European Centre for the Development of Vocational Training

BRIEFING NOTE

# Taxing the mind

## European Union Member States should think about the best ways to use tax incentives to encourage investment in learning

Intellectual assets create wealth. The value of an enterprise's knowledge and expertise often outweighs the value of its fixed assets such as plant and machinery. European Union (EU) Member States use various tax incentives to encourage individuals and enterprises to invest in education and training (see Table 1).

Although widely used, tax incentives covering value added tax (VAT), corporate and personal income taxes are not standard in the EU. A look at six countries (Germany, Ireland, France, the Netherlands, Austria and Finland) reveals some of these differences which reflect Member States' firm control over tax policy ([1]).

### Table 1: Types of tax incentive

| Type | Benefit |
|---|---|
| Tax allowances | Sum deducted from the gross income to reduce the taxable income |
| Tax exemptions | Some particular income is exempted from the tax base |
| Tax credits | Sums deducted from the tax due |
| Tax relief | Some classes of taxpayers or activities benefit from lower rates |
| Tax deferrals | Postponement of tax payments |

*Source:* Cedefop and OECD.

The EU lags behind the United States and Japan in private investment in education and training. Public budgets are likely to face severe constraints following the financial and economic crisis. So, it is increasingly important to think how tax systems should treat investment in the learning that maintains the value of the intellectual assets. Especially as they are vital for enterprises to use their capital assets effectively. Now is probably a good time for Member States to think about how best to use tax policies to encourage individuals and enterprises to put from their own money into education and training.

### Value added tax

In the EU, people paying to send their children to private school or university, or enterprises purchasing vocational training for children or young people, generally, do not have to pay VAT. The only catch is that they must buy these services from bodies governed by public law having education as their aim or by other organisations recognised by the Member State concerned as having similar objectives. Unsurprisingly, different Member States recognise different types of organisations and that affects the price of these services.

If you buy education and training services from bodies governed by public law or recognised organisations, you will not have to pay VAT in any of the six countries examined. However, if you purchase services from organisations not recognised by the Member State you may be charged VAT. For example, in Germany, France, Austria and Finland private (even non-profit) education and training providers have to charge the general VAT rate unless they meet specified criteria and are recognised by the tax authorities and so exempt.

Even recognised training providers that do not charge VAT for their services do not escape completely. They cannot recover the VAT they pay on the goods and services they buy. This adds to their expenses and can be a disincentive to investing in new equipment.

### Corporate income tax

For the purposes of corporate income tax, expenditure on training is regarded as a business cost and is 100% deductible from taxable income.

([1]) *The use of tax incentives for education and training*, 2009 www.cedefop.europa.eu/etv/news/Default.asp?idnews=4499

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However, what is a business cost depends on national interpretations. For example, in Finland, spending on training to maintain and develop skills for the current job is deductible. Basic education or training for employees leading to a degree or certification is not.

### Table 2: Examples of tax incentives for enterprises for education and training

| Country | Tax incentive | Main goal (s) |
|---|---|---|
| France | Tax credit for training expenses for entrepreneurs | Favours training activities of entrepreneurs who are not wage earners |
| | Tax credit in favour of apprenticeship | Encourages employment and education of apprentices |
| | Tax credit for training expenses of employees in enterprise economy and financial participation | Supports small and medium-sized enterprises in these areas |
| The Nether-lands | Payment reduction for education | Encourages enterprises to carry out education and training activities for their employees. |
| Austria | Training tax allowance | Foster enterprises' investments in human resources |
| | Training tax credit | |
| | Apprenticeship tax allowance | Encourages employment and education of apprentices |
| | Apprenticeship tax credit | Some classes of taxpayers or activities benefit from lower rates |
| NB: These tax incentives affect personal income, or corporate taxes (depending on the legal status of the enterprise), except for the Dutch tax incentive, which reduces the salary tax paid by enterprises. | | |

*Source:* Cedefop.

However, as well as the standard deduction of expenditure on training as business costs, France, the Netherlands and Austria have other tax incentives to encourage investment in training (Table 2).

Some encourage training generally, but others promote specific types, such as apprenticeships and training for entrepreneurs. Tax incentives to reduce corporate income taxes for investing in education and training, in most cases, are only obtained when purchased from recognised training providers.

It is also important to note important differences in how Member States tax providers of education and training services.

In Germany, Ireland, the Netherlands, Austria and Finland, private education and training providers pay corporate income tax at the same rate as other private enterprises. Publicly owned providers do not pay corporate taxes. In France, only private providers of continuing vocational training services are taxed like other private sector enterprises. France also exempts non-profit organisations providing education services from corporate income tax provided they meet specified criteria.

## Tax incentives for individuals

All of the six Member States studied provide incentives that reduce personal income tax to encourage people to spend on various kinds of education and training (see Table 3).

The incentives pursue very different goals. Austria and Finland provide tax incentives for job-related training. Germany, while also taking this approach provides tax allowances for income earned by students. Germany also allows other education and training expenses to be offset against tax as does the Netherlands. Ireland provides general tax relief on tuition fees, while France has a range of different incentives covering apprentices and those in secondary and higher education.

Not only those participating in education or training can benefit. In Germany and Ireland, parents of dependent children can claim tax relief on tuition fees.

Although the tax incentives share broad aims, they sometimes cover different things. In some cases tax incentives cover only tuition fees. In others the cost of course materials, travel and subsistence are also eligible. The French income tax credit for higher and secondary education expenses is a fixed sum per student, irrespective of actual expenses.


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### Table 3: Examples of tax incentives for individuals for education and training

| Country | Tax incentive | Main goal (s) |
|---|---|---|
| Germany | Deductions of education or training costs as income-related expenses | Encourages individuals' expenditure on education and training activities |
| | Deductions of education or training costs as special expenses | Encourages individuals' expenditure on education and training activities |
| | Deductions of tuition fees for own children in private schools | Supports taxpayers with children studying in certain recognised private schools |
| France | Tax credit on interest burden of loans incurred by students in higher education to finance their studies | Supports students that finance their tertiary level studies with a bank loan |
| | Income tax exemption on wages earned by apprentices | Promotes apprenticeship, improves the purchasing power of young people |
| | Income tax exemption on pupil and student wages earned during school or university holidays | Improves the financial situation of students working while studying |
| | Income tax exemption on wages earned by apprentices | Improves the financial situation of apprentices working while studying |
| The Nether-lands | Deductions of educational expenses | Increases participation of adults in lifelong learning by reducing the cost of education and training |
| Austria | Deductions of training costs as income-related expenses | Encourages individuals' expenditure on education and training related to earning an income |
| Finland | Allowable expenses related to costs incurred for maintenance of professional or vocational skills | Helps individuals to maintain their professional/vocational skills |
| | Study loan allowance | Encourages students to take study loans instead of paid work, making it possible to graduate in a shorter time period. |

*Source:* Cedefop.

## Assessing tax incentives for education and training

Analysis of the six countries suggests that tax systems are more favourable for bodies governed by public law having education as their aim and other organisations recognised as having similar objectives. This places private providers of education and training that are required to charge VAT at a possible cost disadvantage in supplying comparable services. However, the situation is offset by the fact that providers that do not charge VAT cannot recover the VAT they pay when purchasing goods and services, including equipment they will use to deliver training courses.

Tax systems also appear more generous to enterprises investing in learning than to individuals. Corporate tax policies enable enterprises to treat expenditure on education and training as a deductible business cost and provide additional ways to reduce taxes. Tax policies for individuals are more restrictive. Not all individuals can deduct the costs of their education or training against their taxes. Even those who can are, in some cases, limited in what they can deduct.

Indications are that take-up of tax incentives by individuals is relatively low and that there is a general lack of awareness of what is available. The complexity of some systems may also be a disincentive.

Some of these differences may be due to tax and education and training policies being largely unconnected and pursuing different goals. Certainly there is a lack of data on the effectiveness of using the tax system to encourage participation in education and training.

Although tax incentives for education and training are used by Member States, there are strong reservations over 'dead weight' (the degree to which learning would have taken place without the incentive), especially among large enterprises and highly qualified individuals. Perversely, such tax measures may favour groups that already have the best access to education and training.

However, despite these difficulties, take-up of tax concessions by enterprises is quite high. Tax schemes in the Netherlands, Austria and Finland are also regarded as relatively simple which shows that bureaucracy need not be arduous. Although tax incentives for providers of education and training are limited to those recognised by the Member State, they do not in every case require learning to take place in that Member State. The French tax credit for interests on loans, the German deduction on tuition fees and Irish tax relief for tuition fees cover education and training at home and abroad.

Despite inevitable dead weight, tax incentives can encourage enterprises and people to invest their own money in their own learning. This may be an important first step to increasing private spending on education and training. Dead weight could also be reduced if tax instruments were specific and targeted on groups that tend to train less (small enterprises and their employees, individuals on low income and low skilled). However, in targeting, it is important to get the balance between targeting and bureaucracy.

Tax incentives will only ever be a complement to education and training policy. The sums of money involved are relatively small, but they may prove to be particularly more effective when combined with other policy measures rather than on their own. One problem appears to be that too little attention is given to monitoring and evaluating tax mechanisms to see if they are meeting their objectives.

In short, to be successful, tax incentives need to provide tangible monetary benefits, low levels of bureaucracy and work in tandem with other polices. Tax incentives for education and training have a role to play in getting the balance right between investment in capital and investment in people and in signalling the importance of the latter.

Getting tax policies for education and training right should give Member States plenty to talk about.

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