



14 December 2018

Definitive VAT-system for Cross-Border Trade (update following the European Commission's proposal on the detailed technical amendments for the operation of the Definitive VAT-system)

KEY MESSAGES

- 1** We welcome the European Commission's commitment to the creation of a single VAT-area based on maximum simplicity, clarity and robustness against fraud. We support in particular the Commission's efforts to further improve and broaden the One-Stop-Shop. However, the Definitive VAT-system, as outlined in the Commission's 'cornerstone' and 'technical' proposals, whereby VAT will be charged on cross-border trade between businesses, will significantly increase compliance costs as businesses will have to be continuously informed about the wide range of different VAT-rates in the different Member States. We are also concerned that the proposed model will significantly impact cash-flow and may not reduce overall VAT-fraud.
- 2** We are concerned that the Commission's proposed application of the destination principle, whereby suppliers will have to deal with the tax administration of the country where the goods are transported to, rather than the administration where the customers are established, will bring an unnecessary increase in the overall administrative burden.
- 3** We are concerned, that by not having the same VAT-rules for goods and services at the initial stage, this will increase the administrative burden of businesses who will have to deal with two different systems. Additionally, as the digitalised economy blurs the line between goods and services, having a VAT-system without the same rules between goods and services, would make the system more complicated and less robust against fraud. We would encourage the Commission to undertake an initiative which covers the same place of taxation rules for goods as currently already apply for services.

WHAT DOES BUSINNEUROPE AIM FOR?

- We support the European Commission's efforts to modernise the EU's VAT-system, reduce administrative burden and to close the VAT-gap. The current VAT-system is highly fragmented, complex and subsequently reduces and distorts trade and investment by creating unnecessary extensive administrative burden and trade barriers to businesses. However, the Definitive VAT-system, as outlined in the Commission's proposals, risks creating more administrative burden, with significant impacts for cash-flow.

- Further VAT-reforms should also take into account the fast-changing (digitalised) economy, which blurs the line between goods and services and upcoming technologies which may be helpful in closing the VAT-gap and simplifying VAT-reporting.
- We call on Member States to improve current cooperation between the different national tax administrations to establish greater levels of trust and efficiency. We cannot improve the VAT-system without trust between Member States and cooperation between tax administrations and businesses.



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Introduction

In October 2017, the European Commission presented its initiatives to replace the current VAT transitional arrangements for the taxation of trade between Member States by definitive arrangements in 2022. The Commission has opted for taxation rules according to which, for intra-EU cross-border supplies of goods, the supplier would charge VAT to his customer at the rate of the Member State of arrival of the goods. The VAT would be declared and paid in the Member State where the supplier is established via a One-Stop-Shop mechanism. Within the framework of the definitive arrangements, the Commission also presented 'quick fixes', i.e. proposals for several simplifications the Council asked for in its conclusions of 7 October 2016 regarding the improvement of the current EU VAT-rules. A further technical proposal was put forward in May 2018.

We welcome the initiative taken by the EU Commission for a definitive system based on the destination principle. The current system, which was installed twenty-five years ago, has become highly fragmented, complex and open to fraud. The initiative to reform the VAT-system is a unique opportunity for businesses and Member States to ensure that the new system is simpler, more efficient, less prone to fraud, and promotes cross-border trade and economic growth across the EU. However, it is essential that any change to the current system must lead to an unambiguous improvement of the current state of play for European businesses and other stakeholders.

The definitive system for the taxation of trade between Member States

We support the proposed destination principle, as agreed by the European Council in 2012, however, we are not convinced that the proposed model of taxation of intra-EU cross-border supplies of goods, as outlined in the European Commission's proposals, following the physical flow of the goods, will guarantee a decrease in VAT-compliance costs for businesses.

- Following the flow of goods has caused difficulties in the past both for businesses and tax administrations and has led to different treatment of goods and services. To ensure a facilitation of chain transactions and substantial reduction in administrative costs, we prefer a system where goods are treated in the same way as services (i.e. place of taxation for intra-EU supplies of goods where the customer is established).

For example, under the proposed model, business now will have to prove to, possibly 28 Member States, that the goods have been shipped and arrived in a specific Member State. As a consequence, the proof of arrival will create more administrative burden for businesses, more uncertainty and could carry the risk of double taxation.

In addition, the rules for domestic supplies of goods (taxed at the place of beginning of the dispatch or transport, article 32) differ from the rules for the place of taxation of intra-Union supplies (taxed at the place of the ending of the dispatch



or transport, article 35a). This puts business in an even more difficult situation and provides an in-built risk of double taxation of the supplier and denial of input VAT deduction of the customer.

Moreover, as the proposal envisages that alignment between goods and services will eventually take place at a later stage, this will require substantial investments (once again) from both businesses and tax administrations. We anticipate also that as the digitalization of the economy blurs the line between goods and services, having a system with identical VAT-treatment, would make the system more conducive to growth and robust against fraud. We would support the Commission undertaking a thorough analysis of the pros and cons when it comes to applying the same place of taxation rules for goods as for services and we are very happy to support the Commission in this initiative. We would also need simple and clear rules regarding single and composite supplies that can be translated into code to be used in ERP-system.

- Applying the VAT rates of 28 Member States can also bring higher compliance costs for businesses as in the current system all cross border trade is zero rated in the Member State of dispatch. As a consequence of the proposed model for the taxation of intra-EU cross border supplies, the supplier will have to reliably ascertain whether a standard, a reduced or a zero VAT-rate shall apply. This will result in higher compliance costs as businesses will have to be continuously informed about changes in the VAT-rates of all Member States, as well as other VAT-rules regarding rebates, credit notes and conditions to apply for a zero rating. The anticipated proposal to set free the VAT-rates might also imply an additional layer of complexity in this matter.
- As a consequence of the taxation of intra-EU cross-border supplies, risks of non-payments of VAT will occur. Will traders in case of non-payment be confronted with (in future) 28 different bad debts schemes? It is also unclear whether bad debt will also be covered by the OSS. It is important that rules on bad debt are further harmonised in the future, otherwise suppliers will be confronted with a tangle of bad-debt rules, which may make it impossible to recover unpaid-VAT.
- We are also deeply concerned by the potentially huge impact the proposed definitive system may have on the cash-flow of business. It is important that the working capital of businesses does not come under pressure.
- Furthermore, we are also concerned about potential new fraud practices arising from the proposed model. The model has the incentive to fake exports to low VAT-countries while in fact selling at local markets. Together with the anticipated proposal to set free the VAT-rates, this may in fact generate new opportunities for fraud. In addition, the current fraud is based on the margin between the standard rate and the zero rate. The proposed definitive system may cause this margin to decrease, but due to different VAT-rates in Member States, this margin will never be zero. This underlines again the need for close cooperation between Member States and a strong focus on ensuring and aligning the practical implementation of the proposals.



One-Stop-Shop (OSS)

We believe that a well-functioning One-Stop-Shop is a vital concept. We have welcomed the Commission's initiatives, such as the proposed extension of the Mini-One-Stop-Shop to all B2C services as well as to B2C sales of goods, both intra-Community and from outside the Community. Without a fully functioning OSS, based on home-country audits, scalable simplifications, bad debts schemes, and the ability to offset incurred input-VAT from all Member States the proposed destination-based system will dramatically increase the administrative burden, especially for SMEs.

However, while we fully support the OSS-concept, the proposed OSS is not clear regarding:

- the number of VAT returns in case of both intra-EU and domestic supplies (one OSS-return or both a OSS return and a domestic return?)
- The consequences of an import in and/or a stock point of goods in another Member State. Another domestic foreign return and another foreign OSS return?
- Fictitious supplies: To be reported in the OSS and the other foreign VAT return in the country of destination?
- The requirement regarding input VAT. Are Member States allowed to implement additional requirements?

Certified Taxable Person (CTP)

BusinessEurope finds it important to implement simplification measures in the definite regime in order to mitigate shortcomings, reduce the cashflow impact or streamline trade. However, the design depends on the actual regime and the effectiveness of the OSS. Any mitigation system should be easy to operate – both for business and Member States.

We are strongly concerned that the introduction of a CTP as outlined will be costly for both businesses and tax administrations as they will have to cope with two parallel administrative systems (CTP and non-CTP). If the CTP is set up as a temporary system, the costs will be even higher. A recent European Parliament Study has acknowledged as well that a CTP-system 'will result in a discriminatory treatment of taxable persons and will open new opportunities for fraud'¹. The study added that the correct monitoring of this status would be extremely costly for the Member States.'

Additionally, we were surprised to find that the published technical proposal did not put forward a detailed description of the criteria necessary to obtain CTP-status. This vagueness complicates decisive evaluation.

¹ "Lamensch M. & Ceci, E. (2018): "VAT Fraud: Economic Impact, Challenges and Policy Issues" [http://www.europarl.europa.eu/RegData/etudes/STUD/2018/626076/IPOL_STU\(2018\)626076_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/STUD/2018/626076/IPOL_STU(2018)626076_EN.pdf)



- The need for a CTP is also highly dependent on the One-Stop-Shop. If the One-Stop-Shop can cater for all the VAT obligations and offsetting of input-VAT works efficiently, then the need for a CTP-status could be reduced.
- The application process should be made as easy and smooth as possible to avoid a distorted level-playing field which may put SMEs (who may be impacted by high compliance and administrative costs) and start-ups (who cannot provide a track record) at a competitive disadvantage. Additionally, it is important that the criteria for attaining CTP-status will be defined as precisely as possible to avoid different implementations across Member States. Any CTP-system should not incur any excessive administrative burden and external costs (e.g. external audits or external guarantees). Setting criteria similar to the Authorised Economic Operator (AEO) from customs will be much too restrictive.
- The success of this CTP-status will also depend on post-implementation monitoring by the European Commission to ensure that the criteria are applied in a consistent way across the Member States throughout the years. The different implementations of the Standard Audit File for Tax (SAF-T) across Member States serves as a healthy reminder of how divergent implementations can quickly arise. Once CTP-status is attained, it is important that this status is easily visible and verifiable to all businesses that take part in the transaction.

When the system of the CTP does not apply, it should be ensured that the reimbursement of accruing input-VAT by the Member States of establishment of the purchaser is made very quickly. It would therefore be important to foresee a clear delay-deadline for the refund and interests for late payment due by the authorities to ensure that the resulting impact on cash-flow remains limited. We encourage the Commission to set up a continuous evaluation and monitoring mechanism to ensure that businesses can trade both as and with CTPs with improved legal certainty.

- Group companies outside the EU could be regarded as non-CTP – even if the other group companies achieve the CTP-status. As a consequence, businesses may change their supply chains which risks hampering intra-union trade. This will also cause negative environmental effects due to increased and longer transports. We therefore encourage a broadening of the scope of eligible CTP-applicants to include non-EU established businesses. As harmonized criteria need to be met throughout the EU anyhow, non-EU established entities may be allowed to process their CTP-application either directly or via a fiscal representative in a Member State where they are VAT-registered.
- While the VAT identification number can be an essential element in the direction of increasing solicitation of companies, its effectiveness will depend on the ability of Member States to make these VAT identification numbers more reliable.



Administrative burdens and tackling fraud

The accompanying Commission Staff Working document/Impact assessment (SWD (2017) 325 final) memorises that, according to an evaluation of the EU VAT-system, most of the VAT-fraud is considered to be domestic, but that Missing Trader Intra-Community Fraud (MTIC) has increased following the abolition of the EU's internal fiscal frontiers. It may be expected that the abolition of the VAT-exemption on cross-border trade in the EU potentially contributes to a reduction of MTIC-fraud related to border crossing, but to us it is questionable whether the proposed system will reduce the risk of MTIC. In the one 'domestic' market of 28 Member States that will be created in the proposed system, missing trader fraud is still very possible. E.g. in case a trader in Member State A did not pay the VAT charged to a trader in Member State B to the tax authorities of Member State A, whereas the trader in Member State B deducted the VAT charged? Is there not a danger that MTIC-fraud will be transformed into a 'domestic' missing trader fraud? A recent European Parliament study has acknowledged this as well, noting that 'new forms of MTIC fraud will rapidly arise that have to date been overlooked'. This shows that, in connection with the proposed CTP, the relevant benefit that is being hoped for may not translate into reality, neither for businesses (as the introduction of a CTP status, as currently foreseen, may in fact not lead to any simplification, but instead complicate VAT compliance), nor for tax administrations (as for them as well the monitoring of VAT compliance would become more complex) or the state revenues (as VAT fraud may not be tackled properly).

We strongly support the fight against fraud but we need to ensure that the system becomes simple and that honest traders will face a reduction in the administrative burden. According to the Commission's impact assessment, cross-border trade in the EU amounts to more than 4,1 trillion EUR (exports) and 3,9 trillion EUR (imports). Even a fractional increase in the administrative burden per transaction will have a significant impact. Additionally, it is easier for fraudsters to hide within a complicated VAT-system.

The growing number of Member States introducing (differing concepts of) split payment and Standard Audit File for Tax (SAF-T) for VAT purposes represent an additional barrier to trade. E.g. a trader in Member State A selling goods to a trader in Member State B which applies a VAT split payment system, will be confronted with the following new administrative obligations: Taxation of the transaction according to the VAT rate of Member State B; The opening of a local bank account for each trader in Member State B, which is dedicated to VAT payments. The Trader in Member State A will receive a net amount in his home bank account, whereas the customer has to pay the VAT due to the special VAT bank account. This split in payment compels trader A to control two separate payment flows, which causes a radical extension of the business control system and thus a significant additional administrative burden.

The purpose of a destination-based VAT-system is to create and ensure a level playing field between domestic and non-domestic suppliers. In an increasing number of countries, market operators are obliged to report additional information either in real-time or through SAF-T. It is unclear to us whether non-domestic operators, who operate in the same market under the same VAT-rules, will also have to comply with these additional reporting requirements.



A strong need remains for the harmonisation and stability of administrative practices. Currently, many of the measures are taken locally but with an increasing amount of cross-border trade combined with a destination-based principle, the need for harmonisation and stable common practices are even more necessary. The current fragmentation of administrative practices is increasing to the extent it is increasingly becoming a barrier of trade by itself.