# France Pledges $25 Billion Tax Break to Businesses


To improve business competitiveness and revitalize the economy, France's government has pledged $25 billion in tax credits to businesses in a plan to spark innovation and reduce unemployment in the nation's writhing economy. The measure is part of a "competitiveness pact" with the private sector, but falls short of recommendations in a recent report recommending a "shock" to the French economy, which as shed 750,000 industrial jobs in the last 10 years.

Prime Minister Jean-Marc Ayrault claimed the economic plan, which contains a $638-million fund to bolster ailing small businesses, would put France "back at the heart of the world economy." He added, "This new French model will consist of finding a way back to creating jobs and will no longer be financed by permanent deficits."

Announced on Tuesday, the plan arrived a day after a government report — authored by Louis Gallois, former head of Airbus parent company EADS — affirmed that France's stagnant economy requires a dramatic shock to remain globally competitive. However, while many hailed the measure, it fell short of the $38.2-billion jumpstart Gallois advocated in his report, raising concerns that the Socialist administration of President Francois Hollande is not doing enough to reignite the French economy. The Associated Press explained:

> For example, the $20 billion tax credit is to be implemented over three years — with €10 billion available in 2013 and the rest split over the following two years. Gallois recommended in his report for the government that the breaks should happen over one or two years to have the maximum effect.
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> The measure also takes the form of an income tax credit, rather than a reduction in the social charges employers pay on salaries, as Gallois had suggested. The government argues that its method is designed to have immediate impact, while deferring payment until 2014 when next year's tax bill comes due. That, however, assumes that companies will start spending and hiring right away in anticipation of the credit.

The scope of the tax plan, to some extent, disproved speculation that Gallois' report would be "buried" by a government under pressure from the Left, which has scrutinized the government for considering favorable policies for private-sector interests. But rising unemployment, notched at 10.8 percent, and the imminent threat of economic recession next year appeared to override government restraint.

Ironically, strict labor regulations have largely contributed to business uncertainty, as rigid government rules have made firing difficult and have put job growth at a standstill.

Finance Minister Pierre Moscovici claimed that the tax measures will generate 300,000 jobs over five years and will add half a percentage point to annual growth over that same period. "It is a moment of truth," he affirmed. "It is a step no French government has taken before."

Hollande said the tax credits would be offset by a sales tax increase and spending reductions that have yet to be announced. The controversial sales tax increase clashes with Ayrault's pledge in September to freeze current sales tax levels. Owing to the perception that value-added taxes are harder on the poor than the rich — because the poor spends a larger share of their income — the sales tax provisions are installed in three separate categories, UPI.com reported:

> The sales tax for food and other basic needs will drop from 5.5 percent to 5 percent, but the sales tax for most items will rise from 19.6 percent to 20 percent in January 2014.
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> There is also an "intermediate" value added tax in France that covers items such as home repairs and restaurant meals. That tax will rise from 7 percent to 10 percent.

The new value-added tax model is a blatant reversal by President Hollande, who had earlier quashed a plan put forth by his predecessor for an across-the-board VAT increase of 1.6 percentage points in return for decrements in employer social charges. "I'm slightly surprised, because this is what had been planned and voted by the previous government," said Antoine Lenoir, chairman of Brunet SA, a manufacturer of armrests and mudflaps that is based near Bordeaux.

But Ayrault says the tax credits were a "major and decisive" step toward a new economic model to make France "more competitive" and able to deliver "more solidarity." All in all, French officials claim, the strategy is to shift France's industry up the value chain to better quality and more innovative products, as Germany has achieved.

Laurence Parisot, the head of the MEDEF — the largest union of employers in France — which has campaigned heavily for cuts in labor costs, said the proposals were "good and significant." MEDEF hoped for the government to go further, Parisot added, with labor costs needing to fall by $89 billion to compete with Germany. However, "for the first time the French government has admitted clearly and unambiguously that there is a problem of cost competitiveness," she said. "This is truly an important moment for our economy."

France has largely avoided the enormous budget cuts and reforms pursued by its neighboring countries, despite harboring one of the world's highest ratios of state spending as a share of GDP. Gallois asserted that the largest economic problem in France is that high labor costs have forced businesses to slash prices, leaving them with low profit margins and little money to invest in product quality and innovation.

Gallois said the government's new awareness, which includes a number of his recommendations on fostering investment, innovation, and the fortitude of small- and medium-sized businesses, revealed that the government had "understood the measure of the problem." However, it remains unclear how far Hollande and his socialist acolytes will go in planting deeper structural reforms in their spendthrift government, hyper-regulated labor market, and eminently complex tax code.