France and Tourism VAT

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In 1967, France was one of the first countries to introduce a reduced rate of VAT for hotels. From 1967 until 1981 French hotels were subject to a reduced VAT rate of 7%. In the early 1980s, the reduced rate was withdrawn for four-star and four-star deluxe hotels and the standard rate of VAT, then at 18.6%, applied. In response, many of these hotels downgraded to avoid levying the higher rate of VAT. In 1988, four-star hotels were moved to the reduced rate band and in 1994 four-star deluxe hotels were too, since when and all hotels have applied the reduced rate.

This experience, which mirrored similar experiences in Spain and Italy, demonstrates that hotels are prepared to forego the marketing advantage of a higher quality rating in order to gain the much stronger competitive advantage of being able to charge lower prices as a result of lower VAT. This provides strong evidence of the price-sensitivity of hotels, even at the upper end of the market.

Restaurant VAT Reduction in 2009

The rate of VAT on restaurants in France was reduced from 19.6 per cent to 5.5 per cent as from 1st July 2009, very shortly after the 5th May 2009 decision of ECOFIN to allow EU Member States to apply a reduced rate of VAT to restaurants. It has since risen to 10% (still below the European average).

According to the "Contrat d'Avenir" agreed between the French government, the industry and the unions, the top priority of the VAT cut was to improve wages and working conditions, with a second priority of increasing investment in the sector. The reduction of prices was only the third priority.

Several reports for the National Assembly and the Senate, including Senator Houel's report, showed that 40% of the VAT decrease was passed through to higher staff remuneration, 23% to price decreases, 20% to investments, and the balance to cash improvements.

According to INSEE –France's official office of national statistics – employment in the hotel and restaurant sector increased from 898,100 to 973,100, or by 75,000, between June 30th 2009 and September 30th 2011, which were the first nine quarters following the VAT reduction on restaurant meals from 19.6% to 5.5% on July 1st 2009. In addition to the net impact on job creation, President Nicolas Sarkozy declared on television in early 2012 that the VAT decrease had saved 30,000 cafés and restaurants that were struggling financially. **The minimum monthly wage in the restaurant industry has been increased from €1,350 to €1,620, and annual staff turnover has fallen from 80% to 40%.**

On the basis that, on average, each of these small cafés employed three people, this would imply that 90,000 jobs were safeguarded in the sector. Assuming a sectorial multiplier of 70%, then the 75,000 jobs directly created in the sector would have supported 50,000 jobs further down the supply chain**. On this basis, a total of 215,000 jobs were created or safeguarded by the VAT reduction, being the sum of 75,000 jobs directly created (INSEE), 50,000 jobs indirectly created (through the multiplier effect) and 90,000 jobs safeguarded.** It is too early to fully assess the impact of the increase in VAT from 5.5% to 7% and then to 10%, but early indications are that it is having a negative impact on sector employment.

Given President Hollande's record of introducing significant tax increases, it seems likely that he would have removed the VAT reduction and reverted to levying VAT on restaurants at the standard rate if he doubted the success of the measure, or believed the findings of the Thevénoud report, which suggested fewer jobs had been created. Rather, he announced a rise in the rate from 7% to 10% (still a reduced rate – the standard rate of VAT in France is 19.6%) in January 2014 as part of a package of measures to restore fiscal balance.