Tax incentives as a policy instrument for the social economy

General overview and VAT

Thematic discussion paper

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1 Introduction

Supporting the development of the social economy is one of the goals of the European Commission's 2021 Action plan for the social economy.[1] In the 2023 Council Recommendation on the social economy, Member States were recommended to consider various measures to support the social economy.[2] Generally speaking, governments have several instruments to achieve policy goals such as supporting the social economy. Such instruments include:

1. Legislative obligations and prohibitions, for example an obligation to employ a certain percentage of persons with disabilities or a prohibition of discriminatory job requirements;

2. Information campaigns and facilitating/enabling private parties, for example, a governmental campaign to stimulate buying second-hand goods and reducing administrative burdens on charity shops;

3. Fines or levies, for example, a fine on using new plastic or a plastic tax;

4. Subsidies:

    a) Direct subsidies, e.g. direct transfers of funds from the government, for example, subsidies and grants for sheltered workplaces or food banks;
    b) Tax incentives: provisions in tax law such as tax benefits for social enterprises and/or their funders, and reduced value added tax (VAT) rates for second-hand goods.

These instruments are complementary. For a given policy goal, a government may consider either of these instruments or a combination of instruments. Governments experiment with these instruments, which leads to innovations that are sometimes successful and sometimes not. At times, governments also use these instruments to obtain a competitive advantage. If successful, other countries may follow suit. This might lead to a not-always-desirable crowding out of private investments. In an ideal situation, a government would pick the instrument or combination of instruments that suits the goal pursued best at the least costs for society. Making use of experience elsewhere can be helpful in applying and designing the most effective and efficient instrument. The sharing of experiences on tax incentives in this series of workshops[3] is therefore valuable. This sharing will, hopefully, continue even after the workshops have finished.

An instrument, more specifically a tax incentive, cannot be the starting point of the analysis.[4] First, it must be established that there is a problem that must be solved by

1 European Commission (2021), p. 4. Where this thematic discussion paper uses the term 'social economy' it refers to the concept as defined on p. 5 of European Commission (2021): entities sharing the following main common principles and features: the primacy of people as well as social and/or environmental purpose over profit, the reinvestment of most of the profits and surpluses to carry out activities in the interest of members/users ("collective interest") or society at large ("general interest") and democratic and/or participatory governance. This includes cooperatives, mutual benefit societies, associations (including charities), foundations and social enterprises.

2 Council Recommendation of 27 November 2023 on developing social economy framework conditions, C/2023/1344, https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:C_202301344.

3 Which is a follow up on the European Commission's 2021 Action Plan commitment to enable mutual learning among policymakers.

4 See Hemels (2025) for a successful Thai example where first regulation and then tax incentives for the social economy followed existing practice and need. The UK Social Investment Tax Relief (SITR) on the other hand seemed to have

government intervention. The various instruments to solve the problem must then be weighed. Once it is established that a financial intervention is necessary, direct subsidies must be weighed against tax incentives. Only at that stage can it be concluded that a tax incentive is the most effective and most efficient instrument to obtain the policy goal.[5] Direct subsidies are not necessarily better or worse than tax incentives. These instruments may simply serve different policy objects.

Government agencies sometimes prefer a tax incentive over a direct subsidy as tax incentives do not reduce their budget, but 'only' the income of the Ministry of Finance. For a Ministry of Economic Affairs, an ineffective tax incentive for social enterprises might, therefore, be more attractive than a more effective direct subsidy that reduces its budget. For the government as a whole, this is not desirable. Introducing a tax incentive means that the government must either reduce other spending (direct subsidies or tax incentives), increase the tax burden on other taxpayers, or increase government lending, which means shifting the burden to future generations. In that respect, a tax incentive does not differ from a direct subsidy. Tax incentives are not a 'free lunch' but a cost to the government that must be weighed against alternative, possibly more effective and efficient, policy and spending options, including direct subsidies (Grapperhaus 1971).

An important difference between tax incentives and direct subsidies is that where direct subsidies are usually targeted at certain activities or receivers, tax legislation usually applies broadly. Most tax legislation predates the emergence of social enterprises. It does not always cater for the hybridity of social enterprises that both pursue a financial profit and a social benefit (doing business and doing good). Kilian and O'Regan (2019) noted that for that reason taxation can act as a perhaps unintended systematic constraint on social innovation within for-profit businesses. They define this hybridity as the combination of diverse elements. This includes combining goals of profit and social value creation, elements which were traditionally housed in separate and separately taxed entities. In addition, social enterprises blur the lines between the public sector, the private for-profit sector and the charitable sector. Some social enterprises may meet the definition of charity and thus benefit from tax incentives for charities. However, having to operate within the constraints (including prescribed legal forms) of the charitable status may lead to complications and administrative costs that are such, that the social enterprise might refrain from the charitable status and tax benefits, or it may opt for a - from a non-tax point of view - suboptimal solution (Vitello 2011; Martin 2021; Durand et al. 2021). The European Commission (2020) also noted that tax benefits that only apply to certain legal forms may push social enterprises to choose legal forms that are not consistent with their aims.

The European Commission (2020) observed that in most countries the fiscal framework within which social enterprises operate is rather complex and fragmented. Few countries have developed a specific and consistent taxation framework for social enterprises (European Commission 2021). Some European Union (EU) Member States provide for specific benefits for the social economy,[6] but access to these incentives can be complex. The European Commission (2020) distinguished four main tax incentives Member States grant to social enterprises: (1) corporate tax exemptions, (2) VAT exemptions or reduced rates, (3) social insurance costs reduced/covered by subsidies, and (4) tax reductions for private and institutional donors. Annex 1 provides an overview of the four main tax

been engineered the other way around (Hemels 2023). As it turned out not to be tailored to the needs of the social economy, it was abolished within ten years (Hemels 2025).

5 For example, in the Netherlands it is obligatory to apply an assessment framework before a tax incentive may be proposed: Model 4.55 - Toetsingskader fiscale regelingen, https://rbv.rijksfinancien.nl/modellen/2020/overig/4-55.

6 According to the European Commission (2020, p. 92) Austria, Denmark, Estonia, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Poland, Portugal, Romania, Slovakia and Spain.

incentives. From the point of view of whom the legislation defines as the beneficiary of the tax incentive, roughly two types of tax incentives for the social economy can be distinguished: (1) incentives focussed on social enterprises (paper 2 insofar as it focusses on corporate tax exemptions for social enterprises), and (2) incentives focussed on funders of social enterprises (paper 2 insofar as it focusses on financial instruments to fund social enterprises (investments and loans) and paper 3 on donations). This first paper discusses the instrument of tax incentives in general (section 2) and then, in section 3, focusses on the VAT as an instrument to support the social economy.

It must be acknowledged that this paper takes the policy goal, supporting the social economy, as a given and is not about pros and cons of such policy. The paper (and this series of workshops) is purely about one of the instruments to obtain that policy goal, tax incentives. It is important not to confuse the discussion on pros and cons of one of the instruments with criticism on or support for the goal. This paper takes a neutral point of view as regards this goal: the wish to support the social economy is simply regarded as the outcome of a political decision process and taken as a given.

2 The tax incentive concept and use as policy tool

2.1 Definition and designs

The primary function of tax legislation is to raise a budget for government expenditure, but tax legislation can also be used to achieve certain policy goals. The tax incentive concept[7] was developed in recognition of the fact that the tax system can be used to achieve similar goals as public spending programmes (Whitehouse 1999).

DG TAXUD observed that there is no commonly agreed definition of tax incentives in the EU (DG TAXUD 2024). Jurisdictions across the EU employ varying definitions. However, DG TAXUD found some commonalities and general agreement on some elements. DG TAXUD concluded that a tax provision can be called a tax incentive if it is not considered part of the benchmark and meets the following criteria: (1) it reduces the revenue from taxation (this may include delays in revenue collection); (2) it results from a derogation to the general system of taxes; (3) the derogation aims to benefit a specific group of taxpayers identified by certain criteria or behaviours; (4) the provision intends to achieve certain economic or social objectives. The Organisation for Economic Co-operation and Development (OECD) defined tax incentives as provisions of tax law, regulation or practices that reduce or postpone revenue for a comparatively narrow population of taxpayers relative to a benchmark tax (OECD 2010). This definition is also used by some Member States (DG TAXUD 2024) and by DG ECFIN 2024.

Tax incentives can have various designs. Examples are exemptions from the tax base or from the definition of taxable subject, specific income deductions, tax credits and reduced rates. Tax incentives can be found in almost any kind of tax law. They vary widely between countries and may be country specific. Even superficially similar tax incentives, such as corporate income tax exemptions and benefits for philanthropic giving, may still be different in the, legally very relevant, details. This reflects that each country has its own specific tax system which subsequently reflects the preferences of a country at a certain moment of time, for example, regarding the role of the government in a society.

7 For this concept other names are also used, such as tax expenditure, tax concession, tax benefit, tax relief, tax aid, tax break, fiscal incentive, indirect subsidy, fiscal benefit, and tax subsidy, but this paper uses tax incentive.

2.2 Pros and cons of tax incentives

Many tax experts have reservations about tax incentives. Some arguments against these provisions apply to direct subsidies as well, but others are more specific to tax incentives. In a DG ECFIN discussion paper it was observed that while tax incentives can contribute to achieving long-term policy goals, they make the tax system more complex, less transparent, may have adverse distributional impacts, and can result in substantial revenue loss (DG ECFIN 2024). The OECD (2010) stipulated various theoretical and practical allegations against tax incentives in general. OECD (2020) specifically discussed arguments in favour and against tax incentives for philanthropy. Also, non-tax experts have expressed their reservations, especially on the question of whether tax incentives that promote giving are aligned with democratic values. On the other hand, tax incentives may be effective in obtaining certain policy goals. In this section, various drawbacks and benefits of tax incentives are analysed. These include notions on democracy, fairness, efficiency and effectiveness.

2.2.1 Democracy

In the past 10 years or so, tax incentives for philanthropic giving have been criticised as being undemocratic (Vallely 2020). This discussion is also of relevance for tax incentives for the social economy, not only in relation to donations, but, for example, also in relation to investment incentives. The criticism is related to the more general discussion that emerged in the US on so called 'philanthrocapitalism'. Bishop & Green (2008) considered philanthrocapitalism a more efficient and effective alternative to traditional large-scale grant-making philanthropy. In 2013 Bishop explained: 'The determining feature of philanthrocapitalism is not, as its critics suggest, a determination to replace traditional grant-making or the democratic process of civil society with so-called market-based solutions, but rather its laser like focus on achieving 'impact''. (Bishop 2013, p. 477). Nevertheless, the term philanthrocapitalism gained a predominantly negative connotation (Haydon et. al. 2021). Philanthrocapitalism became regarded as a mode of governance, a means of agenda and priority setting and policy creation by the ultra-rich without any form of control, which posed a threat to democracy (Reich 2018). Critics perceived it as being undemocratic that through tax incentives, rich people are steering money - partly government money- in the direction they prefer without – as is it claimed – democratic checks and balances (Vallely 2020, Bosma & Muskens 2019).

However, Haydon et al. (2021, p. 359) argued that the discussion would benefit from greater nuance. Democratic checks and balances apply to what taxpayers qualify for tax incentives. In addition, this US discussion is often transplanted to continental Europe without acknowledging the differences between the US and the EU. For example, in the EU, the government is often a major donor and agenda-setter through direct grants. Also, the critique on having citizens co-deciding on the allocation of a very small part of government expenditures through tax incentives (within the boundaries set by government regulations) seems to imply that the government always knows better and that only the current government should decide what activities are for the public benefit and deserve support. This raises the question of why the government should have a monopoly on what is and what is not for the public benefit. Not only rich philanthropists, but also governments may at times be capricious, untransparent and shortsighted (Dijkgraaf 2019). Philanthropy may bring stability by softening the effects of government policy or the free market. Allowing for philanthropy suits a pluriform society in which there is room for minority opinions. Philanthropy and incentivising giving to and investing in the social economy by tax incentives may support this and thus be suitable, next to, not instead of, direct subsidies in a democratic society. Furthermore, private support can broaden and strengthen both the financial and social base of the social economy. Tax

incentives oblige organisations to consider not only government preferences, but also those of citizens as they are potential donors or investors. This does not mean that all direct subsidies must be replaced by tax incentives. For certain costs or risky activities, it may be difficult to attract private funds. In such cases, direct subsidies could be a more effective instrument. The second and third workshops and papers are dedicated to such tax incentives, which were also included in the 2023 Council Recommendation.[8]

2.2.2 Fairness

When personal income tax incentives are discussed, such as those aimed at social investments or philanthropic giving, the claim is made that such incentives mainly benefit the rich (Vallely 2020). This argument relates both to the design and the use of such tax incentives. If it is designed as a deduction from taxable income in an income tax system with a progressive tax rate (e.g. a tax rate that increases as taxable income increases), such as, for example, the gift deduction in the USA, the UK, Germany, and Japan, someone in a higher tax bracket will benefit more than someone in a lower tax bracket who gave exactly the same amount. Surrey and McDaniel (1985 p. 87) called this the 'upside-down effect' of tax incentives.

However, this upside-down effect can be neutralised in various ways. An example is allowing such deductions against one fixed rate that is not linked to the amount of income. This is the case in the Netherlands, where the deduction of certain items, such as charitable gifts, is only allowed against a fixed personal income tax rate of 37.48% (2025 rate) where the highest income tax rate is 49.5%. Another option is to not provide for an income deduction ('allowance') but a deduction from the tax paid, a tax credit. In such cases, a percentage of the gift can usually be deducted from the tax due, as is the case, for example, in France and Canada. In this system, the benefit from the same amount of charitable giving is the same for a high-income and a low-income earner. A third option is the system of tax assignment that is applied in several countries, including Italy, Hungary, Lithuania, Poland, Romania and Slovakia (Nährlich 2013, p. 26). In such a system, taxpayers may assign a percentage of the tax due to (usually specific) organisations. These solutions may all solve the upside-down effect, not only for charitable giving, but also for other tax incentives in progressive taxes such as the personal income tax.

The use of tax incentives also requires further thought on their fairness. Many tax incentives, including those for the social economy, are used by higher income groups, simply because they have more 'free' income that they do not need for their daily needs. For example, higher income groups often benefit more from reduced VAT rates, as they consume more, both in volume and price (Thomas 2024). De la Feria and Swistak (2024) note that various studies have shown that consumption, even of essential items, is overwhelmingly associated with the highest income households. This also means that reduced VAT rates are a very inefficient way of supporting low-income groups.

Other examples are tax incentives to stimulate insulation of houses and buying electric cars. Lower income groups often rent their house, and therefore cannot benefit from tax incentives targeted at house owners (usually higher income groups), while, at the same time, they are hit hard by the increase of energy prices ('energy poverty') (Frank, 2024). Furthermore, they usually own a lower amount of energy consuming appliances (Jacobsen 2019). Similarly, as electric cars are still relatively expensive and there is not yet a large second-hand market for such cars, higher income groups are usually the

[8] Council Recommendation of 27 November 2023 on developing social economy framework conditions, C/2023/1344, recommendation 19 on taxation, https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:C_202301344.

beneficiaries of tax incentives for electric cars (Guo & Kontou 2021). Similarly, higher income groups will benefit more from tax incentives for investors in the social economy, simply because they have the spare funds to invest and lower income groups have not. This does not mean that this income effect precludes the use of such tax incentives, but in the weighing of pros and cons of such tax incentives, these considerations of fairness must be taken into account.

This is even more important as decisions on tax incentives are often highly political and influenced by lobby groups. This is especially the case when the beneficiaries each have a high benefit and are a small, well-organised group with good access to policy makers. As the costs of the tax incentive are spread out over a large group of anonymous taxpayers, they are usually unaware that they bear the cost of this privilege for a small group and do not protest it. Policy makers must also consider the interests of this silent majority.

2.2.3 Efficiency and effectiveness

An important condition for tax incentives to be effective is that they target price elastic activities. Price elastic activities are economic activities or consumer behaviours that are highly sensitive to changes in price. This means that a reduction in price because of the tax incentive changes the behaviour of taxpayers. For example, from research in various countries it has become clear that philanthropic giving is, to a certain extent, price elastic (Adena 2021). This means that tax incentives that make philanthropic giving cheaper may have a stimulating effect on gifts. On the other hand, there is an abundance of empirical evidence that a reduction in a VAT rate will not be (fully) passed on to consumers (De la Feria and Swistak 2024). This is caused by relative price-inelasticity of consumers. In an interview, European Commissioner Hoekstra said that tax specialists' warnings are fair that VAT reductions will not benefit consumers because companies will absorb the extra profits (Lamer & Petitjean 2024). However, it is not always easy to measure price (in)elasticity, especially beforehand when the policy is being made.

The better targeted (and thus more equitable) a tax incentive is, the more complicated it will be, both for the tax administration to execute and for taxpayers to make use of it. A detailed and targeted tax incentive will, for example, require proof from taxpayers that they meet all requirements to be in the target group, which proof must be checked by the tax administration. On the other hand, simple incentives that are easy to execute will usually have a broad scope and are difficult to target at specific groups. This reduces the efficiency of these tax incentives. It is often much easier to target a direct subsidy to certain products, producers or consumers. Providing discount cards or vouchers to low-income consumers and government-subsidised school fruit, may, for example be more effective and efficient than a general reduction in the VAT rate for fruit and vegetables.

Furthermore, it is more difficult to allocate a maximum budget to ('cap') a tax incentive than to allocate a specific amount of funds to a direct subsidy. Usually, tax incentives are 'open ended', which means that anyone who qualifies for the tax incentive, may make use of it until it is abolished. Therefore, it is difficult to predict the costs of a tax incentive before the policy is introduced.

Usually, the estimation of the costs of a tax incentive is based on the amount by which tax revenue is reduced because of the introduction of a tax incentive. Often it is assumed that the behaviour of taxpayers and revenue from other taxes will be unchanged. This is understandable, as it is difficult to estimate and include behavioural change as a variable in the calculation, but it also makes the estimation less realistic (Kraan 2004). Not only will taxpayers often change their behaviour in reaction to a tax incentive, usually such

change is the intention of the tax incentive. Without a behavioural change, the incentive would not be effective and, by default, not be efficient either.

These less than perfect estimations of costs and effects upon introduction of an incentive make it important for tax incentives to be accounted for and evaluated properly to establish whether the policy reached its goal (was effective) at the lowest costs (was efficient). In general, tax incentives have the drawback that there is less information and less democratic control on these expenditures compared to direct subsidies. Usually, direct subsidies are accounted for in the annual government budget which has to be adopted by parliament. Tax incentives are usually only implicitly reflected in the budget in the estimated amount of tax income, but they are not explicitly nor specifically accounted for as an expenditure. This makes it difficult to weigh direct expenditures against tax incentives. It also means less budgetary control on tax incentives and complicates control of the lawfulness and effectiveness of expenditures.

To get a better grip on tax incentives, since the 1960s several countries started to account for these incentives in tax expenditure reports. The content and the status of these reports vary widely.[9] In many countries, the parliament does not have to vote on these overviews or discuss these in connection with the direct expenditure budget. Directive 2024/1265 requires EU Member States to publish detailed information on the impact of tax incentives on revenues.[10] In a December 2024 working document, DG TAXUD observed that the practice of tax expenditure reporting is very heterogenous across the EU. Tax expenditure reports provide different levels of detail, refer to different periods, and employ varying definitions and benchmarks (DG TAXUD 2024). Tax incentives are often still not accounted and budgeted for in the same way as direct subsidies.

This relative invisibility of tax incentives makes it even more important to evaluate their effectiveness and efficiency on a regular basis. According to DC ECFIN (2024) regular reporting, monitoring and assessment of tax expenditures is crucial as it allows Member States to review and revise their tax policies. In addition, some countries, especially the US, use so called sunset-legislation when introducing a tax incentive. Sunset-legislation automatically expires after a certain period (for example, five years) unless it is explicitly renewed or extended. This is the reverse of the practice in which tax incentives exist indefinitely unless explicitly abolished.

A regular evaluation of tax incentives or sunset legislation are not a guarantee that ineffective or inefficient tax incentives are abolished. The beneficiaries of a tax incentive will try everything they can to keep a tax incentive. In addition, there is a bias towards the status quo (and hence against efficiency-enhancing reforms) whenever some of the individual gainers and losers from reform cannot be identified beforehand (Fernandes & Rodrik 1991). Introducing a tax incentive is, therefore, much easier than abolishing it. This must also be considered when contemplating the introduction of a tax incentive.

2.3 EU law

EU Member States must consider EU law when designing and implementing tax incentives for the social economy. In this respect there is no difference with direct subsidies. Member States must respect the fundamental freedoms enshrined in the Treaty on the Functioning of the EU (TFEU): the free movement of citizens, goods,

9 A useful overview is provided by the Global Tax Expenditures Database https://gted.taxexpenditures.org/.

10 Council Directive (EU) 2024/1265 of 29 April 2024 amending Directive 2011/85/EU on requirements for budgetary frameworks of the Member States.

workers, services, capital and the freedom of establishment (articles 18, 45, 49, 56 and 63 TFEU). The purpose of these freedoms is the creation of an internal market, a market without internal borders or import and export restrictions.

Furthermore, support may not infringe state aid rules (articles 107-109 TFEU).[11] Granting aid through state resources which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods is prohibited. Several forms of state aid are allowed. This includes aid not exceeding EUR 300 000 over any period of three fiscal years per undertaking (de minimis aid). This helps when incentives are specifically aimed at small-scale sectors of the social economy.

Based on article 107(2)(a) TFEU aid having a social character and granted to individual consumers, is compatible with the internal market provided that such aid is granted without discrimination related to the origin of the products concerned. In addition, article 107(3) includes various forms of aid that may be considered to be compatible with the internal market, such as (a) aid to promote the economic development of areas where the standard of living is abnormally low or where there is serious underemployment, and of certain regions, in view of their structural, economic and social situation; (c[12]) aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest; (d) aid to promote culture and heritage conservation where such aid does not affect trading conditions and competition in the EU to an extent that is contrary to the common interest; and (e) such other categories of aid as may be specified by the decision of the Council on a proposal from the Commission. Notification to and approval of the European Commission is necessary before Member States can introduce such aid.

The General Block Exemption Regulation (GBER)[13] provides that if certain requirements are met, several categories of aid with an incentive effect are exempt from the notification obligation. This includes various form of aid that may be of relevance for tax incentives to support the social economy, such as regional aid; aid to small and medium enterprises (SMEs) in the form of investment aid, operating aid and SMEs' access to finance; aid for environmental protection; aid for research and development and innovation; training aid; recruitment and employment aid for disadvantaged workers and workers with disabilities; social aid for transport for residents of remote regions; aid for culture and heritage conservation; aid for sport and multifunctional recreational infrastructure; aid for local infrastructures. In preamble 21 of the 2023 Council Recommendation on the social economy, it was observed that public authorities often do not make the most of the current scope of the State aid rules to support the social economy, limiting themselves to measures under the general de minimis threshold and not using the option to establish measures under the GBER such as regional aid, risk-finance aid, and aid to recruit disadvantaged workers.[14]

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[11] See for an extensive discussion on the social economy and State aid rules https://social-economy-gateway.ec.europa.eu/topics-focus/state-aid-social-economy_en.

[12] The letters correspond with those in article 107(3) TFEU.

13 Commission Regulation (EU) No 651/2014 of 17 June 2014 declaring certain categories of aid compatible with the internal market in application of Articles 107 and 108 of the Treaty, see for the consolidated version as of 1 July 2023: http://data.europa.eu/eli/reg/2014/651.

[14] Council Recommendation of 27 November 2023 on developing social economy framework conditions, C/2023/1344, https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:C_202301344.

3 VAT incentives and the social economy

In the EU, the VAT Directive has harmonised VAT to a relatively high degree.[15] The starting point for VAT is not the legal form of the entity, but the transaction. For the VAT to apply there must be a supply of goods or services for a consideration. A social enterprise that only provides services free of charge, for example free advice or counselling, or that only receives voluntary donations, does not fall within the scope of VAT.

The VAT Directive defines 'a taxable person' as any person (which includes legal entities) who, independently, carries out in any place any economic activity, whatever the purpose or results of that activity.[16] The term 'economic activity' has a wide scope. It is not relevant that activities are not for profit or pursue a social purpose. Social enterprises that supply goods or services for a consideration will, therefore, in general be considered as taxable persons for VAT.

In general, two tax incentives for the social economy may be distinguished in the VAT: exemptions and reduced rates. An overview of VAT incentives for the social economy in the Member States was provided in Appendix 6 of European Commission 2020 and is copied in Annex 2 of this paper. It seems that different Member States interpreted the question on VAT exemptions and reduced rates for the social economy differently, which implies that this overview must be handled with care.

Unlike what is the case in other taxes, a VAT exemption or being out of scope of VAT might not always be beneficial. In these cases, it would be more correct to speak of a tax *dis*incentive for the social economy. Solutions to solve this problem are also discussed below.

3.1 VAT exemptions

Being a taxable person does not necessarily mean that VAT must be charged on (all) transactions. The VAT Directive obliges Member States to apply exemptions for certain activities in the public interest.[17] These include hospital and medical care; supply of human organs, blood and milk; the supply of services and of goods closely linked to welfare and social security work and to the protection of children and young persons; education; supplies by non-profit-making organisations with aims of a political, trade-union, religious, patriotic, philosophical, philanthropic or civic nature to their members in their common interest in return for a subscription, provided that this exemption is not likely to cause distortion of competition; the supply of certain services closely linked to sport or physical education by non-profit-making organisations to persons taking part in sport or physical education; the supply of certain cultural services, and the supply of goods closely linked thereto.[18]

For several exemptions, conditions may apply such as a prohibition of systematically aiming to make a profit and to distribute any profit that nevertheless arises; management by volunteers; approved prices or prices that are lower than commercial prices; and the

15 Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax as later amended. See for the consolidated version as of 1 January 2025 https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02006L0112-20250101

16 Article 9 VAT Directive.

17 Chapter 2 of Title IX of the VAT Directive (article 132-134).

18 Article 132 VAT Directive.

exemptions not being likely to cause distortion of competition to the disadvantage of commercial enterprises subject to VAT.[19]

In addition, an exemption may be applied for persons with an annual taxable (e.g. non-exempt or outside of VAT) turnover not exceeding a given threshold, so called small enterprises.[20] This threshold varies between countries. As of 1 January 2025, the threshold may not be higher than EUR 85 000. Member States may exempt such small enterprises from certain administrative obligations. Social enterprises that have a turnover below the threshold can, therefore, benefit from this exemption.

3.2 The problem of irrecoverable input VAT

VAT is a consumption tax on nearly all goods and services bought and sold in and into the European Union. Taxable persons for VAT purposes must charge the VAT to their customers as a percentage of their sales prices and pay the VAT to the tax administration. Insofar as those customers are taxable persons themselves and use the goods and services for VAT taxable transactions, they are entitled to deduct the VAT in respect of supplies to them by another taxable person (the so-called input VAT) from the VAT they received from their customers and which they have to pay to the tax administration.[21] Because of this possibility for those taxable persons to reclaim input VAT, VAT is not a cost to them. The result is that VAT is borne by the final consumer who cannot deduct or reclaim the input VAT. This suits the goal of VAT of being a consumption tax. Social enterprises that are in scope of the VAT may thus be able to recover input VAT insofar as no exemption applies on their supplies.

Social enterprises that are not a taxable person, are out of scope of the VAT. They are treated as a final consumer. The VAT they pay on the goods and services they buy, is, therefore, a cost for them. The same applies to social enterprises with exempt activities or that apply the exemption for small enterprises: they can also not reclaim the input VAT related to those exempt activities. For social enterprises with relatively little input VAT charged to them, this disadvantage will probably not outweigh the advantage of not having to comply with administrative VAT requirements. For social enterprises that incur large costs for supplies and services (including investments in real estate and equipment), being able to deduct input VAT may be of great relevance. In such cases, providing exempt services or supplies or making use of the exemption for small enterprises is detrimental.

The European Charities' Committee on Value-Added Tax (ECCVAT) estimated that EU charities lose about EUR 6 billion a year in irrecoverable VAT.[22] For the UK, it was calculated that irrecoverable VAT costs charities GBP 1.8 billion a year (London Economics 2020). It was assumed that significant amounts of the output VAT are absorbed by charities rather than being charged to their ‘customers’ and therefore burden the charity sector. The same problem arises for the broader group of social enterprises to which an exemption applies or that are out of scope.

The problem of irrecoverable input VAT might induce social enterprises to ask for a fee even if they would prefer to supply their goods or services for free. VAT thus negatively affects economic decisions of social enterprises. The OECD (2020) concluded that distortions typically arise from the exemption of philanthropic entities’ output from VAT

19 Article 133 VAT Directive.

20 Article 280a-292d VAT Directive.

21 Article 168 VAT Directive.

22 https://www.eccvat.org/resources/.

and that this may result in a competitive advantage or disadvantage. All in all, the exemptions in certain cases have had the effect of distorting economic decisions and competition, thereby creating economic inefficiencies and a deadweight loss (Cnossen 2003, De la Feria 2009). VAT exemptions may, therefore, not necessarily support the social economy.

3.3 Reduced VAT rates

Member States must apply a VAT rate of at least 15% (article 97 VAT Directive). However, Member States are allowed to apply two reduced rates of at least 5% to a maximum of 24 points of the list of the supply of goods and services listed in Annex III to the VAT Directive (article 98(1)). This includes supply and construction of housing, as part of a social policy, as defined by the Member States (point 10) and construction and renovation of public and other buildings used for activities in the public interest (point 10a). A reduced VAT rate does not restrict the deduction of input VAT.

Such reduced rates may benefit social enterprises. In Sweden, for example, a reduced VAT rate is applied on certain repairs to stimulate the reuse of goods.[23] This was part of the Swedish government's strategy for sustainable consumption. A reduced rate does not apply specifically to social enterprises as every taxable person that delivers such services benefit from it. An exception is Italy, where a 5% VAT rate is applied for certain social cooperatives (European Commission 2020, p. 94).

A reduced rate is not a solution for activities that are exempt from VAT. Furthermore, even if the obligatory exemptions for certain activities in the public interest would be replaced by the possibility to apply a reduced rate, the objective of cost reduction would not be achieved in full. The reduced rate increases the costs of these supplies, especially for organisations that do not suffer much from being unable to deduct VAT. Furthermore, even (super) reduced rates do not solve the problem for organisations that are out of scope, for example because their supplies are for free. They would be in a worse position compared to in-scope charities. An example is a nature reserve that does not charge entry fees. For such organisations the input VAT is an additional burden. A nature reserve that charges entrance fees would not have this burden. Organisations would therefore have an incentive to charge fees even though the object of the exemption (and probably the domestic policy) is to reduce the costs of their activities, not to increase them.

3.4 Zero rate and exemptions with deduction of input VAT

Based on article 98(2) of the VAT Directive, Member States may apply a reduced rate lower than 5% (this includes a rate of 0%) and an exemption with deductibility of input VAT to a maximum of seven points from the list in Annex III. This may only be applied to points 1-5 (food, water, pharmaceutical products, medical equipment, passenger transport), 6 (supply, including on loan by libraries, of books (…), newspapers and periodicals and the production of publications of non-profit-making organisations and services related to such production) and point 10c (solar panels). Both a reduced rate of 0% and an exemption with deductibility of input VAT do not have the drawback of the normal reduced rates leading to an increase of the price of the goods or services provided. However, most parts of the social economy do not provide goods and services for which this incentive may be applied. Furthermore, it is not a solution for parts of the social economy that are out of scope of VAT. The input VAT will remain a burden for

23 Article 9(7) Mervärdesskattelag (2023:200).

them. Finally, this may be a costly solution for the public purse as the right of reimbursement of input VAT applies to anyone supplying the relevant goods or services. This might be a much larger group than the targeted social economy actors.

3.5 Other drawbacks of VAT incentives

Exemptions and reduced VAT rates are not the most efficient way to stimulate certain economic activities. The VAT Expert Group (VEG) (2024) observed that the complexity of the EU VAT system, resulting in distortions of competition, high compliance costs and not insignificant legal uncertainty, arise to a high extent in relation to VAT exempt transactions. In the VEGs view, the exemption conditions are increasing inequality and affecting the level playing field, cost effectiveness and/or innovation in these sectors. For the exemptions for activities in the public interest, the VEG recommends a broad reflection to update and improve these regimes.

In addition, various economic studies conclude that the case for reduced VAT rates is weak. For example, Thomas (2024) found reduced VAT rates to be a poorly targeted means of supporting lower income households, particularly when compared to targeted cash transfer programmes. Similarly, he concluded that reduced VAT rates are unlikely to be a well-targeted way to encourage consumption of merit goods, while they also create significant administrative complexity. Where countries have the administrative capacity to implement effectively targeted cash transfer programmes, he urged them to use these programmes instead of reduced VAT rates.

The VEG (2024) proposes a gradual reduction in the number of VAT rates within the EU, potentially converging toward a single rate per Member State, complemented by a zero rate for essential goods and services. The VEG doubts whether the VAT system, including VAT measures that support circular economy models, such as second-hand goods schemes and eco-friendly construction practices, is the most effective way to achieve sustainability and green policy goals, while such measures likely create exceptions to main rules making the VAT system more complex.

The VEG is also of the view that the VAT system must be sustainable and that as a starting point any disincentives of the current VAT system in areas such as donations, destruction, second-hand goods, etc. should be removed. This relates to the issue that, to prevent fraud with input VAT, VAT is due on the market value of businesses' donations of unsold or returned goods,[24] but not on their destruction. Article 146 of the VAT Directive obliges Member States to exempt the supply of goods to approved bodies which export them out of the EU as part of their humanitarian, charitable or teaching activities outside the EU. However, this exemption means that the donating companies are confronted with irrecoverable input VAT. Companies and charities claim that VAT is the reason that goods are destroyed instead of being donated to charity (Hosford 2023, Caragher 2024). However, there are doubts as to whether a 0% rate (which allows for recovery of input VAT) on donated goods would lead to a significant reduction in the destruction of overstock and returns, as goods are often destroyed to protect brand value and ensure stable prices by reducing availability. This would mean that a change in VAT, which only accounts for a small portion of the cost of donations, would not make a difference as destruction of unsold or returned goods would still be cheaper (Petitjean 2025). This seems an example of starting with the tax incentive after pressure of lobby groups instead of with an analysis of the problem. The first question is whether

24 Article 16 VAT Directive. If the market value is 0 (such as may be the case with food that is near to or past its best before date), this is not a problem (see for example the guidance of the Swedish tax administration in this respect at https://www4.skatteverket.se/rattsligvagledning/edition/2024.7/411274.html under the heading Livsmedelsdonationer för att undvika matsvinn.

companies cannot solve the problem of waste themselves, for example by producing less or by charging more for returns. If it is established that the market will not solve the problem, for example because the costs of the negative externalities of overproduction are not reflected in the market price, more effective and efficient solutions to this problem than a change in the VAT rate seem available, such as a levy on returns and/or destruction to internalise the societal costs of overproduction in the price of products.

The OECD (2020 p. 32, 65) observed that VAT exemptions, reduced rates, and zero rates can create unfair competition, especially if the incentive only applies to philanthropic organisations and the VAT exempt goods or services supplied by a philanthropic entity are also provided by businesses that charge VAT on their sales. Such businesses might include social enterprises that do not meet the non-profit requirement. According to the OECD, unfair competition is the reason why some countries, including Canada and Ireland, do not exempt from VAT certain goods and services provided by philanthropic entities. Belgium, Chile, Colombia, Estonia, Indonesia, Italy, and the Slovak Republic do not have preferential VAT treatment for philanthropic entities and apply the standard VAT rules (OECD 2020).

3.6 Alternatives outside of VAT

The problem of not being able to deduct input VAT is difficult to solve within the framework of VAT. More effective and efficient solutions can be found outside the VAT system, by granting direct subsidies. Obviously, direct subsidies also have budgetary and competition implications, but these implications are less significant than those associated with solutions within the VAT system. Governments can better target direct subsidies than VAT incentives, leading to fewer spill-over effects and fairer outcomes. For example, commercial organisations may be excluded from direct subsidies under domestic law and requirements may be imposed regarding the legal form. Strict, qualitative criteria can be established to decide whether an entity or person qualifies for a direct subsidy or not.

The European Commission (2011) specifically mentioned that Member States can introduce targeted compensation mechanisms outside the VAT system to alleviate the cost of VAT on acquisitions of non-profit-making organisations. The Commission called on Member States to make use of the existing options to alleviate the burden of VAT on non-profit making organisations. De la Feria and Swistak (2024) call this, in more general terms, the ‘modern approach’, pioneered by New Zealand. It is regarded as technically superior as it avoids the significant limitations of the traditional approach of trying to solve societal problems by including exemptions and reduced rates in VAT. There is no reason why this would be different for supporting the social economy.

Several countries have already applied this solution. For example, when public museums and galleries in the UK could no longer charge an entrance fee for their permanent collections, they could no longer (fully) recover VAT. To compensate museums for this disadvantage, the UK introduced a special VAT refund scheme for museums and galleries that meet strict criteria and are listed in the VAT (Refund of Tax to Museums and Galleries) Order 2001 (SI 2001/2879).[25] Eligible museums can reclaim VAT incurred in relation to free rights of admission. In addition, in 2015 the UK introduced a VAT Refund Scheme for charities.[26] This only applies to charities that are defined as a qualifying charity in section 33D of the VAT Act 1994. These are palliative care charities,

25 Article 33A VAT Act 1994 and VAT Notice 998, VAT refund scheme for museums and galleries, https://www.gov.uk/guidance/vat-refund-scheme-for-museums-and-galleries-notice-998.

26 Article 33C and 33D VAT Act 1994 and VAT Refund Scheme for charities (VAT Notice 1001), https://www.gov.uk/guidance/vat-refund-scheme-for-charities-notice-1001.

air ambulance charities, search and rescue charities and medical courier charities. In addition, these charities must meet the charity definition included in Schedule 6 to the Finance Act 2010. These refund schemes do not form part of the general VAT system, but certain rules in UK VAT legislation apply to it.

In Ireland, a VAT compensation scheme for charities applies as well.[27] It aims to reduce the VAT burden on charities and to partially compensate for VAT paid by the charity. Charities are entitled to claim a refund of a proportion of their eligible VAT costs, based on their level of non-public funding. Charities can submit one claim per year, which should relate to VAT paid in the previous year only. The fund for the scheme is capped at EUR 10 million annually. If the total amount of claims exceeds the capped amount, refunds are paid on a pro-rata basis. To qualify for the scheme, a charity must be registered with the Charities Regulatory Authority and the Irish tax administration and hold a charitable tax exemption.

In 2005, European Commissioner Kovács stated that the essential difference between VAT refund schemes and VAT incentives is that, under a refund scheme, the tax is collected in the first place and then the government chooses to allocate it back to certain organisations from which it has been collected. He called this a subtle but important accounting distinction. The decision to set up such a refund mechanism is strictly a national budgetary issue over which the Commission has no say or influence (Kovács 2005, p. 3-4).

As long as Member States remain within the boundaries of EU law, direct subsidies thus offer various ways to mitigate negative effects of VAT exemptions in a more effective and efficient way to support the social economy than would be possible through a solution within the VAT system (in the same way Thomas 2024).

4 Conclusion

Tax incentives are one of the instruments in the government toolbox to support the social economy. It is important for Member States to share their experiences with this tool, the challenges they encounter and the conditions that turn out to be important for tax incentives to be successful or less successful. This series of workshops is therefore very relevant. This is even more so as it brings together civil servants from various ministries that have a role in the design, implementation, and evaluation of tax incentives for the social economy, including from ministries of finance or taxation, of social or labour policy and of economic affairs. Having this dialogue not only across national borders, but also across ministries help to get a better understanding of the instrument (usually the expertise of the Ministry of Finance or Taxation) and the social economy goals pursued (the expertise of other ministries such as Ministries of Social Policy, Labour Policy and Economic Affairs). Also within a Member State it is important to have this open dialogue and knowledge sharing between ministries when contemplating the use of a tax incentive. For some policy goals, other instruments may be more effective and efficient. Also, not all taxes are equally suitable to obtain certain policy goals. VAT incentives, for example, are often problematic because of doubts in general on the fairness, effectiveness and efficiency of this instrument. Introducing such incentives to support the social economy requires, therefore, a strong case and scrutinous weighing of the pros and cons against alternative policy instruments such as VAT compensation mechanisms outside the VAT legislation for which several examples of current use are available.

27 https://www.revenue.ie/en/companies-and-charities/charities-and-sports-bodies/vat-compensation-scheme/vat-compensation-scheme-for-charities/index.aspx.

In parallel with the discussion on the equitable, effective and efficient use of tax incentives to support the social economy, existing disincentives in tax legislation in relation to the social economy also require attention. The first recommendation as regards taxation in the 2023 Council Recommendation on the social economy was to ensure that taxation systems do not hinder the development of the social economy.[28] Current tax incentives in the personal income tax and corporate income tax may not always be adapted to the hybrid characteristics of actors in the social economy.[29] These issues will, amongst others, be discussed in the next two papers and workshops.

[28] Council Recommendation of 27 November 2023 on developing social economy framework conditions, C/2023/1344, recommendation 19(a) on taxation, https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:C_202301344.

[29] See also Council Recommendation 19(b), (c) and (d).

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Annex 1 Main tax incentives granted to social enterprises in EU Member States

Type of fiscal benefits	Yes, without limitations	Yes, with limitations	Not available
Corporate tax exemption on retained profits	AT, DE, EL, FR, HU, IE, IT, LU, LV, MT, PL	BE, BG, CZ, ES, HR, LT, NL, PL, RO, SE, SI, SK, UK	CY, DK, EE, FI
VAT exemption or reduced rate	AT, BE, DE, FR, HU, IT, PL, PT	LU, SK	BG, CY, CZ, DK, EE, EL, ES, FI, HR, IE, LT, LV, MT, NL, RO, SE, SI, UK
Social insurance costs reduced or covered by subsidies	AT, BE, HR, SE	BG, EL, ES, FI, FR, IE, IT, LV, PL, PT, SI, SK	CY, CZ, DE, DK, EE, HU, LT, LU, MT, NL, RO, UK
Tax reductions granted to private and/or institutional donors	-	AT, BE, BG, CZ, DE, EE, ES, FR, HR, HU, IE, IT, LT, LU, LV, NL, PL, PT, SI, UK	CY, DK, EL, FI, MT, RO, SE, SK

Source: European Commission (2020) Social enterprises and their ecosystems in Europe. Comparative synthesis report. Authors: Carlo Borzaga, Giulia Galera, Barbara Franchini, Stefania Chiomento, Rocío Nogales and Chiara Carini. Luxembourg: Publications Office of the European Union. https://op.europa.eu/en/publication-detail/-/publication/4985a489-73ed-11ea-a07e-01aa75ed71a1/language-en, table 13, p. 93.

Annex 2 Exemption or reduced VAT rate granted to social enterprises in EU Member States

Country	Exemption or reduced VAT rate
AT	Yes
BE	Under certain conditions, work integration social enterprises (WISEs) benefit from a reduced VAT rate
BG	The Act on VAT allows conventional enterprises and Social enterprise (SEs) to benefit from VAT exemption on certain goods and services.
CZ	-
DE	Organisations and SEs with the public-benefit status can use a reduced VAT rate of 7%, instead of the normal rate of 19%.
EE	-
EL	No different VAT rate is foreseen for any SEs.
ES	-
FI	The VAT Act includes important areas for most SEs that are not subject to taxation at all.
FR	> Collective interest cooperative societies (SCICs)' VAT rate depends on the activity carried out. >Sporting and cultural associations can be exempt from VAT on services provided to their members. >Foundations are not subject to VAT for activities directly related to their purpose.
HR	All entities performing economic activities are exempted from the VAT if their annual revenue is does not exceed around 40,000 EUR.
HU	Civil society organisations, social cooperatives, non-profit companies and public benefit organisations receive exemption from paying VAT for some activities.
IE	-

IT	A-Type social cooperatives enjoy a favourable (5%) VAT rate.
LT	No VAT is paid on revenues resulting from the provision of public benefit services.
LU	Law does not contain provisions with regard to the treatment applicable to the Societal impact company (SIS).
LV	VAT is not paid (i) if social care, professional and social rehabilitation, social assistance and social work services are provided, and (ii) if an annual turnover from economic activity is less than EUR 40,000.
MT	-
NL	-
PL	Professional activity establishments (ZAZs) and entrepreneurial non-profit organisations (ENPOs) are VAT exempt under certain conditions.
PT	Non-profit organisations (NPOs) are exempt from VAT on sales from the provision of services and directly related exchanges in social services activities.
RO	-
SE	SEs register for VAT on the same terms as other businesses.
SI	Exemption from VAT for activities in the public interest and if taxable income does not exceed 50,000 EUR per year.
SK	> VAT applies only in cases of SEs whose yearly taxable income is >50,000 EUR. > SEs with higher income registered according to the Act on Social Economy and Social Enterprises and those that are socialising 100% of their possible profit may apply for the lowered VAT rate.
UK	-

Cyprus (CY) and Denmark (DK) were not included in the table because the country reports did not provide information on this topic

Source: European Commission (2020). Social enterprises and their ecosystems in Europe. Comparative synthesis report. Authors: Carlo Borzaga, Giulia Galera, Barbara Franchini, Stefania Chiomento, Rocío Nogales and Chiara Carini. Luxembourg: Publications Office of the European Union. https://op.europa.eu/en/publication-detail/-/publication/4985a489-73ed-11ea-a07e-01aa75ed71a1/language-en, p 177-182.

Annex 3 Glossary

Charitable status

A status granted to not-for-profit organisations that are established for an exclusively charitable purpose. The 'purpose' is what the organisation was set up to achieve and must be for public benefit. The legal definition of a charity and 'charitable purpose' is often defined in national legislation.

Grant

A sum of money awarded *una tantum* that is provided for free by a governmental agency or private organisation. Most grants are provided with a view to funding a specific project and require some level of compliance and reporting.

Legal form

The form under which an organisation is incorporated. The legal form determines how aspects like property rights, liability, governance and control, reporting, profit distribution and funding will affect the organisation.

Market

Any exchange that results from a contractual agreement. A market is created whenever potential sellers of goods and services enter into contact with potential buyers and there is a possibility of exchange through a contractual agreement.

Non-profit and Not-for-profit

The most well-known definition is provided by Johns Hopkins University. According to this definition, the sector includes organisations that are: voluntary; formal; private; self-governing; and do not distribute profits. The term "non-profit" refers to organisations that have to comply with a non-distribution constraint. The term "not-for-profit" is more general and refers to the goal pursued (which is other than profit). Non-profit organisation: an organisation that has a legal form which does not permit the distribution of profit and which is able to trade freely in furtherance of a social purpose. Examples include most foundations, associations and non-profit companies.

Profit

The residual return to the entrepreneur, i.e., the difference between total sales revenue and total costs incurred by the enterprise.

Progressive tax rate

A tax rate that increases or progresses as taxable income increases.

Reduced VAT rate

Various types of VAT rates can be applied that depend on the product or service involved in the transaction. Reduced VAT rates refer to special rates which were set according to

standardised VAT rates. In the EU, one or two reduced rates may be applied to supply of specific goods and services based on the VAT Directive.

Social economy

Entities sharing the following main common principles and features: the primacy of people as well as social and/or environmental purpose over profit, the reinvestment of most of the profits and surpluses to carry out activities in the interest of members/users ("collective interest") or society at large ("general interest") and democratic and/or participatory governance. This includes cooperatives, mutual benefit societies, associations (including charities), foundations and social enterprises.

Social enterprise

Social enterprises are now generally understood as part of the social economy. Social enterprises operate by providing goods and services for the market in an entrepreneurial and often innovative fashion, having social and/or environmental objectives as the reason for their commercial activity. Profits are mainly reinvested with a view to achieving their societal objective. Their method of organisation and ownership also follow democratic or participatory principles or focus on social progress. Social enterprises adopt a variety of legal forms depending on the national context. Terms such as "social economy enterprises", "social and solidarity enterprises" and "third sector" are also used by some stakeholders, countries and international organisations to refer to social economy entities. Work integration social enterprises are a common type of social enterprise across Europe. They specialise in providing work opportunities for disadvantaged people.

Social insurance

Protection of the individual against economic hazards (such as unemployment, old age, or disability) in which the government participates or enforces the participation of employers and affected individuals.

Social investment

The term refers to all the targeted actions aiming to develop an economic environment that enables social enterprises to access finance. Social investment includes financial instruments (i.e., grants, loans, equity and hybrid instruments) that together with other types of support aim to maximise social impact. Traditionally, it involves several actors including supply-side (investors), demand-side (social enterprises), intermediaries and business development support organisations. The term is sometimes used more narrowly in reference to the provision of repayable finance with the aim of generating social impact, alongside an expectation of some financial return (or preservation of capital). More recently, social investment is sometimes used interchangeably with "impact investment" or "impact finance". The latter terms usually involve investors who seek a blended return based on several criteria (financial, social and environmental) and who tend to focus on financing scaling-up and replication of social enterprises. As for the use within the EC, it usually refers to policies designed to strengthen people's skills and capacities and support them to participate fully in employment and social life. In more recent years, the European Commission has also been using this term to refer to the provision of repayable finance to social enterprises.

Subsidy

A sum of money granted by the state or a public body to help an industry or business keep the price of a commodity or service low.

Tax exemption

A specific category of income, organisation or activity that is not subject to taxation by the government.

Tax incentive

A reduction made by the government in the amount of tax that a particular type of organisation or group of people has to pay or change in the tax system. They are usually intended by public authorities to encourage particular types of behaviour and/or to favour specific groups.

Tax deduction

An amount deducted from taxable income that lowers the amount of taxes an organisation or group of people owes the government.

Value Added Tax (VAT)

A general tax that applies in principle to all commercial activities involving the production and distribution of goods and the provision of services. It is a consumption tax because it is borne ultimately by the final consumer and is therefore not a charge on business.

VAT exemption

Some supplies of goods and services are exempt from VAT, and most of these are examples of ‘exemptions without the right to deduct’. The right to deduct refers to a taxable person’s right to claim the input VAT they paid on goods and services from tax authorities. VAT is deducted by subtracting the deductible amount from the VAT payable in the regular VAT return submitted to the tax authorities. There are two categories of exemptions without the right to deduct: exemptions for activities carried out in the public interest and exemptions for other activities.

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