REFORM OF RULES ON EU VAT

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Abstract: *In January 2018 the EU has released two proposal designed to simplify the VAT system, specifically around reduced rates, and to reduce compliance costs of smaller businesses in respect of VAT. The EU's common rules on VAT rates do not treat Member States equally. More than 250 exemptions allow several Member States much more flexibility in setting VAT rates than others. While these derogations are due to expire once the reformed VAT system comes into place, the rates proposal will ensure that all Member States have the same flexibility and a uniform structure in which to set their own VAT rates. The second proposal is designed to make trading in other EU member states easier for smaller businesses. Currently, small businesses may benefit from generous thresholds in their state of establishment, but zero thresholds exist for non-established businesses, meaning higher compliance costs. The intended proposals will provide simplification measures (around invoicing, record keeping etc.) for businesses with a turnover not exceeding €2 million and will allow member states to apply thresholds to non-established businesses with a turnover not exceeding €100,000.*

Keywords: *standard rate of VAT, reduced rate of VAT, VAT registration thresholds, VAT compliance, VAT reform*

1. Introduction

The European Union Value Added Tax (EU VAT) applies to all member states. The current VAT system dates from 1993 and was intended to be a transitional system. The abolition of fiscal frontiers between Member States and the taxation of goods in the country of origin required common rules for VAT rates to avoid distortion in cross-border shopping and trade.

The second section of this work gives an overview of the VAT rates, VAT registration and VAT return, applicable this year in each Member States.

A definitive VAT system that works for the Single Market has been a long-standing commitment of the European Commission. The **2016 *VAT Action Plan***[1] explained the need to come to a single European VAT area that is simpler and fraud-proof. Following the adoption of this Action Plan, the European Commission has made a series of proposals to work towards its completion.

In **October 2017** the European Commission agreed on four fundamental principles (named "cornerstones") of a new definitive single EU VAT area:[2]

- **Tackling fraud**: VAT will now be charged on cross-border trade between businesses. Currently, this type of trade is exempt from VAT, providing an easy loophole for unscrupulous companies to collect VAT and then vanish without remitting the money to the government.
- **One Stop Shop:** It will be simpler for companies that sell cross-border to deal with their VAT obligations thanks to a *One Stop Shop*. Traders will be able to make declarations and payments using a single online portal in their own language and according to the same rules and administrative templates as in their home country. Member States will then pay the VAT to each other directly, as is already the case for all sales of e-services.
- **Greater consistency:** A move to the principle of 'destination' whereby the final amount of VAT is always paid to the Member State of the final consumer and charged at the rate of that Member State. This has been a long-standing commitment of the European Commission, supported by Member States. It is already in place for sales of e-services.
- **Less red tape:** Simplification of invoicing rules, allowing sellers to prepare invoices according to the rules of their own country even when trading across borders. Companies will no longer have to prepare a list of cross-border transactions for their tax authority (the so-called 'recapitulative statement').

In **November 2017** the European Commission proposed new rules on administrative cooperation between Member States' administrations in order to fight VAT fraud more efficiently.

In **January 2018** the EU has released a two-fold proposal designed to simplify the VAT system, specifically around reduced rates, and to ease the administrative burden and compliance costs of smaller businesses in respect of VAT. These proposals are detailed in the third section.

2. Overview and comparison of VAT in EU Member States

2.1. VAT rates in EU member states

Each member state's national VAT legislation must comply with the provisions of the Directive no. 112/2006 which sets out a number of general rules on VAT rates. Member States shall apply a standard rate, which may not be lower than 15%, but the Directive does not specify any maximum limit.

[1] http://europa.eu/rapid/press-release_IP-16-1022_en.htm
[2] http://europa.eu/rapid/press-release_IP-17-3443_en.htm

Because VAT rates has not been harmonised, every year the European Commission publishes the official list of VAT rates applied in each member state. ***Table 1*** contains the list of VAT rates for 2018.

Table no. 1. VAT rates in the Member States (01.01.2018)

	Member States	**Standard Rate (%)**	**Super Reduced Rate (%)**	**Reduced Rate (%)**	**Parking Rate (%)**
	Austria	20	-	10/13	13
	Belgium	21	-	6/12	12
	Bulgaria	20	-	9	-
	Croatia	25	-	5/13	-
	Cyprus	19	-	5/9	-
	Czech Republic	21	-	10/15	-
	Denmark	25	-	-	-
	Estonia	20	-	9	-
	Finland	24	-	10/14	-
	France	20	2,1	5,5/10	-
	Germany	19	-	7	-
	Greece	24	-	6,5/13/17	-
	Hungary	27	-	5/18	-
	Ireland	23	4,8	9/13,5	13,5
	Italy	22	4	5/10	-
	Latvia	21	-	12	-
	Lithuania	21	-	5/9	-
	Luxembourg	17	3	8	14
	Malta	18	-	5/7	-
	Netherlands	21	-	6	-
	Poland	23	-	5/8	
	Portugal	23	-	6/13	13
	Romania	19	-	5/9	-
	Slovakia	20	-	10	-
	Slovenia	22	-	9,5	-
	Spain	21	4	10	-
	Sweden	25	-	6/12	-
	United Kingdom	20	-	5	-

Source: https://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/taxation/vat/how_vat_works/rates/vat_rates_en.pdf

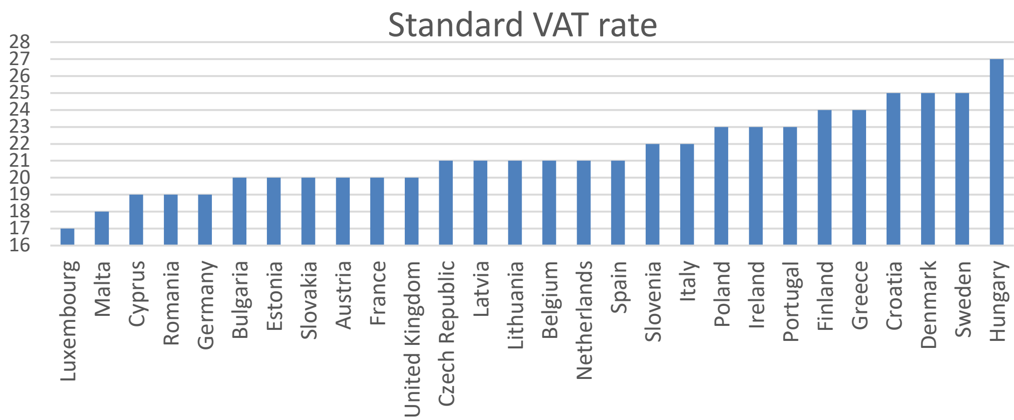
As we see in ***Graph 1*** the country with the lowest **standard rate of VAT** is Luxembourg (17%) while Hungary is the country with the highest standard rate of VAT (27%). In 2018 the average standard rate of VAT in EU28 is 21.46%. In EU15 this rate is 21.67% while in EU13 the average standard rate of VAT is 21.23%.

With the exception of Romania, where the standard rate of VAT has decreased from 20% in 2016 to 19% in 2017, in EU Member States, standard rates have not changed in the last two years.

Regarding **reduced VAT rates,** the differences between Member States are significant: 10 states have one reduced rate, 16 states have two reduced rates, Greece has three reduced rates and Denmark is the single state which doesn't have reduced rate. The minimum reduced rate of 5%, value imposed by European Directives is found in Croatia, Cyprus, Italy, Lithuania, Hungary, Malta, Poland, Romania and United Kingdom. The highest values of reduced rate are found in Hungary (18%), Greece (17%), Czech Republic (15%) and Finland (14%).

These reduced rates of VAT are applied to different categories of goods and services like: food products, water supplies, pharmaceutical products, books, newspapers, hotel accomodation etc.

Graph no. 1. VAT rates in the Member States



Source: https://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/taxation/vat/how_vat_works/rates/vat_rates_en.pdf

Over-reduced rates (under 5%) are applied only in five states: Spain (4%), France (2.1%), Ireland (4,8%), Italy (4%) and Luxemburg (3%), for goods and services as: food products, water supplies, pharmaceutical products, books, admission to cultural services, shows (cinema, theatre, sports), agricultural inputs etc.

A characteristic met among EU countries is represented by the **parking rate**. Member States which, at 1 January 1991, were applying a reduced rate to the supply of goods or services other than those specified in Annex III may apply the reduced rate to the supply of those goods or services, provided that the rate is not lower than 12 %. The parking rate is applied in five Member States (12% in Belgium, 13% in Austria and Portugal, 13.5% in Ireland and 14% in Luxemburg) for certain goods as: certain energy products, wine, agricultural tools and utensils, washing and cleaning products etc.

According to Title VIII, Chapter 4 of the VAT directive 2006/112/EC, the zero rate is applied by seven states: Belgium, Denmark, Ireland, Malta, Finland, Sweden and United Kindom for newspapers, supplies of pharmaceuticals, medicines, supplies of food products for human consumption etc.

2.2. EU VAT compliance

For businesses with an EU VAT registration, and providing taxable supplies of goods or services, there are a number of requirements to follow to ensure they are fully compliant with European VAT regulations. These rules are detailed in the VAT Directive. All member states of the EU must implement these VAT compliance obligations into their own laws.

Companies providing taxable supplies must obtain a valid, unique EU VAT number from their home country. If they are also buying and selling goods in another EU country, they may have to register there, too. This will give them a valid VAT number which they can record all transactions against. Businesses can also provide this number to their foreign EU customers to ensure they are correctly charged nil VAT on intra-community supplies of goods or services.

Table 2 contains a summary of the 2018 VAT registration annual thresholds for **resident** companies in the 28 EU member states. The great variations regarding the annual threshold for VAT registration represent a real trap for those who intend to develop their businesses in different Member States. The threshold varies from zero (Greece, Hungary, Malta, Spain and Sweden) till 85000 euro (UK), so the local advice is necessary even from first stages of a business start-up.

Table no. 2. EU VAT registration thresholds 2018

	Member States	**VAT Thresholds**
1.	Austria	€30,000
2.	Belgium	€25,000
3.	Bulgaria	BGN 50,000
4.	Croatia	HRK 300,000
5.	Cyprus	€15,600
6.	Czech Republic	CZK 1million
7.	Denmark	DKK 50,000
8.	Estonia	€40,000
9.	Finland	€10,000
10.	France	Goods €82,800; Services €33,200
11.	Germany	€17,500
12.	Greece	nil
13.	Hungary	nil
14.	Ireland	Goods €75,000; Services €37,500
15.	Italy	€60,000
16.	Latvia	€40,000
17.	Lithuania	€45,000
18.	Luxembourg	€30,000
19.	Malta	nil
20.	Netherlands	€1,345
21.	Poland	PLZ 150,000
22.	Portugal	€12,500
23.	Romania	ROL 300,000
24.	Slovakia	€49,790
25.	Slovenia	€50,000
26.	Spain	nil
27.	Sweden	nil
28.	United Kingdom	£85,000

Source: https://www.vatlive.com/eu-vat-rules/eu-vat-number-registration/vat-registration - threshold/?sessionId=1522776716266&referrer=https%3A%2F%2Fsearch.yahoo.com%2F &lastReferrer=www.vatlive.com

EU Member States are free to set their own calendars for VAT return reporting, as we see in ***Table no. 3***. Countries typically follow the format below:

- **Monthly** reporting is the most common cycle.
- **Quarterly** reporting is the majority of other situations.
- **Annual** reporting is required in addition in certain countries (e.g. Italy). Other countries may only require a single annual return if there is very limited activity (e.g. Germany).
- **On an activity basis** which is very rarely allowed (e.g. France) for companies with irregular trading.

Irrespective of the period of submission, the mandatory information of VAT return are: chargeable VAT, deductible VAT, net VAT amount (payable or receivable), total value of input transactions and total value of output transactions.

Table no. 3. VAT Return

	Country	**Periodicity of VAT returns**	**Annual VAT declaration deadline**
1.	Austria	Monthly / Quarterly	April
2.	Belgium	Monthly / Quarterly	Not Applicable
3.	Bulgaria	Monthly	Not Applicable
4.	Croatia	Monthly / Quarterly	Not Applicable
5.	Czech Republic	Monthly / Quarterly	Not Applicable
6.	Cyprus	Quarterly	Not Applicable
7.	Denmark	Monthly / Quarterly	Not Applicable
8.	Estonia	Monthly	Not Applicable
9.	Finland	Monthly / Quarterly / Annually	Not Applicable
10.	France	Monthly / Quarterly / Annually	Not Applicable
11.	Greece	Monthly / Quarterly	May, 10
12.	Germany	Monthly / Quarterly	May
13.	Hungary	Monthly / Quarterly / Annually	Not Applicable
14.	Ireland	Biannually / Quarterly / Annually	Not Applicable
15.	Italy	Annually	Not Applicable
16.	Latvia	Monthly / Quarterly / Biannually	1 May
17.	Lithuania	Monthly / Biannually	Not Applicable
18.	Luxembourg	Monthly / Quarterly / Annually	May
19.	Malta	Quarterly / Annually	March
20.	Netherlands	Monthly / Quarterly / Annually	March
21.	Poland	Monthly / Quarterly	Not Applicable
22.	Portugal	Monthly / Quarterly	15th July
23.	Romania	Monthly / Quarterly / Biannually / Annually	Not Applicable
24.	Slovenia	Monthly / Quarterly	Not Applicable
25.	Slovakia	Monthly / Quarterly	Not Applicable
26.	Spain	Monthly / Quarterly	January
27.	Sweden	Monthly / Quarterly / Annually	Not Applicable
28.	United Kingdom	Monthly / Quarterly / Annually	Not Applicable

Source: http://europa.eu/rapid/press-release_MEMO-13-926_en.htm

3. Reform of rules on EU VAT

On January 18th of 2018, the European Commission made two proposals to improve the EU VAT system:

- Equal treatment of Member States in setting VAT rates;
- Elimination of foreign EU VAT obligations for small enterprises.

3.1. Equal treatment of Member States in setting VAT rates

At the moment, VAT rules agreed by all EU countries allow for two distinct categories of products to benefit from a reduced VAT rate of as low as 5% in each country. A number of Member States also apply specific derogations for further reduced rates.

The proposed definitive regime is based on taxation at destination instead of origin, as initially envisaged. Restrictive rules on the application of rates are therefore no longer essential to avoid distortion of competition.

The new rules will give all EU Member States flexibility to apply the following reduced rates to products and services:

- 2 separate rates to be set between 5% and the standard rate
- 1 rate to be set between 0% and the reduced rates
- 1 rate of 0%

The current list of goods and services to which reduced rates can be applied will be abolished and replaced by a new list of products to which the standard rate of minimum 15% must always be applied. This list will include products such as alcoholic beverages, gambling, smartphones, precious metals, consumer electronics, weapons, household appliances, tobacco products, fuel, petrol & diesel, weapons, passenger vehicles.

Synthesising, the difference between the current rules and the new rules is reproduced in the table below:

Current rules	New rules
System based on exceptions	System based on general rules
No uniform application of rules	Uniform application across the EU

To safeguard public revenues, Member States must also ensure that the weighted average of all VAT rates applied is at least 12%.

3.2. Elimination of foreign EU VAT obligations for small enterprises.

On 18 January 2018, the European Commission proposed exempting small enterprises (SMEs) from cross-border VAT obligation.

Currently, EU small businesses selling in their own country are exempt from VAT if their sales are below a set threshold. This threshold varies between member states, e.g. €10,000 in France; and £85,000 in the UK. However, when selling in other EU states, SME’s must register and charge local VAT on the first sale. This imposes a VAT compliance cost on small companies and restricts the free operation of the Single Market for SME's.

The EU is now proposing:

- 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 which would allow companies operating in more than one Member State to benefit from the VAT exemption

4. Conclusions

Under the current EU VAT directive, Member States have the option of applying a maximum of two reduced rates, not lower than 5% to a fairly restricted list of goods and services, which are listed in Annex III of the VAT Directive. Examples of these categories include foodstuffs, water supplies, admission to sporting events and medical care.

Existing reduced rates and derogations will expire upon the introduction of the definitive VAT regime (still being negotiated), and at this time new harmonised and flexible rules will be introduced. In summary, these are:

- Standard rates must remain at 15% or above
- Member states may introduce two reduced rates between 5% and 15%
- Member states will be permitted to implement one zero rate
- A further reduced rate between 0% and 5% may be implemented

In addition to the above, the restrictive list of goods and services to which the reduced rate may apply will be removed, and in its place will be a list of the goods and services to which a reduced rate cannot apply (items such as alcohol, tobacco, smartphones, fuel, precious metals etc.).

The second proposed measure follows up on the *VAT Action Plan towards a single EU VAT area*[3] presented in April 2016 and *the Plans for the biggest reform of EU VAT rules*[4] proposed by *European Commission* in October 2017. Businesses trading cross-border currently suffer from 11% higher compliance costs compared to those trading only domestically. The intended proposals will provide simplification measures (around invoicing, record keeping etc.) for businesses with a turnover not exceeding €2 million and will allow member states to apply thresholds to non-established businesses with a turnover not exceeding €100,000.

These legislative proposals will now be submitted to the European Parliament and the European Economic and Social Committee for consultation and to the Council for adoption.

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[3]http://europa.eu/rapid/press-release_IP-16-1022_en.htm
[4]http://europa.eu/rapid/press-release_IP-17-3443_en.htm

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[1] http://europa.eu/rapid/press-release_IP-16-1022_en.htm

[2] http://europa.eu/rapid/press-release_IP-17-3443_en.htm

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[4] https://www.vatlive.com/eu-vat-rules/eu-vat-number-registration/vat-registration-threshold/?sessionId=1522776716266&referrer=https%3A%2F%2Fsearch.yahoo.com%2F&lastReferrer=www.vatlive.com

[5] http://europa.eu/rapid/press-release_MEMO-13-926_en.htm