



BREAKING THE BARRIERS TO READING

The DA's proposal to scrap VAT on books

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Good education opens the doors to reaching for dreams and using opportunities to the full. But only a small minority of South Africans receive the kind of education that opens these doors. There are many reasons for this, but the cost of books, which puts reading far out of reach to most South Africans, is undoubtedly one. The DA today presents a proposal for substantially reducing the cost of books – one of the most important components of education.

Under current South African legislation, all books are subject to the standard 14% rate of value added tax (VAT). The Democratic Alliance (DA) believes that a tax on books is a tax on learning, knowledge and literacy. Right now, we need to prioritise measures to promote literacy and education, and we believe that a zero-rating on books would be a cost-effective measure to contribute towards this.

South Africa lags behind the rest of the world in our tax policy on books. In numerous countries - including Ireland, Norway, the United Kingdom, Brazil, Mexico, the Philippines, Australia, Ghana, and Kenya - no tax is charged on books at all. Elsewhere, the debate centres on just how low the reduced rate should be, rather than whether the full rate should still apply. Countries that have adopted reduced rates of tax on books include Sweden, Finland, Iceland, China, Austria, France, Germany, Belgium, Cyprus, the Czech Republic, Greece, Hungary, the Netherlands, Spain, Slovakia, Romania, Slovenia, and Malta. Most of these countries adopt a far reduced tax rating on books in the range of 4-5%.

Basic literacy and education in South Africa ought, patently, to be one of our key national priorities. In practical terms, 14% VAT means that a R37 tax is being paid on a book with a R300 shelf price. A university student purchasing R2500 worth of textbooks is paying more than R300 into the fiscus.

Reducing the rate of VAT on books would have two distinct economic effects:

First, a zero-rating on books would act as a kind of **education and literacy subsidy**. The relatively high price elasticity of demand for books means that one can expect that a lower purchase price would significantly increase demand for books.

When the Latvian government, citing the public deficit, increased the tax rate on books from 5% to 21% in January 2009, sales immediately dropped by 30% and it is estimated that 35% fewer titles were published in 2009.

Similarly, on 1 January 2002, the tax rate on books and magazines in Sweden was reduced from 25%, the standard rate, to 6%. Prior to the reduction the most important argument was that book prices would go down and sales would increase, which in turn would facilitate the work of increasing and broadening reading. Their research indicated that the book is a price sensitive commodity, and that if the VAT rate was reduced to 6% sales would increase to the same degree. This in turn happened - sales increased strongly in the first 18 months by 20%, and then subsequently levelled off.

Book prices are unregulated in Sweden and there is unrestricted freedom of establishment for booksellers. This is believed to be a contributing factor to the positive effect of the tax reduction. The same conditions are true of South Africa and it is likely that a similar result will be achieved. With the price reduction passed on to the consumer, the demand for books in all price ranges will increase.

In both cases - in Latvia and Sweden - book prices changed to the full extent of the change in tax.

Second, VAT, like all consumption taxes, is a form of regressive tax, because it takes up a higher percentage of the income of the poor than of the rich. It is for this reason that

some basic foodstuffs in South Africa are zero-rated. We believe that books need to be treated just like bread and milk. Zero-rating would not only help to bring down literature costs across the entire market, for all South Africans, but would also work disproportionately to benefit poorer households, by **removing the regressive tax** they are forced to pay on what ought to be considered essential basic goods.

2. South Africa's policy on book taxes

At present, all books, including newspapers and magazines, are subject to value added tax (VAT) at the standard rate of 14%. VAT is a "cascading" consumption tax, meaning that a good is taxed at each stage of production on the value added to the good at that production stage, rather than only at the point of sale on the final value of the product - as is the case with General Sales Tax (GST).

The concept of VAT was first adopted by France in 1954, and, in 1991, VAT replaced GST in South Africa. Specific basic foodstuff items are listed in the VAT legislation as being zero-rated, and include: brown bread, dried maize, dried beans, lentils, tinned pilchards or sardines, rice, fresh fruit and vegetables, vegetable oil, milk, eggs, and edible legumes. This was intended to relieve the pressure on poorer households, and to take into account the disproportionate burden that a regressive tax places on lower income groups.

A somewhat muted debate over South Africa's tax on books fizzled out in 2006, after a short-lived government review of our tax law failed to meet all of its objectives. In November 2005, the National Treasury advertised a tender for a review of VAT policy and VAT relief on "merit goods" such as books and medicines. This was to take place between March and June 2006. Although a review was done on some aspects of the South African tax regime, a comprehensive review on VAT policy was not completed, nor was there any further mention of relief on "merit goods". The issue, as a matter for policy debate, has since remained dormant, and attention was no doubt diverted further still from the issue of zero rating with the advent of the global recession, which shifted the focus towards retaining existing tax revenue streams, rather than crafting an environment conducive to long-term development.

Yet South Africa's education crisis ought to throw the matter of book taxes into sharp relief. While the international debate has shifted towards issues like whether e-books should be subjected to tax, we are stuck with a mindset that books are somehow the purview of the elite or the wealthy, and that any reduction of tax on books would thus be solely to the benefit of the rich. As noted in the previous section, this argument could not be further from the truth.

3. Options for reform: Zero VAT rate, VAT exemption or reduced rate

Given that South Africa is far out of step with the international practice of tax on books, we believe that reform is absolutely necessary. The question is merely what form it should take.

There are three practical options on the table:

- A **zero VAT rate** ('zero-rating') -- a 0% rate of VAT would be added to the selling price of a book, but the book would fall within the "VAT net" and the vendor would be able to reclaim input VAT on the transaction.
- A **VAT exemption** -- the book would fall outside of the "VAT net" and the vendor would not be able to reclaim input VAT on the transaction.
- A **reduced rate** -- VAT would be charged on books at below the standard rate of 14%.

The distinction between zero rating and exemptions is thus a matter of whether a vendor can recover input tax on expenses incurred in the course of making the book sale.

Reduced VAT rates are commonplace in most developed countries, though multiple rates are often criticised for being too complicated and administratively expensive.

There are also a number of options in terms of the nature of books being subjected to VAT reforms. One option is to include all books, including magazines, e-books and newspapers. A more narrow alternative approach may be to target only those books that are directly used in educational institutions.

4. Impact on tax revenue

The exact cost to the fiscus of book tax reform would depend in large part on the two sets of issues identified in section 3 - the extent to which VAT is reduced, and the number of items to which this reduction is extended.

As such there are a number of different scenarios for the fiscus, and a comprehensive exposition of this would fall under the remit of the Treasury.

Particularly problematic with carrying out preliminary calculations is that figures dealing with the amount of VAT revenue collected on books are not readily available.

This point notwithstanding, an estimated impact of a zero-rating or reduction of the VAT rate on books can be calculated:

	Option 1: Reduced rate (5%)	Option 2: Zero- rate	Option 3: VAT exemption
Total VAT revenue lost (all books included)	R 175 million	R 274 million	R274 million, less input VAT not reclaimed

According to the Nielsen Bookscan, that monitors sales by approximately 80% of retail booksellers in South Africa, R 1 569 006 660 in revenue was generated from the sale of 12 628 234 books, across 276 860 unique titles, in 2009. This would amount to VAT revenue of R219 660 930. If this is assumed correct then approximately R 274 million was collected in VAT generated from retail book sales. This assumption might exclude textbooks purchased directly from wholesalers, where government is the chief procurer. In this event, given that government is paying the VAT, a rate reduction has no fiscal impact.

These are all short-term considerations. What is more difficult to quantify - but certainly needs to be borne in mind - is that these figures fail to take into account the long-run impact of zero-rated VAT on an item that will boost economic activity. Zero-rated VAT on textbooks will ease access to education and result in more economically active individuals, who will in turn contribute relatively more to the tax pool, thus further reducing the loss to the Treasury. This forms part of a virtuous cycle that will boost our economy over time, and will mitigate lost tax revenue.

5. Our proposal

It has already been noted that removing or lowering VAT on books would act as a kind of education subsidy, and would help to address the regressive nature of the tax burden placed by VAT on essential items for poorer South Africans.

The most important benefit of a book tax reform, however, is the multiplier effect that such measures would have for our entire economy. Reducing or zero rating VAT would have profound effects across all parts of our economy. For instance, were books to be zero-rated, a library making a purchase order of 3,000 new books could afford to purchase an additional 400 books. Removing VAT on books would thus have powerful, positive knock-on effects for those South Africans relying on libraries as a source of books. Again, this is likely to particularly benefit poorer South Africans and students using books for basic and advanced learning purposes.

OUR VIEW:

Our view is that steps ought to be taken right away to grant zero-rating to all books and e-books.

Our economy is slowly emerging from the recession and we agree that the impact on tax income needs to be carefully considered before changes to VAT rates on all reading material can be considered. However, we believe that the costs incurred to the fiscus are insignificant in comparison with the boost to literacy and economic activity. We also believe that extending these measures to e-books, which are not widely used in South Africa and are unlikely to be generating significant VAT revenue at present, ought to be considered.

In addition, a zero-rating of VAT should in future be extended to all newspapers and magazines. We believe this ought to be considered as a 'Phase II' development, but only after the National Treasury has initiated a project to establish the impact this will have on our tax revenue stream.

The VAT system already successfully manages dual rates of 0% and 14% and it is unlikely that the system would be unable to manage an additional zero-rated category. Zero-rating is preferable to VAT exemption because vendors ought to be able to claim input VAT on a book - as is the case with basic foodstuff items that are currently zero-rated. It is also preferable to a reduced rating because we already know that our VAT system can successfully administer two rates (0% and 14%) and the introduction of a third rate, reduced for books, may unnecessarily complicate VAT administration.

6. Conclusion

Reading is a primary means of education and disseminating information, through books, newspapers and magazines. Education and the promotion of literacy are powerful weapons in the fight to eradicate poverty. Information is not only a basic requirement for democracy to flourish through the exchange of ideas, it also opens the door to economic participation.

The debate on tax applicable to books, newspapers and magazines is international and ongoing. Tax on books, newspapers and magazines increases the cost of freedom of expression and the acquisition of knowledge. In our pursuit of an Open Opportunity Society, where reading serves as a powerful mechanism for individuals to achieve their full potential, the DA supports the ideal of no tax on books and want a public debate on this matter on behalf of all South Africans who cherish universal access to the written word.

We need to understand that, for the same pro-development, pro-poor reasons that bread, milk and vegetables are zero-rated, we need to zero-rate basic learning material too.

South Africans crave access to opportunity and government must facilitate this process. It can do this by making information more affordable, and therefore more available, to more people. Evidence strongly supports the view that a lower tax on books will do this.

Parliament now has the power to amend the national budget and the people have an opportunity to be heard on how the public financial model can work to the benefit of all South Africans. We need an immediate reduction of VAT on books and the DA will lead the way.