VAT differentiation, Ecopreneur.eu asks for a *tax shift* from labour to raw materials, as advocated by Ex'tax and the "Big Four".** As part of this, to increase the tax on primary raw materials while reducing the tax on recycled materials and labour. We welcome the recent call from the EU Commissioner in charge of taxation to push forward with shifting taxes from labour to natural resources, and call on him to further take the lead in facilitating this.

Such a new framework, with guarantees for stability over a prolonged period of time, will greatly accelerate and increase investments in circular business and infrastructure. Points of action lie at both national and EU level as well as local, regional, per chain and cross-sectoral. **Ecopreneur.eu urges the European Union to ask the Member States to come forward with national action plans on tax reform and link these preferably to the *Country Specific Recommendations*.**

Finally, greater flexibility to member states could create additional costs for businesses besides opportunities. To minimise this risk, it is crucial to define at the EU level what products and services meet what criteria to deserve the term "circular". We therefore ask the EU to take the lead in a process with those member states willing to move forward with tax reform so that they can introduce a harmonised approach.

**About Ecopreneur.eu**

Ecopreneur.eu is the European Sustainable Business Federation of seven national associations whose common aim is a new economic framework in which sustainability is promoted, the environment respected and ecological principles are followed. Ecopreneur.eu represents over 2000 sustainable companies - mostly SMEs.

**Contact information**

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