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## **DRAFT REPORT**

on the implementation of the 6th VAT Directive: what is the missing part to reduce the EU VAT gap?  
(2020/2263(INI))

Committee on Economic and Monetary Affairs

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## CONTENTS

	<b>Page</b>
EXPLANATORY STATEMENT – SUMMARY OF FACTS AND FINDINGS.....	3
MOTION FOR A EUROPEAN PARLIAMENT RESOLUTION.....	8

## EXPLANATORY STATEMENT – SUMMARY OF FACTS AND FINDINGS

In line with its responsibilities under Article 14 TFEU, the European Parliament has sought to assess the application and implementation of the ‘**Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment**’, the so-called ‘6th VAT Directive’.

For the drafting of this implementation report, a key source of mainly ‘**empirical**’ data was a study assessing the directive carried out by DIW Econ, with the support of EPRS.

That study, which also included a detailed review of the literature, launched a reflection on the following issues identified as priorities:

- VAT rates, tax bases and VAT gaps in EU Member States;
- The impact of the diversification of reduced VAT rates on businesses;
- The impact of reduced VAT rates on consumers and on social and environmental objectives.

### Scope of this implementation report

As far as possible, this report assesses the implementation of the transposition of the 6th Directive, as recast in Council Directive 2006/112/EC of 28 November 2006, with a view to drawing conclusions and exploring some ideas for improving its application. It also aims to analyse the VAT gap between Member States.

The VAT gap is the difference between expected VAT revenues and VAT actually collected. It provides an estimate of the revenue foregone not only as a result of tax evasion and avoidance, but also bankruptcies, insolvency and calculation errors.

According to a report on the VAT gap published by the Commission in September 2020, Member States recorded a loss of VAT revenue estimated at EUR 140 billion, which represents a total EU-wide loss of revenue of 11%. The impact of the COVID-19 pandemic, including reduced consumption and an increase in bankruptcies, has seen the forecasts for 2020 being revised upwards, with a potential loss of EUR 164 billion, or 13.7%.

### Background

The purpose of the **Sixth VAT Directive of 17 May 1977**<sup>1</sup> was to achieve a uniform basis of assessment to which harmonised rates were to apply. The aim was to abolish fiscal borders and controls at internal borders for all operations carried out between Member States with a view to the completion of the internal market on 31 December 1992.

When these fiscal borders between Member States were abolished at the end of 1992, a transitional VAT system was adopted on 1 January 1993, owing to a lack of political will and for technical reasons. During the transitional period, it was decided to tax intra-Community transactions carried out by taxable persons other than exempt taxable persons in the Member

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<sup>1</sup> Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment.

## State of destination.

For the sake of clarity, rationality and transparency, the Sixth Directive and its amendments were incorporated and recast in a single text<sup>2</sup> as **Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (the VAT Directive), which is currently in force.**

The recast of the 1977 directive retained all the legal provisions of the Sixth Directive, but also incorporated VAT provisions from other directives and reorganised the text to make it more readable.

As the cornerstone of the existing EU VAT framework, this directive (2006/112/EC) provides for **the transitional rules** to be replaced by a **definitive regime**, but based on the taxation in the Member State of origin of the cross-border supply of goods and services. However, in its *Communication of 6 December 2011 on the future of VAT – Towards a simpler, more robust and efficient VAT system tailored to the single market*, the Commission acknowledged that it was no longer realistic to apply the origin principle and that the destination principle was politically more achievable. This position was supported by Parliament in its resolution of 13 October 2011 on the future of VAT<sup>3</sup>.

A substantial revision of Directive 2006/112/EC was launched back in 2016 to update the EU VAT system and make it less vulnerable to fraud, including the ‘Action Plan on VAT, Towards a Single EU VAT Area – Time to decide’ of 7 April 2016. The proposal for a Directive of 25 May 2018 amending Directive 2006/112/EC laying down detailed technical provisions necessary for the operation of the definitive VAT system for intra-EU business-to-business trade in goods complements Council Directive 2018/1910 of 4 December 2018<sup>4</sup>, which laid the foundations for the definitive VAT system for cross-border business-to-business (B2B) trade in goods by providing detailed technical measures to enable a definitive VAT system to be established for B2B transactions in goods.

The proposal for a Directive of 25 May 2018 on cross-border trade is therefore part of the process of change with a view to establishing the single EU VAT area. This process also includes two other proposals for amendments to the VAT Directive concerning the VAT rate<sup>5</sup> and the special scheme for small enterprises<sup>6</sup>. Directive 2006/112/EC has also been subject to a series of amendments, some of which concern the COVID-19 pandemic and Brexit<sup>7</sup>.

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<sup>2</sup> OJ L 145, 13.6.1977, p. 1. Directive as last amended by Directive 2006/98/EC (OJ L 221, 12.8.2006, p. 9).

<sup>3</sup> European Parliament resolution of 13 October 2011 on the future of VAT (2011/2082(INI)), P7\_TA(2011)0436.

<sup>4</sup> OJ L 311, 7.12.2018, p. 3-7: Council Directive (EU) 2018/1910 of 4 December 2018 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.

<sup>5</sup> COM (2018) 20 final: Proposal for a Council Directive of 18 January 2018 amending Directive 2006/112/EC as regards rates of value added tax. The European Parliament delivered its opinion on 3 October 2018. The European Economic and Social Committee and the Committee of the Regions adopted their opinions on 23 May 2018 and 10 October 2018 respectively.

<sup>6</sup> COM (2018) 21 final.

<sup>7</sup> As a result of the COVID-19 pandemic, Decision (EU) 2020/1109 pushed back the date of entry into force of the second package from 1 January 2021 to 1 July 2021 in order to give EU countries and businesses longer to prepare for the new rules. Directive (EU) 2020/2020 amends Directive 2006/112/EC to ensure more affordable access to deliveries of COVID-19 vaccines and in vitro diagnostic medical devices (test kits) in response to COVID-19 in Europe.

The future VAT system based on the destination principle, as proposed by the Commission but not yet adopted by the Council, aims to give Member States some flexibility in setting VAT rates and maintaining existing reduced rates. However, Member States should not overlook the priority objective of ensuring greater convergence of VAT rates. Reduced rates should therefore remain an exception to the standard rate, ‘in order to avoid disproportionate fragmentation of the VAT system within the internal market’.

In its note of 4 June 2021 to the Permanent Representatives Committee (COREPER), the Council Secretariat provided a detailed analysis of the progress made since 2018, setting out the main outstanding issues<sup>8</sup>. Those outstanding issues were submitted to the Ecofin Council for political guidance on 18 June 2021.

## Conclusions

Directive 2006/112/EC has been continuously improved to broaden its scope. The EU’s transitional VAT system for intra-Community transactions is complex, weak in dealing with tax fraud – in particular so-called ‘carousel’ fraud (or missing trader intra-Community fraud)<sup>9</sup>, the most widespread form of VAT fraud – and unnecessarily creates significant risks for businesses.

In order to meet the challenges of the globalised, digital and mobile economy, the European Union needs a simple, transparent, efficient, improved and modernised VAT system, taking into account the importance of maintaining its competitiveness, adapted to the internal market and fraud-proof. Such a system is essential in order to gain the support of citizens and businesses and to assure them that their money is being used properly.

It is time to move towards a **definitive VAT system**, i.e. a simple system that is fraud-proof and flexible enough that it can be adapted to developments in technology and trade, **based on the principle of taxation in the country of destination** whereby VAT on business-to-business transactions is levied on the basis of the customer’s country of residence, and VAT upstream can be recovered in the country in which it is paid.

The in-depth literature on VAT systems and their effects in the EU Member States furnished by the DIW Econ study backs up our desire to call on the Council to adopt the proposal for a directive of 25 May 2018, as adopted by Parliament on 12 February 2019. The study sets out the main findings on the variation in VAT rates, on tax bases and VAT gaps, on the impact on businesses and consumers of the diversification of reduced VAT rates, and the impact of reduced VAT rates as a potential tool with which to achieve social and climate goals within the European Union.

Noting the many differences in VAT systems and, consequently, in VAT gaps and conformity costs, the study lists the advantages of convergence in order to further narrow the standard rate band by rationalising reduced rates and exemptions. Working towards a uniform VAT rate would make it possible to cut the standard rate by as much as 7%, reduce the compliance

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As a result of Brexit, Council Directive (EU) 2020/1756 of 20 November 2020 amending Directive 2006/112/EC on the common system of value added tax as regards the identification of taxable persons in Northern Ireland.

<sup>8</sup> Note 9420/21 from the General Secretariat of the Council of the European Union of 4 June 2021 to the Permanent Representatives Committee.

<sup>9</sup> This type of fraud, which is very common in trade in electronic components, mobile telephony and textiles, consists of passing goods around between several companies in different Member States, taking advantage of the fact that there is no tax levied on the intra-EU supply of goods.

costs which overburden SMEs disproportionately and, lastly, cut fraud, which places a heavy burden on public funds and consumers and also affects the EU's financial interests since VAT is the EU's second biggest own resource. A system like this – simpler (currently there are over 250 exemptions and reduced rates in the EU) and more transparent, based on close collaboration between Member States and their sharing of information and best practices in line with the subsidiarity principle – would make the internal market function better. The current list of reduced rates and exemptions must be rationalised if the EU wants to have the efficient internal market that is so vital to economic recovery. An analysis examining harmonisation of reduced rates could also be worthwhile.

The study notes that the VAT gap, measured as the difference between the amount of VAT actually collected and the total VAT due to be paid, was around 10% on average in the EU27 in 2019, whereas in 2009 it was 20%. Nonetheless, the study notes yet again that the size of the VAT gap varies considerably between Member States, ranging from 33% in Romania to 1% in Sweden and Croatia.

Tax costs for businesses involve more than just the tax actually paid as compliance costs must also be included. Special attention must be paid to SMEs, the backbone of the EU economy. They are overburdened to an excessive degree, particularly because compliance costs are fixed in most cases. Experts estimate total costs account for 1% to 4% of turnover, which is substantial. While digitisation can help cut costs, it imposes a burden in the short term on businesses, and particularly SMEs, as they must acquire the latest technology and know-how. Looking ahead, the Member States will need a harmonised IT system.

The diversification of VAT rates creates a fragmented internal market, distorting it by fostering unfair competition within the EU's internal market, increasing the compliance burden, damaging competition, encouraging the exploitation of cross-border price differences by shifting consumption to Member States with lower VAT rates, and by distorting the collection of revenue by governments. Diversified VAT systems can also create an uneven playing field for competition with third countries and distort prices, thereby distorting international trade. This is why the principles of transparency, good governance and information-sharing must be adhered to as a VAT system that works is a system that does not impact on trade.

Lastly, the study states that since reduced rates only have a slight and temporary knock-on effect on prices their impact on consumers and on the achievement of social and environmental goals is limited. Other factors, such as price elasticity of demand, must be taken into account. To be effective, reduced rates in this context, which constitute significant costs for governments on account of the erosion of the tax base, must, in addition to being wholly or partially passed on through the lower price paid by the consumer, be coupled with other initiatives such as tax credits and direct subsidies which have the advantage of targeting the consumer or the entrepreneur directly. Reduced rates do not target the poorest households and as such have less of an effect than hoped for as regards achieving social and environmental goals. They create a mechanical loss which can be as high as 22% of total domestic revenue from VAT, and generate higher compliance costs and more risks of VAT fraud. Experts have noted in fact that the reduction in VAT during the COVID-19 pandemic did not have the impact on consumption hoped for because businesses, anticipating this increasing their profit margin, did not lower their prices. What must serve as our compass and guide our decisions is the opportunity cost. Instead of lowering VAT, where the benefit to producers or consumers is determined by the volume involved, we should ask ourselves

whether lowering other taxes that have a more beneficial effect in terms of the environment, justice, employment promotion or stimulation of the local economy offers a better opportunity. In addition to direct incentives, information campaigns and promoting merit goods, particularly to achieve environmental goals, must be regarded as a viable alternative to reduced VAT rates.

With environmental policy becoming ever more important, this study has the merit of opening up avenues for future research.

There is a pressing need to limit the VAT gap between Member States in the context of the economic recovery in order to curb the socioeconomic crisis following the COVID-19 pandemic. This gap can be reduced by simplifying the VAT implementation system and combating fraud, thanks in particular to digitisation, which enables both governments and businesses to take action in real time. The Recovery and Resilience Facility (RRF), which emphasises unity and solidarity, must help Member States to develop a more productive, inclusive and innovative economy focused on environmental and digital transition. Proper funding of VAT will help with repayment of debt. The post-COVID-19 economic recovery is a chance for change to fairer, greener and better targeted taxation systems.

## MOTION FOR A EUROPEAN PARLIAMENT RESOLUTION

### **on the implementation of the 6th VAT Directive: what is the missing part to reduce the EU VAT gap? (2020/2263(INI))**

*The European Parliament,*

- having regard to Articles 4 and 14 of the Treaty on European Union (TEU),
- having regard to Articles 113 and 115 of the Treaty on the Functioning of the European Union (TFEU),
- having regard to the Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment,
- having regard to Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax,
- having regard to Council Implementing Regulation (EU) No 282/2011 of 15 March 2011 laying down implementing measures for Directive 2006/112/EC on the common system of value added tax<sup>1</sup>,
- having regard to its resolution of 13 October 2011 on the future of VAT (2011/2082(INI))<sup>2</sup>,
- having regard to the Communication from the Commission of 6 December 2011 on the future of VAT: Towards a simpler, more robust and efficient VAT system tailored to the single market<sup>3</sup>,
- having regard to the Commission action plan entitled ‘Towards a single EU VAT area – Time to decide’ adopted on 7 April 2016<sup>4</sup>,
- having regard to its resolution of 24 November 2016 entitled ‘Towards a definitive VAT system and fighting VAT fraud’<sup>5</sup>,
- having regard to the proposal for a Council directive amending Directive 2006/112/EC as regards rates of value added tax<sup>6</sup>,
- having regard to the Communication from the Commission entitled ‘Towards a single EU VAT area – Time to act’<sup>7</sup>,

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<sup>1</sup> OJ L 77, 23.3.2011, p. 1-22.

<sup>2</sup> Texts adopted, P7\_TA(2011)0436.

<sup>3</sup> COM (2011) 851 final.

<sup>4</sup> COM (2016) 148 final.

<sup>5</sup> Texts adopted, P8\_TA(2016)0453.

<sup>6</sup> COM (2018) 20 final.

<sup>7</sup> COM (2017) 566 final.

- having regard to the proposal for a Council directive amending Directive 2006/112/EC on the common system of value added tax as regards the special scheme for small enterprises<sup>8</sup>,
- having regard to the 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<sup>9</sup>,
- having regard to Council Regulation (EU) 2018/1541 of 2 October 2018 amending Regulations (EU) No 904/2010 and (EU) 2017/2454 as regards measures to strengthen administrative cooperation in the field of value added tax<sup>10</sup>,
- having regard to Council Directive (EU) 2018/1910 of 4 December 2018 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<sup>11</sup>,
- having regard to its resolution of 12 February 2019 on the 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<sup>12</sup>,
- having regard to its resolution of 26 March 2019 on financial crimes, tax evasion and tax avoidance,
- having regard to Council Directive (EU) 2020/285 of 18 February 2020 amending Directive 2006/112/EC on the common system of value added tax as regards the special scheme for small enterprises and Regulation (EU) No 904/2010 as regards the administrative cooperation and exchange of information for the purpose of monitoring the correct application of the special scheme for small enterprises<sup>13</sup>,
- having regard to Council Directive (EU) 2020/284 of 18 February 2020 amending Directive 2006/112/EC as regards introducing certain requirements for payment service providers<sup>14</sup>,
- having regard to the Communication from the Commission of 15 July 2020 entitled ‘An action plan for fair and simple taxation supporting the recovery strategy’ (COM(2020)0312),
- having regard to Council Directive (EU) 2017/2455, Council Regulation (EU) 2017/2454, Council Implementing Regulation (EU) 2017/2459, Council Directive (EU) 2019/1995, Council Implementing Regulation (EU) 2019/2026 and Implementing Regulation (EU) 2020/194 relating to the VAT e-commerce package,

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<sup>8</sup> COM(2018) 021 final.

<sup>9</sup> COM(2018) 329 final, entry into force deferred until 1 July 2022.

<sup>10</sup> OJ L 259, 16.10.2018, p. 1-11.

<sup>11</sup> OJ L 311, 7.12.2018, p. 3-7.

<sup>12</sup> COM(2018)0329.

<sup>13</sup> OJ L 62, 2.3.2020, p. 13-23.

<sup>14</sup> OJ L 62, 2.3.2020, p. 7-12.

- having regard to the study entitled ‘VAT gap, reduced VAT rates and their impact on compliance costs for businesses and on consumers’ drafted by DIW Econ and published by the Directorate-General for Parliamentary Research Services,
  - having regard to Opinion No 11/2020 of the European Court of Auditors (issued pursuant to Articles 287(4) and 322(2) TFEU) concerning the draft Council Regulation (EU, Euratom) amending Regulation (EEC, Euratom) No 1553/89 on the definitive uniform arrangements for the collection of own resources accruing from value added tax<sup>15</sup>,
  - having regard to the report of the Committee on Economic and Monetary Affairs on the implementation of the EU requirements for exchange of tax information: progress, lessons learnt and obstacles to overcome (A9-0193/2021),
  - having regard to its legislative resolution of 10 March 2021 on the proposal for a Council directive amending Council Directive 2011/16/EU on administrative cooperation in the field of taxation<sup>16</sup>,
  - having regard to its legislative resolution of 19 May 2021 on the Council position at first reading with a view to the adoption of a regulation of the European Parliament and of the Council establishing the ‘Fiscalis’ programme for cooperation in the field of taxation and repealing Regulation (EU) No 1286/2013 (06116/1/2021 – C9-0179/2021 – 2018/0233(COD)),
  - having regard to Regulation (EU) 2021/847 of the European Parliament and of the Council of 20 May 2021 establishing the ‘Fiscalis’ programme for cooperation in the field of taxation and repealing Regulation (EU) No 1286/2013<sup>17</sup>,
  - having regard to the public consultation open from 8 February to 4 May 2021 (VAT rules for financial and insurance services – review),
  - having regard to Rule 54 of its Rules of Procedure, as well as Article 1(1)(e) of, and Annex 3 to, the decision of the Conference of Presidents of 12 December 2002 on the procedure for granting authorisation to draw up own-initiative reports,
  - having regard to the report of the Committee on Economic and Monetary Affairs (A9-0000/2021),
- A. whereas in 1977 the Council adopted a sixth VAT directive with a view to achieving a uniform tax base under which harmonised rates were to be set out; whereas the Member States decided to apply a transitional period in which to achieve this, which has since been extended;
- B. whereas the VAT Directive<sup>18</sup> has recast and repealed the Sixth Directive, for the purposes of greater clarification; whereas this directive provides for the transitional rules to be replaced by a definitive system based on taxation in the Member State of

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<sup>15</sup> Document 12771/20, interinstitutional file 2018/0133(NLE).

<sup>16</sup> COM(2020)0314.

<sup>17</sup> OL L 188/1, 28.5.2021.

<sup>18</sup> Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (OJ L 347, 11.12.2006, p. 1).

origin; whereas the transitional system is complex, flawed and structurally vulnerable to fraud;

- C. whereas in 2013 a major overhaul was initiated to introduce a definitive system based on the destination principle, which makes it less vulnerable to fraud<sup>19</sup>;
- D. whereas on 25 May 2018 a proposal for a directive was adopted which introduced detailed arrangements for a definitive VAT regime for intra-EU business-to-business trade in goods and put an end to the ‘transitional’ system; whereas Parliament adopted its position on 12 February 2019; whereas the Council has not yet adopted a position;
- E. whereas the VAT gap in the EU has been reduced from 20% in 2009 to 10% in 2019; whereas owing to the pandemic and its socio-economic effects, this trend was reversed in 2020; whereas estimated losses of EUR 164 billion have been incurred, of which one third has fallen into the hands of fraudsters and organised crime networks;
- F. whereas Opinion No 11/2020 of the Court of Auditors focuses on the new method put forward for calculating the VAT-based own resource;
- G. whereas the Commission’s ‘Action Plan for fair and simple taxation supporting the recovery’ is part of the EU’s new strategy for simplifying and adapting taxation to the digitisation of the economy and the green transition, and for combating tax fraud and evasion;
- H. whereas, since the adoption of the VAT Directive, financial services have been, with certain exceptions, exempt from VAT on the grounds that they are subject to other taxes (such as tax on insurance premiums);

#### ***Tax rates, tax bases and VAT gaps in EU Member States***

1. Observes that on average the standard rate was applied to 71% of the total tax base in the Member States in 2019; that the taxable base at the standard VAT rate varied from 97% (BG) to 47% (ES); that on average, the VAT gap is 10% in the EU but that it varies greatly from Member State to Member State<sup>20</sup>; that the number of reduced and super-reduced rates varies between Member States; that only five Member States<sup>21</sup> continue to apply super-reduced rates; that only Denmark does not apply reduced rates;
2. Notes that simplifying VAT with the introduction of a single rate and revenue neutrality could reduce the standard rate in the EU by an average of 7%, thus bringing the standard rate down from 13% to 2%;
3. Takes the view that applying a multitude of reduced rates aggravates the complexity and opacity of the tax system, facilitates fraud and increases compliance costs;
4. Observes that the VAT gap fluctuates in line with the business cycle, and that low tax compliance is correlated with high standard VAT rates and multiple VAT rates as well as lower legal and judicial efficiency;

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<sup>19</sup> As outlined in the EU Action Plan on VAT of 7 April 2016.

<sup>20</sup> From 33% in RO as far down to 1% in SE and HR.

<sup>21</sup> FR, IE, IT, LU and ES as of 1 January 2021.

### ***Impact of the wide variety of reduced rates on businesses***

5. Takes the view that the current diversity of reduced rates imposes particularly high compliance costs on businesses; and that compliance costs are estimated to be an average of 2.5% of company turnover and vary considerably from Member State to Member State<sup>22</sup>;
6. Observes that SMEs must pay proportionately higher compliance costs, as these costs are fixed and independent of company size, and that high compliance costs constitute a barrier to entry into the EU internal market; takes the view, therefore, that differentiated VAT regimes within the EU may act as a disincentive to exports;
7. Notes digitalisation's potential to reduce compliance costs; maintains that digital innovations<sup>23</sup> are likely to reduce compliance costs and help increase the transparency of commercial transactions; stresses the need to ensure data security and individual and corporate privacy;
8. Observes that the wide variety of rates causes price distortion in the internal market, creating incentives for cross-border purchases and giving rise to increased tax competition between Member States; recalls that companies need clear and unambiguous VAT rules to encourage cross-border business and reduce their administrative burdens;
9. Stresses that a well-designed VAT system is neutral and should not affect trade, but that in practice this principle is difficult to verify at global level given the application of VAT exemptions, the ineffectiveness of refund systems, the wide variety of rates – incurring higher compliance costs – and the fact that VAT has superseded income taxes with a view to encouraging trade;

### ***Impact of reduced VAT rates on consumers and social and environmental objectives***

10. Observes that the application of reduced rates does not systematically give rise to permanent price reductions for the consumer; that the effectiveness of a reduced rate depends on a number of factors, such as the extent to which businesses pass it on to consumers, its duration over time, the size of the reduction and the complexity of the rate system; that the passing-on of reductions in their entirety is therefore a random process and should not be the basis for policy-making; that it is impossible to target low-income households;
11. Recalls that for it to have a leverage effect, green taxation must be inclusive, strive for social equity and not undermine businesses' international competitiveness; observes that the effectiveness of reduced rates in promoting this type of goods and services or, in a broader sense, merit goods (e.g. culture, health, biodiversity) is chiefly a function of the extent to which they are used to promote such goods;
12. Stresses that reduced rates are not an effective way of achieving social or environmental objectives since they incur high costs for governments owing to the size of the rate gap, reduced tax revenues, increased administrative costs, costly checks and inspections,

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<sup>22</sup> Less than 1% in LU; almost 4% in PL.

<sup>23</sup> Such as AI, big data and blockchain technology.

pressure from lobby groups, compliance costs, economic distortions or even tax evasion, and the difficulty of reaching the target groups;

13. Takes the view that direct tax incentives, such as direct grants or tax credits targeting specific consumers and producers, are more effective, flexible, visible and cost-effective tools for achieving these social and environmental objectives;
14. Stresses that a uniform VAT system, combined with a direct tax incentive tool such as the income-based tax credit scheme for low-income households, together with a raft of social reforms, would be a winning strategy; recalls that New Zealand has a flat-rate VAT system and applies tax credit for low-income households; points out that flat-rate subsidies and information campaigns are an option for the promotion of merit goods;

### ***Conclusion***

15. Recalls that VAT revenue is one of the chief sources of public revenue, accounting for some 21% of total tax revenue in the EU on average; that the VAT gap stands at 10% on average; and that VAT also constitutes an own resource for the EU budget; stresses that any reduction in the VAT base leads to less revenue for public finances; calls on national tax authorities to take initiatives to reduce the VAT gap in order to help lift Member States out of the current socio-economic crisis;
16. Endorses the findings of the DIW Econ study which stresses that on average the standard rate was applied to 71% of the total tax base in the Member States in 2019; points out that diversified VAT systems impose costs on businesses, particularly SMEs via increased compliance costs, create distortions in the internal market and trade, and incur costs on government through lost revenue; adds that reduced rates are an insufficient means of achieving revenue-distribution or environmental objectives;
17. Notes the difficulties in reducing the VAT gap between Member States owing to the need to maintain a number of VAT exemptions for certain goods and services and the willingness of Member States to maintain reduced rates of at least 5%; acknowledges that Member States need to conserve the flexibility to set their own VAT rates given the importance of this tax as a budgetary instrument;
18. Calls for a simplified VAT system with limits on exemptions and non-standard rates to be introduced with a view to promoting competitiveness;
19. Stresses that the VAT gap is chiefly attributable to the ineffectiveness of enforcement and control measures, particularly those against tax evasion and avoidance and aggressive tax planning;
20. Recalls that the effectiveness of reduced rates as a policy tool must always be assessed in the specific context of other existing policy tools; adds that reduced rates are often complementary to existing social and environmental policy tools; and that direct tax incentives are instruments that better target low-income households and are generally less costly;
21. Stresses the need to move to a definitive VAT system based on the principle of taxation in the country of destination; calls on the Council to adopt the proposal for a directive of 25 May 2018;

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22. Instructs its President to forward this resolution to the Council, the Commission and the governments and parliaments of the Member States.