

COMPENSATING FAMILIES WITH CHILDREN FOR THE VAT HIKE

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PETR JANSKÝ AND KLÁRA KALÍŠKOVÁ

Abstract

The study attempts to estimate the impacts of compensating families with children for the harmonization of VAT rates at 17.5 percent - we evaluate the government proposal to increase the tax deduction for a child by CZK150 per month and its alternatives. The study builds on earlier estimates of the impact of VAT harmonization, namely that the long-term income of households will be reduced by an average of approximately 0.8 percent, which amounts to CZK200 per month. The analysis shows that the compensation proposal of government would reduce the share of households that were negatively influenced by the VAT rate harmonization from 80% to 65%, and the decrease in real incomes of families with children would be more or less compensated (households with children would lose an average CZK35 per month). The increased tax deduction for a child does not sufficiently compensate the poorest families, because it is mainly received by families with working parents. Nevertheless, the main advantage of this mechanism is its influence on a large proportion of households with children. Furthermore, we examine the possibility of child benefit increases as an alternative compensation mechanism. This would have a positive impact on poorer families, but would affect a smaller share of families with children. If advantages of both compensation mechanisms are combined, however, for example, by a combined increase of tax deduction for a child by CZK120 and child benefits by CZK115, expenses of the state budget remain the same but at least 99% of families with children become partially compensated and the poorest families are sufficiently protected.

[Download](#) the complete study (in Czech only).

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