



Introducing the definitive VAT system for B2B cross-border goods trade

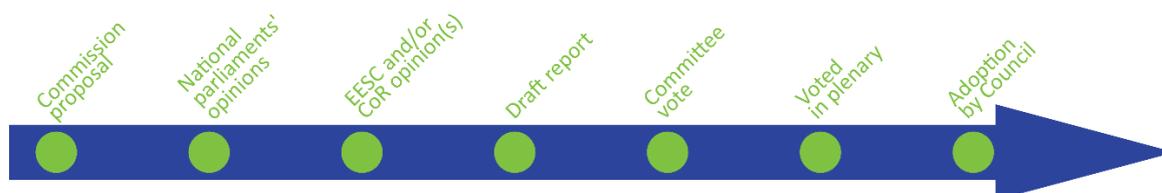
OVERVIEW

Value added tax (VAT) is a consumption tax borne by the final consumer. It is an important source of revenue for national governments and the European Union (EU) budget. However, the existing rules governing intra-Community trade are 25 years old and the current common EU VAT system is still 'transitional'. This framework presents problems such as vulnerability to fraud, compliance costs for businesses and also a heavy administrative burden for national authorities. It is under review along the lines of the April 2016 VAT Action Plan.

The reform of the VAT framework towards a definitive VAT system for intra-Community business-to-business (B2B) transactions is planned in several consecutive steps. The first step focuses on B2B transactions in goods, while the second one in services. Directive 2018/1910, adopted on 4 December 2018, was put forward by the Commission in October 2017 as part of the 'definitive VAT system package'. The directive amends the VAT Directive (Directive 2006/112/EC) so as to introduce the basic features of the definite VAT system for business-to-business (B2B) goods transactions.

Proposal for a Council Directive amending Directive 2006/112/EC as regards harmonising and simplifying certain rules in the value added tax system and introducing the definitive system for the taxation of trade between Member States

<i>Committee responsible:</i>	Economic and Monetary Affairs (ECON)	COM(2017) 569 4.10.2017
<i>Rapporteur:</i>	Jeppe Kofod (S&D, Denmark)	2017/0251(CNS)
<i>Shadow rapporteurs:</i>	Ivana Maletić (EPP, Croatia) Sander Loones (ECR, Belgium) Thierry Cornillet (ALDE, France) Dimitrios Papadimoulis (GUE/NGL, Greece) Molly Scott Cato (Greens/EFA, United Kingdom) Barbara Kappel (ENF, Austria)	Consultation procedure (CNS) – Parliament adopts a non-binding opinion
<i>Procedure completed.</i>	Council Directive (EU) 2018/1910 OJ L311, 7.12.2018, pp. 3-7	



Introduction

Value added tax (VAT) was implemented for the first time in France in the 1950s.¹ In 1967, the members of the then European Economic Community [agreed](#) to replace all turnover taxes with VAT and to have a common value added tax system. It has become an important source of revenue, both for national administrations and as an own resource of the EU budget. VAT represents 7.1 % of GDP ([Eurostat](#), 2017).

The European common VAT system was agreed prior to the 1992 completion of the internal market as a compromise that made it possible to remove internal borders. The VAT framework that is currently under review has become known as 'the transitional VAT system'. It was set up until a definitive destination-based system could be established. It departed from the fundamental principle in international taxation that indirect taxes on consumption are charged in the country in which the goods and services are consumed. The transitional VAT system is generally found to be complex and to have significant compliance costs, as well as generating room for fraud.

Context

VAT framework

VAT is a [consumption tax](#) borne by the final consumer. At the core of the current [EU VAT framework](#) is Council [Directive 2006/112/EC](#) of 28 November 2006 on the common system of value added tax (the VAT Directive), which gathers into one piece of legislation all the amendments to the original (1977) Sixth VAT Directive.

VAT is charged on the supply of goods and services by a taxable person, unless specifically exempted. The business supplying goods or services (as a VAT taxable person) collects the VAT paid by the consumer, while being able to deduct from the VAT they have collected the amount of tax they have paid to other taxable persons on purchases for their business activities. The additional value of each transaction is collected at each stage of production and distribution (difference between the output VAT and input VAT) and this generates the VAT that is due to the tax authorities.

According to the transitional system, a cross-border transaction of goods between taxable persons consists of two parts: a supply of goods in the Member State of departure that is exempt from VAT, and an acquisition of goods liable to VAT in the Member State of destination. The VAT exempt supply breaks the chain of fractioned payments. Both the supplier and the acquirer of the goods should inform the tax authorities of their respective Member State about the transaction, but this does not occur in all cases. The current system is thus vulnerable to fraud as, for instance, the acquirer can subsequently sell the VAT-free goods, charge the VAT to their customer and disappear without paying the VAT to the tax authorities. This is an example of [missing trader intra-Community fraud](#) or '[carousel](#) fraud'.

It is only relatively recently, drawing on the experience of the electronic services regime, the 'mini-one-stop-shop' ([MOSS](#)) as from 2015, that the change to a definitive VAT system operating within the European Union in the same way as it would in a single country was deemed possible.

Reboot of the VAT framework

In April 2016, the Commission adopted an [action plan on VAT](#) that sets out the modifications to be adopted to review and update the VAT framework. The 'rebooting' of the VAT system involves: setting up the definitive VAT regime for cross-border trade; tackling VAT fraud; updating the framework for VAT rates; simplifying and modernising VAT rules for e-commerce; and updating the VAT rules specific for SMEs. A number of legislative proposals amending the VAT legal framework have been put forward, in several instalments since then to implement the VAT action plan. A number of them were adopted in 2017 and 2018.

One important component of the plan is the reform leading towards a definitive VAT system for intra-Community business-to-business (B2B) transactions, i.e. transactions where all the parties involved are taxable persons.

The definitive VAT system for B2B transactions is organised in two legislative steps: the first step addresses the VAT treatment of intra-EU B2B supplies of **goods**, and the second step supplies of **services**. The first legislative step was, in turn, split in two sub-steps. The 4 October 2017 [single VAT area](#) package was the first of these sub-steps. The second sub-step introduces the detailed **technical provisions** for the actual implementation of the definitive VAT system with a [proposal](#) submitted on 25 May 2018. The Commission indicated in its [communication](#) of the same day that the extension of the definitive VAT system to the supply of services is scheduled for after the first evaluation of the implementation of the new VAT system for the supply of goods.²

Existing situation

The current common VAT system is made of VAT provisions and administrative cooperation provisions in the field of VAT (extending to the fight against fraud). The [VAT legal framework](#) consists of the [VAT Directive](#) (2006/112/EC), the [implementing regulation](#) (282/2011 ensuring uniform application of the VAT Directive) and the [VAT Administrative Cooperation Regulation](#) (904/2010). The ongoing review of the VAT framework means mainly amending those instruments.

The transitional nature of VAT is set out in Article 402 (1) of the VAT Directive, which specifically states that the current VAT system is transitional and has to be replaced by a definitive system in which taxation will occur according to the legislation of the country of origin of the goods or services, i.e. using **the origin principle**.

Title III (Articles 9 to 13) of the VAT Directive defines the concept of [taxable person](#) as any person who engages independently in economic activity, without assessing if the person is a reliable taxpayer or not. Taxable persons are identified by a VAT identification number (Articles 214 to 216 of the VAT Directive).

As regards specific provisions for which changes were requested by the Council in order to make it simpler and less prone to fraud, in its conclusions of [8 November 2016](#), the situation in these areas prior to the adoption of the directive, is described below:

Call-off stock arrangements – This is a cross-border transaction where a supplier sends the goods to stock on their own property located in the Member State of the acquirer, in order to make them available for the acquirer. The transfer of rights occurs at the moment the acquirer takes the goods out of stock.

Under the current rules, the transfer of the goods to stock is a VAT-exempt supply, while the arrival of the goods in stock is considered a VAT-liable acquisition by the same business that is selling the goods. Therefore this business is obliged to have a VAT registration number in the Member State of arrival of the goods. When the customer takes the goods out of stock, it is considered a second supply, which takes place in the Member State of the customer and is liable to VAT according to the rules of that country. Because this system is quite cumbersome, some Member States simplify the process in different ways, while others do not, a fact that makes it even more complicated for businesses while adding more heterogeneity to the application of VAT rules in the Union.

VAT identification number – Under the current rules the acquirer is obliged to be registered for VAT purposes, to inform the supplier of their [VAT identification number](#) and to declare the acquisition of goods to the tax authorities of their country. The supplier, in turn, has the obligation to submit a recapitulative statement of the transaction, which includes the VAT number of the acquirer and is sent to and included in the [VIES](#). The tax authorities of the Member State of destination can thus cross-check the information provided by the two parties. In practice, these obligations only work as a formality because the provision of a VAT information number is not a substantive requirement. Therefore, Member States can only fine the fraudsters or impose

administrative sanctions on them if they do not fulfil the requests, but they are not able to refuse the exemption.

Chain transactions – A chain transaction is defined as successive supplies of the same goods by means of a single intra-Community transport operation between two Member States. Current legislation and [a judgment](#) of the Court of Justice establish that the transport of the goods should be ascribed to one supply operation in the chain in order to grant the VAT exemption. If the transport operation has been carried out by or on behalf of the first supplier or the last taxable person in the chain, the issue of attribution is clear, but there is a need to clarify which part of the chain is the relevant supply operation when the transport operation has been carried out by or on behalf of one of the intermediate suppliers.

Parliament's starting position

The Parliament's [resolution of 13 October 2011 on the future of VAT](#) and its resolution of 24 November 2016 entitled [Towards a definitive VAT system and fighting VAT fraud](#), called for the modernisation of the VAT system, strengthened cooperation in the fight against VAT fraud and reducing the VAT gap.

In 2016, Parliament welcomed the Commission's announcement to propose a definitive VAT system by 2017 and supported the objective of making it simple, fair, robust, efficient and less susceptible to fraud, emphasising that a simple VAT system with few exemptions would help with the proper functioning of the digital single market. It also supported the implementation of the **destination principle**, with the application of the rate of the country of destination. Moreover, it noted that the certified taxable person concept and the one-stop shop were essential components of this model.

Council's starting position

In [its conclusions on the future of VAT of 15 May 2012](#) the Council supported the Commission's objective of a EU VAT system that is '[simpler, more efficient and neutral, robust and fraud-proof](#)' and acknowledged the need to simplify the current system in order to reduce compliance costs and administrative burdens both for businesses and for national tax administrations. It then invited the Commission to study possible ways of implementing the destination principle.

In the [conclusions of 25 May 2016](#) it agreed on the need to modernise and improve the EU's VAT system with those objectives in mind and it underlined that it was 'possible and necessary' to improve the current system in the short term.

Finally, and considering that the reforms needed to achieve a definitive VAT system would take some time, in [the conclusions of 8 November 2016](#), it asked the Commission to present proposals to amend the current VAT system with regard to the following four aspects: (1) requiring that the person acquiring the goods in the case of an intra-EU supply has a valid VAT identification number in order to be granted a VAT exemption; (2) proposing uniform criteria and appropriate legislative improvements to increase the legal certainty around the VAT treatment of chain transactions, including triangular transactions; (3) modifying the current VAT rules in order to allow the ongoing simplification of the rules regarding call-off stock arrangements at national level to be applied in a more uniform manner in the EU, and (4) unifying the criteria for the documentation needed to claim an exemption in an intra-Community supply operation. The present proposal addresses the first three requirements, while the fourth requires a change in the VAT Implementing Regulation.³

Preparation of the proposal

The [proposal](#) was part of a package of three proposals ('the October 2017 definitive VAT system package'), representing the first sub-step on the way to the definitive VAT system for B2B transactions, the objectives of which are to:

- tax the sales of goods and services between EU countries in the same way as domestic sales;

- reduce the VAT gap due to fraud by €40 billion. The total VAT gap is estimated to be €147.1 billion,⁴ including VAT fraud;
- make the system more robust and simple; and
- reduce business compliance costs, which are now 11 % higher for cross-border transactions than for domestic trade, by €1 billion.

The two other proposals included in the October 2017 package are:

1. A [proposal amending Regulation \(EU\) No 904/2010 as regards the certified taxable person](#), which includes the notion of certified taxable person (CTP) on the VAT information exchange system (VIES).⁵
2. A [proposal amending Implementing Regulation \(EU\) No 282/2011 as regards certain exemptions for intra-Community transactions](#), requiring a proof of intra-Community transport in order to grant an exemption (this proposal is the response to the fourth change to the current system required by the Council).

The changes the proposal would bring

On 4 October 2017, the Commission adopted proposals to amend the VAT framework. The [proposal](#) for a Council directive amending the VAT Directive (2006/112/EC) introduces the 'certified taxable person' (CTP), by analogy with the '[authorised economic operator](#)' (AEO) in the EU Customs Code, allowing a taxpayer to be considered as reliable when meeting certain conditions. It also provides remedies to shortcomings as requested by the Council (the quick fixes). Finally it introduces the legal cornerstone of the definitive VAT system: the destination principle, with the one stop shop (OSS) through which suppliers need to register once for their transactions in the European Union, based on the extension of the existing MOSS for electronic services.

While this system is being adopted and implemented, businesses will use the reverse charge mechanism,⁶ i.e. the acquirer, who will from now on be required to be a certified taxable person, will pay the VAT.

Provisions moving towards the definitive VAT system

- Change of the heading of Chapter 1 of Title XV to 'Definitive arrangements for the taxation of trade between Member States'
- Amendment of Article 402 to replace the principle of origin with the principle of destination of goods and services
- Establishment of the liability of the supplier, or the acquirer if they are a certified taxable person
- Extension of the existing mini one-stop-shop (MOSS) to a general single registration scheme for the declaration, payment and deduction of the tax, also called a one-stop-shop
- Deletion of Articles 403 and 404

The new article 13a introduces the concept of the '**certified taxable person**'. A taxpayer who complies with a number of requirements will be considered a reliable taxpayer and granted the status of certified taxable person. Only taxable persons will be eligible, and they will have access to certain simplification rules in those operations where there is greater risk of fraud. The introduction of this concept will pave the way for a gradual transition to the definitive VAT system.

The proposal introduces a new article 17a, which defines a **call-off stock arrangement** and states that if a certified taxable person transfers their own goods to another Member State under that kind of arrangement, that transfer will not be considered a supply of goods. In addition, it adds a paragraph 3 to Article 243, stating that all certified taxable persons have to keep registers of the goods supplied to them or transferred by them. Finally, it amends Article 262, adding the obligation

for certified taxable persons supplying goods to identify the certified taxable persons acquiring goods under call-off stock arrangements.

The proposal amends Article 138(1) so the requirement that the acquirer have a valid **VAT identification number** and that the supplier file the VIES documents in a correct manner become substantive conditions for the exemption. It allows a tax administration to reject an exemption if these requirements are not met.

In order to clarify the situation as regards **chain transactions**, the proposal introduces a new article 138a. This states that when the transport operation has been carried out by or on behalf of an intermediary, if the intermediary has a VAT number in a Member State other than the country of origin of the goods *and* has informed their supplier of the country of destination of the goods, the transport operation will be ascribed to the supply operation made to them. Otherwise, the transport operation will be attributed to the following stage of the chain i.e. the supply operation carried out by them.

Advisory committees

On 14 March 2018, the European Economic and Social Committee (EESC) adopted its [opinion on the VAT reform package \(I\)](#), which includes the proposal. It welcomed the Commission proposal and the proposed changes, including the creation of the certified taxable person concept and the simplification of procedures for taxable persons enjoying this status. Finally, it recommended making the transition to the definitive system for goods and services quickly, so that the existence of two parallel systems is limited in time.

National parliaments

The [subsidiarity deadline](#) for national parliaments to submit comments on the proposals was 12 December 2017. No reasoned opinions were submitted but the German [Bundesrat](#)⁷, the Senate of the [Czech Republic](#)⁸ and the [two chambers](#) of the Romanian Parliament⁹ made contributions.

Stakeholder views¹⁰

Stakeholders expressed their views in the consultation relating to the proposal referred to above. BusinessEurope published [a position paper](#) on the proposal 21 December 2017 in which it stressed concerns regarding among others the possible increase compliance costs for business.

Legislative process

In the **European Parliament**, the proposal was assigned to the Economic and Monetary Affairs Committee (ECON) (Rapporteur: Jeppe Kofod, S&D, Denmark).

On 3 September 2018, Parliament's Committee on Economic and Monetary Affairs (ECON) adopted its [report](#) on the proposal, which was subject to the consultation procedure. The amendments aimed at clarifying the CTP (namely specifying further the grounds for refusal) and ensuring consistency with the authorised economic operator (AEO) status as defined by the EU Customs Code, providing for a VAT dispute-resolution mechanism between Member States, introducing an automated notification mechanism to taxpayers on changes and updates in applicable VAT rates of Member States, ensuring that specificities of SMEs are taken into account and strengthening monitoring and reporting under the directive.

The 21 November 2018 [Commission response](#) to the text subsequently adopted in [plenary](#) provided explanations on how the amendments were taken into account. In particular, as regards amendments relating to the notion of certified taxable person and the cornerstones of the VAT definitive VAT system, it was [agreed](#) that the issues would be discussed by the Council in the context of the negotiations of [the proposal on the technical details of the definitive system of 25 May 2018](#) that is still pending.

As for the amendments relating to a VAT dispute-resolution mechanism between Member States, the Commission recognised its importance, but suggested that it relates, not to the VAT Directive but to separate legislation on administrative cooperation and mutual assistance. The same applies to other amendments, in particular relating to automated notifications.

In the **Council**, the proposal was discussed at working party level (Working Party on Tax Questions – Indirect Taxation – VAT). The Council discussed the proposal on [20 June 2018](#).

The Council adopted the directive ([Council Directive \(EU\) 2018/1910](#)) amending Directive 2006/112/EC as regards the harmonisation and simplification of certain rules in the value added tax system for the taxation of trade between Member States on [4 December 2018](#). It entered into force on 27 December 2018. As explained above, some elements of the proposals were agreed to be discussed in the framework of the discussion of the [VAT technical details proposal](#). As adopted, the directive covers three of the 'quick fixes' that will apply until the definitive VAT system is implemented.¹¹

The rules of the amended directive are to be adopted and published by Member States by 31 December 2019 and applied no later than 1 January 2020.

EP SUPPORTING ANALYSIS

Remáč M., [Definitive VAT system and fighting VAT fraud](#), EPRS, Implementation Appraisal, European Parliament, October 2017.

OTHER SOURCES

[Value added tax \(VAT\) system: harmonising and simplifying certain rules and definitive system for the taxation of intra-Union trade](#), Legislative Observatory (OEL), European Parliament.

ENDNOTES

- ¹ See A. Charlet and J. Owens, '[An International Perspective on VAT](#)', in *Tax Notes International*, Vol. 59, No 12, September 2010.
- ² A state of play of the VAT reboot can be read in a 2019 article Merckx M and Gruson J. 'Definitive VAT regime: ready for the next step?', *EC Tax Review*, 2019/3.
- ³ Changes in implementing regulations follow non-legislative procedures.
- ⁴ The latest [VAT gap estimate](#) dates from 2018 for the year 2016. The estimation of VAT fraud and compliance costs was made in '[Implementing the 'destination principle' to intra-EU B2B supplies of goods – Feasibility and economic evaluation study](#)', 2015.
- ⁵ [Legislative procedure 2017/0248 \(CNS\)](#), see separate '[EU Legislation in Progress](#)' briefing.
- ⁶ In the reverse charge mechanism, the acquirer is liable for the VAT on goods and services supplied to them. An [amendment to the VAT Directive](#) generalising its use was adopted in October 2018.
- ⁷ The Bundesrat expressed concerns about the effectiveness of the concept of certified taxable persons.
- ⁸ The Czech Senate disagreed on simplified procedures being accessible only to certified taxable persons. It considered that the two-step timing of the proposals: a first step for the principles (the present proposal) and a second for the technical provisions, did not respect the principles of good legislation.
- ⁹ The Romanian Chamber of Deputies and the Romanian Senate stressed the fact that the administrative capacity of national tax administrations differed across the EU.
- ¹⁰ This section aims to provide a flavour of the debate and is not intended to be an exhaustive account of all different views on the proposal.
- ¹¹ The fourth 'quick fix' on documentary evidence is implemented by a change in the VAT Implementing Regulation.

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eprs@ep.europa.eu (contact)

www.eprs.ep.parl.union.eu (intranet)

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