EU: Single VAT Area: proposals for VAT rate flexibility and SME simplifications

Indirect Tax

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The European Commission's VAT Action Plan aims to reform EU VAT rules with the creation of a single VAT area; seeking to reduce the €50 billion lost to VAT fraud each year in the EU, while easing business administration and securing government revenues. UK businesses trading with EU countries will need to be aware of these changes. See our previous article in June 2016's issue of *Tax Adviser* for background information.

Published on 18 January 2018, the European Commission's proposals seek to give member states more autonomy on VAT rates and create a simplified environment for smaller businesses who suffer from disproportionate VAT compliance costs in relation to cross-border trade.

VAT rate flexibility

Currently, member states can apply a reduced rate as low as 5% to specified categories of products in their country. In addition, specific derogations for further reduced rates can be applied.

Under the new proposals member states would now be able to put in place:

- two separate reduced rates of between 5% and the standard rate chosen by the member state;
- one exemption from VAT (or ‘zero rate’);
- one reduced rate set at between 0% and the reduced rates.
- the current, complex list of goods and services to which reduced rates can be applied would be abolished and replaced by a new list of products (such as weapons, alcoholic beverages, gambling and tobacco) to which the standard rate of 15% or above would always be applied.

Reducing VAT costs for SMEs

Under current rules, member states can effectively exempt supplies made by small businesses by having a VAT registration threshold. This varies from one country to the next meaning there is no level playing field for SMEs trading within the EU. An issue for growing SMEs is that they lose access to simplification measures once the registration threshold has been exceeded. In the UK there is a cliff-edge effect, which has been highlighted by the recent Office of Tax Simplification’s VAT review.

The Commission proposes that current exemption thresholds would remain, with the introduction of:

- A €2 million revenue threshold across the EU, under which small businesses would benefit from simplification measures, whether or not they have already been exempted from VAT;
- The possibility for member states to free all small businesses that qualify for a VAT exemption from obligations relating to identification, invoicing, accounting or returns;
- A turnover threshold of €100,000 in the EU, below which companies would be entitled to claim not only the exemption in the country where they are established but also those in other member states.

What next?

The VAT Action Plan is due to come into force in 2020 and these legislative proposals will now be submitted to the European Parliament and the European Economic and Social Committee for consultation and, ultimately, to the Council for adoption. The changes will become effective only when the new regime comes into force.

These proposals have been scrutinised by the Confederation Fiscale Europeenne (CFE), upon which the CIOT is represented. The CFE issued an opinion statement in December on the EU's single VAT area proposals.

The CIOT is also represented on HM Treasury's VAT Forum and SME VAT Forum, which met in January 2018 to discuss the impact of these measures on businesses. We would encourage members to feedback thoughts and concerns to the ITX Technical Officers (via technical@ciot.org.uk) on these proposals and the action plan in general so that your views can be included in future representations.