

## ROADMAP

<b>TITLE OF THE INITIATIVE</b>	Action Plan for a simple, efficient and fraud-proof definitive system of Value Added Tax tailored to the single market		
<b>LEAD DG – RESPONSIBLE UNIT – AP NUMBER</b>	TAXUD.C.1 2016/TAXUD/005	<b>DATE OF ROADMAP</b>	01/2016
<b>LIKELY TYPE OF INITIATIVE</b>	Communication from the Commission to the European Parliament, the Council and the EESC		
<b>INDICATIVE PLANNING</b>	<a href="http://ec.europa.eu/atwork/planning-and-preparing/work-programme/index_en.htm">http://ec.europa.eu/atwork/planning-and-preparing/work-programme/index_en.htm</a>		
<b>ADDITIONAL INFORMATION</b>	<a href="http://ec.europa.eu/taxation_customs/common/newsflash/index_en.htm">http://ec.europa.eu/taxation_customs/common/newsflash/index_en.htm</a>		
<p>This indicative roadmap is provided for information purposes only and can be subject to change. It does not prejudice the final decision of the Commission on whether this initiative will be pursued or on its final content and structure.</p>			

### A. Context and problem definition

- (1) What is the political context of the initiative?
- (2) How does it relate to past and possible future initiatives, and to other EU policies?
- (3) What ex-post analysis of existing policy has been carried out? What results are relevant for this initiative?

(1) Value Added Tax (VAT) is a general, broadly based consumption tax assessed on the value added to goods and services that are bought and sold for use or consumption in the European Union. The common system of VAT is governed by the VAT Directive<sup>1</sup>. Each of the 28 Member States is responsible for the transposition of its provisions into national legislation and their correct application within its territory. The Commission is responsible for ensuring that the national legislation and general practice complies with EU Law.

VAT is a major and growing source of tax revenue in the EU, yielding about EUR 927 billion in 2012. This represents 7.1% of the EU's GDP or 18.1% of all tax revenues<sup>2</sup>.

While the VAT ultimately falls on final consumers, the fractioned payment at each stage - whereby taxable persons (businesses) deduct from the VAT they have collected the amount of tax they have paid to other taxable persons on purchases for their business activities - ensures the self-policing strength of the VAT and implies that the actual tax burden is visible at each stage in the production and distribution chain.

At the time the common system of VAT was established<sup>3</sup>, the commitment was made to establish a definitive VAT system operating within the European Union (EU) in the same way as it would within a single country. The need to abolish physical borders between Member States by the end of 1992 made it necessary to reconsider the way in which trade in goods was taxed in the EU. The goal was that goods would be taxed in the country of origin (Member State of departure of the goods), so that the same conditions that apply to domestic trade would apply to trade within the EU, perfectly reflecting the idea of a genuine internal market.

Since the political and technical conditions<sup>4</sup> were not ripe for such a system, transitional VAT arrangements were adopted. These arrangements split the cross-border movement of goods into two different transactions: an exempt intra-EU supply and an intra-EU acquisition taxed in the country of destination. This system is de

<sup>1</sup> Council Directive 2006/112/EC of 28 November 2006 – as amended (<http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:02006L0112-20150101&from=EN>).

<sup>2</sup> Taxation trends in the European Union, European Commission (2014).

<sup>3</sup> First Council Directive 67/227/EEC of 11 April 1967 on the harmonisation of legislation of Member States concerning turnover taxes, Second Council Directive 67/228/EEC of 11 April 1967 on the harmonisation of legislation of Member States concerning turnover taxes — Structure and procedures for application of the common system of value added tax.

<sup>4</sup> An origin based system requires a clearing system to reattribute VAT receipts to the Member State of consumption. It implies a high degree of confidence between Member States and a high level of harmonisation of rates and exemptions, in order to avoid distortions of competition.

facto based on the taxation in the Member State of destination of the goods (Member State of arrival of the goods). These rules were regarded as temporary (initially 4 years) and are not without drawbacks: for instance, allowing goods to be bought abroad free of VAT increases the opportunity for fraud<sup>5</sup>, while the inherent complexity of the system is not conducive to cross-border trade.

A recent report<sup>6</sup> estimates that the total VAT Gap<sup>7</sup> for EU-26 amounted to EUR 168 billion.

Since the basic requirements for an origin-based system have proved not to be achievable more than 20 years later, despite several attempts in that direction<sup>8</sup>, the Commission should pursue its work on the way to implement the destination principle for intra-EU supplies of goods.

In line with President Juncker's political commitment to unleash the full potential of the Single Market and make it the launch pad for Europe to thrive in the global economy<sup>9</sup>, the Commission intends to present in its Action Plan the main principles and features for an efficient and fraud-proof definitive regime of VAT and initiatives on VAT rates and e-commerce in the context of the Digital Single Market Strategy for Europe (DSM Communication)<sup>10</sup>. The Commission will also withdraw VAT proposals that have made little progress in the Council or where their simplification potential has been unacceptably watered down<sup>11</sup>. Addressing tax fraud and tax evasion will be essential in this exercise to increase the effectiveness and fairness of Member State's tax systems helping to secure revenues due to them<sup>12</sup>.

(2) The Action Plan fits well into previous Commission initiatives on VAT. To combat VAT fraud, the Commission proposed a Quick Reaction Mechanism (adopted in 2013) and on 1 January 2015 the new place of supply rules for telecommunications, broadcasting and electronic services provided to final consumers and the mini-One Stop Shop (MOSS)<sup>13</sup> were successfully launched. The standard VAT return proposal that would have drastically reduced administrative burden for SMEs will have to be withdrawn<sup>14</sup> as it was denatured during the negotiations.

Following the consultation on the Green Paper on the future of VAT (COM(2010) 695), the Commission in December 2011 adopted a Communication on the future of VAT (COM(2011) 851). It set out the fundamental characteristics that would underlie the new VAT regime and defined for the years to come the priority actions needed to create a simpler, more robust and efficient VAT system tailored to the single market.

Since the discussions with Member States on that Communication confirmed that the objective to implement a definitive VAT regime based on the principle of origin for intra-EU trade was politically unachievable, the Commission abandoned work on achieving this objective and indicated that it would proceed with in-depth technical work and a broad-based dialogue with Member States and business to examine in detail the different

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<sup>5</sup> A typical fraud resulting from these VAT rules is the so-called MTIC ("missing trader") fraud. It occurs when a fraudulent business (or "missing trader") purchases goods from a supplier located in another EU Member State. The missing trader then sells the goods to a business in its Member State and charges VAT. The purchaser, who may be an innocent party, reclaims the VAT charged by the missing trader. The missing trader then disappears without paying the VAT to the Tax Authorities of the Member State in which the VAT is due.

<sup>6</sup> Study to quantify and analyse the VAT Gap in the EU Member States, CASE (2015).

<sup>7</sup> The VAT Gap is an indicator of the effectiveness of VAT enforcement and compliance measures, as it provides an estimate of revenue loss due to fraud and evasion, tax avoidance, bankruptcies, financial insolvencies as well as miscalculations. The VAT Gap is defined as the difference between the amount of VAT actually collected and the VAT Total Tax Liability (VTTL), in absolute or percentage terms. The VTTL is the estimated amount of VAT that is theoretically collectable based on the VAT legislation and ancillary regulations.

<sup>8</sup> See in particular point B, 4) of Council conclusions on the future of VAT adopted on 15 May 2012 ([http://www.consilium.europa.eu/uedocs/cms\\_data/docs/pressdata/en/ecofin/130257.pdf](http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/130257.pdf)).

<sup>9</sup> See the Letter of Intent signed by the President and the First Vice-President and addressed to the Presidents of the European Parliament and of the Council.

<sup>10</sup> A Digital Single Market Strategy for Europe, COM(2015) 192 final ([http://ec.europa.eu/priorities/digital-single-market/docs/dsm-communication\\_en.pdf](http://ec.europa.eu/priorities/digital-single-market/docs/dsm-communication_en.pdf)).

<sup>11</sup> See Commission Work programme 2016: No time for business as usual, COM (2015) 610 final.

<sup>12</sup> Annual Growth Survey 2016: Strengthening the recovery and fostering convergence (COM(2015) 690 final).

<sup>13</sup> MOSS allows taxable persons (both EU and non-EU businesses) supplying certain services (telecommunication, television and radio broadcasting services and electronically supplied services) to non-taxable persons in Member States in which they do not have an establishment to account for the VAT due on those supplies via a web-portal in the Member State in which they are VAT registered.

<sup>14</sup> See Commission Work programme 2016: No time for business as usual, COM (2015) 610 final.

possible ways to implement the destination principle.

The European Parliament<sup>15</sup> and the Council<sup>16</sup> welcomed the Communication. Different ways of implementing the destination principle were then examined in depth with stakeholders (Member States and business) and an expert study was finalised in June 2015<sup>17</sup> analysing the pros and cons of a limited set of options which had been identified by these stakeholders<sup>18</sup>.

In the DSM Communication, the Commission announced that a proposal to enhance and extend the MOSS to all business to consumer (B2C) intra-EU supplies (and implement a Single Electronic Mechanism) would be tabled in 2016.

Furthermore, the move away from the principle of taxation at origin towards taxation in the Member State of destination of goods and services was confirmed as well.

(3) The Action Plan will take stock of the achievements made since the 2011 Communication and set out the direction for future work. It will in particular set out the main features of the definitive VAT regime for intra-EU trade that the Commission wants to propose and the methodology it envisages to use in addressing the structure of VAT rates in a definitive regime characterised by the destination principle.

It will also feature some actions to address the complexity of the VAT system in particular for SMEs, to broaden the scope of the VAT base by examining the appropriate VAT treatment of the activities of public bodies taking into account the evolution in Member States towards privatisation and deregulation of activities traditionally reserved for the public sector and to enhance the fight against VAT fraud notably the cooperation between tax administrations. Any measures on fight against VAT fraud and cooperation between tax administrations will have to respect the fundamental rights, and in particular the right to privacy and the right to personal data protection (Articles 7 and 8 of the EU Charter of Fundamental Rights), and the applicable EU data protection legislation<sup>19</sup>. The Action Plan is linked to the Commission's Regulatory Fitness and Performance Programme.

What are the main problems which this initiative will address?

### **(1) The difficulties arising from the VAT treatment of intra-EU trade under the current system and its exposure to fraud**

The functioning of the single market is affected by VAT rules as they may influence where goods and services are produced, traded, bought and sold. A retrospective economic evaluation of the EU VAT system<sup>20</sup> was carried out in 2011 in parallel with the public consultation launched by the Green Paper on the future of VAT. A recent study<sup>21</sup> confirmed the findings of the evaluation: the costs associated with complying with cross-border VAT obligations are substantially higher (11% higher) than the VAT compliance costs associated with domestic trade. It also confirmed that high levels of VAT fraud resulting from the possibility under the current cross-border trade regime to buy goods free of VAT represent a major revenue loss for Member States, and cause liability risks to any businesses which unknowingly become involved in a fraudulent supply chain. Cross-border fraud alone is estimated to generate a VAT revenue loss of EUR 45 to 53 billion annually.

### **(2) The VAT rates structure and levels**

It is also envisaged to consider options for a review of the current rules on VAT rates<sup>22</sup>. These rules are characterised by multiple country and product-specific derogations leading to a non-level playing field. These

<sup>15</sup> See European Parliament resolution of 13 October 2011 on the future of VAT (<http://www.europarl.europa.eu/sides/getDoc.do?type=TA&language=EN&reference=P7-TA-2011-0436>).

<sup>16</sup> See Council conclusions adopted on 15 May 2012 ([http://www.consilium.europa.eu/uedocs/cms\\_data/docs/pressdata/en/ecofin/130257.pdf](http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/130257.pdf)).

<sup>17</sup> Implementing the 'destination principle' to intra-EU B2B supplies of goods (2015) ([http://ec.europa.eu/taxation\\_customs/resources/documents/common/publications/studies/ey\\_study\\_destination\\_principle.pdf](http://ec.europa.eu/taxation_customs/resources/documents/common/publications/studies/ey_study_destination_principle.pdf))

<sup>18</sup> See Commission Staff Working Document on the implementation of the definitive VAT regime for intra-EU trade, SWD(2014) 338 final ([http://ec.europa.eu/taxation\\_customs/resources/documents/taxation/vat/swd\\_2014\\_338.pdf](http://ec.europa.eu/taxation_customs/resources/documents/taxation/vat/swd_2014_338.pdf)).

<sup>19</sup> In particular Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995 on the protection of individuals with regard to the processing of personal data and on the free movement of such data (OJ L 281, 23.11.1995, p. 31) and Regulation (EC) No 45/2001 of the European Parliament and of the Council of 18 December 2000 on the protection of individuals with regard to the processing of personal data by the Community institutions and bodies and on the free movement of such data (OJ L 8, 12.01.2001, p. 1).

<sup>20</sup> [http://ec.europa.eu/taxation\\_customs/resources/documents/common/publications/studies/report\\_evaluation\\_vat.pdf](http://ec.europa.eu/taxation_customs/resources/documents/common/publications/studies/report_evaluation_vat.pdf)

<sup>21</sup> Implementing the 'destination principle' to intra-EU B2B supplies of goods (2015) ([http://ec.europa.eu/taxation\\_customs/resources/documents/common/publications/studies/ey\\_study\\_destination\\_principle.pdf](http://ec.europa.eu/taxation_customs/resources/documents/common/publications/studies/ey_study_destination_principle.pdf))

<sup>22</sup> In the context of this general VAT reform, the Commission will also explore how to address the tax treatment of certain e-services, such as digital books and online publications as announced in its DSM Communication.

derogations were meant to be temporary (some of them applying only until adoption of definitive regime) so they should be addressed in this context.

### **(3) Simplification of the VAT System**

The complexity of the VAT system may hinder the good functioning of the internal market as it can deter businesses, in particular SMEs, from trading and developing cross-border. A simpler VAT system not only reduces compliance costs to businesses but also facilitates compliance by businesses and therefore contributes to reducing mistakes, tax avoidance and even fraud.

### **(4) Other issues**

Recommendations to Member States to broaden the tax base in order to increase efficiency of their tax revenues already take place in the framework of the European Semester<sup>23</sup>. However, broadening tax bases may result impossible in certain circumstances due to the need to comply with existing VAT rules. In addition, as pointed out already in the 2011 communication, the VAT rules applicable to activities of public bodies which are outdated do not ensure legal certainty and do not ensure a level-playing field between private and public activities which are in competition with each other.

Who will be affected by it?

Since the new system would aim to reduce administrative burden and fight against VAT fraud businesses and Member States would primarily be affected. To a lesser extent citizens/final consumer could also be affected if under a new regime, VAT rates and consequently, consumer prices for certain products in- or decrease.

A reduction of compliance costs to businesses and a positive effect in terms of VAT revenues to Member States is expected which could in turn have a positive effect in terms of prices for final consumers.

Is EU action justified on grounds of subsidiarity? Why can Member States not achieve the objectives of the proposed action sufficiently by themselves? Can the EU achieve the objectives better?

National instruments to fight against VAT fraud, in particular the so-called "MTIC fraud" inherent to the transitional VAT arrangements, have shown not to be efficient enough to stop this typical cross-border fraud. Action at EU level is needed to address EU cross-border fraud.

To create a system which is efficient from an EU perspective, the VAT treatment of certain supplies (e.g. intra-EU, zero-rated or subject to (super) reduced rates supplies) and even suppliers (e.g. public bodies, SMEs) needs to be addressed in a coherent way, that is to say from an EU perspective, so as to avoid businesses within the EU relocating with a view to benefit from more favourable VAT conditions (e.g. derogations granted to some Member States as regards rates, exemptions, special schemes or options to apply certain rules left to the discretion of Member States)<sup>24</sup>.

To enable businesses to take advantage of the Single Market, it is necessary to reduce the administrative obstacles that are caused by the current transitional VAT arrangements. This can only be done through an EU action that would establish a definitive VAT system.

The objectives can only be achieved by amending the current VAT Directive. Such amendments require adoption by the Council, acting unanimously in accordance with a special legislative procedure and after consulting the European Parliament and the Economic and Social Committee. Other legislative instruments may need to be amended as well, in particular to strengthen the tools at European level for the fight against VAT fraud.

## **B. Objectives of the initiative**

What are the main policy objectives?

The initiative aims in particular at:

- considering ways to reduce obstacles to cross-border trade within the Single Market so that doing business across the EU becomes as simple and as secure as engaging in purely domestic activities while minimizing

<sup>23</sup> See more info under following link:

[http://ec.europa.eu/economy\\_finance/economic\\_governance/the\\_european\\_semester/index\\_en.htm](http://ec.europa.eu/economy_finance/economic_governance/the_european_semester/index_en.htm)

<sup>24</sup> Study on reduced VAT applied to goods and services in the Member States of the European Union (2007), Copenhagen Economics,

[http://ec.europa.eu/taxation\\_customs/resources/documents/taxation/vat/how\\_vat\\_works/rates/study\\_reduced\\_vat.pdf](http://ec.europa.eu/taxation_customs/resources/documents/taxation/vat/how_vat_works/rates/study_reduced_vat.pdf).

<p>the risk of a VAT-induced relocation of economic activity, be it production or consumption;</p> <ul style="list-style-type: none"> <li>- initiating a debate on the level of harmonisation and convergence of the VAT rates structure and levels so as to prepare a legislative initiative aimed at balancing subsidiarity and the proper functioning of the Single Market under the 'destination principle' where in particular distortions of competition are avoided;</li> <li>- identifying areas where simplification of the VAT system is needed, in particular for SMEs;</li> <li>- looking for legal, non-legal or technical instruments that could safeguard Member States' VAT revenues by making the EU VAT system more robust, enhancing cooperation between tax administrations and with the Commission, and stepping up the fight against VAT fraud.</li> </ul>
Do the objectives imply developing EU policy in new areas?
No

### C. Options

<p>(1) What are the policy options (including exemptions/adapted regimes e.g. for SMEs) being considered?</p> <p>(2) What legislative or 'soft law' instruments could be considered?</p> <p>(3) How do the options respect the proportionality principle?</p>
<p>As regards the VAT treatment of intra-EU business to business (B2B) supplies of goods, four options have been identified with Member States and business (in addition to maintaining and fine-tuning the current system<sup>25</sup>):</p> <ol style="list-style-type: none"> <li>1. Taxation of intra-EU supplies where the goods are delivered</li> <li>2. Taxation of intra-EU supplies where the customer is established regardless of the place of delivery of the goods</li> <li>3. Reverse charge where the customer is established</li> <li>4. Reverse charge where the goods are delivered</li> </ol> <p>As regards VAT rates policy, the action plan will outline options for reforming the rules on VAT rates which could range from the baseline scenario (no action) to giving Member States full flexibility in rates for as long as they respect EU law (e.g. State Aid rules, fundamental freedoms, protection of consumers). The move away from the principle of taxation at origin towards taxation in the Member State of destination of goods could indeed, amongst other things, entail allowing for a new approach when setting VAT rates as under the destination principle there would no longer be an incentive for business to relocate to Member States with low VAT rates. However, the degree of freedom of Member States in setting VAT rates and its consequences for the Single Market needs to be carefully assessed. For example it could impact on cross-border shopping for certain types of goods purchased by certain acquirers (who cannot fully deduct VAT). The level of convergence and harmonisation of the VAT rates levels and structure needed under a country of destination principle had not been discussed in the Green Paper on the future of VAT. This is an issue which should now be addressed.</p>

### D. Initial assessment of impacts

What are the benefits and costs of each of the policy options?
The in-depth assessment of the benefits and costs of different policy options identified in the Communication will be carried out when preparing the tabling of concrete proposals. Preparatory work is already ongoing in this respect, notably regarding the options for the future VAT treatment of intra-community supplies and acquisitions.
Could any or all of the options have significant impacts on (i) simplification, (ii) administrative burden and (iii) on relations with other countries, (iv) implementation arrangements? And (v) could any be difficult to transpose for certain Member States?
All of the options regarding future initiatives will likely have significant impacts on simplification, administrative burden and implementation arrangements. This initiative is part of the Commission's regulatory fitness (REFIT) programme.

<sup>25</sup> SWD(2014) 338, 29.10.2014

- (1) Will an IA be carried out for this initiative and/or possible follow-up initiatives?
- (2) When will the IA work start?
- (3) When will you set up the IA Steering Group and how often will it meet?
- (4) What DGs will be invited?

An IA will be carried out for all follow-up initiatives that require legislative action.

Preparatory work for impact assessments has already started and the impact assessments themselves and the IA Steering Groups will be set up.

DG Agriculture and Rural Development, DG Budget, DG Communication Networks, Content and Technology, DG Competition, DG Education and Culture, DG Economic and Financial Affairs, DG Energy, DG Environment, DG Financial Stability, Financial Services and Capital Markets Union, the European Anti-Fraud Office, DG Growth, the Joint Research Centre, DG Justice and Consumers, DG Mobility and Transport, DG Regional and Urban Policy, DG Maritime Affairs and Fisheries, Eurostat, , the Secretary General and the Legal Service will be associated to the inter-service steering groups. .

- (1) Is any option likely to have impacts on the EU budget above € 5m?
- (2) If so, will this IA serve also as an ex-ante evaluation, as required by the Financial Regulation? If not, provide information about the timing of the ex-ante evaluation.

(1) Reducing VAT fraud will have some positive impact on the EU budget since VAT is part of Own resources. The precise impact is however difficult to assess due to the calculation method of VAT Own resources and the lack of data on the extent of VAT fraud. Own resources are the EU's revenue. Traditional own resources consist mainly of customs duties on imports from outside the EU and sugar levies. Own resources are also based on VAT and a rate is levied on the harmonised VAT base of each Member State. Moreover, each Member State transfers a standard percentage of its Gross National Income to the EU. The latter has become the largest source of revenue of the EU budget.

(2) Not applicable

### E. Evidence base, planning of further work and consultation

- (1) What information and data are already available? Will existing IA and evaluation work be used?
- (2) What further information needs to be gathered, how will this be done (e.g. internally or by an external contractor), and by when?
- (3) What is the timing for the procurement process & the contract for any external contracts that you are planning (e.g. for analytical studies, information gathering, etc.)?
- (4) Is any particular communication or information activity foreseen? If so, what, and by when?

For certain topics to be addressed in the Action Plan, some economic or technical studies are available: [http://ec.europa.eu/taxation\\_customs/common/publications/studies/index\\_en.htm](http://ec.europa.eu/taxation_customs/common/publications/studies/index_en.htm). Others are already ongoing. Also, a Eurobarometer survey on the general perception of VAT was carried out in October 2014.

Further information will need to be gathered both by public consultation, external contractors and contributions from Member States.

A framework contract for external studies is in place under the Single-Market budget line and will be used to the extent needed for the purpose of analysing more in depth possible aspects that this initiative might identify.

Substantial communication and information activities must be envisaged given the political sensitivity of the envisaged policy initiatives and – depending on the option eventually proposed – the potential significant changes to the current VAT regime.

Which stakeholders & experts have been or will be consulted, how, and at what stage?

A first public consultation and a conference took place in 2011 after the issuance of the Green Paper on the future of VAT.

Also, all stakeholders have been associated to the preparatory work of the key actions set out in the 2011 Communication in particular Member State delegates in the Group on the Future of VAT (GFV)<sup>26</sup> and representatives of business, tax practitioners and academics in the VAT Expert Group (VEG)<sup>27</sup>.

Further public consultations will be carried out for the initiatives launched following the Communication.

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<sup>26</sup> The Group on the Future of VAT provides a forum for discussion with VAT Experts from the Member States on the Commission pre-legislative initiatives and exchange of opinions on the preparation of future VAT legislation.

<sup>27</sup> [http://ec.europa.eu/taxation\\_customs/taxation/vat/key\\_documents/expert\\_group/index\\_en.htm](http://ec.europa.eu/taxation_customs/taxation/vat/key_documents/expert_group/index_en.htm)