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**COVER NOTE**

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From:	European Economic and Social Committee
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To:	General Secretariat of the Council

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Subject:	Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee on an action plan on VAT: Towards a single EU VAT area - Time to decide [doc. 7687/16 FISC 46 - COM(2016) 148 final] – <i>Opinion of the European Economic and Social Committee</i>
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Delegations will find attached the above-mentioned opinion.

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*European Economic and Social Committee*

**ECO/406**  
**Action plan on VAT**

Brussels, 13 July 2016

**OPINION**

of the  
European Economic and Social Committee  
on the

**Communication from the Commission to the European Parliament, the Council and the  
European Economic and Social Committee on an action plan on VAT: Towards a single EU  
VAT area – Time to decide**  
COM(2016) 148 final

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Rapporteur-general: **Daniel Mareels**  
Co-rapporteur: **Giuseppe Guerini**  
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On 7 April 2016, the European Commission decided to consult the European Economic and Social Committee, under Article 304 of the Treaty on the Functioning of the European Union, on the

*Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee on an action plan on VAT: Towards a single EU VAT area - Time to decide*  
COM(2016) 148 final.

The Section for Economic and Monetary Union and Economic and Social Cohesion, which was responsible for preparing the Committee's work on the subject, adopted its opinion on 29 June 2016.

At its 518th plenary session, held on 13 and 14 July 2016 (meeting of 13 July), the European Economic and Social Committee adopted the following opinion by 113 votes to 1 with 1 abstention.

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## 1. **Conclusions and recommendations**

- 1.1 **The EESC welcomes the "Action Plan on VAT"**, which aims to move towards a definitive VAT system in the EU, and endorses both its objectives and the approach based on four components with a short and medium term perspective. It is now high time to take a qualitative step ("quantum leap") forwards, in order to support the single market and contribute to jobs, growth, investment and competitiveness.
- 1.2 In the Committee's view, it is important to strive to implement all parts of the Action Plan as an indivisible whole. This applies in particular to the transition to the definitive VAT system; the aim should be for its actual implementation – which is only scheduled for the second stage of the Action Plan and is conditional on a separate assessment by the Member States – to be carried out in any event and within a reasonable time-frame. If not, there is a risk that the stated objectives could be compromised.
- 1.3 With regard to the first stage set out in the Action Plan, which currently applies only to certain supplies of goods, the Committee urges all stakeholders to look into how **services** can be incorporated into the new system more quickly, which would also alleviate the problems associated with this (transitional) phase. It would also be worth examining methods for ensuring that **financial services** are more generally subject to VAT.

- 1.4 In the Committee's view, the transformation of the current system should result in a **definitive VAT system** that is **clear, consistent, robust and comprehensive**, as well as **proportionate and future-proof**. In this context, the Committee endorses the proposal to opt for the country of destination principle as the basis for the definitive VAT system, as it will create a level playing field for all suppliers in the same national market and will result in less market distortion.
- 1.5 In the Committee's opinion, close attention should also be paid to how **business-friendly** the system is with respect to enterprises, particularly SMEs. Despite the innovations and simplifications proposed in the Action Plan, there is still considerable concern regarding the complex and complicated nature of the forthcoming regulation and the significant administrative burden that it could entail.
- 1.6 Notwithstanding the need for **clarity and legal certainty** to be central to the development of the definitive VAT system, the Committee calls for the possibility of additional and further-reaching **simplification** and of **reducing the administrative burden** to be examined more closely, whereby consideration could be given to a **proportionate approach that benefits SMEs** without undermining the comprehensiveness and other key characteristics of the definitive VAT system. They should ideally be involved in the development process from the outset.
- 1.7 Consideration should also be given to the comprehensive provision of useful information in a modern form, for example via a web portal, for the benefit of businesses. In particular, this must help **small businesses to compete on an equal footing** with other businesses and with suppliers from the public sector. More generally, it is important to make cross-border activities within the EU easier and more attractive for all businesses, particularly for SMEs.
- 1.8 The EESC welcomes the **strong focus on closing the VAT gap and tackling the susceptibility of this tax to fraud**, particularly given the size of the sums involved, amounting to EUR 170 billion a year. It is important to make this objective a **priority** and to deliver **results without delay**, including by improving cooperation between tax administrations and with customs administrations within the EU and with third countries, making tax administrations more efficient and boosting Eurofisc's role, strengthening voluntary compliance with the rules, and improving tax collection.
- 1.8.1 In the Committee's view, the Member States need to strengthen the capacity of their tax administrations in all areas, in terms of human, financial and technical resources. This should put them in a position to ensure that the new system works properly and effectively, such that fraud can also be reduced.
- 1.8.2 Without prejudice to the actions provided for in the Action Plan in this regard, the Committee **wonders** whether or not **other, additional tools** should be used in this area, following the example of a number of recent international commitments on the automatic exchange of information regarding direct taxation.

- 1.8.3 In the same vein, the EESC believes that there should be a strong focus on the intrinsic characteristics and features of the definitive VAT system in terms of its **susceptibility to fraud**. The new rules, appropriate supervision and greater control using the necessary means of enforcement, including judicial means, should consistently lead to **a more comprehensive VAT system applied with greater effectiveness**. In this context, attention should also be paid to the current exemption for small consignments sent by non-EU suppliers, but the Committee advocates taking a nuanced approach to this question.
- 1.9 In the Committee's view, practical actions to combat fraud must be **targeted and proportionate**. “Bona fide” enterprises should be protected and no new excessive measures should be imposed on them.
- 1.10 The Committee welcomes the focus on **new developments in e-commerce and business types**. It is important to provide **clarity** for all those involved in this regard, while at the same time ensuring that all suppliers are given **equal treatment**, irrespective of whether they are following these developments or are sticking to more traditional channels and methods, and for all their transactions, cross-border or not.
- 1.11 The Committee reserves judgement with regard to the greater flexibility granted to Member States regarding **reduced rates**, and the **two options** set out in the Action Plan in this respect, as more information is needed on the options proposed, how they would work and what rules they would be subject to. The **Committee** therefore prefers to set out a number of **criteria** for the future system. It must combine **flexibility and legal certainty**, it must be **transparent**, and for the sake of **simplicity** the number of **reduced rates and exemptions** must be **limited**. In the current circumstances, and based on currently available information, the Committee would prefer option 1, as it is the most closely aligned with the aforementioned criteria.

## 2. **Background**<sup>1</sup>

- 2.1 The Action Plan on VAT sets out a pathway for the creation of a single VAT area in the EU. The area should be able to support the single market, help to promote jobs, growth, investment and competitiveness and meet the demands of the 21st century. The new system should be simpler, more fraud-resistant and more business-friendly.
- 2.2 The current VAT system is highly fragmented and complex, at least in a cross-border context. It has not kept pace with the challenges of the new global, digital and mobile economy. There is a major discrepancy between anticipated and actual VAT revenues (the “VAT gap”) and the system is susceptible to fraud.

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<sup>1</sup> The following is broadly based on the action plan.

- 2.3 The proposed approach would modernise and “reboot” (re-launch) the VAT system. Other approaches are not seen as valid options. Any changes to the system require the unanimous approval of all Member States.
- 2.4 The Action Plan has four components, and includes at least 27 measures<sup>2</sup>. A number of them have been drawn up in accordance with the Better Regulation Guidelines (REFIT).
- 2.4.1 The key principles underpinning a **future single VAT area** undoubtedly form the core of the Action Plan and are the most important chapter thereof. The aim is to put forward a proposal for definitive rules in 2017.
- 2.4.1.1 The **definitive VAT system** will be based on the principle of taxation in the country of destination of goods and services<sup>3</sup>, because the country of origin principle has been shown not to be feasible. This applies to all operations, including cross-border transactions. The method of collection shall gradually move towards a more fraud-proof system. These proposals would be implemented in two stages.
- 2.4.2 In addition, there are a **number of recent and ongoing initiatives**. These are as follows:
- The removal of obstacles to electronic commerce in the single market. The Commission plans to present a proposal in order to modernise and simplify VAT, especially for SMEs, by the end of 2016.
  - Secondly, the launch of a package of measures for SMEs in 2017. These will be simplification measures that will have an impact on VAT compliance costs, which will benefit small enterprises.
- 2.4.3 The largest package relates to **urgent measures to tackle the VAT gap and VAT fraud**. The emphasis here is on the following:
- improving cooperation between tax administrations, and with customs administrations within the EU and with third countries;
  - moving towards more efficient tax administrations and strengthening the role of Eurofisc;
  - strengthening voluntary compliance with the rules;
  - tax collection;
  - In addition, there will also be an evaluation report on the Directive on the mutual assistance for the recovery of tax debts.

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<sup>2</sup> Seven are set out in the Plan and twenty in the document “20 measures to tackle the VAT gap”. See [http://ec.europa.eu/taxation\\_customs/resources/documents/taxation/tax\\_cooperation/vat\\_gap/2016-03\\_20\\_measures\\_en.pdf](http://ec.europa.eu/taxation_customs/resources/documents/taxation/tax_cooperation/vat_gap/2016-03_20_measures_en.pdf)

<sup>3</sup> The “country of destination” principle.

2.4.4 The final objective here is to move - in the longer term - towards a **modernised rates policy**. The idea is to give Member States greater freedom and flexibility on rates, particularly **reduced rates**. Initiatives will follow in 2017.

### 3. **Observations and comments**

#### 3.1 *The Action Plan*

3.1.1 The EESC welcomes the Action Plan, which is aimed at moving towards a single EU VAT area. It is an ambitious, urgent and necessary action plan that is in keeping with efforts to develop a more modern and competitive single market.

3.1.2 The EESC welcomes the approach based on 4 components<sup>4</sup> with a differentiated approach in the short and medium term. The idea is to overcome the weaknesses and shortcomings of the current transitional system and to take a qualitative step (“quantum leap”) forwards, in accordance with the needs of a single market.

3.1.3 The Committee endorses the proposed approach, in which the definitive VAT system will be based on the country of destination principle. It also notes that the new system must be clear, consistent, robust and comprehensive, as well as proportionate and future-proof. In this context, the EESC urges the European Commission, as a precaution, to examine the possibility of introducing a generalised reverse charge system<sup>5</sup> for all cross-border B2B transactions. Although the reverse charge mechanism is already used in some Member States to reduce VAT fraud in specific economic sectors, applying this principle more generally could result in the risk of VAT fraud being shifted to the retail sale stage.

3.1.4 The transition to a definitive system must be properly overseen. It is crucial here to improve the performance of national tax administrations and their cross-border cooperation and to address the system’s susceptibility to fraud. With a view to improving the collection of VAT and combating fraud, it is important to encourage the development and exchange of best practices throughout the EU. For example, the possibility could be considered of setting time limits for VAT accounting between Member States. Every effort should be made to close the VAT gap insofar as possible. This should both benefit authorities (correct VAT receipts!) and make the playing field more level for all suppliers.

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<sup>4</sup> See point 2.4 above.

<sup>5</sup> Also referred to by the English term "reverse charge system".

- 3.1.5 At the same time, it is of the utmost importance to make the system more business-friendly, with clarity and legal certainty being the primary considerations. It is also important to reduce the administrative burden, particularly for SMEs, without however undermining the comprehensiveness and other key characteristics<sup>6</sup> of the definitive VAT system. In this connection, efforts should be made to develop standard forms for VAT refunds, to pay refunds in good time, and to develop an accessible system of VAT rates.
- 3.1.6 Using the country of destination principle gives Member States freedom to define their own rates, but this must not lead to fragmentation and excessive complexity. A proportionate approach needs to be taken, in the interests of SMEs. Account should also be taken both of the latest developments in cross-border trade and the digital and mobile economy, and of all - existing as well as new - types of businesses.
- 3.1.7 For the EESC, efforts to create a modernised rates policy that give Member States greater flexibility on reduced rates<sup>7</sup> should, in principle, come under the objective of applying the “country of destination” principle, given that fewer trade distortions should normally occur under such circumstances. The number of exceptions should be limited and, in order to improve economic efficiency, publicly and privately supplied goods and services should be treated in the same way<sup>8</sup> for VAT purposes. The broader the base on which VAT is applied, the lower the rate needs to be in order to achieve the same tax revenue. At the same time, this allows economic distortions to be avoided.
- 3.1.8 For the EESC, it is important for this Action Plan to be fully implemented in its entirety and as an indivisible whole, with all its elements. The lack of certainty that there may currently be in this respect is not in line with the goal of creating a VAT system for a single market, and is liable to compromise the stated objectives. The EESC believes that all necessary safeguards for achieving this objective should be built into the Action Plan. This applies in particular to the transition to the definitive VAT system in two stages, the second of which is currently<sup>9</sup> dependent on a separate assessment and a decision by the Member States. The aim should be for the actual implementation of the definitive VAT system in the second stage to be carried out in any event and within a reasonable time-frame.

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<sup>6</sup> See point 3.1.3.

<sup>7</sup> See point 2.4.4 above.

<sup>8</sup> For example, in the healthcare sector, private businesses generally have to charge VAT, whereas public suppliers are often exempt.

<sup>9</sup> In the current version of the plan. See the last paragraph of point 4.



- 3.1.9 With a view to the full implementation of the Action Plan, the Committee calls on the Member States to cooperate to enhance and step up the exchange of information and to build trust in the efforts being made to implement the texts and increase VAT revenues. In the Committee's view, the Member States will thus need to strengthen the capacity of their tax administrations, which will need to have adequate human, financial and technical (including ICT) resources. The Committee calls for the Commission to provide support in this regard.
- 3.1.10 The Committee expects the Commission to submit, in due time, an in-depth and comprehensive impact assessment of the proposed measures and of the Action Plan as a whole. It must include an assessment of the impact on SMEs, for which complexity and administrative burden present significant challenges.
- 3.2 *The main objective: moving towards a robust single European VAT area — a definitive VAT system*
- 3.2.1 The EESC supports the choice of the country of destination principle, thus creating a level playing field for all suppliers on the same national market, regardless of where they are based.
- 3.2.2 Under the Action Plan, in the first stage of the transition to the definitive VAT system the country of destination principle will be applied only to goods. For the sake of simplicity and to avoid further complications, the Committee urges the Commission and the Member States to look into how services can be incorporated into the new system more quickly, and to explore ways of making financial services more generally subject to VAT.
- 3.2.3 There is a risk that implementation of the new system could increase the administrative burden for businesses, and the Committee therefore highlights the need for simpler VAT rules, particularly for SMEs, that do not, however, undermine the comprehensiveness of the system. At the same time, considerable attention needs to be paid to the clarity of the rules and legal certainty.
- 3.2.4 It must be an easy and attractive option for businesses to expand their activities across borders within the EU. In cross-border transactions, the country of destination principle means that suppliers apply the VAT rate applicable in their customers' Member States, which can lead to complications and additional burdens. Indeed, it may mean that they have to deal with the systems in all 27 other Member States. In order to ensure that the resulting burden remains manageable, provision should be made for public information systems such as a web portal showing, among other things, the rates applicable in all Member States. It is likewise important that businesses should only need to register in the country where they are established. The EESC therefore welcomes the Commission's proposal that the requirement to register for VAT purposes should apply only in the country of establishment, which should save the businesses concerned an estimated EUR 1 billion.

### 3.3 *Measures to close the VAT gap and tackle fraud*

- 3.3.1 The EESC welcomes the focus on closing the VAT gap and tackling the susceptibility of the VAT system to fraud, particularly as the losses for the authorities amount to EUR 170 billion per year, which is equivalent to 15.2% of total VAT revenue. Cross-border fraud alone represents EUR 50 billion annually.
- 3.3.2 It is important to make this objective a priority and to deliver results without delay. Without prejudice to various actions provided for in the Action Plan in this regard, the EESC wonders whether or not other, additional tools should be used, following the example of the recent international commitments on direct taxation, including those relating to exchanging information and the Commission's plans<sup>10</sup> to combat tax avoidance.
- 3.3.3 In the same vein, the EESC believes that there should be a strong focus on the intrinsic characteristics and features of the definitive VAT system in terms of its susceptibility to fraud. The fact that fraud can be reduced considerably<sup>11</sup> by applying a system of staggered payments to cross-border operations does not mean that we can rest on our laurels.
- 3.3.4 The new rules, appropriate supervision and greater control using the necessary means of enforcement, including judicial means, should consistently lead to a more comprehensive VAT system applied with greater effectiveness.
- 3.3.5 For the EESC, it is important that targeted measures should be taken to close the VAT gap and tackle fraud. Measures to close the gap must be compatible with the proportionality principle and improve the functioning of the internal market. “Bona fide” enterprises should be protected and no new excessive measures should be imposed on them.
- 3.3.6 Weaknesses and gaps in the current system, such as the exemption for imports of small consignments by non-EU suppliers, create an uneven playing field, distort the market and lead to substantial revenue losses for the authorities (estimated to be EUR 3 billion annually). If such a scheme is considered fundamentally inappropriate in a modern EU VAT system, then the Committee calls, with a view to costs, for a nuanced approach whereby transactions that genuinely have no market-distorting effect are possibly exempted, as in the case, for example, of small and sporadic low-value consignments for purely private purposes.

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<sup>10</sup> See the proposal for a Council Directive laying down rules against tax avoidance practices that directly affect the functioning of the internal market, published by the Commission on 28 January 2016 (known as the Anti-BEPS Directive). See <http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1465293669136&uri=CELEX:52016PC0026> and [http://europa.eu/rapid/press-release\\_IP-16-159\\_en.htm](http://europa.eu/rapid/press-release_IP-16-159_en.htm);

In this connection see also EESC opinion ECO/405 of 28 April 2016 on the anti-tax avoidance package; <http://www.eesc.europa.eu/?i=portal.en.eco-opinions.38303>

<sup>11</sup> By approximately EUR 40 billion or 80%.

3.3.7 Lessons could also be drawn from the past. In this connection, consideration could be given to the appropriateness, in future, of a broad evaluation of the VAT system: not only of its rules and how it works, but also, more broadly, of whether it meets the requirements of the economy and of the authorities, and of how it contributes to the European project. Such an evaluation could take place at regular intervals.

#### 3.4 *Taking account of a number of new developments in e-commerce and the types of businesses*

3.4.1 The EESC welcomes the Action Plan's focus on innovative business models and technological progress in an increasingly digital environment. More broadly, it is essential to take account of all major and forward-looking developments. This would also make the definitive VAT system more future-proof.

3.4.2 For the EESC, the important point here is that, in these circumstances, the VAT rules should be set in such a way as to ensure clarity and certainty for all stakeholders.

3.4.3 In the same way, it must be ensured that all suppliers offering the same goods or services – cross-border or not – are treated equally, irrespective of whether they are following the latest developments (the digital approach), or are sticking to more traditional channels and methods (physical). The EESC advocates implementing simplification measures such as the common EU VAT threshold in order to make things easier for e-commerce start-ups, and calls for this to be opened up to all SMEs.

#### 3.5 *Taking account of SMEs' needs*

3.5.1 The Committee welcomes and highlights the consideration given by the Action Plan to SMEs. It is important and essential that the Action Plan provides for a whole host of specific measures with fair and appropriate rules for SMEs. This point has already been made elsewhere in this opinion.

3.5.2 The intention of providing for a broad package of simplification measures for their benefit is welcome. However, these intentions as set out in the Action Plan need to be further clarified and fleshed out. For the EESC, it is important for SMEs to be involved in this from the outset.

3.5.3 For agricultural enterprises, it would be desirable for the current option of providing compensation for the VAT paid on certain purchases to be turned into an obligation on all Member States. At the same time, the transformation of agricultural products by organisations of agricultural producers or similar organisations should be put on a par with agricultural production.

#### 3.6 *Measures on reduced rates*

3.6.1 With regard to the increased flexibility on reduced rates, the Committee highlights its concern that this could lead to greater fragmentation of VAT rates between Member States, which would be detrimental to the clarity and applicability of the system, particularly for SMEs.

- 3.6.2 The Committee reserves judgement with regard to the two options set out in the Action Plan, as more information is needed on the options proposed, how they would work and what rules they would be subject to. The Committee therefore prefers to set out a number of characteristics for the future system. It must combine flexibility and legal certainty, it must be transparent, and the number of reduced rates and exemptions must be limited. In the current circumstances, and based on currently available information, the Committee would prefer option 1<sup>12</sup>, as it is the most closely aligned with the aforementioned criteria.
- 3.6.3 The Committee calls for the role and strategic importance of social enterprises<sup>13</sup> to be taken into account in the future definitive VAT system. In this respect, consideration could be given to revising point 15 of Annex III of Directive 112/2006 or adding a new provision on applying the reduced rate for social, health and education services for disadvantaged persons provided by institutions recognised as being devoted to social wellbeing. In particular, consideration should be given to exempting, or applying a lower rate to, products and services for disabled and disadvantaged people in the new VAT system.
- 3.6.4 It is also important to maintain the existing VAT exemptions for voluntary organisations that have already been authorised in a number of Member States, due to the specific nature of the organisations concerned and the absence of a cross-border component.
- 3.6.5 In the framework of the revised VAT directive the possibility could also be examined of the individual Member States applying higher VAT rates than the standard rate to luxury products, and if so, which rules should apply in this case.
- 3.6.6 Council Directive 2006/112/EC has granted special reduced VAT rates and derogations to certain European islands and remote areas as a counterbalance to their natural, economic and demographic permanent handicaps. Given the importance of these regimes for insular enterprises and local economies, the EESC calls for their continuation.

Brussels, 13 July 2016

The President  
of the  
European Economic and Social Committee

Georges Dassis

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<sup>12</sup> Option 1 involves the “extension and regular review of the list of goods and services eligible for reduced rates”.

<sup>13</sup> On the importance of the social economy, see the Commission's communication on the *Social Business Initiative – Creating a favourable climate for social enterprises, key stakeholders in the social economy and innovation* (COM(2011) 682).