VAT Action Plan

Measures to modernise VAT in the EU

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European Commission

- Action plan on VAT was adopted on 7 April 2016
- Sets out a pathway to **modernise current EU VAT rules**
- Follow up to **Communication on the future of VAT** of 2011
- EU Council and Parliament agreed on **destination principle** (since 1967, objective was origin based system)
- Several initiatives were taken then but it was **not enough**

European Commission

Why we need a VAT reform?

- VAT is a major source of tax revenue for Member States: almost **EUR 1 trillion** in 2014 (17.5% of national tax revenues)
- VAT gap: **EUR 170 billion** - cross-border fraud: **EUR 50 billion**
- **High compliances costs** for businesses (especially SMEs) in particular in cross-border trade
- Need to adapt to **technological progress**
- Adjust **VAT rates** rules to destination principle

What is in the Action Plan? 4 building blocks

1. **Fight against fraud** with conventional and short term measures: reinforcing cooperation between Member States

2. **Definitive VAT system**: Treatment of intra-EU supplies: key principles for a future single European VAT system

3. **E-commerce and SMEs**: establish level playing field between e-commerce and traditional trade and make life easier for SMEs

4. **New approach on VAT rates**: in destination based system, less need for harmonisation of rates

1. Fight against fraud

Fight against fraud

- The **'VAT gap'** between expected revenue and revenue actually collected by national authorities is estimated at **EUR 170 billion** (= 15% of revenue loss)

- Two main ways to tackle fraud:
  - Urgent action on several fronts necessary: conventional measures
  - Medium term measures: tackle the weaknesses of the VAT system

Immediate measures

Conventional measures: reinforce current tools used by Member States to exchange information related to VAT fraud, fraud schemes and good practices

- Improving cooperation within the EU and with non-EU countries
- Towards more efficient tax administrations
- Improving voluntary compliance
- Tax collection
- Temporary derogation for Member States (RCM, reform programmes)

Fight against fraud

Timeline Commission actions:

2016

- **Improve cooperation between tax administrations including from non-EU countries** and with customs and law enforcement bodies and to strengthen tax administrations' capacity for a more efficient fight against fraud
- **Evaluation report of the Directive on the mutual assistance for the recovery of tax debts**

2017

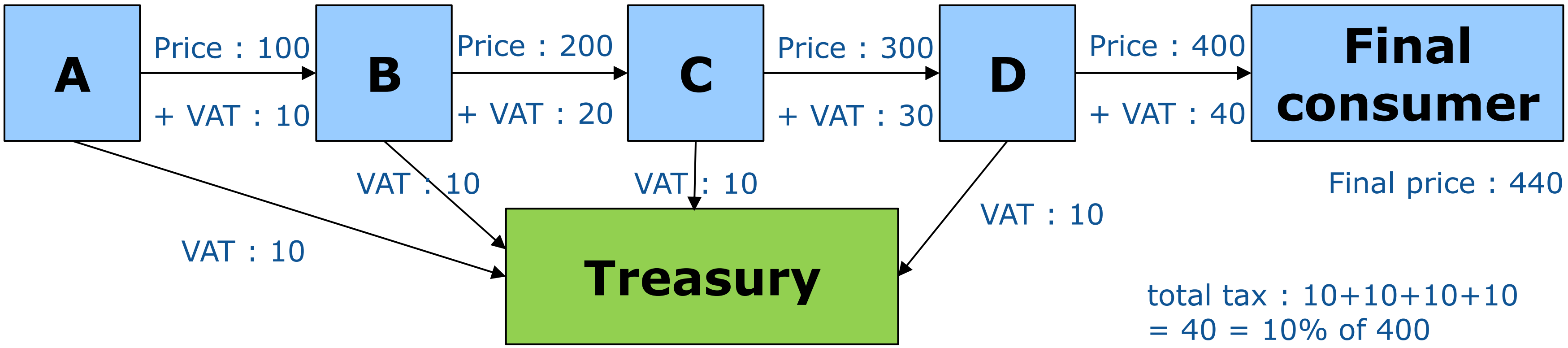
- **Proposal to enhance VAT administrative cooperation and Eurofisc**

2. Definitive VAT system

Why a definitive VAT system?

- Past approach to enhance current system has reached its limits – Attempts to reform system not successful
- Complexity – legal uncertainty. Need to take into account globalisation and digitalisation of economy
- Current system is based on the concept of imports/exports not reflecting adequately Internal Market
- EU Cross-border fraud: **EUR 50 billion** a year

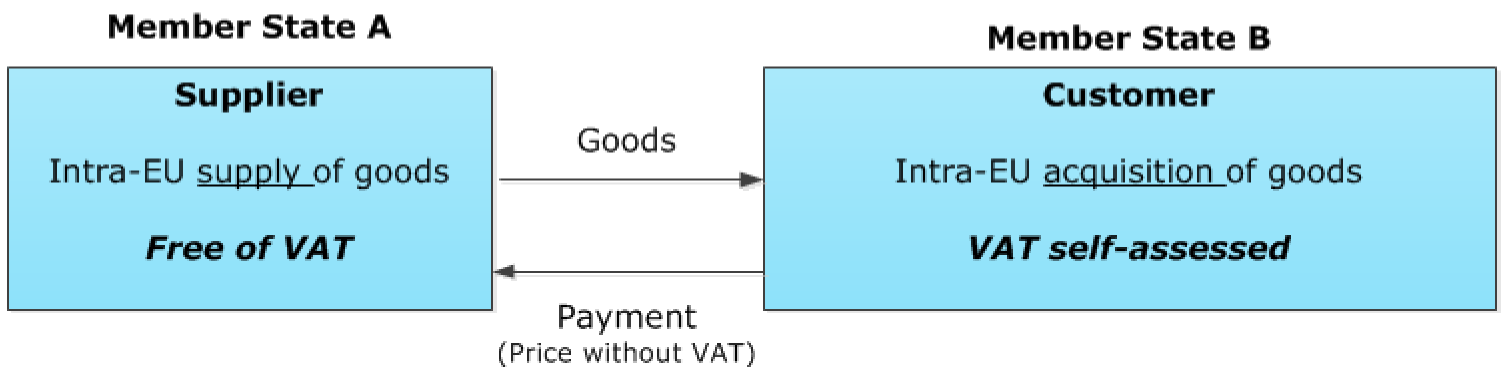
Current domestic VAT system



- At each stage, VAT is paid to the Treasury just on the added-value: neutral and transparent cross-border
- Self-policing character : need an invoice for each customer to deduct the VAT paid by its supplier, who is then in turn discouraged from evading taxes.
- In case of fraud by the retailer (D here), only € 10 is lost.

On the basis of a VAT rate of 10 %

Current transitional intra-EU VAT system



Supply of goods from Member State A to Member State B gives rise to:

- Supply of goods free of VAT in Member State A with <u>full deduction of input VAT</u>
- VAT paid by customer taxpayer in Member State B at the rate of MS B
- **Carrousel and MTIC fraud**

Definitive VAT system features

- Based on the principle of **taxation in the country of destination of the goods**

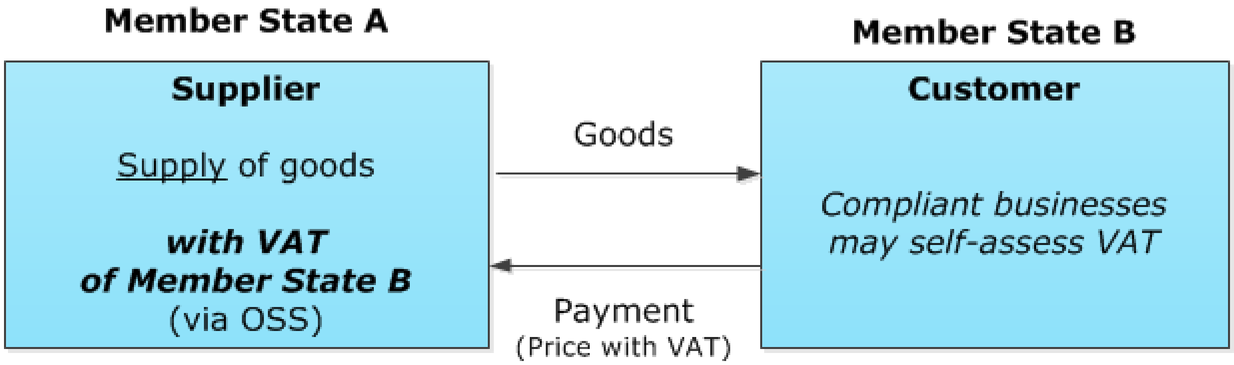
- **The supplier of goods charges VAT** to his customer

- The **VAT on a cross-border supplies is collected by the tax authority of the originating country** and transferred to the country of consumption

- Enhanced **One-Stop-Shop** for suppliers (input and output VAT)

Future intra-EU VAT system based on destination principle

Extend the domestic taxation principle to intra-EU supplies



Supplier of MS A charges VAT of MS B and reports and pays VAT via the One-Stop-Shop (OSS)

Definitive VAT system

- Would re-establish the basic features of the VAT in cross-border trade i.e. the **fractionated payments system** with its self-policing character

- **Estimates show that the future VAT system could reduce cross-border fraud by around EUR 40 billion (or by 80%) a year**

- Would ensure **consistent treatment of domestic and cross-border supplies** along the entire chain of a production and distribution

- **However would require time for adaptation** for both business and tax administrations

First step
Legislative proposal of 2017

- **Principle of taxation of cross-border supplies & OSS**
- **Mitigation measure:** reverse charge for trustworthy businesses that are certified by their tax administrations, including SMEs.

Only when Member States consider all conditions (trust and OSS) are fulfilled, taxation will cover all cross-border supplies within the Single Market.

3. Removing VAT obstacles to e-commerce in the single market and SME VAT package

Removing VAT obstacles to e-commerce in the single Market

- Establish level playing field between traditional business and e-commerce
- legislative proposal by the end of **2016** to modernise and simplify VAT for cross-border e-commerce by:
    - **Extending the current One Stop Shop** concept to all cross-border e-commerce, including distance sales,
    - Introducing common EU-wide **simplifications measures to help small start-up e-commerce businesses**,
    - Streamlining audits in this sector (home country audits), and
    - Removing the VAT exemption for the **importation of small consignments** from suppliers in third countries

SMEs VAT package

- SMEs bear proportionally higher VAT compliance costs than large businesses due to the complexity and fragmentation of the EU VAT system

- Work already started: comprehensive study on-going

- legislative proposal by the end of **2017** will include:
  - Comprehensive simplification package for SMEs
  - The special scheme for small enterprises will be subject to review

4. Reforming the rules on VAT rates

Current framework for VAT rates

Original aim: simple and uniform rules (origin based system)

- One standard rate of minimum 15%, maximum of two reduced rates of minimum 5% **but**
  - **many derogations** were added on, making the **system complicated:** super-reduced, zero-, and parking rates
  - Many derogations specific to individual countries => **no equality of treatment among MS**
- Rules do not take into account **technological development**
- Member States have **limited leeway** to reduce rates on specific goods and services – less relevant under a destination system

More flexibility to Member States on rates

Option 1

Enlargement + regular review of list of goods and services eligible for reduced rates

Option 2

Substitution of the list of goods and services eligible for reduced rates with general principles for applying them

The degree of autonomy on rates to be granted to Member States is not purely a technical matter: **political discussion required!**

2016: proposal on e-publications to align VAT treatment with paper version
2017: detailed legislative proposals based on a mandate from the Council

Next steps

Adapting the VAT system to the digital economy and the needs of SMEs

2016	Proposal for removing VAT obstacles to cross-border e-commerce (Digital Single Market - REFIT) - e-publications
2017	SME VAT package

Towards a robust single European VAT area

2016	Measures to improve cooperation between tax administrations and with customs and law enforcement bodies and to strengthen tax administrations' capacity
2016	Evaluation report of the Directive on the mutual assistance for the recovery of tax debts
2017	Proposal to enhance VAT administrative cooperation and Eurofisc
2017	Proposal for the definitive VAT system for cross-border trade (single European VAT area – first step - REFIT)

Towards a modernised rates policy

2017	Reform of VAT rates (REFIT)

Thank you for your attention!