

Detailed technical measures for the definitive VAT system for cross-border goods trade

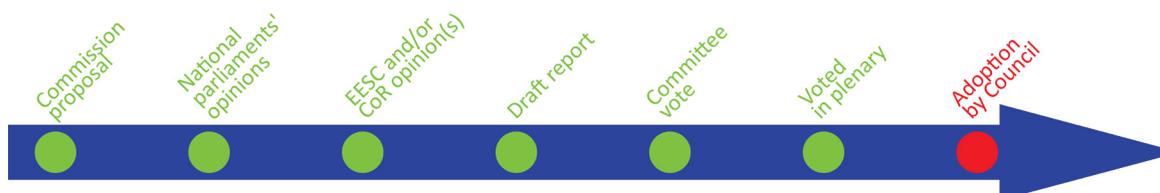
OVERVIEW

The common European value added tax (VAT) system was set up in 1967, and reformed in 1993, to adapt it to the entry into force of the European Union (EU) internal market. The existing rules governing intra-Community trade were therefore intended to be transitory. While VAT has become an important source of revenue for both national governments and the EU budget, the current system is ill-adapted to the challenges of a modern economy.

A substantial review was initiated as from 2016, to update the EU VAT system and make it less vulnerable to fraud, as described in the April 2016 VAT action plan. The proposal, adopted on 25 May 2018, would amend the VAT Directive (Directive 2006/112/EC), to introduce detailed technical measures for the definitive VAT system for intra-EU business to business (B2B) trade in goods. The present proposal follows and complements the adoption of Council Directive (EU) 2018/1910 on 4 December 2018. The Parliament adopted its position on the proposal on 12 February 2019; the Council has yet to finalise its position.

Proposal for a Council directive amending Directive 2006/112/EC as regards the introduction of the detailed technical measures for the operation of the definitive VAT system for the taxation of trade between Member States

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|-------------------------------|--|---|
| <i>Committee responsible:</i> | Economic and Monetary Affairs (ECON) | COM(2018) 329 25.5.2018 |
| <i>Rapporteur:</i> | Fulvio Martusciello (EPP, Italy) | 2018/0164(CNS) |
| <i>Shadow rapporteurs:</i> | Jeppe Kofod (S&D, Denmark) Roberts Zīle (ECR, Latvia) Thierry Cornillet (ALDE, France) Matt Carthy (GUE/NGL, Ireland) Molly Scott Cato (Greens/EFA, United Kingdom) Barbara Kappel (ENF, Austria) | Consultation procedure (CNS) – Parliament adopts a non-binding opinion |
| <i>Next steps expected:</i> | Adoption by the Council | |



Introduction

Value added tax (VAT) is a [consumption tax](#) borne by final consumers. The European common VAT system was agreed prior to the 1992 completion of the internal market as a compromise permitting the abolition of internal frontiers. The VAT framework currently under review is known as 'the transitional VAT system', as 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 considered complex and to have significant compliance costs, as well as generating room for fraud. VAT has become an important revenue source, both for national administrations and as an EU budget own resource. It represents 7.1 % of EU GDP (Eurostat, 2017).

As part of the [action plan on VAT](#), the European Commission prepared several packages of proposals with the objective of adapting the common value added tax system. In October 2017, it adopted a 'definitive VAT system [package](#)', which is the first step on the path to a definitive VAT system for B2B transactions for goods, including two legislative proposals, both of which were adopted at the end of 2018 and are complemented by the 25 May 2018 proposal.

Context

Value added tax framework

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 all the amendments to the original (1977) Sixth VAT Directive in one piece of legislation.

Unless specifically exempted, VAT is charged on the supply of goods and services by a taxable person. 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 output VAT and input VAT), and this generates the VAT that is due to the tax authorities.

When the transitional system entered into force in 1993, Member States agreed that the definitive system should be based on the origin principle: taxation would occur in accordance with the legislation of the country of origin. 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 of 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 that is one of the main features of VAT. 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. Initially planned for four years, the transitional system continues to this day.¹ Nevertheless, the current system is 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 (an example of [missing trader intra-community](#) (MTIC) fraud or '[carousel](#) fraud').

The change to a definitive VAT system operating within the EU in the same way as it would in a single country took place only recently. This advance became possible through the 2015 launch of the electronic services regime, the 'mini-one-stop-shop' ([MOSS](#)).

Reboot of the value added tax framework

In April 2016, the European 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. Since then, a number of legislative proposals amending the VAT legal framework have been put forward, in several instalments, 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 will address the VAT treatment of intra-EU B2B supplies of goods, and the second step will address supplies of services. The first legislative step will, in turn, be split in two sub-steps. The 4 October 2017 [single VAT area](#) package is 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 the [proposal](#) adopted on 25 May 2018. In its [communication](#) of the same day, the European Commission indicated that the extension of the definitive VAT system to the supply of services is scheduled to follow the first evaluation of the implementation of the new VAT system for the supply of goods.²

Current situation

The current common VAT system incorporates VAT 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 \(282/2011\)](#) as amended since its adoption, it ensures uniform application of the VAT Directive); and the [VAT Administrative Cooperation Regulation \(904/2010\)](#) as amended since its adoption). The ongoing review of the VAT framework largely involves amending these instruments.

In the current transitional VAT system, the cross-border trade of goods in B2B transactions is split into two operations: an exempt supply in the Member State of departure of the goods and an intra-community acquisition taxed in the Member State of arrival.

The October 2017 [definitive VAT system package](#) provided for the introduction of the definitive VAT system for goods in B2B cross-border transactions by way of an amendment to the VAT framework, which is referred to as the first sub-set of measures. [Amendments to the VAT Directive](#) by [Council Directive \(EU\) 2018/1910](#) introduce three of the 'quick fixes' that will apply until the definitive VAT system is implemented.³ Amendments to the administrative cooperation regulations on VAT aim at [bolstering cooperation](#) between Member States, enhancing cooperation between tax authorities and law enforcement bodies, and cross-border refunds, as well as adding measures specifically tackling the main types of cross-border fraud schemes, through both the 2 October 2018 [Regulation 2018/1541](#) and 4 December 2018 [Regulation 2018/1909](#).

Once these proposals are adopted, measures are planned to address the identified shortcomings through 'quick fixes', as well as others preparing for the move to the definitive VAT system, which are not yet applied.

Parliament's starting position

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

In 2016, Parliament welcomed the Commission's announcement that it would 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 ease the proper functioning of the digital single market. Moreover, it noted that the concept of 'certified taxable person' was an essential component of this model.

Council's starting position

In its [conclusions](#) on the future of VAT of 14 May 2012, the Council supported the European Commission's objective of an EU VAT system that is '[simpler, more efficient and neutral, robust and fraud-proof](#)' and acknowledged the need to simplify the current system to reduce compliance costs and administrative burdens both for businesses and for national tax administrations.

In its [conclusions](#) of 25 May 2016, Council agreed on the need to improve administrative cooperation between national tax administrations, including by reinforcing the automatic exchange of information. Council also 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 its [conclusions](#) of 8 November 2016, Council asked the European Commission to present proposals to amend the current VAT system, in particular with regard to four aspects that would become known as the '[quick fixes](#)'.

Preparation of the proposal

As an element of the 'reboot' of the EU VAT framework, and more precisely as the review of B2B cross-border trade, the proposal was prepared in the context of the European Commission debate '[On the future of VAT – Towards a simpler, more robust and efficient VAT system](#)', launched in 2010. A wide [consultation](#), the 2011 [On the future of VAT – Towards a simpler, more robust and efficient VAT system tailored to the single market](#), set out the desirable features of the definitive system and the priorities for the years ahead.

The April 2016 [action plan on VAT](#) drew up the modifications to be adopted to review and update the VAT framework as a whole. One of its pillars was the definitive VAT regime for cross-border trade, which splits into two stages, starting with cross-border trade for goods. This stage was divided in two sub-steps. The first, dating back to October 2017, was a 'definitive VAT system [package](#)', now completed. The second sub-step of the introduction of the definitive VAT system for B2B cross-border trade in goods, the 25 May 2018 [proposal](#), introduces the detailed **technical provisions** for the actual implementation of the definitive VAT system for intra-Union trade in goods. Consultations during negotiations on the package covered both the October 2017 and May 2018 proposals.

Changes the proposal would bring

[Council Directive \(EU\) 2018/1910](#) laid the foundations for the definitive VAT system for business-to-business (B2B) cross-border trade in goods. The [proposal](#) analysed in this briefing supplements the Directive by providing the detailed technical measures to allow for the establishment of a definitive VAT system for B2B transactions for goods. Articles referred below refer to the VAT Directive as it would be amended by the proposal. The main changes are outlined below.

The proposal aims to replace the current two-transaction system – the exempt supply of goods and the VAT-liable intra-community acquisition – with a single-transaction system: taxed intra-Union supply of goods. Therefore, all references to 'intra-Community acquisition', including entire chapters, throughout the VAT Directive (Articles 2 to 4) would be deleted.

Moreover, Article 14 would be amended to introduce the concept of '**intra-Union supply of goods**'. Paragraph 5 of Article 14 would exclude certain supplies of goods from this definition: (i) the supply of goods with assembly or installation pursuant to Article 36, (ii) the supply of goods that are exempt under Articles 148 and 151 (inter alia referring to goods for the fuelling and provisioning of certain vessels and aircraft, goods in diplomatic and consular arrangements and goods for international organisations), and (iii) the supply of goods by a taxable person covered by the common flat-rate scheme for farmers.

A new Article 35a would establish the place of supply of an intra-Union supply of goods as the place where the transport of the goods to the customer ends. This provision, combined with the amendment of Article 14, would establish the application of the destination principle. In the new system, the **person liable for payment of VAT** would normally be the supplier. The reverse charge mechanism, making the buyer liable for payment of VAT, remains an option for supply of services under the revised Article 194. For supply of goods, under the new Article 194a, the buyer becomes responsible for the VAT payment only if the supplier is not registered in the Member State of acquisition, and the person to whom the goods are supplied is a **certified taxable person (CTP)** according to the new Article 13a. A firm would be considered a reliable taxpayer if it complies with a certain number of requirements mentioned in Article 13a and can obtain CTP status. [Authorised Economic Operators \(AEO\)](#) for customs purposes are considered to meet the CTP requirement and may apply for and obtain CTP status. However, CTP firms will not automatically satisfy AEO requirements (AEO status has further requirements with respect to compliance with technical standards).

Changes to Articles 369a to 369za would amend the provisions for the **special scheme for taxable persons established in the EU but not in the Member State of consumption**, allowing for the extension of the single registration scheme for declaration, payment and deduction of the tax, known as the one-stop-shop (OSS), to B2B transactions in goods. Use of the OSS will end the need for suppliers to register for VAT purposes in all the countries in which the firm sells to customers, thereby substantially reducing the administrative costs for firms deriving from the 'destination' principle based VAT regime. Under the OSS, the firm will pay the national authorities of the Member State where it is located; it is then up to that fiscal authority to transfer the VAT to the treasury of the Member State of consumption. Currently, the [mini one-stop-shop \(MOSS\) scheme](#) applies to telecommunications, broadcasting and electronic services providers, to supply those services throughout the EU, while being registered in a single Member State. More recently, [Council Directive \(EU\) 2017/2455](#), amending the VAT Directive, and [Council Regulation \(EU\) 2017/2454](#), amending the VAT Administrative Cooperation Regulation, have extended the MOSS scheme to all cross-border business-to-consumer (B2C) e-commerce (the OSS), which should be effective from 1 January 2021.⁴ The extension of the OSS is fundamental to reducing suppliers' otherwise increased administrative costs from having to register in multiple Member States, considering that only transactions involving CTP buyers would be covered by the reverse charge mechanism. The OSS would also be available to taxable persons not established in the EU, if they use an intermediary established in the Union. Also, if the annual turnover of persons using the scheme is more than €2 500 000, VAT returns must be submitted every month, instead of quarterly. Finally, the VAT return would need to provide additional information compared with the current requirements.

Under Article 67, VAT would be chargeable upon issue of an invoice, or no later than the fifteenth day of the month after the chargeable event occurred.

As this proposal would only establish a definitive system for trade in goods, Article 402 would be amended to maintain a transitional system for trade in services.

Advisory committees

The European Economic and Social Committee (EESC) adopted its [opinion](#) on 24 January 2019, reiterating its support for the move to the definitive VAT system, while stressing the need to ensure that goods and services are treated the same way as soon as possible.

The EESC highlighted, among other things, the need for clarity regarding bad debt and refund management within the OSS. It also insisted on the need for clear and proportionate criteria regarding the CTP concept. It stressed a related need for adequate investment in hardware/software assets to properly develop a solid and reliable OSS, and greater collaboration between national fiscal and enforcement authorities to make the new destination-based VAT system more effective in terms of both effectiveness against fraud and reliability. The Committee also considered that European

enterprises would benefit from an extensive communication initiative from the European Commission to explain adequately, in clear and practical terms, the new VAT system's main features.

National parliaments

The [subsidiarity deadline](#) for national parliaments to submit comments on the proposals was 24 September 2018. The German [Bundesrat](#) issued an opinion in the framework of political dialogue mentioning concerns with respect to CTP status and to the OSS frameworks.

Stakeholders' views⁵

A number of stakeholders published positions on the switch to a definitive VAT regime for cross-border trade (such as [BusinessEurope](#), [Tax Advisers Europe](#), [PwC](#), [Friedrich Ebert Stiftung](#)), focusing on compliance costs, the extension of the OSS to B2B transactions⁶ and the CTP status. Specific challenges for small and medium-sized enterprises (SMEs) might face in obtaining CTP status were also stressed (UEAPME).

Legislative process

The proposal follows the consultation procedure, which means the Parliament's opinion is not binding. In the **European Parliament**, the file has been assigned to the Economic and Monetary Affairs (ECON) Committee (Rapporteur: Fulvio Martusciello, EPP, Italy).

The European Parliament adopted its [resolution](#) on the proposal in plenary session on 12 February 2019. The Parliament recalled the urgent and far-reaching need to reform the VAT system in order to achieve a definitive VAT system that facilitates and simplifies intra-EU cross-border trade and to proof the system against fraud.

The proposed amendments relate firstly to the **CTP**. The report introduces amendments on the stricter application of the CTP criteria, such as required evidence of an applicant's financial solvency during the three years prior to application and possession of a bank account in a financial institution in the Union; time limits for a new application from applicants who have been refused CTP status or whose CTP status is withdrawn; and introduction of proportional sanctions if a CTP holder does not disclose within one month any factor which could have affected the CTP status.

The amendments also introduce the refusal of CTP status to an applicant denied AEO status during the last three years. Another suggested amendment deals with concerns regarding SMEs' capacity to apply for CTP status; the amendment requests the European Commission institute a tailored procedure for SMEs. Proposed amendments introduce guidance from the Commission by way of implementing provisions and guidelines on withdrawal and monitoring of status.

Furthermore, a periodical review of the status granted by Member State authorities is added (at least every two years), as well as the obligation to update the status in VAT information exchanges. Cooperation is also strengthened, to disclose applications refused and the reasons for doing so to tax authorities' counterparts in other Member States.

The amended version requests the European Commission, in cooperation with the Member States, provide a comprehensive, multilingual and publicly accessible Union **VAT web information portal** where businesses and consumers can quickly and effectively obtain accurate information on VAT rates – including which goods or services benefit from reduced rates or exemptions – and information on the implementation of the definitive VAT system in the different Member States.

The committee report also amends the provision regarding Eurofisc.

Reporting requirements are also added: the European Commission must present a report on the implementation and application of its new provisions four years after the adoption of the directive, and, two years after adoption, must present a report to Parliament and Council on the effectiveness of the exchange of information between Member States' tax administrations.

In the **Council**, the proposal is being examined by the Working Party on Tax Questions – Indirect Taxation. Discussion of the proposal builds on the debate on the proposal to introduce a definitive system and the 'VAT quick-fix'.

The Council [agreed](#) to discuss some of the proposal's elements relating to the CTP and the text of amendments to Article 402 of the VAT Directive that were part of the October 2017 package of legislative proposals, in the context of other legislative proposals in the area of VAT (in particular the proposal analysed in this briefing).

Assessment of the proposal is [ongoing](#) in the Council. The discussion on the definitive VAT system remains a priority in the VAT area, while improving the current VAT system, which will remain in place until the agreement is reached on the definitive regime, is also addressed.

EP SUPPORTING ANALYSIS

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

OTHER SOURCES

[Operation of the definitive VAT system for the taxation of trade between Member States](#), Legislative Observatory (OEIL), European Parliament.

ENDNOTES

- ¹ At that time, the origin-based system was preferred, with the objective of introducing a system for VAT which would treat the single market as if it was a single country. To function correctly, a VAT system based on the origin principle needs an appropriate level of harmonisation of VAT rates. Without such harmonisation, that kind of VAT regime introduces competitive distortions within the internal market, as firms would delocalise to the countries with the lowest VAT rates to price their goods lower and gain a competitive edge. The level of harmonisation required was never achieved, as derogations and exceptions to the harmonised rules multiplied.
- ² For the state of play of the VAT reboot, see the 2019 article by M. Merckx and J. Gruson, 'Definitive VAT regime: ready for the next step?', European Commission Tax Review, 2019/3.
- ³ The first three elements were addressed in the amendments to the VAT Directive proposed in the same package and adopted by [Directive \(EU\) 2018/1910](#) of 4 December 2019. The fourth element was implemented in the in the [VAT Implementing Regulation](#), also adopted on [4 December 2019](#).
- ⁴ Once these amendments enter into force, the MOSS will be referred as the OSS.
- ⁵ 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. Additional information can be found in related publications listed under 'EP supporting analysis'.
- ⁶ [PwC](#) raises doubts regarding the possibility of extending the OSS to B2B transactions by 1 July 2022, as it considers that the 2021 e-Commerce Package OSS (the OSS covering B2C transactions) will need to be in place and functioning smoothly before it can be expanded again to cover the definitive VAT regime for B2B transactions.

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