Europaudvalget 2017
KOM (2017) 0569
Offentligt

Brussels, 4.10.2017
SWD(2017) 325 final

COMMISSION STAFF WORKING DOCUMENT

IMPACT ASSESSMENT

Accompanying the document

Proposal for a Council Directive

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

{COM(2017) 567final}
{COM(2017) 568 final}
{COM(2017) 569 final}
{SWD(2017) 326 final}

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Abbreviations

B2B	Business to Business
B2C	Business to Consumer (not VAT registered)
CJEU	Court of Justice of the European Union
CTP	Certified Taxable Person
EU	European Union
EUR	Euro
FTE	Full Time Equivalent
GDP	Gross Domestic Product
GFV	Group on the Future of VAT
MOSS	Mini One Stop Shop
MTIC fraud	Missing Trader Intra-Community (MTIC) fraud
OSS	One Stop Shop
SME	Small and Medium-sized Enterprises
VAT	Value Added Tax
VEG	VAT Expert Group
VIES	VAT Information Exchange system.

Glossary of terms in their meaning within this document and for its specific purpose

Administrative costs	Costs for tax administrations. Administrative costs for a tax administration will include costs relating to the following activities: processing VAT registrations, undertaking VAT audits, reviewing VAT returns, reviewing recapitulative statements, helpline and written query handling and the implementation of new legislation.
Business types Large business Micro business SME Type 1	 A large business is defined as a business with a turnover exceeding EUR 50 million, having more than 250 employees, and possessing VAT registration in six or more Member States. For further details on the definition of a large business, please see Annex 4. A micro-business is a business which has fewer than ten employees and a turnover or balance sheet total of less than EUR 2 million. An SME (Small and Medium-sized Enterprises) Type 1 business is defined as a business with a turnover of less than EUR 50 million, having less than 250 employees and a single VAT registration in its Member State of establishment. Further details on the definition of an SME Type 1 business are available in Annex 4.

SME Type 2	An SME (Small and Medium-sized Enterprises) Type 2 business is defined as a business with a turnover of less than EUR 50 million, having less than 250 employees and VAT registrations in more than one (but less than six) Member States. Further details on the definition of an SME Type 2 business are available in Annex 4.
Compliance costs	Costs for businesses. Compliance costs for businesses will include costs relating to the following activities: registration for VAT, completion of periodic VAT returns, dealing with a VAT audit, obtaining customer's VAT registration details, completing recapitulative statements and obtaining proof of the intra-EU movement of goods.
Cross-border trade	Refers solely to intra-EU cross-border B2B trade. The terms "trading across the EU", "trading cross-border", "trading in another Member State", "doing business in other Member States", "doing business across the EU", "intra-EU transactions, "intra-EU trade" refer to any situation where a business: (i) makes supplies of goods taxable in a Member State other than that in which he is established; (ii) acquires goods from a business established in another Member State; or (iii) supplies goods to a customer established in another Member State.
EU VAT Forum	The EU VAT Forum was set up by a decision of the European Commission 2012/C198/05 of 3 July 2012 and offers a discussion platform where business and VAT authorities meet to discuss how the implementation of the VAT legislation can be improved in practice.
EUROFISC	EUROFISC is a network for the swift exchange of targeted information between Member States. See information under following link EUROFISC.
Expert stakeholders	Members of the VAT Expert Group
Full Time Equivalent (FTE)	A Full Time Equivalent is a unit that indicates the workload of an employed person of a business or a Member State Tax Authority. For the purposes of this document, it is defined as forty hours per week.
Group on the Future of VAT (GFV)	The Group on the Future of VAT is an informal Commission expert group set up in 2011 in response to the need for a forum where more in-depth discussions on the topics raised in the 2010 Green Paper can be held. The Group is composed of delegates (VAT experts) from the 28 EU Member States' tax administrations and serves as a forum for in-depth discussion and exchange of opinions on the Commission's pre-legislative initiatives and the preparation of future VAT legislation.
Treasury	A government department related to finance and taxation of a particular jurisdiction (of a Member State or a third country)
VAT Committee	Under Article 398 of the VAT Directive (Directive 2006/112/EC), the VAT Committee deals with the obligatory consultations required by certain Articles of that Directive. In

	addition, it examines questions on the application of the Community VAT provisions raised by the Chairman on his own initiative or at the request of a Member State. The VAT Committee is also a forum for the exchange of views in order to reach guidelines on a uniform application of common practices with regard to VAT provisions.
VAT Expert Group (VEG)	The VAT Expert Group was set up in 2012 by Commission Decision 2012/C 188/02 of 26 June 2012 in response to the request by stakeholders for greater involvement in the process of preparing EU VAT legislation expressed during the public consultation launched by the 2010 Green Paper on the future of VAT. The Group is composed of 40 members: individuals with the requisite expertise in the area of VAT and organisations representing in particular businesses, tax practitioners and academics, and serves as a bilateral forum to allow for an open, structured and transparent dialogue between the Commission and stakeholders on any matter relating to the preparation and implementation of EU legislation and other policy initiatives taken at EU level in the field of VAT.
VIES	Electronic means of validating VAT-identification numbers of economic operators registered in the European Union for cross-border transactions on goods or services. See more info on: http://ec.europa.eu/taxation_customs/vies/

1. INTRODUCTION AND CONTEXT

1.1. Introduction

Value Added Tax (VAT) is a general tax on consumption applied to supplies of goods and services along the whole production and distribution process. It is a major and growing source of tax revenue in the European Union (EU). VAT raised slightly more than EUR 1 trillion in 2015, which corresponds to 7% of EU GDP or 17.6% of total national tax revenues[1]. One of the EU's own resources is also based on VAT (12.4% of the EU budget in 2015)[2]. As a broad-based consumption tax, it is considered to be one of the most growth-friendly forms of taxation.

One of the key strengths of VAT is that, by allowing businesses to exactly offset the tax incurred in previous stages of the production chain, it is much better suited than other types of indirect taxes to operate an internal market free of tax distortions. This was the main reason for its early adoption by the EU. It is governed by the VAT Directive[3] which aims at ensuring that the principles underlying the functioning of this tax apply consistently in all Member States.

In recent years, however, the VAT system has been unable to keep pace with the challenges of the global economy and the opportunities offered by new technologies. Therefore, the Commission adopted on 7 April 2016 an Action Plan on VAT[4] (hereinafter "Action Plan") setting out ways to modernise the VAT system so as to make it simpler, more fraud-proof and business-friendly. In this context, the Commission announced its intention to adopt in 2017 four VAT-related proposals:

1) a definitive VAT system for intra-EU cross-border trade based on the principle of taxation in the Member State of destination[5] in order to create a robust single European VAT area (first legislative step[6]);
2) a modernised VAT rates policy so as to allow Member States greater autonomy on setting the VAT rates;
3) a comprehensive simplification VAT package for SMEs[7];
4) a proposal to enhance VAT administrative cooperation and EUROFISC[8].

This impact assessment relates to the first mentioned proposal on a definitive VAT system for intra-EU trade (hereafter the "initiative").

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[1] Eurostat, Tax revenue statistics, Eurostat (gov_10a_taxag) http://ec.europa.eu/eurostat/statistics-explained/index.php/Tax_revenue_statistics

[2] European Commission, EU Budget 2015, Financial Report http://ec.europa.eu/budget/financialreport/2015/lib/financial_report_2015_en.pdf

[3] Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax – as amended (OJ L 347, 11.12.2006, p. 1).

[4] See 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).

[5] The principle of taxation at destination, as well as of taxation at origin, is commented under Section 1.4.2 below and in Annex 5, Section 2.

[6] See Sections 1.2.2 and 8.1 for more explanations.

[7] See Glossary.

[8] See Glossary.

This initiative is part of the Commission's Regulatory Fitness and Performance Programme (REFIT). All the options (except baseline) of this initiative will likely have significant impacts on simplification and will reduce administrative burden and compliance costs. These benefits for businesses (including SMEs) would have a positive impact on economic growth and competitiveness.

1.2. Scope of the initiative

1.2.1. Taxation of trade between Member States

The VAT Directive defines the way in which VAT is to be collected both on domestic transactions (involving one single Member State) and on cross-border transactions (involving more than one Member State). As explained in Section 1.4 below, the current system for the taxation of trade between Member States is based since 1993 on "transitional arrangements"[9].

These transitional arrangements suffer from numerous shortcomings which result in the VAT system being neither fully efficient nor compatible with the requirements of a true single market. This has been confirmed by the large majority of stakeholders during the broad based public consultation on the Green Paper on the future of VAT[10] and by more recent feedback received from business stakeholders via the REFIT Platform[11](see further details in Annex 2 and Annex 5, Section 3). The European Parliament, the European Economic and Social Committee and the Tax Policy Group[12] also confirmed the need to reform the VAT system.

Further consultation with the Member States and other stakeholders in the framework of specialised and structured forums for discussion, respectively the Group on the Future of VAT (GFV[13]) and the VAT Expert Group (VEG[14]) (see more detailed information in Annex 1, Section 4), led to the conclusion that the transitional arrangements are too complex and costly for the growing number of businesses operating cross-border. It also showed that the transitional arrangements leave the door open to fraud.

While the reform of the taxation of trade between Member States regarding transactions between businesses and final consumers (hereafter "B2C[15] transactions") has started to be effective as from 1 January 2015[16] and its further development is currently the subject of negotiations in Council[17], the initiative that is here being assessed is focussed exclusively on transactions between businesses (hereafter "B2B[18] transactions").

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9 See Article 402 of the VAT Directive and further explanations in the next sections.

10 COM(2010) 695, Commission Staff Working Document, SEC(2010) 1455, 1.12.2010.

11 https://ec.europa.eu/info/law/law-making-process/overview-law-making-process/evaluating-and-improving-existing-laws/reducing-burdens-and-simplifying-law/refit-platform/refit-platform-recommendations_en

12 Composed of the personal representatives of the EU's finance ministers.

13 See Glossary.

14 See Glossary.

15 See Abbreviations.

16 For telecommunications, broadcasting and electronic services - see Council Directive 2008/8/EC and related legislation here: https://ec.europa.eu/taxation_customs/business/vat/telecommunications-broadcasting-electronic-services_en#new_rules

17 See VAT "e-commerce" proposal (COM(2016) 757 final).

18 See Abbreviations.

The purpose of this initiative is to put in place a definitive VAT system so as to pave the way for the creation of a genuine single EU VAT area for the internal market. This means a VAT system simpler for businesses trading across the EU while at the same time more robust to fraud, to the benefit of the Member States and also of compliant businesses. The efficiency of the VAT system needs to be further improved, in particular by exploiting the opportunities of digital technology and by enhancing greater trust between business and tax administrations and between EU Member States' tax administrations.

1.2.2. Rationale for a two-step approach

As announced in the Action Plan, the introduction of the definitive VAT system will be made through a gradual two-step approach[19]. As a first legislative step, the VAT treatment of intra-EU B2B supplies of goods would be settled. As a second legislative step, this treatment would be extended to all cross-border supplies, therefore also covering supplies of services. Only the first legislative step is the subject of the initiative that is here being assessed.

There are several reasons for this. In the first place, the introduction of the definitive VAT system means, above all, doing away with the transitional arrangements. These arrangements basically refer to goods. This owes to the fact that prior to 1 January 1993 only cross-border intra-EU supplies of goods (and not of services) gave rise to imports and exports. The transitional arrangements were a practical means of accommodating this situation. Therefore any attempt to replace those transitional arrangements will have to focus essentially on goods.

Second, the application of the principle of taxation at destination becomes particularly necessary when it comes to goods. As regards services, on 4 December 2007 the Council reached a political agreement on two draft Directives and a draft Regulation (the so-called "VAT package") aimed at changing the rules on VAT so as to ensure that VAT on services accrues to the Member State where consumption occurs[20], i.e. according to the principle of taxation at destination. Its adoption by the Council on 12 February 2008 was an important step towards simplification for businesses[21].

The rules regarding B2B supplies of goods remained however unchanged. Despite the fact that, in practice, their taxation effectively occurs at destination (i.e. where the goods arrive) the logic of the origin principle with its two transactions[22] still remains.

Third, intra-EU B2B trade in goods still requires a number of obligations which do not exist for services (e.g. proof of intra-EU transport of the goods, need to register in another Member State for particular transactions like consignment stocks, need to ascribe the intra-EU transport to a specific supply in the case of chain transactions - see further explanation under Section 2.4). There is therefore now a particular need to simplify the rules for goods.

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[19] See Action Plan.

[20] See press release on http://europa.eu/rapid/press-release_IP-08-208_en.htm?locale=en

[21] See further information on this "VAT package" on http://ec.europa.eu/taxation_customs/business/vat/eu-vat-rules-topic/where-tax_en

[22] A supply of goods taxable in the Member State of origin but exempt of VAT in case it can be proved that these goods have been transported to another Member State, and an intra-EU acquisition of goods taxed in the Member State of destination – see further explanations under Section 1.4.3 below.

Fourth, as will be seen further the preferred option for the definitive VAT system[23] builds on certain new technical solutions (a one-stop-shop mechanism (OSS) which includes the right to deduct input VAT - see further explanation in box 5 below). It seems reasonable to provide for a staged application of these solutions so that once they have proven to be efficient on transactions in goods, they will be also extended to intra-EU supplies of services. Such an approach has the advantage of limiting to one category[24] the number of transactions that will be affected by the new rules and of reducing the amounts of VAT channelled through the OSS.

In this regard, the staged approach is consistent with the one taken in VAT matters regarding the OSS. Initially a Mini One Stop Shop (MOSS - see further explanation in box 5 below) was established for B2C telecommunications, broadcasting and electronic services provided by third country suppliers[25]. That MOSS was later extended to intra-EU cross border supplies of those same services[26]. Next, it is foreseen in the e-commerce proposal for the OSS to be extended to intra-EU B2C supplies of goods and services and to supplies of goods imported from third countries or third territories[27]. The initiative means a further step in this direction targeting intra-EU B2B supplies of goods. Finally, the process will be completed at a later stage with the extension of the OSS to intra-EU B2B supplies of services.

In any event, the stage embodied by the initiative is an essential one since, as can be seen from the figures below, goods remain the main elements that are being traded across the EU as services represent only one third of the share of goods' transactions[28]. In focussing on goods, as a first step, the objective of reducing VAT losses resulting from cross-border fraud would also be better targeted.

Cross-border transactions in the EU single market, 2015	
Intra-EU 28 trade (2015)	**In billion EUR**
Goods	
Export (dispatches)	3.068
Imports (arrivals)	2.993
Services	
Export (credit)	1.016
Imports (debit)	923

23 The preferred option for the implementation of the definitive VAT system is Option 2 (see full description of Option 2 under Section 5.4).

24 Note that the VAT system relies on a fundamental distinction between supplies of goods and supplies of services with consequences on a number of other elements of the tax (e.g. taxable moment, VAT rates).

25 Council Directive 2002/38/EC of 7 May 2002 (OJ L 128, 15/05/2002 P. 0041 – 0044).

26 Council Directive 2008/8/EC of 12 February 2008 (OJ L 44, 20.2.2008, p. 11–22); Council Implementing Regulation (EU) No 1042/2013 of 7 October 2013 amending Implementing Regulation (EU) No 282/2011 as regards the place of supply of services (OJ L 284, 26.10.2013, p. 1–9).

27 See VAT "e-commerce" Proposal (COM(2016) 757 final).

28 Both for exports/dispatches and imports/arrivals – according to the EU terminology for intra-EU trade.

Source: Eurostat

In addition and with a view to accommodate the specific request from Member States in Council[29], the initiative will also propose certain improvements to the current VAT legislation. These improvements (hereafter the "quick fixes") are meant to address specific concerns with the current rules and are without prejudice to the more fundamental reform aimed at[30].

1.3. Interaction of the initiative with the upcoming VAT proposals on rates, SMEs and administrative cooperation

The initiative on the definitive VAT system is an important step towards a modernised VAT system. It builds upon previous initiatives[31] and creates opportunities for the following particular areas that will each give rise to own legislative proposals.

1.3.1. VAT rates

Although the destination principle has been progressively implemented since 2008[32], the initiative operates a fundamental (and therefore "definitive") change in the basic logic of the VAT system. The choice of a destination-based system raises the question of whether, and to what extent, the existing legal limits on rates are still necessary. Indeed, while harmonisation of the VAT rates is needed under an origin-based system to avoid distortions of competition[33], this is not the case under a destination-based system. That is what the proposal on VAT rates will address. However, even without a change in the current VAT rates structure, the initiative[34] will have consequences on the collection of VAT. Therefore, the initiative will, independently from the proposal on VAT rates, provide for a central web-portal that will include information on the VAT rates applicable in all Member States.

1.3.2. SMEs

The fundamental nature of the changes made by the initiative means that all businesses will be impacted. While the simplification measures provided for under the initiative would also benefit SMEs, they are not specifically targeted to help SMEs. The

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[29] See Council conclusions on improvements to the current EU VAT rules for cross-border transactions of 8 November 2016 (No. 14257/16 FISC 190 ECOFIN 1023 of 9 November 2016).
http://data.consilium.europa.eu/doc/document/ST-14257-2016-INIT/en/pdf
This followed a first reaction on the VAT Action Plan of the Council of 25 May 2016
http://www.consilium.europa.eu/en/press/press-releases/2016/05/25-conclusions-vat-action-plan/

[30] As will be explained further on, these improvements are those covered by Option 1. Although Option 1 is not as such retained as the preferred option for the implementation of the definitive VAT system, Option 1 has been retained to solve on a "quick" basis specific problems with the current transitional VAT system. Since the benefit for businesses of some simplifications provided for under this Option 1 are linked to a concept (the concept of CTP – see Box 4) that will be used under the preferred option, this Option 1 is viewed as preparing the grounds for the implementation of the preferred option.

[31] Above mentioned "VAT package" concerning supplies of services and recent proposals on e-commerce.

[32] See Section 1.2.1 above.

[33] Because suppliers located in lower-rate jurisdictions would benefit from a tax advantage.

[34] As explained in the rest of the document, the preferred Option 2 provides that the supplier will, as a rule, collect the VAT on his cross-border supply at the rate applicable in the Member State of his customer.

difficulties of SMEs, in particular when trading cross-border, will be addressed through a specific proposal[35].

1.3.3. Administrative cooperation

As will be explained later, one of the problems the initiative intends to tackle is VAT cross border fraud. However, since the full operation of the initiative will take some time, it is necessary to already improve the mechanisms in place in order to fight this type of fraud. Improved administrative cooperation between the Member States and a better functioning of the VIES system[36] (which will allow enhancing the quality and reliability of the information exchanged between the Member States) are elements which, at the same time, will in the short term improve the fight against fraud and in the medium term will support each step of the implementation of the definitive VAT system. Further, it will allow building trust between the Member States, which will facilitate the proper operation of the initiative[37].

As can be seen, there is a direct link between the four proposals in that they together result in a coherent reform as put forward in the Action Plan. This is why they are planned to be adopted by the Commission this year as a package. However, although they are logically connected, the four proposals are nevertheless technically not linked. This means that each proposal can work on its own independently of the others although it would be preferable, for the sake of soundness of the reform, to have them all adopted by the Council.

1.4. Functioning of the common system of value added tax

1.4.1. Basic principle: the fractioned collection of VAT

VAT is assessed on the value added to goods and services that are bought and sold for use or consumption in the EU[38]. It is, as a rule, collected fractionally[39] by businesses[40] and, as a consumption tax, is borne ultimately by the final consumer[41].

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35 As explained under Section 5.4, the preferred Option 2 entails, as a rule, the necessity for the supplier to charge the VAT of the Member State of his customer. While the use of the OSS is in this respect a simplification for most businesses, further simplification for SMEs will be considered under the upcoming VAT package for SMEs (see Section 1.1.).

36 See Glossary.

37 As explained in the rest of the document, the preferred Option 2 notably relies on the assumption that the VAT due on a cross-border transaction in a given Member State is collected by another Member State that will also have the main responsibility for auditing the VAT due.

38 Further explanations on the common VAT system can be found here: http://ec.europa.eu/taxation_customs/taxation/vat/what_is_vat/index_en.htm

39 The supplier of a good or a service is considered for VAT purposes to be the person liable to pay the VAT collected to the Treasury (Article 193 of the VAT Directive). However, under particular circumstances (Articles 194 to 199b of the VAT Directive), the VAT Directive provides for (or allows Member States) the application of the so-called "reverse charge mechanism" that deviates from this rule which is the basis of the fractioned collection of VAT. Under a reverse charge, the liability is moved to another person, in general the customer.

40 Reference is made to “businesses” for simplification reasons but the correct terminology would be “taxable persons”. The scope of the concept of “taxable person” can be found in Articles 9 to 13 of the VAT Directive.

41 A final consumer means for VAT purposes the last person in a production/distribution chain who is not allowed to deduct the VAT he paid on his purchases (contrary to VAT taxable persons who can do so).

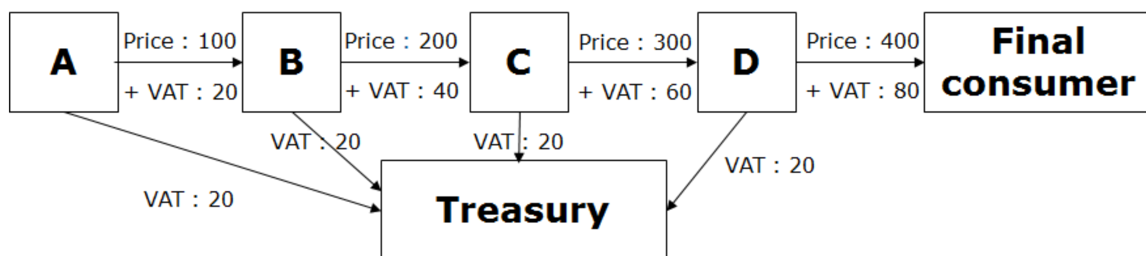
This system of partial payments allows the tax to be collected at each stage in the production and distribution chain[42] and ensures the self-policing character of this tax (see box 1 below).

Box 1: VAT system based on fractioned payments

On each supply made by a business, VAT is charged to its customers at the rate applicable. That business then deducts from the VAT collected from its customers the amount of tax it has itself paid to other businesses on purchases used for its own business activities. Where the customer is also a business, this system is replicated until it reaches the final consumer. At this last stage of the supply chain, the VAT is no more deductible and the tax is definitively vested to the Treasury.

Example: VAT rate is 20%

A, B, C and D are businesses, i.e. taxable persons with a right to deduct input VAT



A sells goods to B for 100 and charges 20 VAT which is paid over to the Treasury. B supplies the goods to C for a total amount of 240 (including 40 VAT). B then deducts its input VAT of 20 from the 40 received from C and pays the difference of 20 to the Treasury. C sells these goods on to D for 360 (including 60 VAT). Then C deducts its input VAT of 40 from the 60 received from D and pays the difference of 20 to the Treasury. Finally, D sells the goods for 480 (including 80 VAT) to a final consumer. D deducts its input VAT of 60 from the 80 received and pays the difference of 20 to the Treasury.

At each stage, VAT is paid to the Treasury on the added-value. For a given business that is the difference between the price paid to it by its customer and the amount paid by the business to its supplier.

The self-policing character of the VAT system is linked to the need for each customer to pay VAT and to hold an invoice in order to be allowed to deduct the VAT paid to its supplier who, in turn, is discouraged from evading taxes (as it has issued an invoice). In case of fraud by the retailer (D) or anyone else in the chain (A, B or C), EUR 20 is lost, but not the total amount of EUR 80.

1.4.2. VAT treatment of intra-EU supplies of goods before 1993

When the common system of VAT was established in 1967[43], intra-EU cross-border supplies of goods between businesses were treated differently as compared with domestic

[42] The amount of tax collected at a particular stage of the production/distribution process corresponds to the tax on the value added at that stage.

transactions (see box 8 in Section 1 of Annex 5). They gave rise to exports exempted in the Member State of origin (Member State of departure of the goods) and were taxed upon import in the Member State of destination (Member State of arrival of the goods), according to the principle of taxation at the Member State of destination (for further explanation on origin and destination concepts see Section 2 of Annex 5).

However, the commitment was made already at that time to establish a definitive VAT system, based on the principle of taxation in the Member State of origin, which would therefore operate within the EU in the same way as it would within a single Member State.

1.4.3. VAT treatment of intra-EU supplies of goods since 1993

The abolition of fiscal frontiers between Member States by the end of 1992, of which the objective and timing were set out in the Single European Act[44], made it necessary to reconsider the way in which trade in goods was taxed in the EU. That was due to the fact that exports and imports were no longer possible for VAT purposes as far as intra-EU cross-border trade in goods was concerned. At that time, the goal remained that goods would be taxed in the Member State of origin, perfectly reflecting the idea of a genuine internal market.

Under that origin system, a business established in a Member State ("MS1") would invoice its cross-border supplies of goods to other Member States ("MS2") in exactly the same way as the domestic supplies in MS1; i.e. by charging the VAT of MS1. The taxable customer would be allowed to deduct that VAT, collected by MS1, in his VAT return submitted in MS2. Because of that so-called cross-border deduction, a compensation or clearing system had to be put in place for reallocating the revenues between the Member States. This system would, in practice, create a collective responsibility whereas under the then existing system each Member State was individually responsible for the administration, control and collection of its own VAT. A high degree of trust between Member States was therefore a pre-condition for the new system.

Another essential element in order for the origin system to work properly was the convergence or approximation of VAT rates (and some other technical aspects such as exemptions). Otherwise major distortions of competition would occur since consumers would tend to acquire goods, for fiscal reasons, from Member States applying low VAT rates. This would run counter to the basic principle of VAT neutrality.

However, on these two essential points Member States were unable to agree before the foreseen date and since the political and technical conditions were not ripe, transitional arrangements were instead adopted and entered into force on 1 January 1993 (see box 2 below). These arrangements split the cross-border intra-EU movement of goods into two different transactions: an intra-EU supply of goods exempt in the Member State of origin (the supplier does not charge VAT on his supply) and an intra-EU acquisition of goods taxed in the Member State of destination (the customer self-accounts for the VAT due via

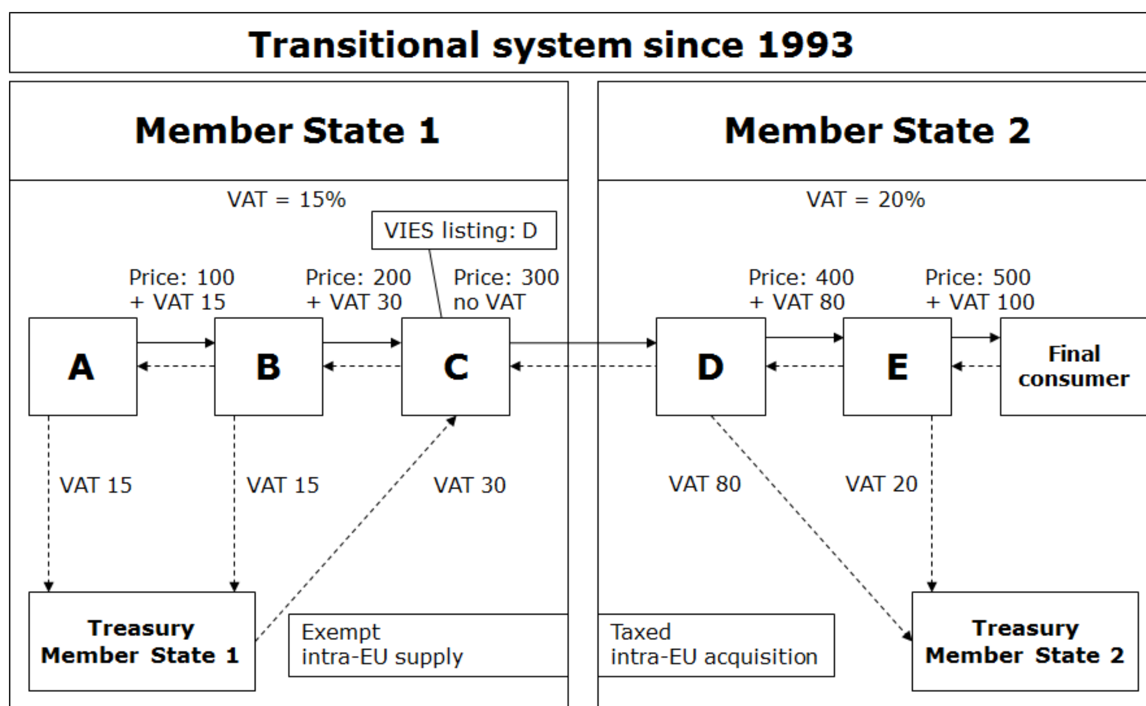
[43] First Council Directive 67/227/EEC of 11 April 1967 on the harmonisation of legislation of Member States concerning turnover taxes (OJ 71, 14.4.1967, p. 1301), Second Council Directive 67/228/EEC of 11 April 1967 on the harmonisation of legislation of Member States concerning turnover taxes — Structure and procedures for application of the common system of value added tax (OJ 71, 14.4.1967, p. 1303).

[44] Single European Act (SEA) signed in Luxembourg and The Hague, (OJ L 169 of 29.06.1987)

a mechanism equivalent to a "reverse charge[45]"). With some few exceptions, these arrangements are essentially equivalent to the previous export/import customs system.

These rules were intended to be temporary (initially four years) but are still in force. Further, the currently applicable VAT legislation provides that these temporary arrangements (hereinafter referred to as the "current transitional VAT system") have to be replaced by definitive arrangements based on the principle of taxation in the Member State of origin[46].

Box 2: Transitional VAT system since 1993



As from 1 January 1993, the fiscal frontiers and all corresponding export/import schemes between Member States have been abolished and replaced by a system of exempt supplies in the Member State of origin and taxed 'intra-EU acquisitions[47]' (a new taxable event) in the Member State of destination thus mirroring, but without customs procedures, the previous scheme. As customs documentation no longer guaranteed the follow-up of the physical flow of the goods, a new reporting system was put in place: the VAT Information Exchange System (VIES). Via a system of listings, submitted by the supplier in the Member State of origin (Member State 1) and subsequently sent to the Member State of destination (Member State 2), the latter is informed about the arrival of goods on its territory destined for D, a business registered for VAT purposes in Member State 2 and obliged to declare this intra-EU acquisition in its VAT return. Preceding supplies (A to B and B to C) and subsequent supplies (D-E) are, as in the previous system, domestic supplies taxed with VAT. Both the VAT charged on the supply made by A to B, by B to C and by D to E and the VAT due by D on the intra-EU acquisition are as a rule deductible (as regards C through a refund since there is no output VAT on the

[45] See footnote 39.

[46] See Article 402 of the VAT Directive.

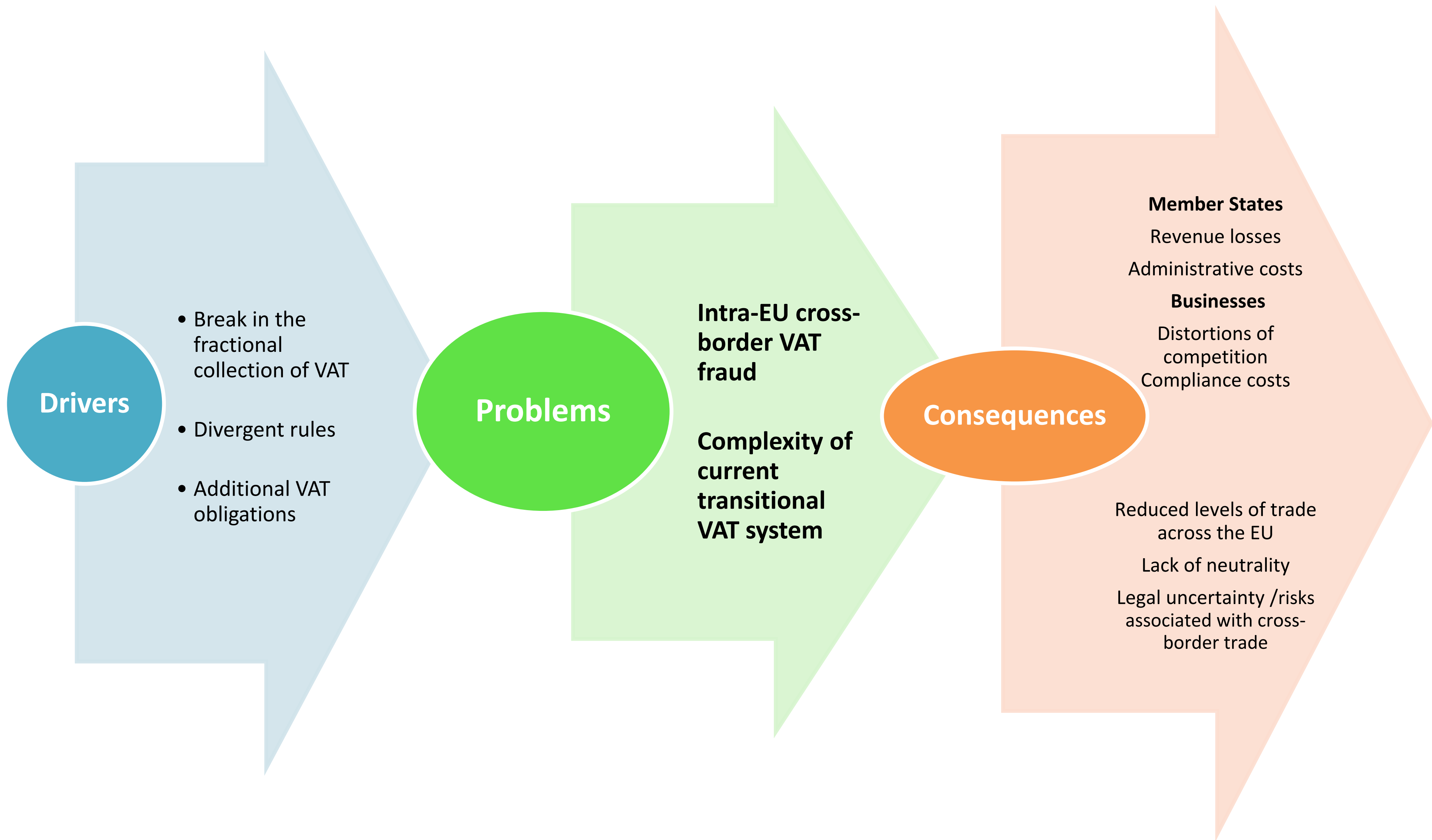
[47] The VAT Directive still refers to the "Community" instead of the "European Union" (EU). In the rest of the document, it is referred to "intra-EU acquisitions of goods" but the term used in the VAT Directive is "intra-Community acquisitions of goods".

supply made by C against which the deductible VAT of 30 can be offset). With regard to the intra-EU acquisition, D will account for VAT and deduct it in the same VAT return; the result is therefore nil.

2. WHAT IS THE PROBLEM AND WHY IS IT A PROBLEM?

2.1. Problem tree

The following figure summarises the problems, the problem drivers and the consequences as explained in the next sections.


Drivers
Break in the fractional collection of VAT
Divergent rules
Additional VAT obligations
Problems
Intra-EU cross-border VAT fraud
Complexity of current transitional VAT system
Consequences
Member States
Revenue losses
Administrative costs
Businesses
Distortions of competition
Compliance costs
Reduced levels of trade across the EU
Lack of neutrality
Legal uncertainty /risks associated with cross-border trade

2.2. Evaluation of the EU VAT system and other sources attesting to the problems

A comprehensive retrospective evaluation of the EU VAT system[48] was conducted in 2011 and its findings have been used as a starting point for the examination of the current transitional VAT system. This evaluation was a comprehensive exercise that covered all important aspects for the design of an improved VAT system.

The evaluation had been carried out before the Better Regulation Guidelines were put in place. This means in practice that the structure of the 2011 evaluation was not organized around the five evaluation criteria (Relevance, Effectiveness, Efficiency, Coherence and EU added value) that became mandatory later on. Nevertheless, the evaluation provided solid analysis of the problems underlying the current transitional VAT system, the results of which have been confirmed by further consultation of stakeholders (open public consultations, targeted stakeholder consultation through the GFV and the VEG - see Annex 2) as well as recent studies (see Annex 6). It looked in particular into the design and implementation of the most important elements of the current VAT system, including the functioning of the transitional VAT arrangements, and assessed their effectiveness and efficiency in terms of results (meeting objectives they were serving) and impacts (direct, indirect, expected and unexpected) they had created. It also examined their relevance and coherence with the smooth functioning of the single market and the requirement to avoid distortion of competition specified in Article 113 of the Treaty on the Functioning of the European Union.

The findings of the evaluation are therefore still valid and relevant for use in this impact assessment. A summary of the key elements of this evaluation organised around the five evaluation criteria mentioned above is provided in Annex 6.

According to the evaluation and further research, there are two fundamental problems regarding the current transitional VAT system:

1) The existing levels of VAT fraud within the EU caused by fraudulent activities such as Missing Trader Intra-Community fraud (hereinafter MTIC fraud)[49].

   This problem is referred to as "Intra-EU cross-border VAT fraud".

2) The complexity of the current transitional VAT system leading to additional costs for those businesses which engage in intra-EU cross-border trade.

   This problem is referred to as "Complexity of the current transitional VAT system".

The problems, their drivers and consequences are further developed below. For more details on the reform process and the sources attesting to the existence of the problems see respectively Sections 3 and 4 of Annex 5.

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[48] IFS et al., 2011.

[49] The concept of Missing Trader Intra-Community fraud (MTIC fraud) has no official definition. However it is commonly referred to as a particular type of VAT fraud committed by organised crime gangs which exploit the fact that, under the current transitional VAT system, trading between EU jurisdictions is VAT-free. The term "missing trader" refers to the fact that the trader goes missing with the VAT. See further development under Section 2.3.3 below.

2.3. Problem 1: intra-EU cross-border VAT fraud

2.3.1. The problem and its EU dimension

The evaluation of the EU VAT system[50] underlined the revenue losses that the Member States face as a result of the high levels of VAT fraud. According to this evaluation, although most of the VAT fraud is considered to be domestic, it has increased at EU level because of the growth in the phenomenon of MTIC fraud following the abolition of the EU's internal fiscal frontiers[51]. This particular fraud is associated to the fact that the current transitional VAT system allows trading VAT free across Member State borders (see further explanation under Section 2.3.3).

The size of the VAT fraud is difficult to measure but the VAT gap[52] offers a useful and also unique EU-wide indicator. According to the latest Commission report on the VAT gap[53] which relies on data from 2014, the overall EU VAT gap in nominal terms is estimated at almost EUR 160 billion in revenue losses each year or 14.06% of the total expected VAT revenue. The VAT gap varies considerably between Member States. The smallest gaps are observed in Sweden (1.24%), Luxembourg (3.80%), and Finland (6.92%). The largest gaps are registered in Romania (37.89%), Lithuania (36.84%) and Malta (35.32%). Overall, half of the EU-27 Member States[54] record a gap above 10.4% (see Figure 1 below).

That VAT fraud problem has been made worse, according to views expressed by certain Member States in the GFV and in the VAT Committee[55] by the case-law of the Court of Justice of the European Union (CJEU). According to that case-law the exemption of an intra-EU supply of goods cannot be refused if the material conditions for the exemption are met, even in absence of the VAT identification number of the customer acquiring the goods[56].

The problem created by this case-law stems from the fact that the EU legislator established the VAT identification number as the basic tool to control the proper functioning of the current transitional VAT system for intra-EU trade. In fact, the recapitulative statements and the VIES system[57], which are also essential elements of control in this regard, are all based on the VAT identification number and cannot work without it.

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50 IFS et al., 2011.

51 Abolition of intra-EU border controls for the completion of the single European market in January 1993.

52 The VAT gap is a measure of VAT compliance and enforcement that provides an estimate of revenue loss due to fraud and evasion, tax avoidance, bankruptcies, financial insolvencies, as well as miscalculations. The VAT gap is defined as the difference between the VAT revenue expected (the VAT Total Tax Liability or VTTL) and the VAT actually collected by national authorities. It is expressed in both absolute and relative terms.

53 CASE, 2016.

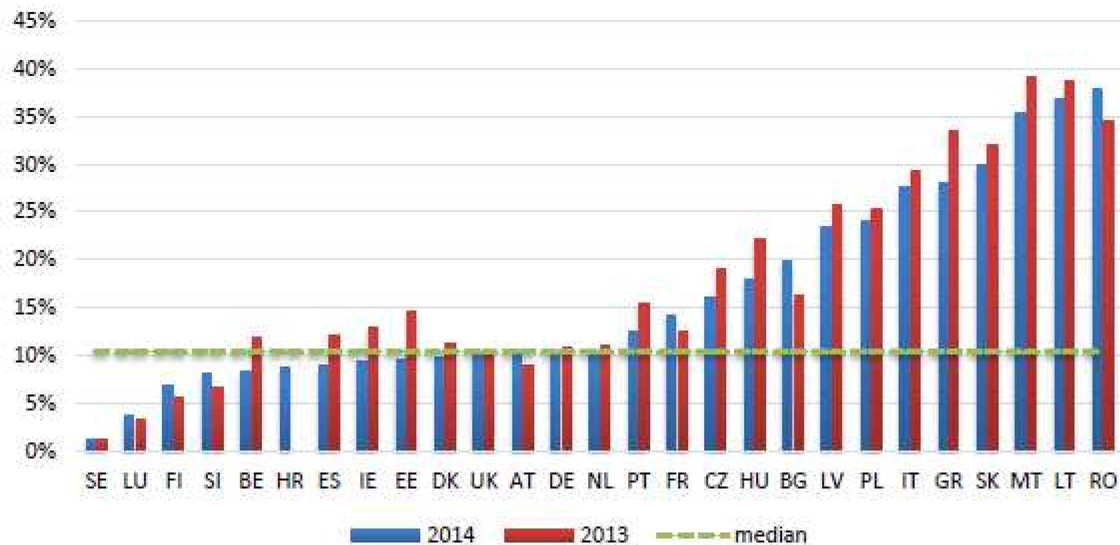
54 The report does not include estimates for Cyprus due to incomplete national accounts data.

55 See information about the role and functioning of GFV and this Committee in the Glossary.

56 According to the CJEU the possession of the VAT identification number of the customer is a formal condition, and not a substantive condition, for the exemption of an intra-EU supply – see the judgments of the CJEU in cases C-273/11 Mecsek-Gabona, C-587/10 VSTR, C-24/15 Plöckl and C-21/16 Euro Tyre.

57 See explanations under Box 10 in Annex 5, Section 6.

Figure 1: VAT Gap as a percent of the VAT Total Tax Liability (VTTL) in EU-27 Member States, 2014 and 2013 (source CASE, 2016)

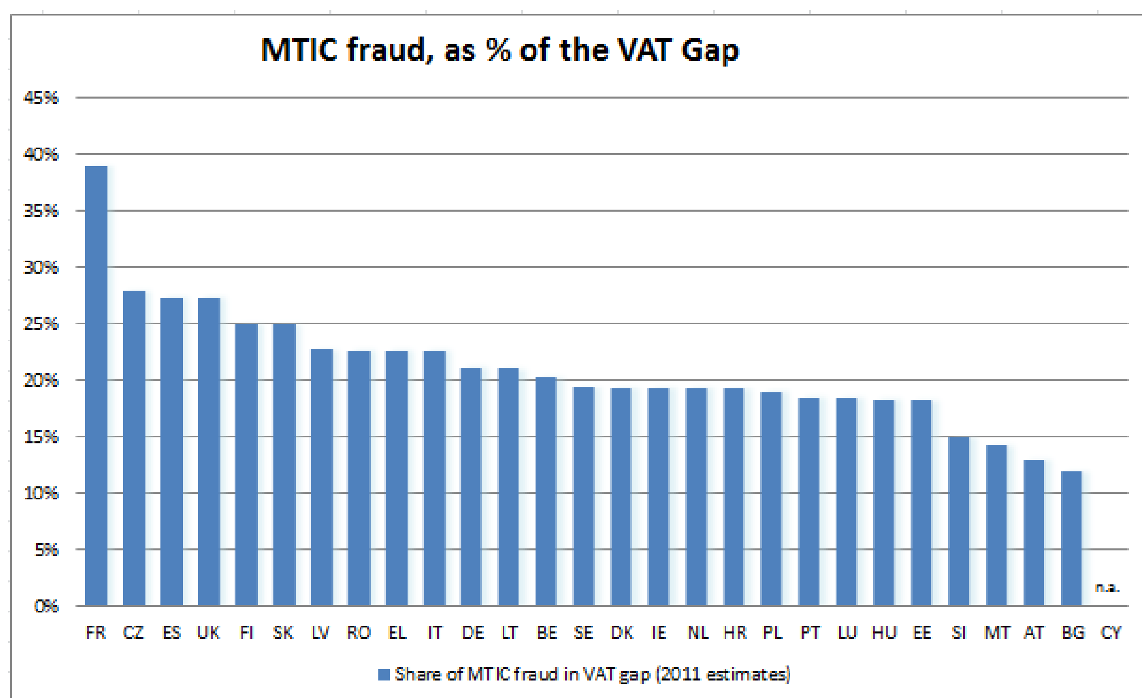


Very few Member States publish estimates of the size of MTIC fraud, supposedly because the nature of this type of fraud makes it difficult to measure. However, a recent study commissioned by the Commission confirmed the findings of the evaluation as MTIC fraud alone is found to be responsible for VAT revenue losses of approximately EUR 45 billion to EUR 53 billion annually[58].

The MTIC fraud portion of the VAT gap ranges from 12% in Bulgaria to 39% in France (see Figure 2 below on the share of MTIC fraud in the VAT gap). On average (weighted average) it is estimated that 24% of the overall VAT gap is due to MTIC fraud. The rest of the VAT gap is attributed to losses of revenue due to domestic fraud and evasion, tax avoidance, bankruptcies, financial insolvencies, as well as miscalculations.

[58] EY, 2015.

Figure 2: Share of MTIC fraud in the VAT gap (source "Own calculations" based on EY, 2015 study)



2.3.2. Evolution of the problem

Monitoring at EU level of VAT collection by individual Member States is relatively recent as the first study on the VAT gap dates back to 2009. The methodology is continually improved and annual updates of the study include the latest revised figures. Although the Commission is seeking to develop methods to extract data on fraud from the VAT gap, such information is still not available. The next VAT gap study is expected for 2018. The above estimations on MTIC fraud were provided by one specific study[59] and, contrary to the VAT gap study, no further data on its trend evolution is available.

The trend of the VAT gap over the period 2010-2014 is shown in Table 1 below. For the EU-26[60] as a whole, the VAT gap has increased from 13.53% in 2010 to 14.06% in 2014, which in absolute monetary terms amounts to an increase of about EUR 25 billion.[61].

Table 1: VAT Gap estimates, 2010 - 2014

EU-26	2010	2011	2012	2013	2014
VAT Gap (EUR million)	134 806	152 237	162 537	161 442	159 460
VAT Gap (%)	13.53	14.41	14.97	14.75	14.06

[59] EY, 2015. Note that this study is based on the 2013 VAT Gap study (CASE, 2013) which is based on data from 2011.

[60] The report does not include estimates for Croatia and Cyprus due to incomplete national account statistics.

[61] CASE, 2016.

VAT Gap (change pp)	0.88	0.56	-0.22	-0.69

Source: CASE, 2016 and own calculations based on CASE, 2016.

Information on the VAT gap and on MTIC fraud for the period 1993-2009 (which followed the entry into force in 1993 of the current transitional VAT system put in place at the time the fiscal frontiers between the Member States were abolished) is not available, although it is likely that MTIC fraud (which finds its roots in the way the transitional VAT system is designed) has taken a few years to appear and to develop.

2.3.3. Problem driver: the endemic weakness of the current transitional VAT system resulting from the break in the fractioned collection of VAT

In domestic trade, as a rule[62], the collection of VAT is based on fractioned payments. VAT is collected at each stage in the production and distribution chain and this ensures the self-policing character of this tax (see box 1 above). Customers pay the VAT due on their purchases to their suppliers who will remit it to the Treasury after deduction of the VAT charged to them by their own suppliers[63]. The collection of VAT on behalf of the Treasury is therefore ensured by suppliers through direct payments received from their customers.

In intra-EU trade in goods, this fractioned payment system is broken. The rules of the current transitional VAT system split every cross-border sale of goods between businesses into an exempted supply in the Member State of origin (i.e. no VAT is charged by the supplier to his customer) and a taxable acquisition in the Member State of destination (i.e. the customer is liable to pay the VAT due to the Treasury but no VAT is actually paid as he has an immediate right of deduction[64] - see further explanation in box 2 above). It is like a customs export-import scheme[65], but lacks equivalent border controls and is therefore at the root of MTIC fraud, the typical intra-EU cross-border fraud.

MTIC fraud exploits the endemic weakness of the current VAT system (which was meant to be transitional – see explanation in box 2 above), that allows for goods to be bought cross-border VAT-free because of the break in the fractioned payment chain. The basic MTIC fraud scheme (see further details in box 3 below) involves a cross-border purchase of goods by a fraudster, followed by a domestic supply by that fraudster. The cross-border purchase of goods allows the fraudster to make a VAT neutral purchase (no payment of VAT, either to the supplier or to the Treasury). The subsequent domestic supply allows the fraudster to charge and collect the VAT from his customer. Instead of paying the whole of this VAT over to the Treasury, he takes the VAT with him and disappears.

Another type of fraud which must be mentioned here is "diversion fraud". Although not considered as typical intra-EU cross-border fraud because it mainly happens regarding

[62] Except in cases of reverse charge: see comment in footnote 39.

[63] To note that the customer will also be allowed to deduct the VAT charged to him by his supplier from the VAT due on his own supplies.

[64] Based on the assumption that he has a full right of deduction.

[65] Exportation of goods is VAT exempt and importation of goods is VAT taxable – see functioning under box 8 in Annex 5, Section 1.

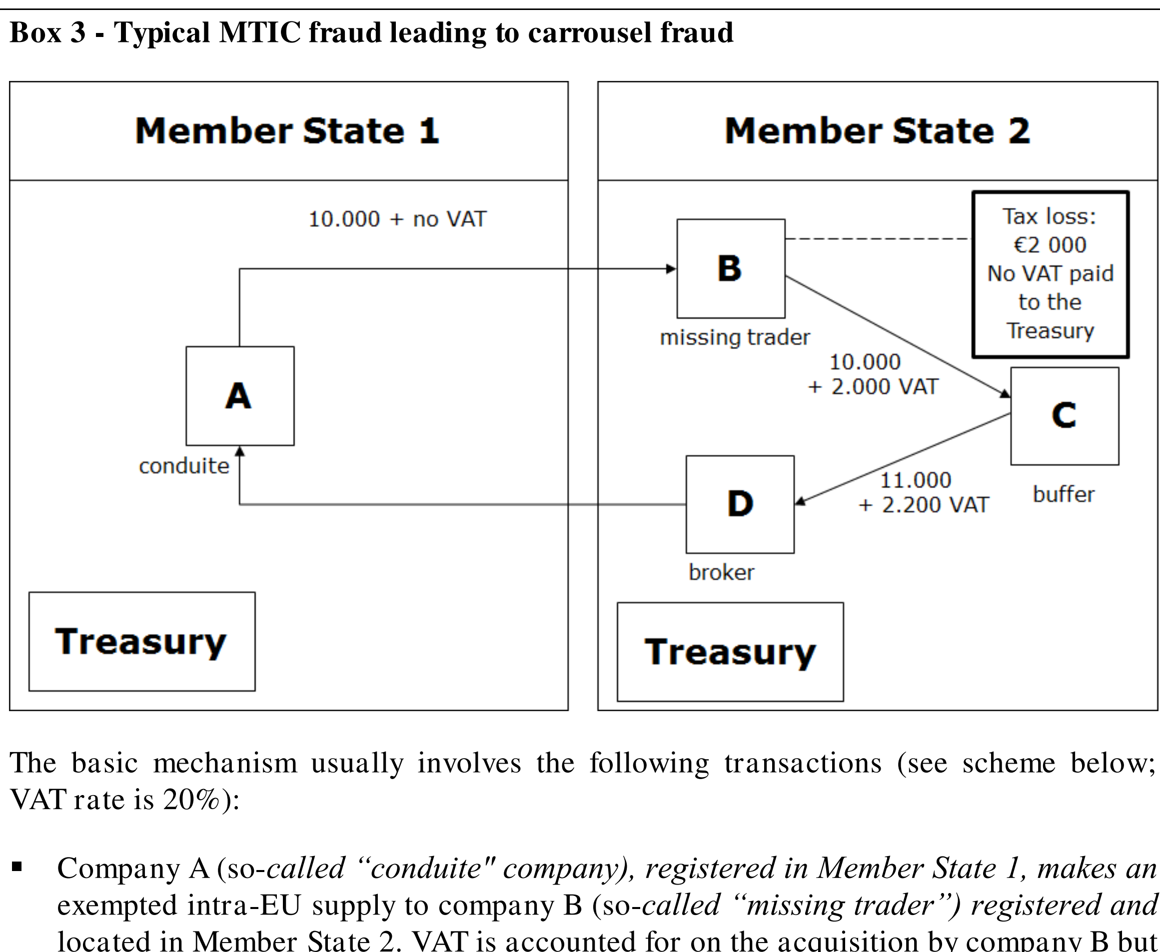
exportation of goods to third countries[66], diversion fraud also exploits the rules of the current transitional VAT system.

Intra-EU diversion fraud occurs when a fraudster reports an intra-EU supply of goods but then "diverts" the goods to the domestic market so that they remain in the same Member State and are sold without leaving the territory. The VAT fraud is crystallised in the amount of VAT charged by the fraudster to the customer, which is not accounted for to the Treasury (since the fraudster has reported to the authorities a fake intra-EU supply exempt from the VAT) (see Section 5, box 9 in Annex 5).

MTIC fraud can be committed in many different ways and the schemes become more elaborated every time. During the nineties of the last century, the fraudsters started their fraudulent activities in the simplest way. The typical MTIC fraud was committed by three or four companies involving two Member States. The most serious form of the fraud – known as carousel fraud – involves a series of contrived transactions within and beyond the EU, with the aim of creating large unpaid VAT liabilities and fraudulent VAT repayment claims. Similar to how a carousel goes round and round, the goods are passed around between companies and jurisdictions, generating each time losses for the Treasuries involved.

The following scheme illustrates the typical MTIC fraud leading to carrousel fraud.

Box 3 - Typical MTIC fraud leading to carrousel fraud



The basic mechanism usually involves the following transactions (see scheme below; VAT rate is 20%):

- Company A (so-*called "conduite" company), registered in Member State 1, makes an* exempted intra-EU supply to company B (so-*called "missing trader") registered and* located in Member State 2. VAT is accounted for on the acquisition by company B but

[66] For this reason, diversion fraud as such is not the focus of the present impact assessment. However, it is mentioned because some of the further developed policy options (those that restore the fractioned payment system – see Sections 5.4 and 5.7) would also impact this type of fraud.

deducted in the same VAT return so that no actual payment of VAT has to be made to the Treasury of Member State 2.

- Company B subsequently makes a domestic supply to company C (so-called *"buffer"). Company B charges VAT on the invoice sent to co*mpany C, collects it but does not pay the VAT to the Treasury of Member State 2. Company B then rapidly disappears.
- Company C (which on the basis of the invoice issued will deduct the VAT charged by B) is usually used as a means to distort VAT investigations (in a three-company carrousel there is no buffer company).
- Company C resells on the domestic market the goods to company D (broker) which will deduct the VAT charged on its purchases. D will eventually make an intra-EU supply to company A in Member State 1 in order to ask for refund of the VAT charged on its purchases.

Following the scheme, the missing trader will not declare and/or pay the charged VAT to the Treasury.

At the end of the chain, the broker company will claim a refund because he makes an intra-EU supply to another Member State. At this moment money is paid out by the Treasury which has not been received from the missing trader earlier in the chain.

The loss of VAT receipts can be unlimited as the same goods can be supplied several times over by including again exempt intra-EU supplies. The profit of the fraudulent chain can be easily shared between all the participants.

In practice the scheme as illustrated can be combined with all possible types of MTIC VAT fraud and developed over the borders of several Member States and eventually third countries.

The recent legislative proposal submitted by the Commission to Council[67], which echoes the request from certain Member States to be allowed to apply a generalised reverse charge mechanism as an urgent measure to combat carrousel fraud, shows how the shortcomings of the current transitional VAT system can severely affect certain Member States. It also reveals the limits of traditional measures to combat such fraud. This is corroborated by recent reforms implemented in several Member States (e.g. new collection methods introduced in respect of certain transactions, compulsory electronic invoicing transiting via the tax administration) with a view to improving VAT collection.

2.3.4. Consequences: who is affected and how?

- **Member States**: MTIC fraud represents a cost for Member States through losses in tax revenue of approximately EUR 45 billion to EUR 53 billion annually. It is also likely to generate additional administrative costs through the need for additional audits, administrative and/or judicial proceedings.

- **Businesses**: MTIC fraud may also generate unexpected costs for businesses that inadvertently and unknowingly become involved in a fraudulent supply chain and

[67] See Proposal for a Council Directive amending Directive 2006/112/EC on the common system of value added tax as regards the temporary application of a generalised reverse charge mechanism in relation to supplies of goods and services above a certain threshold (COM(2016) 811)
Impact assessment for the Proposal (SWD(2016) 457) and its Executive summary (SWD(2016) 458)

may need to bear the unpaid VAT and any relevant penalties. Further it creates unfair competition between compliant and non-compliant businesses since fraud enables the latter to sell goods in the market at a lower price than the former[68]. Finally, it generates extra compliance costs, since Member States in an attempt to fight fraud impose new obligations which fall upon honest businesses. This problem was raised on various occasions by businesses including in submission XVIII.1.a provided via the REFIT platform.

- **Citizens/Society**: By depriving Member States of tax revenues, MTIC fraudsters are effectively robbing EU citizens of the means for governments to fund the provision of infrastructure such as schools and hospitals as well as other public services[69]. Losses in tax revenues might also have to be compensated by other forms of additional taxation. MTIC fraud is associated to organised crime. Fraudsters often use their profits to fund other forms of criminality, such as cigarette smuggling or drug trafficking[70]. MTIC fraud also appears to be used to launder money and return a healthy profit[71]. During the consultation process (see Annex 2), stakeholders concurred that MTIC fraud and other fraudulent schemes have negative effects on the tax collected and the protection of the rights of the honest businesses. Stakeholders insisted that fraud must be tackled by specific long term remedies addressed only to fraudulent businesses and the vast majority of the respondents commented that antifraud measures should be harmonised to be effective. Over 74% agreed that the current system is not sufficiently resistant to VAT fraud.

2.4. Problem 2: The complexity of the current transitional VAT system

2.4.1. The problem and its EU dimension

The establishment in 1993 of the single market was meant to reduce compliance costs associated with intra-EU trade, chiefly through the abolition of customs procedures. However, according to the evaluation of the EU VAT system[72], the parallel introduction of the current transitional VAT system resulted in a very complex system for intra-EU trade in goods (as compared with the previous one) which led, as a consequence, to higher compliance costs for businesses trading cross-border as compared to businesses trading only domestically.

According to the evaluation, this complexity arises not only from the new specific VAT rules but also from other related provisions. In this regard, the statistical requirements that were put in place to allow identification of VAT-taxable transactions and to help record trade between Member States (the Intrastat system[73]) have resulted in a substantial burden for intra-EU traders (estimated at 5% of the value of trade, with wide variation according to size and country).

[68] See box 3 above – Typical MTIC fraud leading to carrousel fraud.
[69] Source: Europol.
[70] Source: Europol.
[71] International Tax Review – "UK: Missing trader intra-community fraud: Are businesses really prepared?", 25 June 2013.
[72] IFS et al., 2011.
[73] Intrastat is the data collection system, operational since 1 January 1993, for compiling statistics on international trade between the EU Member States. See for further details on: http://ec.europa.eu/eurostat/statistics-explained/index.php/Glossary:Intrastat

A recent study[74] confirmed the findings of the evaluation: on average, the VAT cost of compliance per euro of turnover is 11% higher for intra-EU trade compared with the corresponding VAT compliance per euro of turnover for domestic trade.

2.4.2. Introduction and VAT notions

The next sections describe the two main drivers leading to the complexity of the current transitional VAT system which are (i) the additional VAT obligations associated with the current transitional VAT system and (ii) the divergent application of the VAT rules across the Member States. They make reference to particular VAT notions. To avoid repetition, these VAT notions are explained in box 10 in Annex 5.

2.4.3. Driver 1: The additional VAT obligations associated with the current transitional VAT system

In comparison with domestic trade, doing business across the EU triggers additional obligations. These obligations are meant to ensure an "administrative" follow-up of the goods traded within the EU, in order to remedy the break in the VAT 'audit trail' resulting from the abolition of intra-EU border controls. In this regard, some stakeholders consider that the customs controls at the internal borders between Member States that were abolished in 1993 have been replaced by controls and administrative obligations shifted onto the economic operators. Moreover, they are of the view that there is no consistency between domestic and intra-EU cross-border supplies (see Annex 2).

Further feedback collected from expert stakeholders and Member States (see Annex 2) allowed identifying the main elements triggering these additional obligations which make trading in the EU more complex, and therefore more onerous, than engaging in domestic trade (see list of main additional obligations and further details in Section 7, box 11 in Annex 5). These obligations must be fulfilled in the Member State of establishment of the business and in any other Member State where the business performs economic activities. This requires particular investigations and maintenance of appropriate records and details, in addition to normal commercial documentation, if the VAT obligations linked to intra-EU transactions are to be fulfilled.

2.4.4. Driver 2: Divergent application of EU VAT rules across the Member States.

The complexity of the current transitional VAT system is partly the result of the divergent application of the EU VAT rules by the Member States. According to the evaluation of the EU VAT system[75], differential requirements for dealing with different tax administrations are the determinants of intra-EU additional transaction costs. The evaluation also pointed out that so long as the application of the EU VAT rules across the Member States varies, small businesses will undoubtedly continue to have considerable difficulties with intra-EU trade.

This further impacts on key issues like the place of taxation, leading to potential double taxation (to the detriment of businesses) or non-taxation (to the detriment of Member States). In this regard different application of the EU VAT rules by the Member States is seen by stakeholders as one of the most serious obstacles to benefiting from the single market (see Sections 2, 4, 5 of Annex 2). This is also the main reason why respondents

[74] EY, 2015.
[75] IFS et al., 2011.

(see Sections 2 and 6 of Annex 2) considered the current transitional VAT system to be extremely complex and creating high administrative burdens.

Such differences stem firstly from the numerous derogations and options in the VAT Directive, secondly from the discretion left to the Member States in their implementation and application and thirdly from divergent interpretations. These differences can affect the scope of the tax, the scope and number of exemptions, the chargeability of the tax, the structure of the VAT rates applied, formal obligations such as invoicing, the rules on deduction or the organisation and efficiency of the tax authority.

However, the focus of the initiative that is here being assessed, and of the in-depth discussions held with the Member States and expert stakeholders, is limited to the complexities resulting from differences that are specifically linked to the functioning of the current transitional VAT system.

The main differences can be grouped in the following two categories: (i) divergences in obligations and procedures imposed on businesses by the different Member States and (ii) divergences in the qualification of certain transactions and their VAT treatment between Member States (see list of main discrepancies and further details in Section 8, boxes 12 and 13 in Annex 5).

2.4.5. Consequences: who is affected and how?

- **Member States**: Ensuring business compliance with complex rules makes monitoring and audit tasks more difficult which results in higher administrative costs. Although national administrative practices established unilaterally by Member States can be held partly responsible for the complexity, a greater part is due to the rules laid down in the VAT Directive aimed to ensure the follow-up of the goods circulating VAT-free across the EU.

- **Businesses**: Businesses trading cross-border bear an extra compliance cost of 11% in comparison to businesses trading only domestically. Further there are additional risks associated with legal uncertainty for businesses engaged in cross-border trade. Those costs and risks can deter businesses, in particular SMEs, from trading across the EU. The functioning of the single market is therefore affected by the VAT rules as they influence where goods and services are produced, traded, bought and sold. This goes against the basic principle of neutrality governing VAT, according to which VAT must be neutral regarding economic activities.

The evidence collected through the whole consultation process (see Annex 2) demonstrates that the current transitional VAT system is extremely complicated and entails costs for businesses and difficulties for Member States when it comes to ensuring compliance. Complexity was pointed out as leading businesses to seek specialised advice when embarking in cross-border activities. The added cost was referred to as high and one which SMEs might not always have the resources to deal with. Moreover, errors were mentioned as resulting in substantial and sometimes disproportionate penalties[76]. Complexity was also found to make it difficult for businesses to have legal certainty with regards to the VAT treatment of their transactions.

[76] See for instance the ruling of the CJEU of 20 June 2013 in case C-259/12 Rodopi-M 91.

2.5. Conclusion

It results from the analysis of the problems that the functioning of the current transitional VAT system is causing disturbance to both Member States and businesses. The problems are interrelated since complexity creates opportunities for fraudsters and increased fraud leads to more complexity. These are problems that are exacerbated by the increase in cross-border activity that is the result of globalisation of the economy and the extension of the EU VAT area (from 12 to 28 Member States) since these rules entered into force in 1993.

2.6. Summary of main causes/consequences to the complexity of the current transitional VAT system

Table 2: Causes/consequences - Complexity of current transitional VAT system

	VAT identification number	**Liability rules for non-established business**	**Consign-ment/call-off stocks**	**Chain transactions**	**Proof of transport**	**VAT returns/ recapitulative statements/ audits**	**Supplies of goods and services**	**Input deduction**
Main causes to the complexity								
Divergent application of VAT rules	Divergent (des-) attribution process	Inconsistent application of reverse charge	Some Member States apply simplifications and others do not	No uniform rules on assignment of the transport to a specific supply in the chain	No clear and uniform rules Different storage period	Different format, content and filing deadlines of VAT returns Different requirements, format and deadlines for recapitulative statements Different audit procedures	Inconsistent qualification	Different rules on exclusions and restrictions of the right to deduct and on calculation of deductible proportion

Additional VAT obligations	Need to validate status of customer Need to be registered in another Member State/to have a fiscal representative	Need to be registered in another Member State in case no reverse charge is applicable in that Member State	Need to be registered in another Member State	Need to be registered in another Member State in case no simplification applies	Maintenance of appropriate records and details Additional investigations	Need to submit VAT returns in other Member States Need to add special mention in the VAT return Need to present recapitulative statements Subject to other Member States' audits and need to have a fiscal representative	Need to investigate the treatment given in each Member State	Need for recourse to the refund procedure
Main consequences to the complexity (costs/risks)								
	Risk of being denied the exemption thus having to pay VAT without being	Risk for customers to be held jointly and severally	Risk of penalties if business applies simplification in a Member State which does not	Risk of penalties if business applies simplification in a Member	Risk of being denied the exemption thus having to pay VAT without being	Risk of penalties if obligations not correctly fulfilled	Risk of double taxation or non-taxation Administrative/	Refunds postponed (cash flow disadvantage)

	able to pass it on to customer Costs linked to multiple VAT registrations	responsible	allow it	State which does not allow it	able to pass it on to customer No common IT process possible		judicial claims Need for recourse to tax experts	

2.7. Evolution of the problem without action at EU level (dynamic baseline)

2.7.1. Intra-EU cross-border VAT fraud perspective

For the time being, Member States and the Commission have joined efforts to combat MTIC fraud through the so-called "conventional measures"[77], i.e. by improving administrative cooperation between the Member States. Amongst these measures are the set-up of the EUROFISC platform and the recourse to multilateral controls (i.e. controls involving tax administrations of more than one Member State).

In order to improve their fight against intra-EU cross-border VAT fraud, it is expected that Member States will continue reinforcing their cooperation in order to speed the exchange of quality information between them. The following upcoming proposals will soon be tabled by the Commission:

- A set of 20 measures[78] by which urgent action will be taken on the following fronts:
  - Improving cooperation within the EU and with non-EU countries.
  - Moving towards more efficient tax administrations.
  - Improving voluntary compliance and tax collection.
- Directive on the fight against fraud to the Union's financial interests by means of criminal law[79].
- Regulation on the establishment of a European Public Prosecutor's Office[80].

These measures are expected to help improve the fight against fraud in general. Improvements to the quality of information exchanged between the Member States and the speed of such an exchange through the use of electronic means will be particularly helpful in fighting against cross-border fraud. However, these measures alone would not be sufficient to radically reduce the level of cross-border fraud as they are not targeted at putting an end to the endemic weakness of the current transitional VAT system leading to the specificity of MTIC fraud.

2.7.2. Complexity perspective

Regarding the main issues linked to the complexity problem (need for certain transactions to be VAT registered/liable, need to comply with specific rules in Member States other than the Member State of establishment, proof of transport), any improvement would require a change in the EU rules.

Concerning the complexity linked to the VAT treatment/qualification of certain transactions, Member States might continue trying to agree common guidelines in the VAT Committee. However, this would be based on a case-by-case basis and further guidelines issued by the VAT Committee are merely views of an advisory committee.

[77] Conventional measures focus on increasing the audit and enforcement capacity of the tax administration e.g. by improving (de-)registration process for taxable persons, by increasing the number of audits, via enhanced use of electronic data, by applying existing legal possibilities such as 'joint and several liability', etc.

[78] https://ec.europa.eu/taxation_customs/sites/taxation/files/docs/body/2016-03_20_measures_en.pdf

[79] Proposal for a Directive of the European Parliament and of the Council on the fight against fraud to the Union's financial interests by means of criminal law (COM(2012) 363).

[80] Proposal for a Council Regulation on the establishment of the European Public Prosecutor's Office (COM(2013) 534).

They do not bind either the European Commission or the Member States who are free not to follow them.

Regarding the input tax deduction, improvements to the cross-border intra-EU refund procedure have been introduced in 2010 (an electronic procedure for submission of the refund applications via a web portal only in the Member State where the business is established and not in all Member States where VAT has been incurred as under the old rules)[81]. While certain improvements could still be made by the Member States at national level (e.g. speeding-up the processing of applications, facilitating access to information and guidance as regards national implementing rules) there is no solution to overcome the cash flow disadvantage intrinsic to such a refund procedure.

2.7.3. Limits to the effectiveness of the current transitional VAT system

The current transitional VAT system was designed to provide a one-off solution to the abolition of the fiscal frontiers in 1993 and was a short-term practical system meant originally for four years. This system quickly showed its shortcomings[82] which the Member States tried to address each in their own way. This has led to a fragmented VAT system, making intra-EU cross-border transactions difficult and risky for businesses, in particular SMEs. The consequence is that the VAT rules have the potential to see businesses refrain from trading across borders.

The development in recent years of e-governance has provided Member States' tax administrations new tools to improve their tax collection systems through better efficiency in collecting, processing, controlling and exchanging information. However, the pace of development but also the type of Information and Communication Technology (ICT) used differ from one Member State to another. This entails challenges for the cooperation between Member States' tax administrations not only in terms of technological factors but also from an administrative, legal and institutional perspective. If no fundamental solution is found at EU level, this might in turn entail that Member States focus on the development of own specific measures which deviate from the normal functioning of the VAT system.

The recent history of the VAT Directive[83] shows the spill-over effect linked to the use of the reverse charge mechanism in an effort to combat MTIC fraud. Requests for derogating measures in order to introduce new methods for the collection of the VAT are also likely to continue. The solutions sought by the Member States are not only likely to increase fragmentation of the VAT system, but they can also lead to disproportionate or even legally doubtful measures. All this means a high risk that businesses will be faced with individual rules specific to each one of the Member States although the problem to solve is common to all of them. For these reasons, in the REFIT Platform, businesses called for a common solution[84].

[81] Council Directive 2008/9/EC of 12 February 2008 laying down detailed rules for the refund of value added tax, provided for in Directive 2006/112/EC, to taxable persons not established in the Member State of refund but established in another Member State (OJ L 44, 20.2.2008, p. 23).

[82] See COM(94) 515 final of 23 November 1994; COM(2000) 348 final of 7 June 2000; COM(2003) 614 final of 20 October 2003.

[83] The VAT Directive was several times modified to extent the scope of the reverse charge mechanism: introduction of Article 199a in 2010 and of Article 199b in 2013 and proposal for a Generalised Reverse Charge Mechanism (GRCM) in 2016, see COM/2016/811.

[84] Submission vXVIII3.a the Danish Business Forum

As long as an EU-wide systemic solution is not put in place to counter the problems created by the current transitional VAT system, fraudsters and Member States will continue the endless loop of efforts in which the former will develop more aggressive fraud schemes while the latter will need to implement new control measures that will increase costs for both businesses and Member States.

Without action at EU level, the endemic weakness of the current transitional VAT system will continue to be exploited by fraudsters. Fraud levels might be stabilise but this will be to the detriment of compliant businesses that will pay the price through high compliance costs (already 11% higher than for domestic trade) or even increasing compliance costs.

The complexity of the current transitional VAT system will continue to negatively impact the functioning of the internal market by failing to capture new business models, new markets and technologies, which translates into losses of competitiveness of honest EU businesses and losses in efficiency of tax administrations.

3. WHY SHOULD THE EU ACT?

According to the principle of subsidiarity, as set out in Article 5(3) of the Treaty on European Union (TEU), action at EU level may only be taken if the envisaged aims cannot be achieved sufficiently by the Member States alone and can therefore, by reason of the scale or effects of the proposed actions, be better achieved by the EU.

VAT rules for cross-border EU trade can, by their nature, not be decided by individual Member States since, inevitably, more than one Member State is involved. Moreover, VAT is a tax harmonised at EU level. The problems identified in Section 2 of this impact assessment are embedded in the rules of the VAT Directive. Therefore any initiative to change the current transitional VAT system into a definitive system as regards intra-EU trade requires amending the current VAT Directive. This entails a proposal from the Commission and its adoption by the Council, acting unanimously in accordance with a special legislative procedure, and after consulting the European Parliament and the Economic and Social Committee.

The legal basis for the present initiative is Article 113 of the TFEU according to which: "The Council shall, acting unanimously in accordance with a special legislative procedure and after consulting the European Parliament and the Economic and Social Committee, adopt provisions for the harmonisation of legislation concerning turnover taxes, excise duties and other forms of indirect taxation to the extent that such harmonisation is necessary to ensure the establishment and the functioning of the internal market and to avoid distortion of competition".

Given the need to modify the VAT Directive, the objectives sought by the present initiative cannot be achieved by the Member States themselves. Therefore, it is necessary for the Commission, which has responsibility for ensuring the smooth functioning of the internal market and for promoting the general interest of the European Union, to propose action to alter and improve the situation.

As regards the provisions to harmonise and simplify rules within the current transitional VAT system (the "quick fixes"), they have unanimously been requested by the Member States which demonstrates that action at Union level is likely to be more effective as action at national level has proven not to be sufficiently successful.

Furthermore, the 2011 retrospective evaluation (see annex 6) already referred to the "piecemeal" approach by Member States as an unsatisfactory way to solve the problems of the transitional arrangements.

4. WHAT SHOULD BE ACHIEVED?

4.1. General objectives

The general objectives of the initiative are:

- **To contribute to fiscal consolidation** within the EU – by ensuring that taxes due are collected to feed national and EU budgets.
- **The smooth functioning of the internal market** – by reducing obstacles to intra-EU cross-border trade.
- **To ensure fair taxation** – so that all businesses are treated equally in order to avoid distortions of competition.

4.2. Specific objectives

The specific objectives of the initiative are:

- **To make the EU VAT system more robust** – by addressing the endemic weakness of the current transitional VAT system linked to the break in the fractional collection of VAT.
- **To make the EU VAT system simpler** – by addressing the complexities of the current transitional VAT system and by providing a level playing field for businesses whether engaged in domestic or cross-border transactions[85].

4.3. Linking the objectives to the problem

Table 3: Links objectives-problems-solutions

Specific objectives	Link to the problems and criteria for reaching a solution
To make the EU VAT system more robust – by addressing the endemic weakness of the current transitional VAT system	**Addresses the problem of intra-EU cross-border VAT fraud** Meets the following general objectives: • To contribute to fiscal consolidation within the EU • To ensure fair taxation The assessment of possible solutions is based on the

[85] No specific objective is targeting SMEs as their particular needs will be addressed by the upcoming SME VAT package proposal (see Section 1.1).

	following qualitative criteria*: • Budgetary impact • Prevention of fraud and abuse
To make the EU VAT system simpler – by addressing the complexities of the current transitional VAT system and by providing a level playing field for businesses whether engaged in domestic or cross-border transactions	**Addresses the problem of complexity of the current transitional VAT system** Meets the following general objectives: • The smooth functioning of the internal market • To ensure fair taxation The assessment of possible solutions is based on the following qualitative criteria: • Equality and simplicity; • Ease of administration and cost of collection;

***Qualitative assessment criteria**:

- Equality and simplicity – Domestic and intra-EU transactions should be treated the same so that doing business across the EU becomes as simple (reducing compliance costs) and as safe (providing legal certainty) as engaging in purely domestic activities. Rules should not be an obstacle to the proper functioning of the single market.

- Budgetary impact – VAT revenues should be allocated to the Member State of the final consumption of the goods in accordance with its conditions in particular its VAT rates. The impact on the cash-flow of business should be similar to that for domestic transactions to ensure a genuine level playing field.

- Ease of administration and cost of collection – An increase in costs for the tax administrations and business should be avoided in order to allow that the cost of collecting tax revenues is similar to that for domestic transactions.

- Prevention of fraud and abuse – Breaks in the VAT chain within the single market should be avoided to the extent possible to ensure that the VAT system remains robust and fraud-proof.

4.4. Consistency with other EU policies and with the Charter for fundamental rights

The creation of a simple, modern and fraud-proof VAT system is one of the fiscal priorities set out by the Commission for 2017 (Annual Growth Survey 2017[86]) which should contribute to deepening the single market and making national markets bigger.

[86] ttps://ec.europa.eu/info/publications/2017-european-semester-annual-growth-survey_en

The main objectives of the initiative of reducing cross-border VAT fraud and lowering compliances costs for businesses trading across the EU by using new technologies are in line with this priority. The initiative would prompt Member States to put in place modern tax systems that can support growth and fairness between businesses and bring a new level of cooperation between Member States and between Member States and businesses to improve tax collection.

MTIC fraud is also one of the nine EMPACT[87] priorities, the European Union's priority crime areas, under the 2014-2017 EU Policy Cycle of Europol.

Reducing administrative burdens, particularly for SMEs, is also an important objective highlighted in the EU's growth strategy for the coming decade (Europe 2020 – A strategy for smart, sustainable and inclusive growth[88]).

The proposed initiative and its objectives would be consistent with the EU SME policy as set out by the Small Business Act (SBA)[89], in particular principle VII on helping SMEs to benefit more from the opportunities offered by the Single Market. It would be consistent with the Single Market Strategy (SMS)[90] which referred to the single European VAT area mentioned in the Action Plan. It would also be consistent with the EU objectives under REFIT[91].

The objectives envisaged do not affect fundamental rights.

5. WHAT ARE THE VARIOUS OPTIONS TO ACHIEVE THE OBJECTIVES?

5.1. Selection of options

When looking at possible options to tax B2B transactions at destination, two fundamental issues have to be considered, namely:

- the place of taxation (whether it will be based on the physical flow of the goods or not); and
- the person liable for payment of VAT (whether the supplier charges the VAT of the Member State of destination and pays the VAT via the One Stop Shop or if instead the customer accounts for the VAT through the reverse charge).

The following qualitative assessment criteria were suggested and agreed by both the GFV and the VEG: (i) equality and simplicity; (ii) budgetary impact; (iii) ease of administration and cost of collection; and (iv) prevention of fraud and abuse (see Section 4.3 above).

[87] European Multidisciplinary Platform Against Criminal Threats (EMPACT). See https://www.europol.europa.eu/crime-areas-and-trends/eu-policy-cycle-empact

[88] http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2010:2020:FIN:EN:PDF

[89] http://ec.europa.eu/growth/smes/business-friendly-environment/small-business-act_en

[90] http://ec.europa.eu/growth/single-market/strategy_en

[91] Regulatory Fitness and Performance programme: http://ec.europa.eu/info/law/law-making-process/overview-law-making-process/evaluating-and-improving-existing-laws/reducing-burdens-and-simplifying-law/refit-making-eu-law-simpler-and-less-costly_en

On the basis of the outcome of a series of technical discussions in the GFV and the VEG on the possible options[92] , in addition to the Baseline, the five options discussed in the next section were selected (out of thirteen different options initially identified in close collaboration with stakeholders in the VEG and representatives of Member States in the GFV) to be assessed in-depth in an external study.

5.2. Baseline

The baseline option assumes that no legislative action will be taken at EU level as regards the VAT treatment of cross-border transactions and that the current transitional VAT system will continue to apply. The functioning of the current transitional VAT system as such is described in Section 1.4 Functioning of the common system of value added tax and Box 2: Transitional VAT system since 1993.

The baseline takes into account the current applicable rules and not those which are contained in proposals currently discussed in Council or which might be adopted by the Commission in the future. However, it seems appropriate to dwell on the impact that those proposals might likely have in case they would be adopted.

A reference is needed, in the first place, to the VAT proposals on e-commerce, on a Generalised Reverse Charge Mechanism (GRCM - see footnote 83) and on reduced VAT rates on e-publications that are currently under discussion in the Council. While once adopted the e-commerce proposal should have positive effects on the baseline as it is expected to raise Member States' VAT revenues and decrease compliance costs to businesses, the effect of the adoption of the other proposals is uncertain, especially concerning the GRCM[93] which might pending its final design result in further fragmentation of the VAT system and have negative impact on compliance costs of business.

Finally, it is appropriate to make a reference to the impact that in the baseline might entail the adoption of the three other VAT legislative proposals (rates, SMEs and administrative cooperation)[94] which, according to the VAT Action Plan, should be adopted by the Commission in the near future.

The VAT rates proposal could be adopted even in the absence of an adoption of the initiative on the definitive VAT system. The current transitional VAT system is indeed de facto based on the destination principle which limits the distortions of competition due to the differentiation of VAT rates between the Member States[95]. As the current transitional VAT system would continue to apply, the business customer will also

[92] See Section 9 of Annex 5 for more details in relation to the selection of the options and the inventory of all the thirteen options identified and discussed in the GFV and the VEG.

[93] See impact assessment: https://ec.europa.eu/taxation_customs/sites/taxation/files/swd_2016_457_en.pdf

[94] The assumption is that the initiative on the definitive VAT system that is here being assessed is not adopted while the other three are adopted.

[95] The "origin principle" enshrined in Article 402 of the VAT Directive would however be at odds with the change in the VAT rates rules but these rules will be in line with the current transitional VAT system which remains unchanged.

continue to self-assess the VAT due on his cross-border purchases in his own Member State[96].

The proposals on the SME VAT Package and on administrative cooperation could also be adopted even in the absence of an adoption of the initiative on the definitive VAT system. Only the specific parts of these proposals linked to the initiative on the definitive VAT system would need to be adapted. Both proposals should on their own have positive impacts on administrative and compliance costs once adopted. Further the proposal on administrative cooperation should also have a positive impact regarding the problem of cross-border VAT fraud.

The baseline option will serve as the benchmark against which the other options will be assessed.

5.3. Option 1: Limited improvement of current rules

Option 1 consists in improving the current rules for intra-EU B2B supplies of goods without modifying them fundamentally. This means that the underlying principles and functioning of the transitional VAT system for intra-EU supplies of goods would remain unchanged (see also Diagram 1 in Section 10 of Annex 5 for its functioning).

The improvements that would be made to the current system under this option cover very specific set of rules that have been identified by national tax administrations and stakeholders, in particular during the consultation process, the discussions in the GFV, the VEG and by way of feedback from the REFIT platform, as the main areas of the existing legislation where legal clarity and certainty need to be enhanced. As requested by the Council in its conclusions on "Improvements to the current EU VAT rules for cross-border transactions" adopted on 8 November 2016, the following four issues will be addressed[97]:

1) **The legal value of the VAT identification number of the customer as regards the exemption for the intra-EU supplies of goods in the Member State of departure of the goods**

   Providing a valid VAT identification number of the purchaser would become a substantive condition (and not merely a formal condition, as stated by the CJEU with regards to the current VAT rules) for applying the exemption of intra-EU supplies of goods. This modification would be proposed in reply to the demand made by Member States to amend the current VAT Directive in order to allow for better monitoring of the flow of goods using the recapitulative statements and the VIES system.

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[96] Therefore the implementation of a OSS as provided for in the initiative on the definitive VAT system is not a necessity. Note also that each Member States is responsible for providing accurate information on the applicable rules and therefore the VAT rates to its taxable persons. The absence of a web-portal as provided for by the initiative on the definitive VAT system should also not cause problems to the suppliers in other Member States (as they will not be liable to pay the VAT due), except for very specific transactions where the supplier could be liable to pay the VAT due (mainly B2C transactions outside the scope of this initiative).

[97] See EY study 2015 *Implementing the 'destination principle' to intra*-EU B2B supplies of goods. In the EY study of 2015 additional simplifications were examined as part of the possible improvements to the current system but after consultation with expert stakeholders and Member States some had to be excluded due to lack of agreement on the steps forward.

2) **The VAT treatment applied to call-off stock arrangements**

Call-off stock refers to the situation where a supplier moves stock to a Member State where he is not established, in order to sell it at a later stage to an already known buyer. Currently this gives rise to (i) a (deemed) intra-EU supply made by the transferor, (ii) a deemed intra-EU acquisition in the Member State of arrival of the goods made by the transferor (who has to register there), (iii) a domestic supply. The proposed amendment under Option 1 would consist in treating the cross-border transfer of goods and subsequent domestic sale as a single exempt intra-EU supply, with an intra-EU acquisition of goods made by the buyer (thus avoiding any obligations for the transferor in the Member State of arrival of the goods).

3) **The VAT treatment applied to chain transactions**

Chain transactions refer to cases where multiple parties are involved in one commercial transaction: company A sells to B, who sells to C, who sells to D and the goods are transported directly from company A to D, so B and C are simply intermediaries. Under the current VAT rules it is difficult to determine which supply involves the intra-EU movement of goods (which will be the only exempt supply in the chain). The proposed amendment under Option 1 would consist in establishing a legal presumption in this regard, which would bring legal certainty to tax administrations and businesses.

4) **The rules on the proof of transport or dispatch of goods sold cross-border**

That proof is necessary in order to justify, before the tax authorities of the Member State of departure of the goods, the application of the VAT exemption of the intra-EU supply of goods.

A legal presumption would be proposed establishing that when the supplier holds a certain number of non-contradictory commercial documents to certify the transport or dispatch made to another Member State, the goods will be presumed to have left the Member State where the supplier has declared an exempt intra-EU supply. This presumption will be rebuttable by national tax administrations providing evidence to the contrary.

The benefit of the last three simplification measures (call-off stock, chain transactions and proof of transport) would be limited only to Certified Taxable Persons (see box 4 below).

Box 4: Certified Taxable Person (CTP)

The concept of Certified Taxable Person does not currently exist in EU VAT legislation but would be introduced as part of the definitive VAT system. It would be relevant for all options (except Option 3) examined in this impact assessment with however different practical implications.

This new concept would apply only to taxable persons trusted by the tax administration and not to final consumers. It would create a new category of taxable persons (CTPs) who would benefit from certain simplifications.

Under Option 1, it will allow CTP suppliers to benefit from simplifications as regards their call off stocks and chain transactions and the proof of their intra-EU supplies, with

a reduction of administrative burdens related to these supplies. The cost of compliance will therefore be reduced.

Under Option 2 and Option 5, it will allow CTP customers to continue purchasing goods free of VAT in other Member States and applying the reverse charge on these supplies. For the Member States, the introduction of the CTP status will reduce the amounts of VAT channelling through the OSS (since liability will take place through reverse charge), while at the same time ensuring that the application of the reverse charge does not give rise to fraud, given that only reliable traders are allowed to apply the reverse charge.

Under Option 4, a simplification measure would be introduced whereby supplies to CTP customers would not require a recapitulative statement.

Taxable persons would be certified at their request by the Member State where they are established and this status would be recognised by all other Member States. In order to obtain the status of CTP, a taxable person would need to meet a set of common, objective, harmonised at EU level, criteria (see description below).

Not all the categories of businesses would become eligible to apply for this status, but only those which meet certain criteria since the objective is to ensure that only reliable taxpayers are certified. Further the certification would not be granted to non-taxable persons, flat-rate farmers, exempt SMEs, other exempt taxable persons without the right to deduct and occasional taxable persons since they do not have the obligation to declare VAT (or that obligation is purely occasional).

The criteria to grant the status would be similar to those used to certify traders for customs purposes (Authorized Economic Operator or AEO[98]), i.e.:

- the absence of any infringement or repeated infringements of taxation rules and customs legislation, as well as of any record of serious criminal offences relating to the economic activity of the applicant;

- the demonstration by the applicant of a high level of control of his operations and of the flow of goods, either by means of a system managing commercial and, where appropriate, transport records, which allows appropriate tax controls, or by means of a reliable or certified internal audit trail ;

- evidence of financial solvency of the applicant, which shall be deemed to be proven either where the applicant has good financial standing, which enables him to fulfil his commitments, with due regard to the characteristics of the type of business activity concerned, or through the production of guarantees provided by insurance or other financial institutions or by other economically reliable third parties.

[98] See further information on the AEO here: http://ec.europa.eu/taxation_customs/general-information-customs/customs-security/authorised-economic-operator-aeo_en. The proportion of AEO businesses has been used as a proxy of the CTP simplification to evaluate the cash flow impact of two options, namely Option 2 and Option 5. The cost/benefit of the CTP simplification for businesses and Member States has been assessed as a component of compliance costs/administrative costs of the options (see methodology in Annex 4).

Except for the categories specifically excluded, the certification would thus be open to all businesses. The implementation of the criteria by the Member States would need to be proportionate so as to be capable of encompassing smaller businesses[99].

Therefore, compliant businesses could apply for such certification and obtain it after due control by the national tax authorities.

5.4. Option 2: Taxation following the flow of goods

Option 2 consists in modifying the current rules whilst still following the flow of the goods (see also Diagrams 2 and 3 in Section 10 of Annex 5 for its functioning).

When the goods sold are transported cross-border, VAT is due in the Member State where the goods arrive at the end of the transport or dispatch (i.e. the place of supply for VAT purposes is in the Member State of destination of the goods). If the goods are not transported or dispatched, the place of supply is in the Member State where the goods are located when the supply takes place.

The person liable for collecting the VAT due in the Member State of destination is, by default, the supplier of the goods. When the supplier is not established for VAT purposes in the Member State of taxation, VAT on that particular supply would be accounted for using a OSS in the Member State of establishment. The OSS would allow offsetting output VAT due on supplies made against input VAT incurred on purchases made within the EU.

Owing to the use of the OSS under this option and contrary to the rules of the current VAT system, a single VAT registration in the Member State of establishment would be sufficient for the supplier to report and account for all VAT due on sales made within the EU. Thus the supplier would no longer need to be registered in all Member States where he sells goods.

However, certain cross-border supplies of goods would continue to be subject to the reverse charge. This means that the place of taxation would still remain in the Member State of arrival of the goods but the person liable for collecting the VAT due would be the business customer rather than the supplier as explained above under the default rule. This would be possible only when the customer has requested and obtained the CTP status (see box 4 above). If the certified customer is not established in the Member State of arrival of the goods, VAT due on this transaction will then have to be reported and accounted for by the customer using the OSS in the Member State where he is established.

In this option, the supplier will not have to submit a periodical recapitulative statement. However, in order to combat fraud, the customer will be required to report his purchases from suppliers established in Member States other than that where he is established (except those for which the reverse charge is applied) and to mention the supplier's VAT identification number. When the transport of the goods is not organised by or on behalf of the supplier, the customer will have to provide the supplier with the name of the Member State of arrival of the goods within ten working days following the month in which the supply took place.

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[99] Those that are not exempt – See further explanation in Annex 3, Section 1.4.

For this option to apply in a simpler and more consistent manner across the EU, it would be desirable to standardise the definitions of products eligible for reduced rates[100] and provide such information via a central web portal.

Box 5: One Stop Shop (OSS)

A Mini One Stop Shop (MOSS) has been operating since 1st January 2015 for a limited number of services and only with regard to business-to-consumer (B2C) transactions. The MOSS is an optional scheme allowing taxable persons to account for the VAT due on those supplies via a web-portal in the Member State in which they are identified. Such B2C supplies are taxable in the Member State of the consumer.

This possibility has been introduced as a simplification measure following the change to the VAT place of supply rules[101] for telecommunications, television and radio broadcasting, and electronically supplied services. This scheme allows businesses supplying such services to final consumers in Member States where they are not established to avoid having to register for VAT purposes in each Member State of consumption.

The MOSS that already exists for telecommunication, broadcasting and electronic services is due to be extended to all e-commerce B2C transactions[102].

Some of the policy options examined in this impact assessment rely on a OSS scheme which would build upon the existing MOSS and extend its use to supplies of goods in business-to-business (B2B) operations.

This could simplify the obligations of business operators who would then not need to register in all the Member States where they sell goods to other businesses but could instead use a single registration point in the Member State where they are established to report, pay and deduct VAT. This would also allow them to be subject to home country audits and have as a main contact point the tax administration of that Member State.

5.5. Option 3: Reverse charge following the flow of goods

Option 3 consists in adapting the current rules whilst still following the flow of the goods and applying the reverse charge for the collection of the VAT (see also Diagram 4 in Section 10 of Annex 5 for its functioning).

[100] Note that although the application of standard rates by all Member States could be seen, from a conceptual point of view, as an interesting approach (notably in terms of simplicity for businesses) it is not a realistic one. Options referring to a uniform rate for intra-EU supplies, such as VIVAT, CIVAT and SEVA (see explanation in Section 9 of Annex 5) were discarded at an early stage because Member States opposed to it. In addition, the mandatory application of standard rates would not be in line with the favourable views expressed by the Member States in Council (Council conclusions of 25 May 2016 on the Commission 2016 Action Plan on VAT) on the intention of the Commission to present a proposal for increased flexibility concerning the VAT rates setting by the Member States. It is worth noting in this respect that Member States that so wish would nevertheless continue to be free to impose the standard rate to all supplies (or parts thereof) since the application of reduced rates is always an option and not an obligation for Member States.

[101] Since 1 January 2015 the supply takes place in the Member State of the customer, and not in the Member State of the supplier as it used to be the case previously.

[102] See e-Commerce proposal (COM(2016) 757 final).

The current transitional VAT system splits every cross-border transaction into an exempt intra-EU supply and a taxable intra-EU acquisition. Under Option 3, the two separate concepts of intra-EU supply and intra-EU acquisition are abolished and replaced by one single transaction, the intra-EU supply, taxable in the Member State of destination. This means that from a practical point of view there will be no significant changes compared to the current system: goods sold and transported to another Member State will continue to cross borders free of VAT but from a conceptual and legal point of view, there will be only one rather than two intra-EU transactions.

When goods are dispatched or transported from one Member State to another the place of taxation will be in the Member State of arrival of the goods. If the goods are not transported or dispatched, the place of supply is in the Member State where the goods are located when the supply takes place.

Since this option involves a collection method based on the reverse charge, the person responsible for accounting for and collecting the VAT due will be the customer receiving the goods supplied rather than the supplier of the goods. The customer will therefore declare and deduct simultaneously the VAT relating to the cross-border supply in his domestic VAT return.

This option does not make use of a OSS for the reporting and collection of the VAT due. In any event, the customer will be obliged to provide the supplier with his VAT identification number attributed by the Member State of taxation. Further information would be exchanged via the recapitulative statement to be submitted by the supplier.

5.6. Option 4: Alignment with the place of supply of services

Option 4 consists in aligning the place-of-supply rules for goods with those governing the place of supply of services and using the reverse charge for the collection of the VAT. There will be only one taxable transaction – the supply of goods – meaning that the concept of intra-EU acquisition of goods will be abolished (see also Diagrams 5 and 6 in Section 10 of Annex 5 for its functioning).

Irrespective of whether or not goods are dispatched or transported, the place of supply will be where the customer has his main place of business and VAT will accrue to the Member State where that main place of business is located. This is also valid if the goods are transported to a Member State where the customer has no presence at all (neither in the form of his main place of business nor in the form of a fixed establishment) – the VAT due on that supply will still be due in the Member State where the main place of business of the customer is located.

However, where the goods are provided to a fixed establishment of the business customer, and this is in a Member State other than that where he has his main place of business, the place of supply will be where the fixed establishment is located. If the taxable person has neither a place of establishment nor a fixed establishment, then his permanent address or usual residence will serve as the place of supply.

In any event, to be subject to VAT the goods must be located within the EU. If a transaction involves goods located outside the EU, the transaction will not be taxable. On the other hand, if goods are in the EU, VAT will always be due, even if the customer is not established in the EU.

This option does not allow to completely disregarding the physical flows of the goods. In cases where the goods are provided to a fixed establishment of the business customer, and this is in a Member State other than that where he has his main place of business, the actual destination of the goods will remain the essential element to take into account.

When the supplier is not established in the Member State of taxation, the customer will be liable for the payment of VAT by applying the reverse charge.

The customer will be obliged to provide the supplier with his VAT identification number attributed by the Member State of taxation. In order to combat fraud, the location of the goods will need to be mentioned on the invoice/recapitulative statement and information would be exchanged via the recapitulative statement to be submitted by the supplier.

A simplification measure would be introduced whereby supplies to CTPs (see box 4 above) would not require a recapitulative statement. Given that the reverse charge will be applicable in all cases where the goods are supplied to a customer established in a Member State other than that of the supplier and that in those cases the supplier will not have to charge VAT, a fully extended OSS is not required under this option. A limited OSS would however be needed for goods supplied to a non-EU customer where those goods are located within the EU.

5.7. Option 5: Taxation following the contractual flow

Option 5 consists in aligning the place-of-supply rules for goods with the contractual flow and having the supplier charge the VAT of his customer (see also Diagrams 7 and 8 in Section 10 of Annex 5 for its functioning)**.**

This means that the supplier will have to charge the VAT of the Member State of establishment of the customer which has contracted the supply of the goods, irrespective of whether or not the goods are transported cross-border.

If the supplier is not established in the Member State of taxation, he will report the VAT due using the OSS.

If the contracting party reallocates the cost to another establishment of the contracting party, that will be treated as a deemed supply and this entity will be required to account for and report the VAT due, once again using the OSS if the entity is not already registered for VAT in the Member State of taxation.

In any event, to be subject to VAT the goods must be located within the EU. If a transaction involves goods located outside the EU, the transaction will not be taxable. On the other hand, if goods are in the EU, the VAT will always be due, even if the customer is not established in the EU. In this last case, the place of supply will be the Member State where the supplier is established, or the customer will have the obligation to register in a Member State of the EU and all the supplies made to him will be located in this Member State.

A simplification measure will allow supplies made to CTPs to be subject to the reverse charge with the customer accounting for and paying the VAT.

For this option to apply in a simpler and more consistent manner across the EU, it would be desirable to standardise the definitions of products eligible for reduced rates[103].

In order to combat fraud the customer will be required to report all purchases from non-established businesses (except those for which the reverse charge is applied).

5.8. Summary: main features of the options

5.8.1. Place of taxation

In addition to the baseline, the five alternative policy options ensure taxation at destination of cross-border B2B supplies of goods. However, they differ as to the actual place of taxation (see Table 4 below). Similar to the baseline, Option 1, Option 2 and Option 3 deem the place of taxation to be the Member State of arrival of the goods (follow the flow of goods), whilst Option 4 and Option 5 deem the place of taxation to be where the customer is established (follow the contractual flow). This distinction is important from a Member State's audit perspective (e.g. impact on administrative costs, efficiency of VAT collection) as following the flow of goods means that the movement of goods is monitored by the Member States. Such control instrument does not exist when taxation follows the contractual flow.

5.8.2. Person liable for the payment of VAT

When considering the way VAT would be collected, the options can be further classified in two main models (see Table 4 below): the "taxation model" (Option 2 and Option 5) and the "reverse charge model" (baseline, Option 1, Option 3 and Option 4). The taxation model, with the supplier charging the VAT to his customer, is based on fractionated payments. It ensures the self-policing character of the VAT system[104] and is also the system that applies in domestic trade. The reverse charge model, with the customer self-assessing the VAT due, suspends the collection of VAT until the final consumption stage (it allows VAT-free purchases by businesses) and therefore differs from domestic trade treatment. This is an important element as regards equal treatment but also more particularly with regard to MTIC fraud.

Table 4: Classification of the options

	Taxation model	Reverse charge model
Flow of goods	Option 2 *"Taxation following the flow of goods"*	Baseline Option 1 *"Limited improvement of current rules"* Option 3 *"Reverse charge following the flow of goods"*
Contractual flow	Option 5	Option 4

[103] See also footnote 100 on the discarding of standard rates.

[104] See Section 1.4 above.

	"Taxation following the contractual flow"	*"Alignment with the place of supply of services"*

5.8.3. Technological dimension

Option 2, Option 4 and Option 5 build on the existing MOSS (in excess of EUR 3 billion was collected through the MOSS in 2015. This is estimated to account for 70% of total cross-border B2C sales of electronic services). These options would extend the use of such system which has shown to be successful in collecting VAT as a central point of contact.

Option 1 builds on the existing VIES system. Through the introduction of the CTP concept and the mandatory reference of the VAT identification number of the customer, it is expected to improve the quality of data exchanged between Member States.

5.8.4. Summary table

As can be seen from the summary Table 5 below, the five options have a number of similarities and differences. The summary table shows the scope of the obligations under each option and the applicable rules. It further outlines whether specific legislative issues[105] identified with the current transitional VAT system are addressed under each option.

[105] See Section 2.4 above: treatment of call-off stock and chain transactions, as well as the means of proof of intra-EU transport of goods.

Table 5: Main features of the options[106]

Criteria	Option 1	Option 2	Option 3	Option 4	Option 5
Implementation of Destination Principle	Utilises existing reverse charge model Supplier in Member State 1 does not charge VAT Customer self-accounts for VAT in Member State 2 (where goods are located at the time when transportation ends) using the reverse charge	Supplier in Member State 1charges VAT of Member State 2 (where goods are located at the time when transportation ends) If customer is a CTP he will account for VAT via the reverse charge	Supplier in Member State 1 does not charge VAT Customer self-accounts for VAT in Member State 2 (where goods are located at the time when transportation ends) using the reverse charge	Supplier in Member State 1 does not charge VAT Customer self-accounts for VAT in Member State 2 (place of establishment) using the reverse charge	Supplier in Member State 1 charges VAT of Member State 2 (place of establishment of the customer) If customer is a CTP he will account for VAT via the reverse charge
Equal treatment with domestic supplies	No	Yes	No	No	Yes
Place of supply	Follows actual flow of goods – where the goods are located at the time when transportation ends (Member State 2)	Follows actual flow of goods – where the goods are located at the time when transportation ends (Member State 2)	Follows actual flow of goods – where the goods are located at the time when transportation ends (Member State 2)	Follows customer's place of establishment (Member State 2)	Follows where the contracting party (customer) is established (Member State 2)
Mechanism used to account for VAT	Customer's VAT return in Member State 2 – acquisition tax	Supplier's One Stop Shop return in Member State 1	Customer's VAT return in Member State 2 – reverse charge	Customer's VAT return in Member State 2 – reverse charge	Supplier's One Stop Shop return in Member State 1

[106] Table 4 based on the outcome of EY study 2015 Implementi*ng the 'destination principle' to intra*-EU B2B supplies of goods

Criteria	Option 1	Option 2	Option 3	Option 4	Option 5
		Input VAT for each Member State of taxation offset via deduction on VAT return in Member State 1			Input VAT for each Member State of taxation offset via a deduction on VAT return in Member State 1
Reporting	Existing VAT return	One Stop Shop return	Existing VAT return – If not already registered, customer will have an obligation to register for VAT in the Member State of taxation	Existing VAT return	One Stop Shop return
Recapitulative statements	Required	Obligation to submit is removed	Required	Required (unless the customer is a Certified Taxable Person)	Obligation to submit is removed
Additional reporting obligations	N/A	Customer required to report purchases from non-established businesses (except if the customer is a CTP and reverse charge is applied). When transport of goods is not organised by or on behalf of the supplier, the customer shall provide the supplier with the name of the Member State of arrival of the goods within ten working days.	N/A	Location of goods to be mentioned on invoice/recapitulative statement	Customer required to report all purchases from non-established businesses (except if the customer is a CTP and reverse charge is applied).
Simplification measures relating to main legislative	VAT identification number of the	Rates simplification:	N/A	Introduction of a limited One Stop Shop for goods	Rates simplification:

Criteria	Option 1	Option 2	Option 3	Option 4	Option 5
issues and additional considerations	acquirer made compulsory for the exemption of the intra-EU supply of goods. Harmonisation of the call-off stock, the treatment of chain transactions across EU and the means of proof of intra-EU transport of the goods[107].	Definitions of products eligible for a reduced rate would be standardised and provided via a web portal Reverse charge for supplies to Certified Taxable Persons.		supplied to a non-EU customer but staying within the EU.	Definitions of products eligible for a reduced rate would be standardised and provided via a web portal Reverse charge for supplies to Certified Taxable Persons.

[107] Note that under Option 2, Option 4 and Option 5 the problem of complexity linked to the VAT treatment of call-off stocks and chain transactions across EU and the means of proof of intra-EU transport of the goods is intrinsically solved by the change in the system provided under each of these options. In other words, the problem of complexity is solved independently from the implementation of Option 1.

5.9. Discarded option: Option 3

The changes proposed under Option 3 are of a technical legislative nature. Instead of having two transactions (exempt intra-EU supply and taxed intra-EU acquisition), Option 3 provides for one single transaction, the intra-EU supply taxable in the Member State of destination. There is no significant difference between this option and the current transitional VAT system. In both situations, the place of taxation is the Member State of arrival of the goods and it is the customer that pays the VAT.

Even if the legislative changes are minor, their implementation is expected to have some impacts on different elements as compared to the baseline (see further details in box 6 below). However, their magnitude compared to other options (in particular Option 2, Option 4 and Option 5) is negligible. Although, when compared to Option 1, it might seem to have slightly more positive impacts (mainly due to compliance costs reduction for large businesses), it does not address any of the legislative issues raised by the current transitional VAT system[108]. Moreover, it does not address MTIC fraud. Therefore this option has been discarded as an alternative option for future policy reform.

Box 6: Main impacts of Option 3 compared to the baseline

MTIC fraud - No changes expected to the scale of VAT fraud

This option is unlikely to materially affect the occurrence of VAT fraud as goods will continue to circulate cross-border VAT free as currently the case.

Administrative costs of Member States[109] **-** Increase

Member States' administrative costs would increase by EUR 88 million in the year of implementation and by EUR 43 million annually after the year of implementation.

Compliance costs of businesses[110] **-** Reduction

The average ongoing cost reduction for all businesses would be 5% although the impact would vary depending on the entity size and trade profile. For SME Type 1 businesses, the average ongoing cost reduction would be 3%; for SME Type 2 and for large businesses it would be 7%[111]. In aggregate, this option is estimated to result in a cost reduction of EUR 318 million and EUR 952 million in the year of implementation and annually respectively.

Cash flow - Neutral for businesses and Member States

VAT on intra-EU purchases of goods continues to be declared and recovered (to the extent the business is entitled to do so) by businesses in the same VAT return.

Macroeconomic impact – Slightly positive but well below other options

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[108] See Section 2.4 above: treatment of call-off stock and chain transactions, means of proof of intra-EU transport of goods.

[109] Two areas of VAT administration are expected to be impacted: VAT return audit and compliance checks as a result of (i) a new VAT accounting mechanism and (ii) the need to notify businesses about the new policy requirements.

[110] The following aspect is expected to result in a reduction in compliance costs: application of the reverse charge. Conversely, the following aspect is expected to have an additional cost implication: businesses must update the format of their invoices to state that their supplies are subject to the reverse charge.

[111] See Glossary and Annex 4 for a description of the classification of business types.

The 3-year cumulative real EU GDP growth is estimated to be 0.005% higher than the baseline[112]. This corresponds to a net impact of EUR 0.5 billion in EU GDP.

6. WHAT ARE THE IMPACTS OF THE DIFFERENT POLICY OPTIONS AND WHO WILL BE AFFECTED?

6.1. Methodology

A specific study[113] has been commissioned to assess the impacts of the implementation of each of the policy options on the MTIC/VAT fraud, the administrative costs[114] and the cash flow of Member States, and on the compliance costs[115] and the cash flow of businesses. The macroeconomic impacts and in particular the effects on macroeconomic variables such as gross domestic product (GDP) are also assessed. The impact of the policy options from an internal market perspective, in particular the overall consistency in the VAT treatment of domestic and cross-border supplies of goods, is also covered.

A range of methodological tools are used to analyse the various impacts. In particular, the study relies on primary and secondary data (business survey and interviews, tax experts' survey, Member States' survey and interviews) collected across all 28 EU Member States to inform the analysis of compliance costs for businesses, administrative costs of Member States, cash flow impacts on businesses and Member States and the economic impacts. The data collected has been used to develop useful qualitative (technical, legislative, etc.) and quantitative insights, and inform also the assumptions and the parameters in the macro econometric Vector Autoregressive (VAR) model used for analysing the economic impacts.

The findings are therefore sensitive to the opinions of a sample of business respondents, tax officials and tax experts on questions that do not cover every possible element that might be required in order to fully assess the implications of the current and proposed policy options.

A detailed description of the overall methodology, the variety of data collection tools, the VAR model used, the key assumptions, and the limitations and caveats of the study is presented in Annex 4.

Finally, the environmental and social impacts of all policy options should be negligible or even zero and are not therefore covered in the below analysis.

6.2. Analysis of the impacts of each of the options

6.2.1. Baseline

Section 2 outlines in detail the problems and the problem drivers of the baseline. In summary, the situation is as follows.

[112] See Section 6.2.1 Baseline below - baseline forecasts based on a 3-year period (2014-2016).
[113] EY, 2015
[114] See Glossary for definition.
[115] See Glossary for definition. For a description of the classification of the business types (Type 1 SME, Type 2 SME and Large businesses) for which the assessment is carried out, see Glossary and Annex 4.

1. **MTIC fraud -** Ranges from EUR 45 billion to EUR 53 billion annually[116].

2. **Administrative costs of Member States[117] -** The monetary value of the labour costs associated with VAT administration is estimated at approximately EUR 1 730 million in the EU. In addition, Member States' non-labour costs associated with the administration of VAT (including external consultancy, IT systems and staff training costs) are on average EUR 27 million per Member State or EUR 745 million for the EU.

3. **Cash flow of Member States[118] -** Neutral as VAT on intra-EU purchases of goods continues to be declared and recovered (to the extent the business is entitled to do so) by businesses in the same VAT return.

4. **Compliance costs of business -** The intra-EU VAT compliance cost of businesses is estimated to be 0.62% of turnover from intra-EU trade[119]. On average, the VAT cost of compliance per Euro of turnover is 11% higher for intra-EU trade as compared with the corresponding VAT compliance per Euro of turnover for domestic trade.

5. **Cash flow of businesses[120] -** Neutral as VAT on intra-EU purchases of goods continues to be declared and recovered (to the extent the business is entitled to do so) by businesses in the same VAT return.

6. **Internal market perspective** - Non-equal treatment domestic/cross-border supplies of goods.

7. **Macroeconomic forecast** – The EU-28 per capita real EU GDP is estimated to grow at a cumulative rate of 4.465% over an estimated 3-year period[121]. In absolute terms, the baseline real EU GDP at 2005 prices in 2013 was EUR 11 768 billion.

Box 7: Cash flow impacts of the different options

Impact on business cash flow

Cash flow implications are likely to occur under some of the policy options.

Under Option 1, the implementation of the call-off stock simplification across all Member States may result in a positive cash flow impact for some businesses. This is due to businesses no longer being required to account for VAT on the deemed intra-EU acquisition and subsequent domestic sale to their customer. Instead, when the goods are moved, the customer in the other Member State will self-assess the VAT on their local

[116] Diversion fraud has not been quantified because, as such, it is not the focus of the present impact assessment (see footnote 66). However, the impact on diversion fraud of the alternative options to the baseline has been taken into account because some of these policy options would have implications on this type of fraud.

[117] See further explanation of labour and non-labour administrative costs in Annex 4.

[118] See further explanations on cash flow impact in box 7 below.

[119] Business survey data, EY, 2015.

[120] See further explanations on cash flow impact in box 7 below.

[121] EY, 2015. The baseline has been calculated for a 3-year period (2014-2016) and the forecast is based on the VAR model. The estimated baseline forecast of GDP growth (4.465%) is not substantially different from the EC's spring 2015 forecast which indicates a cumulative growth of 5.3% during the 2014-2016 periods.

VAT return. Under Option 4, a similar impact is expected. However, this particular cash flow effect will only impact a small population of businesses since at most 13% of businesses engage in call-off stock transactions. As a result, the overall effect of the cash flow implications under Option 1 and Option 4 is assumed to be negligible.

Cash flow implications are however expected under Option 2 and Option 5 as these two options will affect all intra-EU sales of B2B goods (under these two options the supplier will charge the VAT to his customer), and not just specific transaction types such as call-off stock.

Impact on Member States cash flow

The baseline scenario for Member States is cash flow neutral, on the basis that the self-assessed VAT on intra-EU purchases of goods can be declared and recovered (to the extent the business is entitled to do so) in the same VAT return. This is also the case for Option 1 and Option 4.

However, as a result of the clearing system to be implemented as part of the OSS system under Option 2 and Option 5, cash flow has been identified as either a particular cost or benefit for Member States.

6.2.2. Option 1: Limited improvement of current rules

Summary

Member States

1. *No significant changes to the scale of MTIC fraud*
2. *Limited administrative costs increase in all Member States (around EUR 35 million)*
3. *No cash flow implications*

Businesses

4. *Compliance costs decrease for all businesses (around EUR 0.5 billion annually)*
5. *No cash flow impact*
6. *Non-equal treatment domestic/cross-border supplies of goods*
7. *Net increase of EUR 0.4 billion in EU GDP over a 3-year period*

1. MTIC fraud and other fraud aspects

No significant changes are expected to the scale of MTIC fraud.

Providing evidence of transport for an intra-EU supply of goods is not designed to combat MTIC fraud[122] and therefore the proposed legislative changes should not materially positively or negatively impact the current level of fraud carried out through MTIC or diversion[123].

2. Administrative costs

In monetary terms, an increase of administrative costs by EUR 79 million in the year of implementation and by EUR 35 million annually post implementation is expected across all Member States.

This increase is mainly driven by increased non-labour costs both in the year of implementation (increase by EUR 26 million) and annually in the years post implementation (increase by EUR 12 million) associated with IT systems[124].

3. Cash Flow of Member States

Cash flow neutral[125].

4. Compliance costs

The impact of the changes on compliance costs varies depending on the entity size and trade profile of businesses.

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[122] Although this evidence may have some implications for the perpetrators of diversion fraud - see box 9 in Annex 5, Section 5.

[123] Although diversion fraud as such is not the focus of the present impact assessment and as therefore not been quantified (see footnotes 66 and 116), the likely impact of the different options on this type of fraud has also be taken into account.

[124] More detailed figures on the changes of administrative costs are available in the specific study EY, 2015 (see in particular table 21 on page 99 of the study).

[125] See box 7 above.

SME Type 1: the average annual ongoing cost reduction would be 5%.

SME Type 2: the average annual ongoing cost reduction would be 29%.

Large business: it could result in an average annual cost reduction of up to 37%.

Although large VAT compliance costs savings are expected, these will only impact a limited number of businesses; an estimate of the maximum percentage of businesses positively impacted is 13%. In addition, it may result in reduced benefits in those Member States that have already implemented elements of this option. Therefore, for all businesses, the monetary impact of the implementation is estimated to reduce business costs by EUR 571 million in the year of implementation and by EUR 522 million annually after the year of implementation[126].

5. Cash flow of businesses

Negligible[127].

6. Internal market perspective

Domestic vs cross-border transactions

No equal treatment between domestic and cross-border supplies of goods as domestic supplies follow the taxation model while cross-border supplies follow the reverse charge model.

Overall consistency in the VAT treatment of transactions

Divergent place of supply rules for supplies of goods and supplies of services (less simple) but cross-border supplies of goods follow the same reverse charge model as cross-border supplies of services.

7. Macroeconomic impact

The 3-year cumulative real EU GDP growth is estimated to be 0.004% higher than the baseline. This corresponds to a net impact of EUR 0.4 billion in EU GDP.

[126] More detailed figures on anticipated net percentage and monetary costs changes expected for each business type as well as an "all business" aggregate are available in the specific study EY, 2015 (see in particular table 14 on page 82 of the study).

[127] See box 7 above.

6.2.3. Option 2: Taxation following the flow of goods

Summary

Member States

1. *Reduction of MTIC fraud by EUR 41 billion*
2. *Administrative costs increase in all Member States*
3. *Cash flow benefit for the majority of Member States*

Businesses

4. *Compliance costs decrease for all businesses (close to EUR 1 billion), except for SME type 1*
5. *Either a cash flow benefit or a cash flow cost depending on trade pattern and filing deadlines/remittance timeframes*
6. *Equal treatment domestic/cross-border supplies of goods*
7. *Net increase of EUR 18.5 billion in EU GDP over a 3-year period*

1. MTIC fraud and other fraud aspects

Although there will still be an opportunity for MTIC fraud to be perpetrated, it will be significantly reduced in scale. This is because a fraudster who is intent on perpetrating MTIC fraud will only be able to abscond with the VAT on the mark-up (mark-up is the difference between the cost of a good and its selling price) on the purchase price of the goods rather than the VAT on the entire sales value of the goods as is currently possible with the VAT free cross-border purchases. This has the effect of significantly reducing the scale of VAT fraud per transaction.

According to estimates[128] and assuming a uniform mark-up on cross-border goods by businesses across the EU, the MTIC gap (which ranges from EUR 44.5 billion to EUR 53.2 billion[129]) will shrink to an estimated EUR 8.2 billion, a reduction of EUR 41 billion (83%). This is equivalent to 4.5% of the total VAT revenues and 0.31% of the GDP in the EU.

These estimated reductions in MTIC fraud are deemed conservative because they do not consider the further reduction in VAT fraud that a less attractive VAT fraud value per unit of transaction creates[130].

2. Administrative costs

In monetary terms, an increase of administrative costs by EUR 239 million in the year of implementation and by EUR 182 million annually post implementation is expected across all Member States.

This increase is mainly driven by increased labour costs both in the year of implementation (increase by EUR 101 million) and annually in the years post implementation (increase by EUR 121 million).

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[128] EY, 2015.

[129] See estimates under Section 2.3.1 above.

[130] More detailed figures on the VAT gap for each Member State and the impact that Option 2 will have on the scale of the reported magnitudes of MTIC fraud are available in the specific study EY, 2015 (see in particular table 33 on page 118 of the study).

Increase in non-labour costs is mainly driven by IT system cost increases, especially in the year of implementation[131].

In addition to these costs, where Member States would be asked to standardize the definitions of products eligible for reduced VAT rate and to establish a central web portal, an increase of administrative costs by EUR 146 million in the year of implementation and by EUR 129 million annually post implementation is expected across all EU Member States.

This increase would be mainly driven by increases in labour costs in the year of implementation and annually in the years post implementation, while the IT system is estimated to have the biggest non-labour costs impact in the year of implementation[132].

3. Cash flow of Member States[133]

Cash flow arising from acquisitions

Where a Member State has a filing period that is less than 40 days[134], it will suffer from a cash flow cost. This is due to businesses that incur VAT on intra EU purchases netting off this amount on their domestic return prior to the Member State receiving this VAT from the OSS clearing system[135].

Where a Member State has a filing period that is more than 40 days, it will have a cash flow benefit. This is due to the Member State receiving the VAT due to them from the clearing system prior to the businesses in their Member State accounting for this on their domestic VAT return.

Cash flow arising from supplies

As Member States will be holding VAT that they would not under the current rules, this will always result in a cash flow benefit.

Overall impact on Member States

The majority of Member States will have an overall cash flow benefit. As there is limited asymmetry between countries based on trade patterns within the EU, the overall cash flow benefit for Member States arises as a result of either having a filing period that is greater than 40 days (Member State is in a positive cash flow position in relation to acquisitions) or the fact that the cash flow benefit on dispatches (Member States are always in a positive cash flow position in relation to dispatches) outweighs the cash flow cost incurred on acquisitions.

4. Compliance costs

[131] More detailed figures on the changes of administrative costs are available in the specific study EY, 2015 (see in particular table 30 on page 100 of the study).

[132] More detailed figures are available in the specific study EY, 2015 (see in particular table 24 on page 102 of the study).

[133] More detailed figures on the individual and aggregate cash flow impact for each Member State based on their trade levels with every other Member State are available in the specific study EY, 2015 (see in particular table 31 on page 111 of the study).

[134] Refers to the VAT return filing deadline which can vary, depending on the Member State, from 10 days to 54 days following the reporting month.

[135] The supplier has 20 days from the end of the period to remit the VAT to its Tax Authorities who will hold the VAT for 20 days before remitting it to the Tax Authorities of the Member State of consumption (i.e., a total of 40 days). See EY, 2015 (p. 107 to 112) for further details on the calculation.

The impact of the changes on compliance costs varies depending on the entity size and trade profile of businesses.

SME Type 1: the average annual ongoing cost increase would be 6%.

SME Type 2: it could result in an average annual cost reduction of up to 17%.

Large business: it could result in an average annual cost reduction of up to 11%.

For all businesses, the monetary impact of the implementation is estimated to increase business costs by EUR 457 million in the year of implementation, but results in a net business decrease of costs by EUR 938 million annually after the year of implementation[136].

5. Cash flow of businesses

Cash flow implications are expected due to the requirement for businesses to levy and collect VAT on transactions where previously no cash may have been received or paid. Impact would depend on whether a business is in a net payment or a net repayment position in its OSS return[137].

Net payment position on OSS

Where a business is in a net payment position on its OSS return (it receives more VAT on its sales of goods to other Member States than it incurs VAT on purchases of goods in those Member States), and it has received payment from its customer, it will benefit from a positive cash flow due to receiving VAT from its customers and holding this VAT until the OSS filing deadline.

Net repayment position on OSS

Where a business is in a net repayment position on its OSS return (it incurs more VAT on purchases of goods in other Member States than it receives from sales of its goods in other Member States), the business will experience a negative cash flow position due to having paid VAT to its supplier and not being able to benefit from an immediate repayment of this VAT (repayment will take place after OSS filing deadline).

Overall impact on businesses

Businesses are likely to either have a cash flow benefit or cash flow cost. This will depend on the trade profile of businesses, filing deadlines and, in the case of net repayment traders, remittance timeframes.

6. Internal market perspective

Domestic vs cross-border transactions

Equal treatment between domestic and cross-border supplies of goods as both domestic and cross-border supplies of goods follow the taxation model.

136 More detailed figures on the anticipated net percentage and monetary costs changes expected for each business type as well as an "all business" aggregate are available in the specific study EY, 2015 (see in particular table 15 on page 84 of the study).

137 See EY, 2015 (p. 90 to 93) for further details on calculation.

Overall consistency in the VAT treatment of transactions

Divergent place of supply rules for supplies of goods and supplies of services (less simple) and cross-border supplies of goods follow the taxation model while cross-border supplies of services follow the reverse charge model[138].

7. Macroeconomic impact

The 3-year cumulative real EU GDP growth is estimated to be 0.157% higher than the baseline. This corresponds to a net impact of EUR 18.5 billion in EU GDP. It is estimated that EUR 2 billion of this impact is due to compliance cost reduction, while EUR 16.5 billion is due to the reduction in VAT fraud.

[138] However, this model dissimilarity would only be temporary as the taxation model would further extend to cross-border supplies of services – see Action Plan.

6.2.4. Option 4: Alignment with the place of supply of services

Summary

Member States

1. *No significant changes to the scale of MTIC fraud with risk of new types of fraud*
2. *(Limited) administrative costs increase in all Member States (around EUR 35 million)*
3. *No cash flow implications*

Business

4. *Compliance costs decrease for all businesses (close to EUR 2.7 billion)*
5. *No cash flow impact*
6. *Non-equal treatment domestic/cross-border supplies of goods*
7. *Net increase of EUR 2 billion in EU GDP over a 3-year period*

1. MTIC fraud and other fraud aspects

An increase in the level of fraudulent activity could occur since in addition to the possibility to commit MTIC fraud as under current rules (under Option 4, the customer is still in a position to buy goods cross-border VAT free), new fraudulent schemes are made possible. That is because the VAT could be self-assessed in a Member State (payment and immediate deduction of VAT there) while the goods are effectively used in another Member States (possibly for private use although VAT has been deducted as if it were for business purposes). Also, diversion fraud is facilitated due to the fact that taxation of the supply is disconnected from the movement of the goods.

The anti-fraud measures proposed consisting in reporting obligations (obligation to mention the location of the goods on the invoice and the recapitulative statement) would help to counter these forms of fraud but only to the extent that Member States would exchange the information from recapitulative statements submitted by the supplier on a real time basis and have the capacity to effectively utilise the data to identify incidences or potential incidences of fraud.

Therefore, Member States have a reduced ability to identify and reduce the occurrence of fraud.

2. Administrative costs

In monetary terms, an increase of administrative costs by EUR 154 million in the year of implementation and by EUR 82 million annually post implementation is expected across all Member States.

This increase is equally driven by increased labour costs and non-labour costs associated to IT systems in the year of implementation (increase by EUR 50 million). Increase of administrative costs in the years post implementation is mainly driven first by labour costs (increase by EUR 32 million) and then non-labour costs associated with IT systems (increase by EUR 34 million)[139].

[139] More detailed figures on the changes of administrative costs are available in specific study EY, 2015 (see in particular table 21 on page 99 of the study).

3. Cash flow of Member States
Neutral[140].
4. Compliance costs
The impact of the changes on compliance costs varies depending on the entity size and trade profile of businesses. ***SME Type 1:*** the average annual ongoing cost reduction would be 5%. ***SME Type 2:*** the average annual ongoing cost reduction would be 20%. ***Large business:*** it could result in an average annual cost reduction of up to 23%. For all businesses, the monetary impact of the implementation is estimated to reduce business costs by EUR 2 620 million in the year of implementation and by EUR 2 690 million annually after the year of year of implementation[141].
5. Cash flow of businesses[142]
Negligible.
6. Internal market perspective
Domestic vs cross-border transactions No equal treatment between domestic and cross-border supplies of goods as domestic supplies follow the taxation model while cross-border supplies of goods follow the reverse charge model. ***Overall consistency in the VAT treatment of transactions*** The place of supply rules for supplies of goods and for supplies of services are aligned (simpler as both are at the place of the customer) and both cross-border supplies of goods and cross-border supplies of services follow the same reverse charge model.
7. Macroeconomic impact
The 3-year cumulative real EU GDP growth is estimated to be 0.017% higher than the baseline. This corresponds to a net impact of EUR 2 billion in EU GDP.

[140] See box 7 above.

[141] More detailed figures on the anticipated net percentage and monetary costs changes expected for each business type as well as an "all business" aggregate are available in the specific study EY, 2015 (see in particular table 17 on page 86 of the study).

[142] See box 7 above.

6.2.5. Option 5: Taxation following the contractual flow

Summary

Member States

1. *Reduction of MTIC fraud by EUR 41 billion with some risk of new types of fraud*
2. *Administrative costs increase in all Member States*
3. *Cash flow benefit for the majority of Member States*

Business

4. *Compliance costs decrease for all businesses (above EUR 1 billion) , except for SME type 1*
5. *Either a cash flow benefit or a cash flow cost depending on trade pattern and filing deadlines/remittance timeframes*
6. *Equal treatment domestic/cross-border supplies of goods*
7. *Net increase of EUR 18.5 billion in EU GDP over a 3-year period.*

1. MTIC fraud and other fraud aspects

Similar impacts to those of Option 2 are expected concerning MTIC fraud. However, Option 5 may be susceptible to a different type of fraud similar to that under Option 4. Under Option 5 (like under Option 4) the VAT is chargeable in the Member State where the customer is established. This could increase fraud on the basis that the goods can be shipped to a different Member State than that where the customer is established. Therefore, as under Option 4, the customer may use the goods for exempt or private/non-business purposes in another Member State and incorrectly recover in its Member State of establishment the VAT incurred.

The anti-fraud measures proposed consisting in reporting obligations (obligations for the customer to report all purchases from non-established businesses, except those for which the reverse charge is applied) would help to counter these forms of fraud but only to the extent that Member States would exchange the information on real time and have the capacity to effectively utilise the data to identify incidences or potential incidences of fraud.

2. Administrative costs

In monetary terms, an increase of administrative costs by EUR 230 million in the year of implementation and by EUR 236 million annually post implementation is expected across all EM Member States.

This increase is mainly driven by increased labour costs in the year of implementation (increase by EUR 92 million) but also annually in the years post implementation (increase by EUR 173 million).

Increase in non-labour costs is mainly driven by IT system cost increases, especially in the year of implementation[143].

In addition to these costs, where Member States would be asked to standardize the definitions of products eligible for a reduced VAT rate and to establish a central web portal, an increase of

[143] More detailed figures on the changes of administrative costs are available in specific study EY, 2015 (see in particular table 27 on page 105 of the study).

administrative costs by EUR 158 million in the year of implementation and by EUR 141 million annually post implementation is expected across all EU Member States.

This increase would be mainly driven by increases in labour costs in the year of implementation and annually in the years post implementation, while the IT system is estimated to have the biggest non-labour costs impact in the year of implementation[144].

3. Cash flow of Member States

Similar impacts to those of Option 2.

4. Compliance costs

The impact of the changes on compliance costs varies depending on the entity size and trade profile of businesses.

SME Type 1: the average annual ongoing cost increase would be 5%.

SME Type 2: it could result in an average annual cost reduction of up to 17%.

Large business: it could result in an average annual cost reduction of up to 11%.

For all businesses, the monetary impact of the implementation is estimated to increase business costs by EUR 460 million in the year of implementation, but results in a net business decrease of costs by EUR 1 008 million annually after the year of implementation[145].

5. Cash flow of businesses

Similar impacts to those of Option 2.

6. Internal market perspective

Domestic vs cross-border transactions

Equal treatment between domestic and cross-border supplies of goods as both domestic and cross-border supplies of goods follow the taxation model.

Overall consistency in the VAT treatment of transactions

The place of supply rules for supplies of goods and for supplies of services are aligned (simpler as both are at the place of the customer) but cross-border supplies of goods follow the taxation model while cross-border supplies of services follow the reverse charge model[146].

7. Macroeconomic impact

[144] More detailed figures are available in specific study EY, 2015 (see in particular table 29 on page 107 of the study).

[145] More detailed figures on the anticipated net percentage and monetary costs changes expected for each business type as well as an "all business" aggregate are available in the specific study EY, 2015 (see in particular table 18 on page 88 of the study).

[146] However, this model dissimilarity would only be temporary as the taxation model would further extent to cross-border supplies of services – see Action Plan.

The 3-year cumulative real EU GDP growth is estimated to be 0.158% higher than the baseline. This corresponds to a net impact of EUR 18.5 billion in EU GDP. It is estimated that EUR 2 billion of this impact is due to compliance cost reduction, while EUR 16.5 billion is due to the reduction in VAT fraud.

7. HOW DO THE OPTIONS COMPARE?

7.1. Summary assessment of the impacts

A summary assessment of the options against the baseline is presented below.

The Table 6 below gives a summary of the net impacts on Member States and the impacts on MTIC fraud, administrative costs (in the year 1 of implementation and annual ongoing post implementation) and cash flow under each policy option.

Table 6: Summary impacts on Member States in net monetary terms (EUR millions)[147]

Policy Options	Option 1	Option 2	Option 4	Option 5
Impact on MTIC fraud	-	41,130	-	41,130
Impact on Administrative costs				
Year 1 Implementation	-79	-385	-154	-388
Annual ongoing	-35	-311	-82	-377
Impact on cash flow	-	2,397	-	2,397
Net Impact[148]	**-35**	**43,216**	**-82**	**43,150**

Source: Based on EY, 2015.

7.1.1. Impact on MTIC fraud and on other fraud aspects

Under Option 1, the proposed legislative changes should not impact the current level of fraud carried out through MTIC or diversion. Under Option 4, a new exposure to fraud may arise. This is due to the fact that the Member State of destination of the goods may be different to the Member State where the VAT is required to be reported. As such, Member States have a reduced ability to identify and reduce the occurrence of fraud. Although under Option 2 and Option 5 there will still be an opportunity for MTIC fraud to be perpetrated, it will be significantly reduced in scale. The magnitude of this reduction will be influenced by the level of the mark-up applied by businesses on their purchases. A notable observation under Option 5 is that since the VAT is chargeable in the Member State where the customer is established, this could (similarly to Option 4) increase fraud on the basis that the goods could be shipped to a different Member State from where the customer is established.

In the public consultation[149], almost all tax advisors and academics (94%) expressed the opinion that taxation of B2B intra-EU supplies[150] would improve fighting fraud, while businesses seem to be less persuaded as only 43% of SMEs[151] and 39% of large businesses agreed with this view. This important difference could be explained by the fact that academics and tax advisors have usually more global approach and a wider understanding of the key elements of the VAT system as such. In the context of the proposal on the definitive VAT system the understanding of the importance of the self-

[147] A negative figure provided in this table refers to **a cost increase**.

[148] The net impact only considers annual ongoing administrative costs hence excludes the year of implementation administrative costs.

[149] More detailed information collected during the public consultation on responses provided by identified groups of stakeholders on fraud aspects can be found in Annex 2 and part 11 of Annex 5 (replies relevant are under questions 20, 21, 22 and 37).

[150] This refers to the taxation models under Option 2 and Option 5 – see Table 4 above.

[151] SMEs are businesses with turnover of 50 million or less, employing less than 250 people.

policing character of fractioned payments is very relevant for the assessment of the proposed options. On the other hand it should be pointed out that businesses are open to changes but at the same time they are more cautious in respect of possible additional costs that could be generated in this respect.

Further it is worth to note that over 74%[152] of the respondents agreed that the current system is not sufficiently resistant to VAT fraud within the EU.

In addition, the reverse charge mechanism as applied currently was recognised by 67% of all the stakeholders (within the group this position was held by 64% of SMEs and by 68% of larger business) as an effective, but rather costly measure to fight fraud.

7.1.2. Impact on administrative costs

Option 1 has the lowest cost impact from a VAT administration perspective in the year of implementation and annually post implementation. This may be due to the fact that some Member States have already implemented elements of this option. With regards to labour costs, under Option 2, Option 4 and Option 5, some additional FTE[153] requirements are expected in the year of implementation. However, only Option 5 would require notable additional FTEs in the years post implementation. With regards to non-labour costs, the implementation of IT systems is associated with the most significant cost increase expectations under Option 2, Option 4 and Option 5[154].

7.1.3. Impact on cash flow of Member States

For Option 1 and Option 4 there should be no material impact on cash flow of Member States. Option 2 and Option 5 will result in the majority of Member States having a cash flow benefit. This is due to Member States receiving and holding VAT for a period of time before businesses in their local Member State seek to recover the VAT on their domestic VAT return.

7.1.4. Impact on compliance costs

Table 7 below presents a summary of the impacts on compliance costs of businesses (both as percentage change and as change in monetary terms, in comparison to baseline) under each policy option for each type of business (SME Type 1, SME Type 2 and Large Business) as well as for an 'all businesses' aggregate.

Table 7: Summary impacts on compliance costs of businesses[155]

Summary	SME Type 1		SME Type 2		Large Business		All Businesses[156]	
Net cost	Year 1	Ongoing	Year 1	Ongoing	Year 1	Ongoing	Year 1	Ongoing

[152] Replies "strongly agree or agree" to Question "do you agree that the current taxation system is not sufficiently resistant to VAT fraud within the EU": 67% – the whole business, 79% – SMEs, 64% – large businesses , 68% – business associations, tax advisors and academics – 94%, members of the public – 100% and 100% – public authority.

[153] See Glossary.

[154] Information received come from the EY study. Feedback received via the public consultation is not sufficiently representative.

[155] A negative figure provided in this table refers to a **cost reduction.**

[156] The overall business impact is calculated as weighted average of SME Type 1 (39.8%), SME Type 2 (18.3%) and Large Business (41.9%) in the EU in 2013. The percentage of businesses in the EU in terms of gross value added (GVA) is reported in brackets. Source: Eurostat, Enterprise and Industry.

impact								
Option 1[157]	-4%	-5%	-36%	-29%	-40%	-37%	-25%	-23%
Option 2	15%	6%	-7%	-17%	-5%	-11%	3%	-5%
Option 4	-4%	-5%	-20%	-20%	-23%	-23%	-15%	-15%
Option 5	14%	5%	-7%	-17%	-4%	-11%	3%	-6%
Monetary impact (million EUR)								
Option 1[158]	-36	-46	-151	-121	-383	-355	-571	-522
Option 2	1,051	420	-225	-548	-369	-811	457	-938
Option 4	-280	-350	-644	-644	-1,696	-1,696	-2,620	-2,690
Option 5	981	350	-225	-548	-295	-811	460	-1,008

Source: EY, 2015.

As the above Table 7 shows, Option 1 is estimated to result, in percentage terms, in the largest VAT compliance cost savings for all types of businesses analysed and for all businesses. However, this option will only impact a limited number of businesses: approximately 13% of the business community would benefit which is also likely to be an over representation[159]. Therefore, the positive monetary impact of this option is significantly less than the other options. Option 4 is estimated to generate in monetary terms the highest compliance cost reductions for all types of businesses analysed. A notable observation is that the implementation of the OSS under Option 2 and Option 5 could result in cost increases for SME Type 1 businesses in the year of implementation and annually post implementation. However, with respect to SME Type 2 and large businesses cost reductions are expected in the year of implementation as well as on an ongoing basis.

Feedback from the open public consultation[160] showed that for 47% of the stakeholders the change that would introduce only one taxed transaction[161] would reduce business compliance costs whereas for 16% such costs would increase. Others believed that they will not be affected (17%) or had no opinion on this question (19%). The above information should be read together with the reply indicating that more than 89% of the respondents confirmed that businesses are confronted with some or many additional compliance costs linked with the application of the current VAT rules to intra-EU supplies of goods in comparison with the domestic supplies. None of the respondents replied that there are no additional compliance costs for the current situation. It is worth to note that more than 79% of the stakeholders believe that because of the additional compliance costs linked with VAT rules small companies do not engage in cross-border supplies.

[157] The implementation of this option would only affect approximately 13% of businesses across EU. The estimates in the table are not adjusted for this.

[158] The cost impact reported in the table reflects the fact that only 13% of businesses benefit from the implementation of this option.

[159] The percentage of businesses operating as Non-Resident Traders (NRTs) has been used as a reasonable proxy to use as an indicator of the percentage of businesses that undertake call-off, consignment or chain transactions. This is on the basis that NRTs may be operating in another Member State because of such transactions. Analysis of NRT data produces a proxy estimate of 13% of businesses engaged in these transaction types within the EU. However, this is likely to be an over estimate as there are likely to be a number of other reasons as to why an NRT is operating in other Member States.

[160] More detailed information collected during the public consultation on responses provided by identified groups of stakeholders on business's compliance costs can be found in Annex 2 and part 11 of Annex 5 (replies relevant are under questions 17, 19, 35, 39, 43 and 44).

[161] This concerns all options except Option 1.

80% of the stakeholders supported the extension of the OSS which would remove the obligation from the business to register in Member States in which it is not established and in this way reducing the compliance costs.

31% of the stakeholders believed that the introduction of the CTP would reduce the compliance costs of the suppliers while 45% indicated their potential increase.

Further it is important to note that the final assessment of the level of compliance costs linked with the CTP measure highly depend on whether the criteria to apply it would not be too burdensome[162]. 44% of the stakeholders would wish to request for such a status only if its application would not be too burdensome in practice. Only 8% would apply regardless of the level of difficulty linked with the requirements.

The feedback received from some business stakeholders via the REFIT Platform (see Annex 2), shows nevertheless support to measures for a correct VAT collection based on the concept of CTP (provided that the criteria used to define a CTP are easy and that information on CTPs is accessible to businesses on-line) and an extended OSS, as provided for under Option 2.

7.1.5. Impact on cash flow of businesses

There should be no significant impact upon cash flow of businesses under Option 1 and Option 4. Under Option 2 and Option 5, businesses are likely to either have a cash flow benefit or a cash flow cost. This will depend on the trade profile of businesses, filing deadlines and, in the case of net repayment traders, remittance timeframes. Where there is a cash flow cost, it is expected that this will be offset by the compliance cost savings the business would enjoy as a result of the implementation of these options.

In respect of the possible impacts on the cash flow, the stakeholders in the public consultation[163] had a visible preference for the customer being liable for VAT 56% in comparison with the supplier – 25%. Further, in the context of the cash flow the stakeholders had a strong preference – 88% - for including in the OSS the possibility to deduct the input VAT.

7.1.6. Internal market perspective

For over 50% of the respondents of the public consultation[164] the fact that domestic and intra-EU supplies of goods are currently treated differently for VAT purposes can be

[162] It is however important to note that the granting by the Member States of the CTP status to their businesses overall equates in maintaining the current reverse charge in place, therefore limiting the amounts of VAT being collected by other Member States. This means that the CTP status should in practice only be denied in very limited cases, i.e. when there is a risk that their businesses would commit fraud or be involved in a fraudulent scheme. The certification would be open to all businesses (except those specifically excluded) and the implementation of the criteria for its granting would need to be proportionate to also encompass smaller businesses. The process of certification remains optional for businesses.

[163] More detailed information collected during the public consultation on responses provided by identified groups of stakeholders on cash flow of business costs can be found in Annex 2 and part 11 of Annex 5 (replies relevant are under questions 34 and 40).

[164] More detailed information collected during the public consultation on responses provided by identified groups of stakeholders on internal market perspective can be found in Annex 2 and part 11 of Annex 5 (replies relevant are under question 15).

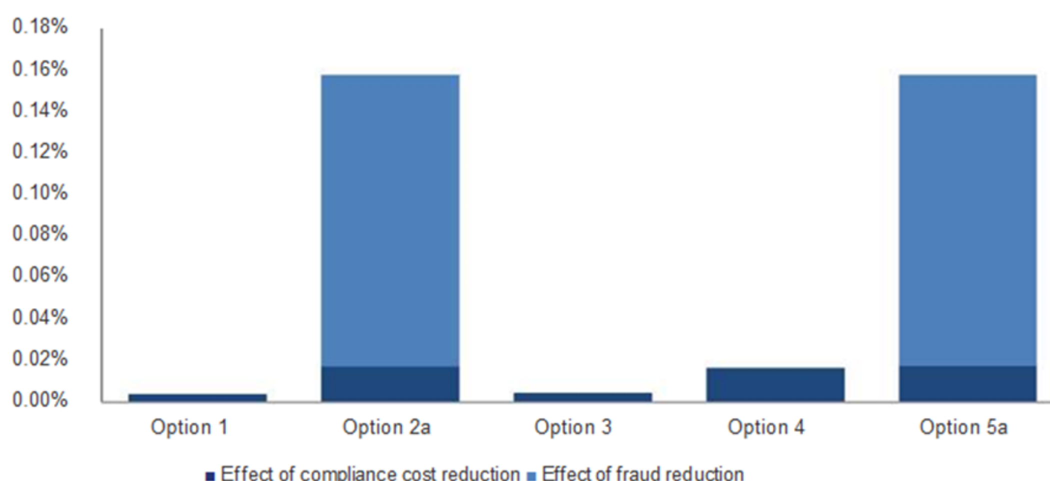
discouraging when making a decision about cross-border supplies which hampers the functioning of the internal market.

Although the specific legislative issues identified for the current transitional VAT system[165] are adequately addressed by Option 1[166], Option 2, Option 4 and Option 5, only Option 2 and Option 5 would ensure equal treatment between domestic and cross-border supplies of goods. In addition, under these two options, the single VAT registration through the OSS allows simplification for businesses as they would only have to comply with the VAT obligations (reporting, payment and deduction of VAT, including VAT due and incurred in other Member States) in the Member State in which they are established. This means that the tax administration of that Member State will also be their main contact point for practical issues (seeking information, etc.) and for audit purposes.

7.1.7. Macroeconomic impact

Figure 3 below represents a summary of the estimated net impact of each policy option on the 3-year cumulative real GDP growth, distinguishing between impact due to the effect of the compliance costs reduction and the effect of fraud reduction.

Figure 3: Differences of the EU 3-year cumulative per capita real GDP growth from the baseline under each policy option



Source: EY, 2015.

As illustrated in Figure 3 above, on the basis that Option 1 and Option 4 would reduce compliance costs but that there will be no material reduction in the level of MTIC fraud, the economic analysis shows that these options would have a relatively small but positive effect on the EU economy. On the basis that Option 2 and Option 5 assume a reduction in VAT fraud in addition to businesses' compliance cost savings, the economic analysis shows that these options would create a further boost to the EU economy. Either of these two options is expected to increase EU GDP by EUR 18.5 billion over a 3-year period, compared to the current situation.

[165] VAT identification number (legal value for intra-EU exemption, multiple VAT registrations), VAT treatment of consignment/call-off stock arrangements and chain transactions, evidence of transport required to exempt B2B intra-EU supplies of goods.

[166] See footnote 97 (some additional simplifications envisaged initially could not be proposed due to the lack of consensus of expert stakeholders and Member States).

However, it must be emphasised that the favourable economic forecasts of Option 2 and Option 5 are primarily due to the assumption that the expected additional VAT revenues from a reduction in the scale of VAT fraud are used to fund a VAT rate reduction. When the implication of the fraud reduction on the economic outcome is disregarded, Option 2, Option 4 and Option 5 are estimated to generate similar impacts on real EU GDP (about EUR 2 billion)[167].

7.2. Overall feedback of stakeholders on the options

Taking together the feedback received from stakeholders through the different channels[168], Option 1 appears to be the preferred option of both businesses and Member States. The reason is that Option 1 does not imply fundamental changes to the current transitional VAT system and as such is considered by both as a reasonable means to settle, at least in the short term, the most "easy" problems (reason why it is referred to these improvements as "quick fixes"). However, apart from Option 1, and as a more far-reaching option, Option 4 is the preferred option of businesses because it is more close to the treatment of services. However, Option 4 is not acceptable for the Member States because it does not solve the MTIC fraud problem and because the physical flow of the goods is not followed anymore. Option 2 is, among those which solve the fraud problem (Option 2 and Option 5) the preferred one of Member States because it allows following the flow of the goods and therefore ensures better control of the transactions.

7.3. Comparison of options

The following comparison assesses the options against the following criteria - effectiveness, efficiency and coherence - as defined below.

Options are compared to the baseline (0) by rating them as neutral/no significant change (0), slightly positive (+), positive (++), very positive (+++), slightly negative (-), negative (--) and very negative (---).

7.3.1. Comparison of effectiveness

As far as **effectiveness** is concerned, Table 8 below assesses how the options achieve the two objectives.

1) **Making the EU VAT system more robust**. The rating takes into account whether and to what extent current MTIC fraud can be reduced. It also takes into account whether occurrence of a new type of fraud is likely to happen under each option and to what extent additional anti-fraud measures could eventually counter such new types of fraud.

2) **Making the EU VAT system simpler**. The rating looks at whether and to what extent current burden of obligations is reduced and to what extent new obligations are likely to contribute to further reducing compliance costs for businesses while

167 To note that the economic impact estimated is considered to be conservative as compliance cost savings and the reduction in VAT fraud could well be higher; this is because the compliance cost estimates do not consider further cost savings that may occur in subsequent years due to increased compliance efficiencies while the VAT fraud reduction estimates do not include reduction in diversion fraud.

168 Open public consultation, REFIT Platform, spontaneous contributions, work in the VEG and GFV, Fiscalis seminar, business and Member States surveys, Council (see Annex 2).

maintaining administrative costs for Member States at an acceptable level. The rating also takes into account the simplicity and level of harmonisation of EU rules with the aim to ensure better compliance by business and legal certainty to the benefit of both businesses and Member States. Moreover, it takes into account whether and to what extent the VAT treatment of domestic and cross-border transactions in goods are aligned.

7.3.2. Comparison of efficiency

As far as **efficiency** is concerned, Table 8 below assesses the costs and benefits to both Member States and businesses. It takes into account the implementation costs of the policy options and their on-going costs expected for Member States and businesses. It looks in particular to the benefits in terms of VAT receipts for the Member States (including cash flow) and how the variation in compliance costs for businesses and the variation of VAT revenues for Member States (including administrative costs) would translate into the economy.

7.3.3. Comparison of coherence

As far as **coherence** is concerned, Table 8 below assesses how the options fit with the previous legislative proposal on e-commerce[169] and with future legislative proposals announced in the VAT Action Plan as regards VAT rates, the VAT package for SMEs and administrative cooperation.

1) As regard previous legislative proposals, for the record, the recent e-commerce proposal includes simplifications such as the extension of the use of the MOSS (introduced in 2015 to deal with B2C transactions on cross-border electronic services) to all cross-border B2C e-commerce supplies. While the e-commerce proposal focusses on B2C transactions, the rating takes into account whether the options for reforming cross-border B2B transactions are coherent with and to what extend build on the existing simplification provided under the MOSS.

2) As regards future legislative proposals, the rating takes into account the following considerations:

   - **Rates**: whether the option for reform is compatible with more flexibility to be given to the Member States in setting their VAT rates. It takes into account the impact that such flexibility might have on compliance to business and the extent to which simplification measures (e.g. VAT due by the CTP customer, standardisation of definitions of VAT rates rules) would facilitate the application of possible more divergent VAT rates rules;

   - **SMEs package**: whether some aspects of the option could negatively impact cross-border trade for SMEs and to what extend this can/would be addressed by the targeted proposal on SMEs;

   - **Administrative cooperation**: how each option is capable of taking stock of improvements envisaged at the level of exchange of information (quality and speed of exchange of information) and cooperation between the Member States.

[169] COM(2016) 757 final.

To what extent technological developments (OSS, CTP concept) under certain options would build on current MOSS and VIES systems.

Table 8: Summary analysis of impacts

Key impacts	Baseline	Option 1	Option 2	Option 4	Option 5
1- Effectiveness	*0*	*++*	*++++++*	*+*	*++++++*
Making the EU VAT system more robust	0	0	+++	--	++
Making the EU VAT system simpler	0	++	+++[170]	+++	++++[171]
2- Efficiency	*0*	*+*	*++++++++*	*+*	*++++++++*
Impact on Member States					
MTIC fraud/fraud reduction	0	0	+++	--	+++
Administrative costs	0	-	--	-	--
Cash flow	0	0	+++	0	+++
Impact on businesses					
Compliance costs	0	+	++	+++	++
Cash flow	0	0	+ or -	0	+ or -
Macroeconomic impact	0	+	++	+	++
C- Coherence	*0*	*0*	*++++++*	*+++++*	*+++++*
E-commerce proposal	0	0	+++	+++	+++
Future initiatives (rates, SMEs, Administrative cooperation)	0	0	+++	++	++

7.4. Identification of the preferred option: Option 2 (combined with Option 1)

7.4.1. Option 2 and final target

The analysis above indicates that Option 2 and Option 5 are the options that can best address altogether the specific objectives of making the EU VAT system more robust and simpler. By re-establishing the fractionated payments system in cross-border supplies of goods, their collection model based on the "taxation model" remedies the great flaw of the transitional arrangements that leads to MTIC fraud[172] and to complexity[173]. In doing

[170] An extra point is given for providing a level playing field for businesses
[171] An extra point is given for providing a level playing field for businesses
[172] Because they allow VAT-free cross-border purchases.

so they also fulfil the key objective of providing a level playing field for businesses as both Option 2 and Option 5 ensure that cross-border supplies of goods are taxed within the EU in the same way as domestic supplies. In addition, they could both further extend the taxation model to all cross-border B2B supplies in goods (and therefore extend to B2B supplies of goods made to CTPs) and cross-border supplies of services. This would then make the VAT system for intra-EU transactions fully coherent.

Option 2 and Option 5 would broadly provide comparable effects. However, Option 2 appears to score slightly better in terms of administrative costs for the Member States and with respect to making the VAT system more robust (conversely, Option 5 appears to score slightly better in terms of compliance costs for business but includes a risk of developing new types of fraud) as it allows continuing to follow the flow of the goods. As such an approach is prioritised by most Member States[174], **Option 2** has been retained as the preferred option for reform.

Option 2 allows for a gradual implementation[175] of the taxation model to all supplies of goods and services, being it domestic or cross-border. By providing, as a first legislative step, that the taxation model would only apply to cross-border B2B supplies of goods made to non-CTPs, it ensures a smooth transition for businesses and Member States. It would allow testing the functioning of the OSS before its further extension. Only where all necessary conditions would be met (i.e. Member States and businesses are legally and technically ready for it) would the second legislative step extend the taxation model to all businesses and to supplies of services so that the definitive system is fully implemented. It is to note that the changes envisaged under the second legislative step are not covered by Option 2 as described and analysed in this impact assessment.

7.4.2. A staggered and balanced implementation: combining Option 1 and Option 2

The implementation by the Member States of a proposal based on Option 2, including its negotiation in Council, is expected to require several years. Therefore, it would make sense to meet the request of Member States and businesses by also including in that proposal swift improvements to the current system ("quick fixes") as a short term measure. The right balance would therefore consist in combining in one proposal the benefits of two options:

- Option 2 as the preferred option for implementing the definitive VAT system (of which the entry into force of the different elements would be gradual);
- Option 1 allowing in the short term swift and limited improvements to the current transitional VAT system.

Improvements such as those contained under Option 1 are realistic as the concrete solutions it includes result from long discussions with the stakeholders[176], are in line with the contributions received through the REFIT platform (particularly relevant in this respect are submissions XVIII.2.a, and XVIII.7.a)[177], and should therefore easily get consensus. The entry into force of these improvements at an earlier date would already be

173 Because of additional and divergent obligations imposed on businesses trading cross-border.

174 See Section 4 of Annex 1 on the selection of options and Vienna Fiscalis results and Section 9 of Annex 5.

175 The VAT Action Plan announced a gradual two-step reform of the current transitional VAT system.

176 See Section 4 of Annex 1 for the work carried out by the GFV, the VEG and on-purpose sub-groups.

177 See Section 5 of Annex 2

beneficial for both Member States and business in the meantime the first step of the definitive VAT system is put in place. With limited administrative costs[178], Member States would gain legal certainty as regards the VAT treatment of intra-EU transactions in goods. Although Option 1 is not expected to have a significant impact on tax revenues, as it does not address the endemic weakness of the current transitional VAT system leading to MTIC fraud, it would however contribute to enhancing the quality of information exchanged between the Member States. Further, it is expected to bring some simplifications which should reduce compliance costs at least for some businesses.

The implementation of Option 1 should further not be seen as an additional layer but as complementary to Option 2. Indeed, the simplifications envisaged under Option 1 would be based on the new concept of CTP. The introduction of this concept and the simplifications linked to it are in line with the request formulated by stakeholders (see Sections 2 and 6 of Annex 2 and the REFIT initiatives reported in the same annex Section 5) to limit burden on compliant businesses. It would further allow testing the process of certification by the Member States and also its practical functioning and scope. On this basis adjustments might still be done if needed before the implementation of Option 2.

In order to ensure a smooth transition for business and allow all Member States to reach higher levels of cooperation and administrative capacity, a staggered implementation (divided into two sub-steps) of the first legislative step[179] is therefore envisaged as follows.

The sub-step 1 will consist of a first Directive and two Regulations. In the Directive the legal cornerstones of the definitive VAT system (cornerstones of the preferred Option 2) are introduced together with the short-term improvements to the current transitional VAT system ("quick fixes") requested by the Member States (Option 1). This first Directive therefore comprises the following elements:

Cornerstones of Option 2:

- Modification of Articles 402 to 404 of the VAT Directive[180]. The new wording of these articles would state, in connection with the definitive VAT system, the following:

  (i) the definitive VAT system will be based on the principle of taxation of the intra-EU supplies in the Member State of destination;
  (ii) the supplier will be liable to VAT unless the customer is a CTP, since in this later case the customer would be liable to VAT;
  (iii) where the supplier is not established in the Member State of destination he will declare the VAT through the OSS;
  (iv) the OSS will allow not only declaration-payment of the VAT due but also deduction of input VAT.

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[178] As previously mentioned, Option 1 is reported to have the lowest costs of administration, as this has the lowest cost of implementation.

[179] See Section 1.1.

[180] Article 402 currently states that the definitive VAT arrangements will be based in the principle of taxation in the Member State of origin.

Option 1:

- Legal value of the VAT identification number of the customer;
- Concept of Certified taxable person (CTP);
- Special scheme for call-off stocks arrangements between CTPs;
- Harmonisation and simplification of the rules as regards 'chain transactions' where CTPs are involved;
- Simplification where CTPs are involved of the rules as regards the evidence to prove the transport of goods to another Member State.

The sub-step 2 will consist of a second Directive (which will be likely accompanied by an Implementing Regulation), currently scheduled for adoption by the Commission in 2018 but with a later entry into force (2022). There the detailed implementing rules related to the following issues would be addressed (remaining elements of Option 2):

- Place of taxation in the Member State of arrival and single supply (abolition of the intra-EU acquisition concept);
- Taxation of intra-EU supplies (with reverse charge if the customer is a CTP);
- Technical functioning of the OSS and extension of the OSS for non-established taxable persons;
- Abolition of recapitulative statements.

7.5. Subsidiarity of the preferred option

The preferred Option 2 is considered to be consistent with the principle of subsidiarity as the main problems which have been identified (MTIC fraud leading to lost VAT revenues, complexity leading to high compliance costs) are triggered by the rules of the existing VAT Directive. Given that VAT is an EU-harmonised tax, Member States are currently not allowed by themselves to set different rules and therefore any further improvements require a proposal by the Commission to amend the VAT Directive. Therefore Option 2 will clearly offer value over and above what can be achieved at Member State level.

The same is valid for the combined implementation with Option 1. Although some improvements could already be introduced by the Member States by themselves without a need for an EU action the fact is that even where this has been done in some Member States, the measures differ from one Member State to another. Without mandatory and uniform improvements (contrary to what would be the case with the implementation of Option 1) complexity and legal uncertainty would not be solved.

7.6. Proportionality of the preferred option

The preferred Option 2 is considered to be consistent with the principle of proportionality i.e. it does not go beyond what is necessary to meet the objectives of the Treaties, in particular the smooth functioning of the internal market.

1. There is an overall positive impact on the revenues for EU Member States through a reduction in the VAT fraud and a positive cash flow impact which together more than compensate administrative costs changes.

2. There is equal treatment between domestic transactions in goods and intra-EU transactions in goods (in a second legislative step, there will be also equal treatment with transactions in services).
3. The main legislative issues leading to complexity of the current transitional VAT system are addressed.
4. There is an overall reduction in compliance costs to businesses[181].
5. The CTP status will be open to all businesses (including the smallest ones, start-up businesses[182]) but will remain optional for them. The certification would allow businesses to maintain existing arrangements until the implementation of the second step of the definitive VAT system. In the short term, it provides simplification for businesses (see Option 1 below). Once granted by a Member State, the CTP status will be valid in all EU Member States.
6. The OSS would build upon the existing MOSS[183] and therefore will be integrated into the web portal of each business' tax administration.

Prior implementation of Option 1 is also consistent with the principle of subsidiarity as it provides Member States and business with limited but nevertheless quick solutions for the most straightforward problems. It maps out the way to the implementation of Option 2 as simplification rules would be linked to the new concept of CTP, a cornerstone under Option 2.

1. Member States have more legal certainty with respect to the current exemption of intra-EU supplies of goods. Exchange of information between Member States about goods circulating across the EU is improved.
2. Certain businesses will benefit from simplification measures once they will be recognised as CTP. Such certification could already be requested by all business (and be granted by Member States) so that they would be ready when Option 2 is implemented.
3. Administrative costs for Member States are relatively small due to low cost of implementation and compliance costs reduction is expected for all businesses (although it will only be of benefit of a maximum of 13% of the business population due to the limited scope of the simplification envisaged).

As outlined in Section 2.7, a soft law approach, such as a Member State volunteering to introduce new anti-fraud measures or further simplification rules, is either not feasible or would lead to an even more fragmented VAT system.

As with the subsidiarity test, it is not possible for Member States to address the problems and problem drivers without a proposal to amend the VAT Directive.

7.7. Impact on SMEs

The initiative is not specifically targeted to SMEs as it does not foresee a preferential VAT treatment for SMEs. It addresses the problems of fraud and complexity of the current transitional VAT system and related compliance costs for all businesses.

[181] See however next Section 7.7 on SMEs.

[182] To note that businesses that are exempt from charging VAT (e.g. charities, financial institutions), businesses that have opted for certain special VAT schemes (e.g. farmers, small enterprises) and non-taxable legal persons (e.g. public bodies acting as such) are excluded because they do not have the obligation to declare VAT.

[183] MOSS is soon expected to be further extended (see proposal COM(2016) 757 final currently in negations in Council).

Simplifications such as the use of the OSS or those linked to the granting of the CTP status, including the granting of such status, would also be available to SMEs.

In this context, it is however important to underline that SMEs, which currently benefit from the VAT exemption scheme for small enterprises (see Chapter I of Title XII of the VAT Directive which encompasses Articles 282 to 294 of the VAT Directive) will continue to be exempt. Concerning their intra-EU acquisitions of goods, they would no longer have to report them as their suppliers would instead charge and be liable for the payment of VAT in the Member State of arrival of the goods (see more details in Annex 3). As for their intra-EU supplies of goods the new rules would theoretically imply the need for SMEs to charge to their customers the VAT in the Member State of destination[184]. However, the Commission will in parallel come forward with a proposal in the form of a comprehensive VAT simplification package for small enterprises which, inter alia, will address this problem[185].

The impact of the various options on smaller businesses has nevertheless been taken into account through the definition of two specific categories, to take account of differences in the extent to which SMEs engage already in intra-EU trade and have to deal with VAT obligations in other Member States: SME Type 1 and SME Type 2[186].

The benefits/costs of the preferred Option 2 to both types of SMEs can be summarized as follows:

1. The extended use of the OSS could result in cost increases for SME Type 1 in the year of implementation and annually post implementation. However, with respect to SME Type 2, costs saving are expected in the year of implementation as well as on an ongoing basis.
2. The main legislative issues linked to the complexity of the current transitional VAT system are addressed and would benefit to both categories of business.

As regards Option 1, the reduction in compliance costs is expected to benefit all businesses, thus including SME Type 1 and SME Type 2 as confirmed by the study[187]. However, as already mentioned, the maximum percentage of businesses positively impacted would be 13%.

8. HOW WOULD ACTUAL IMPACTS BE MONITORED AND EVALUATED?

8.1. Indicators for monitoring and evaluation

In line with the VAT Action Plan and following, inter alia, the views of stakeholders from the VEG, the definitive VAT system for intra-EU trade is to be introduced

184 See further explanation in Annex 3.
185 See Section 1.1 above.
186 Both SME Type 1 and Type 2 are businesses with a turnover of less than EUR 50 million and having less than 250 employees. **From a cross-border trade perspective**, whilst **SME Type 1** has a single VAT registration only in its Member State of establishment, engages predominantly in domestic trade and has begun trading outside its Member State, **SME Type 2** has VAT registrations in up to 6 Member States and is engaged in both domestic and intra-EU trade. See Section 2 in Annex 4 for further explanation on the definition of these business categories.
187 See information reported in Section 3 of Annex 2.

progressively via two main legislative steps[188]. It is recalled that the initiative that is here being assessed only covers the first legislative step.

The results of the monitoring will be used as a basis for deciding on the feasibility and timing of the second legislative step which would imply the extension of the system to all B2B supplies in goods (no distinction any more between CTP and non-CTP customers) as well as to supplies of services.

Table 9 below gives an overview of the main policy objectives, the indicators to measure whether they will be achieved, the tool for measuring these and the operational objectives. A specific indicator meant to evaluate the pace of implementation and the readiness for the second legislative step is provided.

Table 9: Monitoring and evaluation framework

Objectives	**Indicator**	**Measurement tool**	**Operational objectives**
To make the EU VAT system more robust	MTIC fraud VAT gap Administrative costs for tax administrations	EU VAT gap study and possibly other studies Data provided by the Member States	Very substantial decrease of MTIC fraud Target: 80% decrease at EU level Positive trend in VAT gap Target: EU average lower than 14% Stabilisation of increase in administrative costs through improved efficiency in monitoring VAT compliance Target: At least EUR 40 billion net positive impact on EU VAT revenues
To make the EU VAT system simpler	Compliance costs for businesses	Study to estimate the compliance costs Data and feedback provided by the business (VEG)	Reduction of compliance costs in cross-border trade Target: Reduction by 5% (all businesses[189])
To provide a level playing field for businesses	Compliance costs for businesses	Study to estimate the compliance costs Data and feedback provided by the business (VEG)	Substantial reduction of compliance costs in cross-border trade Target: Compliance costs gap domestic/cross-border below 11% and gradually close to zero.
Implementation process			

[188] See Section 7.4 on identification of the preferred option.

[189] For SMEs, compliance costs reduction will be monitored in the framework of the structures and according to the criteria to be put in place in the upcoming SMEs VAT package proposal (see Section 1.1 above).

	The flow of VAT revenues through the OSS The number of taxable persons recognised as CTP	Real time reports in OSS Data provided by the Member States	Correct re-distribution of VAT revenues between Member States

8.2. Monitoring structures

The VAT Committee, an advisory committee on VAT issues in which representatives of all Member States participate and which is chaired by Commission officials from DG TAXUD, will monitor the implementation of the definitive VAT system for intra-EU trade and discuss and clarify possible interpretation issues between Member States regarding the new legislation. It is also envisaged that the Standing Committee on Administrative Cooperation (SCAC) will deal with all possible issues regarding administrative co-operation between Member States resulting from the new rules on the taxation of intra-EU trade. In case new legislative developments are required, the GFV and the VEG might be further consulted.

8.3. Evaluation

Member States and the Commission shall examine and evaluate the functioning of the definitive VAT system provided for in the new legislation. To that purpose, Member States shall communicate to the Commission any relevant information as regards the level and the evolution of the administrative costs, MTIC fraud and number of businesses recognised as CTPs necessary for the evaluation of the effectiveness, efficiency, coherence with other interventions with similar objectives, and continued relevance of the new legislation. The evaluation should also seek to collect input from all relevant business stakeholders as regards the level and the evolution of their compliance costs. The Commission will prepare a retrospective evaluation of the functioning of the new legislation five years after its entry into force.

ANNEX 1: PROCEDURAL INFORMATION

1. Agenda planning and Work Programme References

The proposal for a definitive VAT system is linked to the VAT Action Plan.

TAXUD is the lead DG for this initiative. The Agenda Planning Reference is [2017/TAXUD/006]. The Inception Impact Assessment was published on 22 December 2016[190].

2. Inter-Service Steering Group (ISSG)

The meetings of the Inter-Service Steering Group have taken place on 5 December 2016, 6 April 2017, 14 June 2017 and 27 July 2017. The following Directorates-Generals (DG) and services were part of the group: Secretariat-General, Legal Service, DG Agriculture and Rural Development, DG Budget, DG Competition, DG Communications Networks, Content and Technology, DG Environment, DG Energy, DG Justice and Consumers, DG Financial Stability, Financial Services and Capital Markets Union, DG Internal Market, Industry, Entrepreneurship and SMEs, and European Anti-Fraud Office. The feedback received from these directorates and services has been taken into account in the final public consultation document.

It has to be noted that the ISSG as such had been set-up back in 2010 and had been consulted on all the main issues relating to the reform of the VAT system (Green Paper on the future of VAT, EY study (2015) on implementing the destination principle, Action Plan).

3. Consultation of the Regulatory Scrutiny Board (RSB)

The Regulatory Scrutiny Board was consulted on 12 July 2017. On 14 July 2017, the Board gave a positive opinion on the report. The recommendations made by the Board to further improve the report were taken into account. The main changes introduced concern the following aspects:

- Under the policy context (Section 1), clarification on the two-step approach to the initiative and its rationale is provided. The interrelations and sequencing of the initiative with recent proposals and upcoming VAT proposals on rates, SMEs and administrative cooperation is explained.
- Expected evolution of the baseline as well as risks are further described under the "dynamic baseline" (Section 2.7). Under the options section (Section 5), the components of the baseline are further explained, with specific clarification on its scope in relation to recent and upcoming proposals. Options are streamlined and differences between them are better described and illustrated (Section 5 and Annex 5, Section 10).
- The concept of Certified Taxable Person and its application in practice is explained in more details (Box 4). Clarification is given on the eligibility of this concept under the various policy options.
- The REFIT dimension of the analysis is strengthened by making more explicit reference to the feedback received from stakeholders under the problem definition,

[190] http://ec.europa.eu/smart-regulation/roadmaps/docs/2017_taxud_006_taxud_definitive_vat_en.pdf

the selection of options and the impacts sections. Annex 2 on stakeholders consultation is further strengthened with detailed analysis of feedback received from the REFIT Platform.

Other specific changes were also made in the report in order to take account of more technical recommendations made by the Board.

4. The Group on the Future of VAT (GFV) and the VAT expert Group (VEG)

Following the publication of the 2011 Communication on the Future of VAT, the Commission started in-depth technical discussions with Member States in the GFV[191] and stakeholders in the VEG[192]. A total of 12 meetings of the GFV and 14 meetings of the VEG took place to discuss different issues related to the possible ways to implement the destination principle in intra-EU trade of goods, in particular in the process of identifying the possible options and the criteria for their qualitative assessment, examining how they work, their pros and cons. Both groups had several occasions to comment on the findings of the various studies discussed and presented to the groups which served to feed the debate on possible options (see Section 6.2 of Annex 6).

A Fiscalis seminar was organised in June 2015 in Vienna which brought together both the GFV and VEG to discuss the results of the EY's study on implementing the destination principle to intra-EU B2B supplies of goods. In addition, both the GFV and the VEG had already an opportunity, earlier in the process, to express their views on the draft terms of reference for the study on the selected options.

Moreover, both GFV and the VEG discussed in-depth during several meetings the shortcomings of the current VAT system and identified the priority areas in which improvements to the current rules could be undertaken. In this respect, following the request of many delegates in GFV and VEG, the Commission services created two sub-groups, composed of members from the VEG and the GFV, to examine the VAT treatment of consignment stocks and chain transactions[193]. As regards the burden of proof to exempt intra-EU supplies, a third mixed sub-group[194] was established in the framework of the EU VAT Forum[195]. Each sub-group had to examine the precise problems faced by business and tax administrations, look at practical examples and

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[191] See Glossary.

[192] See Glossary.

[193] The **sub-group on chain transactions** was made up of 4 individuals, 6 organisations and 7 Member States (AT, BG, DE, HU, LU, NL and UK). The **sub-group on consignment stock** was made up of 3 individuals, 6 organisations and 3 Member States (BE, FI and IT). Each sub-group held **five meetings** in Commission premises with their first meeting taking place respectively on 18 and 19 June 2013. In both groups a rapporteur from the Member States and another from the stakeholders were nominated by consensus. The membership list of the sub-groups is available as annex to GFV N° 42 and VEG N° 26 B2B supplies of goods – Taxation at destination - Sub-Groups – Overview of the outcome.

[194] The **sub-group on the proof of exemption of intra-EU supplies** was made up of 9 organisations and 15 Member States (AT, BE, BG, DE, DK, ES, EE, IE, HU, IT, LT, PL, PT, NL and SK) members of the EU VAT Forum. The sub-group held **three meetings** with the first meeting taking place on 31 July 2013. The report was presented by two rapporteurs (one from the tax administrations and one from the business members) in a plenary meeting of the EU VAT forum on 3 December 2013. The report was then finalised and sent to the GFV chair. The membership list of the sub-group is available as annex to GFV N° 42 and VEG N° 26 B2B supplies of goods – Taxation at destination - Sub-Groups – Overview of the outcome.

[195] See Glossary.

identify possible ways to address these problems. All three sub-groups reported back with their recommendations to both the VEG and GFV[196].

During two rounds of discussions in 2016 both the GFV and the VEG were given opportunity to examine and express their views on the main features of the definitive VAT system as well as to identify and analyse the issues which would arise and to develop the ways to tackle them with a view of preparing the legislative proposal to be tabled in 2017. Among others the concept of Certified Taxable Person (CTP) was examined[197].

Finally, in January 2017, the GFV and the VEG met to discuss a series of questions prepared by the Commission services[198] which dealt with the issues of the VAT identification number, chain transactions, call-off stock and proof of intra-EU supplies, in respect of which in its conclusions of 8 November 2016 the ECOFIN Council[199] invited the Commission to present a legislative proposal on improvements to the current EU VAT rules for cross-border transactions. Both groups were once more also asked to provide feedback on the suggested list of conditions for granting the status of Certified Taxable Person (CTP).

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[196] All these documents are publically available in CIRCABC, see
GFV N° 041 and VEG N° 027 Sub-Groups report - Proof of intra-EU supplies
GFV N° 039 and VEG N° 028 Sub-Groups report - Consignment stocks
GFV N° 040and VEG N° 029 Sub-Groups report - Chain transactions

[197] See GFV N° 054 and VEG N° 057 Definitive VAT regime for intra-EU trade – First step – Issues to be examined.

[198] See GFV N° 56 and Veg N° 60 Elements for the 2017 proposal – Definitive VAT regime for intra-EU trade.

[199] http://data.consilium.europa.eu/doc/document/ST-14257-2016-INIT/en/pdf

ANNEX 2: STAKEHOLDER CONSULTATION

1. Introduction

The consultation with stakeholders on the best possible solutions for the definitive VAT system included several different elements and started as early as 2010. It was organised around several main axes:

1) **Open public consultation** on the **Green Paper** on the future of VAT (2010) which took place between 1 December 2010 and 21 May 2011 and resulted in around 1 700 contributions providing a detailed view of problems linked with the application of VAT in Member States;

2) An in-depth, targeted and **on-going consultation process with key stakeholders (from 2012 until 2017)** via the **GFV** (representing Member States – 12 meetings) and the **VEG** (representing business, academics and accounting professions – 14 meetings);

3) Consultations with stakeholders (businesses, tax professionals and Member States) through **online surveys** and **direct interviews** undertaken by an independent consultant (EY) as part of the study on 'Implementing the 'destination principle' to intra-EU B2B supplies of goods' (2015);

4) Contributions received via the **REFIT platform** and as a spontaneous feedback from business;

5) **Open public consultation** which took place between 21 December 2016 and 20 March 2017.

The consultation strategy had two main purposes. The first was to identify the problems of the current transitional VAT system and the possible ways of solving them. The second was to get the views of the stakeholders on how to shape the definitive VAT system.

This approach, developed in line with the Better Regulation Guidelines, allowed the public to give valuable input at all stages of the preparatory work of the initiative over an extended period of time (from 2010 until 2017). Stakeholders were given the opportunity to provide feedback on all key elements, including the problems experienced, the design of regulatory alternatives and possible impacts. Thanks to the various instruments used, all stakeholder groups (Member States, general public, businesses and tax experts) were consulted in the process and the outcome of the whole consultation process was of high quality. Further it provided a valuable input for the proposal.

Tables 10 and 11 – Overview of the consultation strategy

Table 10: Stakeholders consulted

Stakeholders consulted	**Assessment of the current VAT system**	**Assessment of the possible elements of the future policy options**	**Assessment of the possible quick improvements to the current VAT system**
Businesses	✓	✓	✓

Business Associations	✓	✓	✓
Practitioners (tax advisors)	✓	✓	✓
Academics	✓	✓	✓
Members of the public	✓	✓	✓
Member States (administration)	✓	✓	✓

Table 11: Consultation activities

Consultation activities	**Assessment of the current VAT system**	**Assessment of the possible elements of the future policy options**	**Assessment of the possible quick improvements to the current VAT system**
Open public consultation on the Green Paper (2010-2011)	✓	✓	
The conference in Milan on the Green Paper in (2011)	✓	✓	
The GFV (2012-2017)	✓	✓	✓
The VEG (2012-2017)	✓	✓	✓
The EY study on 'Implementing the 'destination principle' to intra-EU B2B supplies of goods' (2015)	✓	✓	✓
The Fiscalis seminar in Vienna (for GFV and VEG) - the results of the EY's study discussed (2015) and the way forward	✓	✓	✓
The REFIT platform and spontaneous contributions	✓	✓	✓
The open public consultation (2016-2017)	✓	✓	✓

2. Open public consultation: the Green Paper on the future of VAT

The open public consultation on the 'Green Paper on the future of VAT' – Towards a simpler, more robust and efficient VAT system"[200] resulted in around 1 700 contributions. On 6 May 2011, the European Commission organised a one day conference in Milan on the Green Paper which brought together policy makers, experts, businesses and other stakeholders and the general public from all over Europe, and beyond.

The results of the public consultation were endorsed by the Commission in the Communication on the future of VAT[201] adopted on 6 December 2011. The main problems identified in the document could be summarized under two key headings:

1) The VAT fraud, and
2) The complexity of the VAT system.

1) VAT fraud

VAT fraud has negative effects on: (i) the tax collected by each Member State, (ii) the EU own resources and (iii) the protection of the rights of taxpayers (the honest traders).

The stakeholders consulted noted that carousel fraud and other fraudulent schemes must be tackled by specific remedies addressed only to fraudulent taxpayers, rather than measures that could involve indirectly compliant taxpayers creating a disadvantage for them. The vast majority of the respondents commented that antifraud measures should be harmonised to be effective.

Improving the administrative cooperation between tax authorities and a faster exchange of information were mentioned as the first step towards a fraud proof system. This should be combined with the improved efficiency of VIES in order to protect bona fide traders. A few respondents suggested, as possible measures to combat fraud, the generalised (domestic) reverse charge on individual transactions exceeding specific value thresholds, the targeted reverse charge or the exemption of B2B transactions.

Destination principle and One Stop Shop

A considerable group of respondents stressed that the destination principle should be applied together with One-Stop-Shop arrangements (OSS) as an alternative to the reverse charge mechanism. Some stressed that an OSS mechanism like the one introduced for the e-commerce sector in 2015 would be a significant improvement. The establishment of a comprehensive OSS system (especially one including the possibility of cross-border deductions) would allow the fulfilment of all VAT obligations in the Member State of establishment. However, several respondents were worried that the Member States would not be ready to cope with a major change in the system for the collection of VAT given the limited amount of public finance available for further technological advancement.

[200] COM(2010) 695 final
[201] COM(2011) 851 final

Certified Taxable Person

Some respondents thought the model of certification of taxable persons is promising as a tax collection method. It would be the easiest system in the short term and would require the lowest initial investment as there are no real changes to the collection system. However amongst all the proposals recorded, this would seem to be the least efficient in preventing carousel fraud. To be truly attractive to businesses, it should provide the certified business with incentives e.g. the possibility of benefitting of reduced obligations, fewer audit queries, reduction of penalties, faster refunds of tax credits and greater legal security and reliability. Some respondents insisted that the conditions of the certification process should be the same and recognised in all Member States.

2) Complexity of the system

The complexity of the system leads to high administrative costs both for taxable persons (which have to understand and to comply with the individual requirements of up to 28 different VAT systems) and for tax administrations. It further leads to a lack of legal certainty.

With regards to this issue the main areas of concern are: (a) the evidence needed for the exemption of intra-EU supplies; (b) the rules on chain transactions; (c) the rules on consignment stocks; (d) certain rules on tax compliance that create administrative burdens.

a) The evidence needed for the exemption of intra-EU supplies

There are no clear and uniform rules about the evidence to be provided by the supplier to prove that the conditions for the exemption for intra-EU supplies of goods are met. Many issues are related to the proof of cross-border transport. The main problems derive from the mismatches between national forms or documentation in different languages and the different procedures in force in each Member State.

For that reason the majority of respondents requested EU-wide harmonised forms of proof. Some respondents mentioned the need to introduce also supporting or alternative means of proof in cases where the main proof is unavailable.

b) The rules on chain transactions

The VAT Directive provides a simplification for triangular transactions but this is not applied in a uniform way by Member States and it is the only simplification provided by the current rules. There are no common guidelines on the treatment of chain transactions.

c) The rules on consignment stocks

Rules for consignment stocks are not applied uniformly. Some Member States allow for certain simplifications (not provided for in the current rules) while others do not.

d) The rules for tax compliance that create administrative burdens

Rules for VAT registration should be standardised with the aim to clarify and make uniform the requirements in each Member State in respect of non-established businesses. Further a standardisation of the recapitulative statements and Intrastat reporting obligations is needed. Some respondents requested the abolition of the recapitulative statements.

3. Targeted consultation with key stakeholders (GFV and VEG)

The Commission has organised an in-depth, targeted, technical and on-going consultation with key stakeholders: businesses, academics, accounting professions and Member States. It started in 2012 and lasted until the beginning of 2017.

It took the form of regular meetings of the two groups. One composed of representatives of national tax administrations (GFV) and the other composed of businesses, academics and tax practitioners (VEG).

Both groups discussed on several occasions the shortcomings of the current transitional VAT system and the possible ways to implement the destination principle in intra-EU trade of goods. In parallel, they also discussed in-depth the priority areas in which improvements to the current VAT rules could be undertaken.

In June 2015, a Fiscalis seminar was organised in Vienna which brought together both the GFV and VEG in order to discuss the outcome of the EY study on "Implementing the 'destination principle' to intra-EU B2B supplies of goods". The discussion showed that views diverge as regards the five possible options to implement the destination principle. For almost all Member States following the physical flow of goods remained fundamental. Therefore, options which do not follow the goods appeared not acceptable (options 4 and 5). Among those Member States' representatives that share this view, there was a preference for option 2, given its potential to combat MTIC VAT fraud. Very few delegations advocated for option 3. Mitigation measures, such as the certified taxable person (CTP), were considered very important to alleviate the negative cash flow impact on businesses for options under which the supplier charges the VAT of the Member State of destination. It was concluded that a phased entry into force of the definitive regime is needed.

At the same time, members of both groups underlined the need of introducing short term improvements of the current VAT system ("quick fixes"), namely: chain transactions, call-off stock and proof of transport of intra-EU supplies. Additionally Member States requested that the role of the VAT identification number for the exemption for intra-EU supplies be also addressed in the scope of the "quick fixes".

4. EY study on 'Implementing the 'destination principle' to intra-EU B2B supplies of goods' (2015) – Consultations of stakeholders (businesses and Member States) online surveys and direct interviews – relevant elements

The EY study focused on the assessment of the current VAT environment and the possible impacts of the analysed options to change the existing VAT system. As part of the analysis businesses, Member States and tax experts were consulted.

In respect of the stakeholder consultation the following instruments were used: (1) a business survey addressed to stakeholders in 28 Member States on compliance costs and monetary and non-monetary impacts of the presented VAT policy options; (2) a tax experts' survey addressed to tax experts in 28 Member States on compliance costs and technical information on the proposed policy options; (3) a Member States' survey

addressed to tax authorities in the 28 Member States on administration costs and the VAT Gap problem in the context of the policy options[202].

The feedback received through the consultation, performed within the scope of the EY study, concerned: (i) compliance costs[203] (identified as a fundamental issue for business); (ii) impact on VAT fraud (identified as a fundamental issue for Member States); (iii) legal certainty; (iv) administrative costs[204]; (v) cash flow implications.

The current VAT situation

The businesses' perspective

Business representatives were asked about: (1) the structure and the scope of their current trade activities; (2) the way in which they deal with fulfilling VAT obligations, separately in the domestic and intra-EU supplies contexts; (3) the estimation of the detailed costs (increase, decrease, no change) under the proposed changes.

Based on the data collected from the business survey it was estimated that on average for the current VAT system, the VAT cost of compliance per Euro of turnover is 11% higher for intra-EU trade as compared with the corresponding VAT compliance per Euro of turnover for domestic trade.

The Member States' perspective

In order to assess the current state of administrative labour and non-labour costs, Member States were asked to provide an average cost per hour for employees responsible for dealing with VAT. Based on the survey results, the monetary value of the labour costs associated with VAT administration was estimated at approximately EUR 1 730 million in the EU. In addition, Member States' non-labour costs associated with the administration of VAT were also considered. These included external consultancy, IT systems and staff training costs.

Assessment of the possible VAT options

Different taxation policy options were analysed with a view to reducing compliance costs (making EU cross-border trade as simple and safe as domestic trade); reducing the VAT fraud and assessing the possible shift in burdens with which tax administrations could be confronted. Detailed description of the impacts of the options and on how they compare is included in Sections 6 and 7 of the Impact Assessment.

5. Contributions received via the REFIT platform

Stakeholders disclosed their position also through the Refit Platform where it is possible to participate actively in the law making process by providing an overview with the aim to evaluate and improve existing laws. Some stakeholders submitted their contributions along 2014, 2015 and 2016 regarding specific issues they are facing and the way to

[202] 25 Member States replied to the survey.
[203] See Glossary for definition.
[204] See Glossary for definition.

overtake them. All the submissions on taxation provided up to date can be found under the following link[205].

VAT registration – CTP[1]status

One of the contributors (DIHK) provided some proposals to improve the VAT system, in particular on the simplification of chain transactions by the extension of the rules on triangulation, avoiding the registration of the intermediate businesses in the transactions. Further input was related to the extension of the MOSS to avoid multiple registrations which are expensive for businesses, and for improving the cross border refund process.

In 2015 Business Europe complained about the negative effects of unjustified geo-blocking due to excessive administrative burdens related to VAT on companies involved in cross border trade. The same association with its position paper on the VAT Action Plan stated that the current system – exempting cross-border supply and taxing cross-border acquisition - should be changed and simplified. Amongst the detailed measures for a correct VAT collection, providing a single online service was mentioned which could be used by businesses to easily determine if their customer is a Certified Taxable Person, and ensuring that the criteria used to define a Certified Taxable Person do not increase current administrative burdens on business. Further, there must be equal treatment of both domestic and cross-border suppliers and of goods and services as this supports the supply chain. They supported the destination principle and its implementation via improvement of the MOSS.

Fraud – Reverse charge mechanism

The Ministry of business and growth in Denmark with the Danish business forum mentioned that the problem of VAT fraud should be addressed with long term solutions limiting the use of the reverse liability (the reverse charge mechanism) which requires changing sales and accounting systems thus increasing administrative burdens for businesses. Another contributor clearly expressed the need for EU support with respect to honest businesses, avoiding the increase of administrative burdens. They are affected in particular by the increased burden of proof related to cross-border supplies which hinders the development of the single market. Effective tools against VAT fraud should be used in combination with simplification measures, like the possibility for small business to use a VAT reporting threshold on B2C sales across EU.

In 2016 Confcommercio in its contribution stated that VAT fraud generates unfair competition. At the same time VAT obligations should be reduced, amending the current rules without introducing new systems like the Generalised Reverse Charge that will entail very heavy reporting obligations. The OSS should be used in order to reduce the burdens for companies. It has to be noted that such a system would be affordable for middle and big companies but the charges would be still high for small businesses.

Stakeholders presented in the Refit Platform[1] their position regarding the application of the reverse charge mechanism applicable to all the domestic transactions. The message from the economic operators reported by one business forum is that it would be worth to "replace that measure with a simpler and more basic VAT regime in the EU".

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[205] https://ec.europa.eu/info/sites/info/files/taxation_and_customs_union.pdf

In fact, according to operators the reverse liability has as a disadvantage since it obliges businesses to "operate different sales and accounting systems for different business transactions", notably increasing the administrative burdens. In their opinion the same results could be achieved by enhancing the administrative cooperation between Member States and businesses.

In the same context another group stressed that the reverse charge is very important when it comes to combating VAT fraud at cross border level. Also the application of that measure in certain sectors has given satisfactory results.

Reference should also be made to the opinions adopted by business federations as well as to input received from academics in scientific publications. All these contributions are mentioned in detail in the impact assessment related to the General Reverse Charge Mechanism proposal[1].

6. Contributions received as spontaneous feedback from businesses

The Commission also received spontaneous contributions from experts, academics, members of the VEG and delegates of Member States.

Regarding the current system, it was pointed out that the exemption for intra-EU supplies should be conditional only upon the possession of a valid VAT number by the acquirer. At the same time the identification procedure and the control of registered taxpayers should be harmonised at EU level to be reliable. Recapitulative statements should be considered only as an additional piece of evidence.

Regarding the CTP status, it could be used to improve the current rules during the passage to the definitive regime but the criteria to provide the status should be common for all Member States, like the AEO certification for customs. However the CTP should not be a condition for the application of the rules on burden of proof in order to ensure legal certainty for all the businesses, not only for the certified. Further the CTP status could be a useful tool for the simplification of complex transactions like chain transactions.

Academics expressed their position that the VAT identification number is totally inadequate to ensure effectiveness of the VAT regime for intra-EU trade. Regarding the CTP they believe that this status can be defined as effective only if the requirements and the procedures are harmonized.

The simplification of the VAT system and the introduction of some quick measures (for chain transactions, call-off stock and use of the VAT number) were deemed necessary. It is believed that new measures should not be more burdensome than existing ones.

With regard to the extension of the OSS it is necessary to balance the need of simplicity for stakeholders and the duty of the tax authorities to ensure revenues. It is questionable whether a system designed as a “pay only” scheme is capable of adaptation to incorporate refunds of VAT or deductions.

7. Open public consultation

The open public consultation for the initiative was held for 13 weeks between 21 December 2016 and 20 March 2017 using the EU survey tool. The Commission received 121 submissions therefore the results of this open public consultation should be

read taking into account this rather limited number of responses. Nevertheless business community was much better represented than Member States (only two replies). This is especially true having in mind that 37 business associations provided their input to this consultation. All public submissions are available on the DG TAXUD website under following link [https://ec.europa.eu/taxation_customs/consultations-get-involved/tax-consultations_en].

The profile of the participants is presented below:

	Answers	**Ratio**
a Business	48	39.67%
a Business Association	37	30.58%
a Tax advisor	13	10.74%
a Public authority	2	1.65%
an Academic	4	3.31%
a Member of the public	5	4.13%
Other	12	9.92%

In terms of the Member States where the contributors indicated where they were based most replies came from Germany (almost 30%), Belgium (almost 15%), United Kingdom (10%), Sweden (6.6%), Netherlands (5.8), Italy (almost 5). No reply was received from 10 countries[206].

The purpose of the consultation was to seek feedback on the following issues:

(i) the problems linked to the current transitional VAT system;
(ii) the main elements constituting different options:

- option 1 – 'quick fix measures to the current system;
- options 2-5 based on the combination of 2 factors: the place of supply (the destination principle following the flow of goods or the contractual arrangements) and the person liable to account for VAT (the supplier or the customer), accompanied by the concepts such as OSS + CTP.

The current transitional VAT system

Complexity/costs

The current transitional VAT system is burdensome because of its complexity and costs incurred. Almost 90% of the contributors[207] confirmed that there are additional costs linked with intra-EU supplies of goods in comparison with domestic ones. 79%[208] indicated that small businesses are deterred from cross-border supplies for those reasons.

Fraud – Reverse charge

Over 74%[209] agreed that the current system is not sufficiently resistant to VAT fraud. More than 67%[210] believed that the reverse charge mechanism is an effective measure to

[206] Bulgaria, Croatia, Cyprus, Estonia, Finland, Greece, Lithuania, Malta, Romania and Slovenia.
[207] The whole business – 95%, SMEs – 85.5%, large businesses – 100%, business associations – 89%, tax advisors and academics – 100%, members of the public – 100%, Member States – 100%
[208] The whole business – 71%, SMEs – 71%, large businesses –71%, business associations – 78%, tax advisors and academics – 94%, members of the public – 80%, Member States – 100%
[209] The whole business – 67%, SMEs – 79%, large businesses – 64%, business associations – 68%, tax advisors and academics – 94%, members of the public – 100%, Member States – 100%

combat fraud. But at the same time 54%[211] admitted that the current application of the reverse charge increased the compliance costs. 30%[212] of respondents were of the view that these costs decreased.

Quick fix measures – Option 1

Over 90%[213] confirmed that a VAT identification number is a reliable proof of the status of the customer regarding intra-EU supplies. But only 55%[214] believed that the lack of a VAT number of the customer should deprive the supplier from the possibility to exempt intra-EU supplies.

There was strong support for the need to improve the rules on chain transactions (83%[215]), proof required to demonstrate that the goods were moved from one Member State to another (almost 80%[216]) and simplification of call-off stock situations (75%[217]).

Elements of the possible future options – Options 2 to 5

More than 68%[218] of the respondents stated that there should be only one taxed intra-EU transaction as it is currently the case for the domestic supplies. However, 19%[219] of the respondents disagreed.

<u>Compliance and administrative costs</u>

For 47%[220] of the stakeholders the change to only one taxed transaction will reduce compliance costs. 25%[221] of the respondents believed that administrative costs for Member States will be reduced but 51%[222] did not have opinion on that.

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[210] The whole business – 60%, SMEs – 64%, large businesses – 68%, business associations – 70%, tax advisors and academics – 88%, members of the public – 60%, Member States – 100%

[211] The whole business – 60%, SMEs – 50%, large businesses – 61%, business associations – 51%, tax advisors and academics – 53%, members of the public – 20%, Member States – 50%

[212] The whole business – 21%, SMEs – 14%, large businesses – 29%, business associations – 38%, tax advisors and academics – 24%, members of the public – 60%, Member States – 50%

[213] The whole business – 92%, SMEs – 87%, large businesses – 93%, business associations – 95%, tax advisors and academics – 94%, members of the public – 80%, Member States – 100%

[214] The whole business – 63%, SMEs – 86%, large businesses – 54%, business associations – 32%, tax advisors and academics – 76%, members of the public – 80%, Member States - 50%

[215] The whole business – 90%, SMEs – 79%, large businesses – 93%, business associations – 68%, tax advisors and academics – 88%, members of the public – 80%, Member States - 100%

[216] The whole business – 90%, SMEs – 79%, large businesses – 93%, business associations – 68%, tax advisors and academics – 82%, members of the public – 80%, Member States – 50%

[217] The whole business – 88%, SMEs – 71%, large businesses – 93%, business associations – 54%, tax advisors and academics – 82%, members of the public – 40%, Member States – 100%

[218] The whole business – 69%, SMEs – 64%, large businesses – 68%, business associations – 62%, tax advisors and academics – 94%, members of the public – 80%, Member States – 50%

[219] The whole business – 23%, SMEs – 21%, large businesses – 25%, business associations – 24%, tax advisors and academics – 6%, members of the public – 20%, Member States – 0%

[220] The whole business – 44%, SMEs – 64%, large businesses – 32%, business associations – 30%, tax advisors and academics – 94%, members of the public – 40%, Member States – 50%

[221] The whole business – 19%, SMEs – 21%, large businesses – 21%, business associations – 14%, tax advisors and academics – 59%, members of the public – 40%, Member States – 0%

[222] The whole business – 48%, SMEs – 50%, large businesses – 54%, business associations – 73%, tax advisors and academics – 29%, members of the public – 20%, Member States – 100%

Place of taxation (the flow of goods or the contractual arrangements)

As for the place where goods should be taxed, 53%[223] believed that it should be the place where the goods arrive and 48%[224] that it should be the place where the customer is located.

Liability rules (the supplier or the customer)

In relation to the question of the liability for VAT due on B2B intra-EU supplies of goods 56%[225] indicated the customer and 25%[226] the supplier.

OSS

80%[227] supported the extension of the OSS to taxable intra-EU B2B supplies of goods seeing it as a simplification measure eliminating the need for multiple registrations. 88%[228] of the respondents agreed that the OSS system should also allow for the deduction of input VAT.

CTP status

There was no clear cut majority in relation to the introduction of the Certified Taxable Person (CTP). Almost 44%[229] of the respondents indicated that they would be interested to apply for CTP if the criteria were not too burdensome. 8%[230] were ready to apply regardless of the difficulty. 14%[231] informed that they are not interested in using this measure and more than 33% did not provide any answer on this issue. However there was clear support for the idea that the criteria for obtaining the CTP status should be harmonised at EU level (79% of the support[232]).

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[223] The whole business – 46%, SMEs – 64%, large businesses – 36%, business associations – 54%, tax advisors and academics – 76%, members of the public – 60%, Member States – 50%

[224] The whole business – 62%, SMEs – 57%, large businesses – 68%, business associations – 32%, tax advisors and academics – 35%, members of the public – 40%, Member States – 50%

[225] The whole business – 69%, SMEs – 50%, large businesses – 79%, business associations – 54%, tax advisors and academics – 41%, members of the public – 60%, Member States – 50%

[226] The whole business – 25%, SMEs – 43%, large businesses – 14%, business associations – 11%, tax advisors and academics – 53%, members of the public – 40%, Member States – 50%

[227] The whole business – 81%, SMEs – 64%, large businesses – 89%, business associations – 70%, tax advisors and academics – 88%, members of the public – 60%, Member States – 100%

[228] The whole business – 94%, SMEs – 79%, large businesses – 100%, business associations – 84%, tax advisors and academics – 82%, members of the public – 80%, Member States – 50%

[229] The whole business –79%, SMEs – 71%, large businesses – 86%, business associations – No answer 68%, tax advisors and academics – 35%, members of the public – 20%, Member States – 0%

[230] The whole business – 13%, SMEs – 7%, large businesses – 11%, business associations – No answer 68%, tax advisors and academics – 12%, members of the public – 0%, Member States – 0%

[231] The whole business – 8%, SMEs – 21%, large businesses – 4%, business associations – No answer 68%, tax advisors and academics – 24%, members of the public – 40%, Member States – 50%

[232] The whole business – 94%, SMEs – 93%, large businesses – 93%, business associations – 68%, tax advisors and academics – 76%, members of the public – 100%, Member States – 100%

Fraud – taxation options/reverse charge

In relation to improved fraud fighting thanks to taxation of B2B intra-EU supplies, 50%[233] of respondents believed it would be helpful and 24%[234] were of the opposite opinion.

On the optional application by Member States of a generalised reverse charge mechanism on domestic transactions 40%[235] agreed that such a measure would help fighting fraud, while 42%[236] were of the opposite opinion. More than 58%[237] of the contributors indicated that such a solution would increase compliance costs.

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233 The whole business –38%, SMEs – 43%, large businesses – 39%, business associations – 43%, tax advisors and academics – 94%, members of the public – 80%, Member States – 50%

234 The whole business – 33%, SMEs – 21%, large businesses – 36%, business associations – 24%, tax advisors and academics – 6%, members of the public – 0%, Member States – 50%

235 The whole business – 50%, SMEs –64 %, large businesses – 43%, business associations – 24%, tax advisors and academics – 41%, members of the public – 40%, Member States – 0%

236 The whole business – 38%, SMEs – 21%, large businesses – 46%, business associations – 41%, tax advisors and academics – 59%, members of the public – 40%, Member States – 100%

237 The whole business – 67%, SMEs –43 %, large businesses – 75%, business associations – 54%, tax advisors and academics – 53%, members of the public – 60%, Member States – 100%

ANNEX 3: WHO IS AFFECTED BY THE INITIATIVE AND HOW

The initiative will directly impact businesses and Member States. Businesses in the way they comply with their VAT obligations and Member States in the implementation of the new rules and the audit of their application by businesses. Citizens should not be affected by the changes. They will continue to purchase goods and services with payment of VAT in exactly the same way as is currently the case. They might be indirectly impacted through lower consumer prices although these are not expected to be substantially altered by the initiative.

1. Businesses

The scope of the initiative is limited to intra-EU transactions in goods that take place between businesses[238]. Therefore it will only affect businesses that sell or buy goods cross-border within the EU. Businesses carrying out only domestic transactions (i.e. only in the Member State in which they have established their business) will not be affected.

No distinction is made between types of businesses trading cross-border since the changes proposed are of a general nature. They consist in a change in the VAT collection principle which will be applicable to all businesses (see however below exception for CTP businesses and special scheme for SMEs).

The quantitative impacts on businesses have been measured in terms of changes in compliances costs and cash flow in the year of implementation of the initiative and in the years after (for more details on such quantification see Section 6 of this impact assessment).

1.1. CTP

Businesses that are granted the CTP status will continue to purchase goods cross-border in the same manner, i.e. they will buy without the payment of the VAT due and will instead self-account for the VAT in their VAT return via the reverse charge.

When they supply goods cross-border, they will benefit from VAT obligation simplifications in respect of certain transactions (call-off stocks, proof of transport). Further when acting either as a buyer or as a purchaser simplifications regarding chain transactions will also be applied to them.

The certification would be open to all businesses[239]. The implementation of the criteria for its granting would need to be proportionate to encompass small businesses but also start-ups.

The process of certification will require some administrative procedures but remains optional for businesses.

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[238] In VAT terms, the wording "business" refers to a taxable person or a non-taxable legal person acting as such and identified for VAT purposes. It therefore does not include businesses that only carry out exempt transactions or SMEs that benefit from the special exemption scheme.

[239] To note that since the CTP certification entails VAT reporting and payment obligations, non-taxable persons will not be eligible. For the same reason, the proposal excludes flat-rate farmers, exempt SMEs and exempt taxable persons from the possibility of obtaining the CTP status.

1.2. OSS

Instead of having to register in multiple Member States and resort to different tax administrations, businesses trading cross-border will use a single point of registration (the one that currently have in their Member State of establishment) to comply with their cross-border VAT obligations.

Technical changes in the accountancy systems (e.g. invoices, listings, VAT returns) are expected.

1.3. VAT identification number

The proposed change in the VAT Directive makes the mentioning in the invoice of the valid VAT identification number of the customer compulsory for the supplier to be allowed to exempt his intra-EU supplies. This means that businesses will need to check in the VIES system the validity of the "taxable" status of their customers. For businesses having a great number of transactions combined with a large number of customers this can be cumbersome.

Although the change might appear as important, it is however not a new issue. Indeed, under the current rules, the mentioning in the invoice of such a valid identification number is already required (penalties can be imposed on the supplier if such an obligation is not fulfilled). The difference with the proposed change is that the exemption for the intra-EU supply that today cannot be questioned on grounds that the VAT number of the customer is lacking (according to the CJEU) will in future be refused where this is the case. Compliant businesses trading with other compliant businesses should not be affected at all by the changes. Compliant suppliers may however not be aware that they are trading with customers that do not possess a valid identification number (to note that the reason might be due to the fact that the VAT identification process of the customer is not yet completed or that information/updates put by tax administrations in the VIES system are delayed). Therefore, the functioning of the VIES system needs to be improved (this will be the purpose of another legislative proposal on administrative cooperation - see Introduction in Section 1.1 and Action Plan) so that it can provide easy access to up-to-date information.

1.4. SMEs

Under certain conditions and optionally, SMEs may currently benefit from the special exemption scheme for small enterprises (see Section 2 of Chapter I of Title XII of the VAT Directive which encompasses Articles 282 to 294). When they are covered by such special scheme, SMEs are relieved from practically all the VAT obligations imposed on businesses. In particular they should not charge VAT to their customers on their supplies and are, as a consequence, also not able to deduct their input VAT. In this respect, they are not much different from private individuals who sell personal goods.

SMEs that currently benefit from the VAT exemption scheme for small enterprises will continue to be exempt. However, according to the current rules (Article 283(1)(b) of the VAT Directive), the exemption scheme only applies to supplies made in the Member State where the SME is established. Given that under the current rules, intra-EU supplies are technically located at the Member State of origin the exemption for SMEs also applies to their intra-EU supplies of goods, so that SMEs are currently not charging any VAT on such supplies. Once the move to the destination principle takes place, the fact that intra-EU supplies will be located at the Member State of destination would mean that

SMEs would have to charge the VAT due in that Member State of destination to their customers. In theory the situation would be as follows:

- Concerning their domestic supplies, they will continue supplying their goods without having to charge the VAT.
- Concerning their intra-EU purchases of goods, their suppliers will charge and be liable for the payment of VAT (through the OSS) in the Member State of arrival of the goods.
- Concerning their intra-EU supplies of goods the new rules would theoretically imply the need for SMEs to charge to their customers the VAT in the Member State of destination. However, the Commission will in parallel to the current initiative come forward with a proposal in the form of a comprehensive VAT simplification package for small enterprises which, inter alia, will address this issue[240].

2. Member States

All Member States will be impacted by the changes proposed. They will need to implement the new rules and ensure their correct application by the businesses. In particular, they will need to introduce and control the new concept of CTP and make changes in their IT systems (provide for an OSS, adapt the current VIES system).

The quantitative impacts on Member States have been measured in terms of changes in administrative costs, cash flow and tax revenues in the year of implementation of the initiative and in the years after (for more details on such quantification see Section 6 of this impact assessment) .

[240] See Section 1.1 above.

ANNEX 4: ANALYTICAL MODELS USED IN PREPARING THE IMPACT ASSESSMENT

1. Overview of the methodology

A specific study[241] has been commissioned to assess the impacts on Member States and on businesses that would result from the implementation of each of the policy options for reforming the EU VAT rules applicable to cross-border supplies of goods.

In particular the impacts on the MTIC/VAT fraud, the labour and non-labour administrative costs[242] and the cash flow of Member States, as well as on the compliance costs[243] and the cash flow of businesses have been examined.

The macroeconomic impacts and in particular the effects on macroeconomic variables such as gross domestic product (GDP) have also been covered.

The assessment is carried out in comparison with what is currently applicable under the current tax rules (baseline), from both a qualitative and a quantitative perspective.

The methodology described here underpins the approach to estimating the impacts of each policy option and is based on the following steps:

- **Primary and secondary data collection across all EU Member States** (businesses, tax experts[244] and EU Member States' tax authorities) to inform the technical, legislative, compliance cost, administration cost and economic analysis; and
- **Analysis of data collected** to develop useful qualitative (technical, legislative, etc.) and quantitative insights and inform the assumptions and the parameters in the **macro econometric Vector Autoregressive (VAR) model used for the economic analysis**.

The above approach has been selected in view of the nature of the information available and the appropriate analysis techniques. It has been developed specifically for the study and tailored accordingly to ensure that each element of the analysis is suitable for the particular study objectives.

Full details on the methodology are available in the various annexes of the above-mentioned study. These are specifically referred to, where relevant, in the various sections that follow below.

2. Data collection tools for the analysis of the impacts

2.1. Primary data collection

As part of the specific study, a set of primary data[245] have been collected from businesses, tax experts and Member States' tax authorities across the 28 EU Member

[241] EY, 2015
[242] See Glossary for definition. Further explanation about labour and non-labour costs is available under section 2.4 below.
[243] See Glossary for definition.
[244] This is a network of EY indirect tax experts in the EU Member States which provide tax compliance and tax advice services to hundreds of small, medium and large businesses and which participated in the EU indirect tax experts' survey.
[245] A survey is an example of primary data collected by a researcher.

States to carry out the assessment and also inform variables and assumptions in the economic model.

The objective has been to gather information from businesses and tax experts on VAT compliance costs and from Member States on administrative costs and on the size of MTIC fraud (and the share of the MTIC fraud gap) associated with the B2B trade of goods across the EU under the baseline, as well as the expected likely changes under each reform policy option.

Table 12 below presents a summary of the primary data instruments used as well as their purpose.

Table 12: Primary data collection instruments

Data collection instrument	Description
Business Survey	Issued to businesses across all 28 Member States to determine the cost of compliance relating to the baseline scenario, as well as the monetary and non-monetary impact of the various policy options.
Tax experts' survey	Issued to tax experts across all 28 Member States to obtain technical and compliance cost information as it applies to the policy options.
Member State Survey	Issued to Tax Authorities in all 28 Member States to understand potential impact of the policy options on costs of administration and certain activities, as well as understand the make-up of the VAT Gap.
"As Is"/"To Be" Legislative Matrix	Issued to tax experts across all 28 Member States with the aim of illustrating the VAT treatment of a selection of goods transactions under the current rules and under the proposed policy options.

Source: EY, 2015

2.2. Business Survey

A survey of businesses across all 28 Member States has been conducted in order to establish the compliance obligations and costs of businesses regarding the baseline, as well as how these obligations and costs would change under each policy option. The survey has also provided data used for the calculation of the potential cash flow impact on businesses under some of the options[246].

The survey has been published through the online survey tool Survey Monkey. It consisted of a total of 32 questions[247] which were categorised as follows:

- Section 1: Trade related information. This section involved basic questions about the business profile of the respondent and certain specific questions about the VAT profile with regard to the sales and purchases, as well as trading partner information. The information was required and used to calculate the cash flow impact on businesses under some of the options.

[246] Cash flow implications are likely to occur under Option 2 and Option 5 due to the requirement for businesses to levy and collect VAT on intra-EU transactions.

[247] The survey template is available in Annex B of the 2015 EY Study.

- Section 2: VAT information. This section requested information in relation to the costs businesses incur in order to comply with the VAT legislation. The information was required to gain an understanding of how the business managed its VAT compliance obligations and the associated current compliance costs both as regards domestic and intra-EU B2B trade.

- Section 3: Estimation of detailed cost information. This section sought to obtain information in relation to how certain VAT compliance costs for businesses might change under the different policy options.

The Business Survey responses cover both implementation and ongoing annual intra-EU B2B compliance costs. The focus is on four categories of costs in relation to the policy options, namely (i) employee costs; (ii) training and retraining costs; (iii) system (software) related costs; and (iv) consultancy fees.

Against this background, the elements of the cost changes that the five proposed policy options may create through more compliance requirements[248] have been analysed. This analysis sets out a number of statistical measures to further underline the impact of policy options to businesses. These measures include:

- A frequency distribution of cost estimates to identify the compliance cost change ranges that were most or least prevalent amongst business respondents;
- The mean and median cost differences outlined by the survey respondents with respect to how costs will change under each of the alternative policy options.

As part of the process of verifying the data received from the survey, additional information via direct interviews has been collected from businesses which had completed the business survey. Interviews were held with seven different businesses: three based in the UK, one based in Germany, two based in Poland and one based in Sweden.

The purpose of the interviews was to discuss in detail the expected benefits and costs of each policy option. The business representatives were asked to comment on whether they associated each option with an overall cost or benefit and, where possible, to quantify the value of these costs or benefits. They were also asked to provide comments on any further costs/benefits that they foresaw under each option[249].

Due to the low response rate overall to the survey itself (146 responses) and to limited or no responses in some Member States, reliance placed on the results was limited to understanding the current compliance costs for businesses[250].

Cash flow

Cash flow implications are expected under Option 2 and Option 5 for which the supplier will charge the VAT to his customer. The extent of these cash flow implications, whether

[248] Such requirements include: additional documentation to prove transport of goods, business cost increases related to the establishment of the One-Stop Shop, the additional requirement of obtaining the name of the Member State on arrival of the goods within ten working days, and the associated additional cost related to the charge of VAT in the Member State of contracting party establishment.

[249] Details are available in Annex D of the 2015 EY Study.

[250] The detailed results, analysis and findings of the Business Survey are available in Annex D of the 2015 EY Study.

positive or negative, depends on a number of factors, such as (i) the average remittance time for payments to businesses from their local Tax Authority; (ii) applicable VAT rates; (iii) the value of VAT payable to other Member States by the business; and (iv) interest rates applicable to businesses on saving/borrowing. In calculating the cash flow cost or benefit, a number of assumptions were made as regards the above factors[251]. To quantify the cash flow implications for businesses, the study has examined three different examples, based on different trade profiles of three businesses, assuming a set value of EUR 100 000 of VAT per return. To estimate what impact the concept of CTP would have on the overall cash flow, a proxy was used, namely the proportion of businesses that have applied for 'Authorised Economic Operator' (AEO)[252] status compared with the number of businesses that have an 'Economic Operator Registration and Identification' (EORI)[253] number used in the area of customs. It is anticipated that if a business registers for CTP status, the business would benefit from simplifications in relation to the purchase and sales of goods within the EU. Applying the AEO proxy, approximately 0.3% of businesses within the EU would potentially register for CTP status[254]. Therefore, whilst this would reduce any cash flow benefit or cost, it is likely to be limited.

The analysis identified that where a business is in a net payment position on its One-Stop Shop (OSS) return, and it has received payment from its customer, then it will benefit from a positive cash flow due to receiving VAT from its EU customers and holding this VAT until the One-Stop Shop filing deadline. On the other hand, where a business is in a net repayment on its OSS return, the business will experience a negative cash flow position under this option; this is due to paying VAT to its EU supplier and not being able to benefit from an immediate right of deduction.

2.3. Tax experts' survey

Further to the business survey, to quantify how compliance costs for businesses will be impacted as a result of the implementation of the proposed policy options, a tax experts' survey has been carried out across all 28 EU Member States[255]. These tax experts provide tax compliance and tax advice services to hundreds of small, medium and large businesses.

To ensure representation of all business sizes, the assessment covered three distinct business types[256]: Type 1 SME, Type 2 SME and Large Businesses. The criteria for defining the three business types are outlined in Table 13 below.

Table 13: Criteria for defining business types

Criteria	Type 1 SME	Type 2 SME	Large Businesses
1. Annual Turnover	Less than EUR 50 million	Less than EUR 50 million	

[251] For full details, see section 6.3 Cash flow analysis of the EY Study.
[252] http://ec.europa.eu/taxation_customs/general-information-customs/customs-security/authorised-economic-operator-aeo_en
[253] http://ec.europa.eu/taxation_customs/business/customs-procedures/general-overview/economic-operators-registration-identification-number-eori_en
[254] This figure is based on the proportion of businesses that have been issued certificates to verify their AEO status (15 034 as of 15 January 2015) to the number of businesses currently registered in the EORI scheme (4 486 452). Source: European Commission.
[255] Full details of the survey template are available in Annex B of 2015 EY Study.
[256] Defining typical businesses for analysis and survey purposes is a reliable approach that had been used in several reports in the past such as the "Paying Taxes" report published for several years by PwC and the World Bank Group.

			More than EUR 50 million
2. Employees	Less than 250 employees	Less than 250 employees	More than 250 employees
3. Establishment	Only 1 EU Member State	Only 1 EU Member State	Numerous EU Member States
4. VAT Registration	Single VAT registration in Member State of establishment	VAT registration in more than 1 (but less than 6) Member States	VAT registration in 6 or more Member States
5. Trade	Predominantly domestic trade and has begun trading outside its Member State	Domestic and intra-EU trade	Domestic and intra-EU trade
6. Invoices	Less than 50 Accounts Payable and Accounts Receivable invoices per month for each VAT registration	Less than 50 Accounts Payable and Accounts Receivable invoices per month for each VAT registration	More than 50 Accounts Payable and Accounts Receivable invoices per month for each VAT registration

Source: EY, 2015

These business types have been identified by the survey respondents as being the three company types to consider in determining the scale of any cost changes under each policy option. In addition, these company types are also likely to be the ones engaged in cross-border trade and thus impacted by the proposed policy options. Micro businesses[257] have been excluded given that they are unlikely to engage in cross-border trade hence rendering them irrelevant for the purposes of the analysis.

Specific areas which will have implications for businesses' compliance costs were identified. The tax experts' survey assessed, on average, how each of the business types would be impacted by the policy options from a compliance cost perspective. The tax experts were asked to provide an estimate of the percentage change in the annual number of hours spent dealing with VAT compliance of these areas. They were asked to provide this percentage for both the initial year of implementation ('Year 1') and for the years after that ('Ongoing') for each of the three types of business.

In estimating compliance costs impact, the study adopted the arithmetic average of the estimates provided by the respondents to the tax experts' survey in order not to assign weights to the views of respondents.

For the analysis of the collected data the following statistical measures have been used:

- A frequency distribution of the compliance cost estimates to identify the range of cost estimates that were most or least prevalent amongst respondents; and
- The median[258] compliance cost estimates outlined by the survey respondents with respect to how costs will change under each of the policy options.

[257] SMEs are defined in the EU recommendation 2003/361. A micro-business is defined as one which has fewer than ten employees and a turnover or balance sheet total of less than EUR 2 million. The study has made the assumption that these micro businesses do not engage in cross-border trade.

[258] Median is the number separating the higher half of a data sample, a population, or a probability distribution, from the lower half.

The tax experts' survey was also used to collect technical and legislative information in relation to the 'As Is'/ 'To Be'[259] Legislative Matrix. This matrix was prepared with the aim of illustrating the VAT treatment of a selection of common types of transactions in goods both under the current VAT rules ("As Is" analysis), and from the perspective of the five policy options ("To Be" analysis)[260].

2.4. Member State survey

A Member State survey, distributed to all 28 Member States' tax authorities across the EU, has been carried out to collect data on the current VAT administrative costs of Member States and how these costs would change under each of the proposed policy options[261]. In addition, Member States had been asked to provide estimates of the share of VAT fraud in the VAT gap, the share of MTIC fraud in the VAT fraud gap, etc. These estimates have been used to assess the impacts of the policy options on MTIC fraud.

Prior to the design and circulation of the Member State survey, interviews were conducted with tax authority representatives from six Member States (Belgium, France, Italy, Poland, Sweden and the UK). The purpose of these interviews was to gain a clearer understanding of what data could be expected to be received in relation to questions on VAT administration activities, VAT administrative costs and potential impact of changes to VAT legislation on certain activities of the Member States.

The Member State survey consisted of a set of 34 questions in relation to:

- the current VAT fraud gap that arises from intra-EU B2B trade;
- the current labour and non-labour[262] administrative costs associated with intra-EU B2B VAT administration;
- how administrative costs are expected to change under each policy option; and
- how each Member State intends to resource any additional labour requirements.

Survey responses were received from 25 EU Member States Tax Authorities.

<u>Labour and non-labour administrative costs</u>

The scale of administrative costs depends on a wide range of factors, including the number of businesses registered for VAT, the complexity of the tax, the structure of tax rates, the frequency of reform and the efficiency of the tax authority. In order to estimate the impact the policy options will have on the magnitude of Member States' administrative costs, the current and expected levels of the costs were assessed.

To assess the current level (baseline) of labour costs, the Member States' tax authorities were asked to provide:

- an estimate of the Full Time Equivalents (FTEs)[263] currently employed in all of their tax offices and the number of FTEs employed dealing specifically with VAT

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259 'Baseline' / 'Reform policy options'

260 The types of transactions analyses include domestic supply of goods, intra-EU supply of goods, transfer of own goods between Member States, call-off stock and consignment stock, triangular supply of goods and chain transaction involving four or more parties in the supply of goods.

261 The survey template is available in Annex B of 2015 EY Study.

262 Non-labour costs refer to consultancy costs, IT systems, staff training and other costs.

263 See Glossary for definition.

administration, including a percentage breakdown of the number of FTEs employed who deal with domestic, intra-EU and other VAT administration;

- an average cost per hour (compensation) for employees responsible for dealing with VAT. In the context of this study, average cost is the aggregate of the average wage cost and other employee benefits excluding training costs.

To assess the current level of non-labour costs associated with the administration of VAT, the Member States' tax authorities were asked to provide the annual total non-labour costs, including a percentage breakdown of the total costs as per external consultancy, IT systems, staff training costs and other costs.

To assess the impact of each proposed policy option, the Member States' Tax Authorities were asked to report estimates of changes (in %) in administrative labour and non-labour costs under each policy option for both the implementation phase (Year 1) and the subsequent ongoing annual administration. The responses were then grouped in the following ranges:

- No change - 0% impact
- Increase 1%-5%
- Increase 6%-20%
- Increase 21%-35%
- Increase 35%-100%
- Increase of more than 100%.

MTIC Fraud

The impact of the policy options on MTIC fraud has been estimated using primary data from the Member States' survey results. Nine Member States' Tax Authorities[264] were able to provide the level of detail required. On average, according to the Tax Authorities 36% of the VAT gap is due to VAT fraud. Three Member States' Tax Authorities explained that the fraud portion of the VAT gap is entirely driven by MTIC fraud, while the other six respondents considered that only a proportion of the VAT gap is due to MTIC fraud. On average, 20% of the overall VAT gap was considered to be due to MTIC fraud, while the estimated weighted average (based on overall VAT gap proportion) is 24%[265]. For countries where no data was available, MTIC fraud was estimated using 3 different approaches:

- arithmetic average of the data provided (20%);
- weighted average of the data provided (24%);
- using proxies based on similarities of size of VAT gap.

Cash flow

Cash flow has been identified as either a particular cost or benefit for Member States due to the clearing system to be implemented as part of the OSS system under Option 2 and Option 5. This is due to Member States receiving and holding VAT for a period of time

[264] Austria, Bulgaria, Czech Republic, Cyprus, Finland, France, Slovakia, Slovenia and United Kingdom.

[265] These estimates are based on eight responses, as one Tax Authority did not provide a MTIC fraud specific estimate.

before businesses in their local Member State seek to recover the VAT on their domestic VAT return.

In order to calculate the net cash flow position of Member States, Eurostat data for the calendar year 2013 on the value of intra-EU supplies and acquisitions have been used. Based on the 2013 trading levels between each Member State, it was identified that the majority of Member States will have an overall cash flow benefit under Option 2 and Option 5[266]. There is limited asymmetry between Member States based on trade patterns within the EU. Instead, the overall cash flow benefit for Member States arises as a result of either having a filing period that is greater than 40 days or the fact that the cash flow benefit on its dispatches outweighs the cash flow cost incurred on its acquisitions.

Finally, the same assumptions as regards (i) the average remittance time for payments to businesses from their local Tax Authority; (ii) applicable VAT rates; (iii) the value of VAT payable to other Member States by the business; and (iv) interest rates applicable to businesses on saving/borrowing applied for calculating the cash flow impact on business hold here as well[267].

2.5. Limitations and assumptions in relation to the primary data collection

There are a number of difficulties associated with the collection of detailed compliance costs information for businesses and administrative costs of Member States' Tax Authorities in general. Such methodological issues have become apparent in previous studies on compliance costs[268]. As such, there are inherent limitations in gathering this information.

Similarly, for the purposes of the 2015 EU study, there are a number of limitations that it is pertinent to draw the attention to as these may impact the results and conclusions. These **limitations** include:

- the findings are highly sensitive to the opinions of a sample of business respondents, tax officials and tax experts on questions that do not cover every possible detail and element that might be required in order to fully assess the implications of the current rules and the proposed reform policy options;
- the implementation of Options 2a and 5a is considered to have similar impacts in terms of compliance costs of businesses and administrative costs of Member States' Tax Authorities and therefore any differences between these two options may be due to a perception bias;
- technical and legislative implications of the proposed policy options have been identified based on the literature provided in relation to the details and mechanisms for each proposed option. Any legislative implications arising from factors not explicitly stated in the narrative for each option are not considered;
- the study focuses predominantly on the economic impact of each of the policy

[266] See Table 31 of the 2015 EY Study for details of the individual and aggregate cash flow impact for each Member State based on their trade levels with every other Member State.

[267] For a full description, see section 7.2 Impact on Tax Authorities cash flow of the 2015 EY Study.

[268] The European Commission's publication 'Compliance costs related to cross-border activity' (2014) sought to quantify compliance costs related to tax on individual cross-border activities. Local tax experts were surveyed in order to obtain this information. Another European Commission's publication, 'A review and evaluation of methodologies to calculate tax compliance costs' (2013), reviewed and analysed a variety of methodologies used to measure tax compliance costs borne by businesses and individuals within the EU.

options. Political implications of implementing the options in different Member States are not considered;
- legislative conditions beyond those of the immediate tax legislation affected by the alternative policy options are not considered;
- certain aspects of the policy options may shift the legal, political or economic patterns within the EU in a manner which goes beyond the specific scope of the study;
- data provided by Eurostat in relation to intra-EU trade statistics is subject to specific limitations, namely that the calculation and reporting method used by Member States to report figures may differ throughout the EU.

3. Secondary data collection and literature review

3.1. Secondary data collection[269]

The specific 2015 EY study undertook a comprehensive review of relevant publicly available economic and business data which was used to complement the primary data collection exercise.

The relevant economic data on the EU has been collected primarily from Eurostat, covering the period 2000-2013. For data not available on Eurostat, alternative resources, such as the World Bank, OECD, UNECE, National Statistics Office Databases as well as Bloomberg were explored.

In addition to the results from the primary data collection which inform the policy inputs, the macroeconomic analysis relies on secondary data about the historical levels of macroeconomic indicators. The macroeconomic variables on which the impact of the policy options have been analysed are per capita real GDP growth, per capita real consumption growth, per capita real exports growth and employment growth. The econometric method, as detailed in the next section, requires quarter-on-quarter growth rate of these variables as input. Also, two intermediary variables through which the policy inputs affect macroeconomic indicators, namely, aggregate inflation (GDP deflator inflation) and the export price inflation were needed.

The quarterly data was collected over the 2000-2013 period from Eurostat. Reliable EU-28 data on employment for periods earlier than 2000 was imprecise as some Member States have not been EU members long enough to provide data or data was not collected at the required frequency. Deseasonalised data on GDP, exports and consumption for period beyond 2013 for a number of Member States, hence EU 28 in aggregate, was not yet available.

3.2. Literature review

A literature review was conducted which encompassed: (i) a review of literature screened by the Commission services; and (ii) a desk top literature research exercise to identify any additional studies/reports which will help to complement the approach adopted in this study.

[269] Secondary data is data collected by someone other than the user (for example data published by Eurostat).

Based on a literature review and after considering the specific objectives of the study, two econometric modelling approaches were identified.

- Structural/General equilibrium models

General equilibrium models fully specify the structure of the economy, and hence reduce the need for lengthy time series data. These models are adequate for evaluating structural changes to the economy, as they make use of more detailed data and relate to different economic sectors.

However, within the context of the specific EY study, these models do not allow the gains arising from the policy options to be linked onto a single activity within the economy. This is because, within the general equilibrium framework, the government and firms in the economy dynamically decide on how to allocate these savings across different activities.

- Reduced form/Vector Autoregression (VAR) models

Vector Autoregression (VAR) models do not attempt to specify a detailed structure for the economy, which makes them less prone to the risk of imprecise structural assumptions regarding the economy.

VAR models aim to capture the dependencies between current and past levels of macroeconomic indicators using simple linear forms. Although these models do not allow structural interpretation of results, using appropriate additional assumptions, they can be used to assess the response of the macroeconomic indicators to a shock that affects one or more of them.

4. Econometric modelling in relation to the macroeconomic analysis

The econometric modelling methodology followed in the 2015 EY study focuses on modelling the dynamic macroeconomic impact of VAT fraud and VAT compliance costs on macroeconomic variables such as real GDP growth, consumption growth, export growth and employment growth. The impact is modelled for each of the policy options and has been obtained as the difference between the 'Baseline' and the 'To Be' forecasts for each policy option of the selected macroeconomic variables. These forecasts have been estimated using **a Vector Autoregression (VAR) model.**

The VAR modelling approach relies on the assumption that the current levels of the macroeconomic variables can be predicted using the past history of these variables. Based on this approach, the movements in the variables can be explained by the past growth rates as well as the changes in the aggregate consumption price and export price levels. The current level of the macroeconomic variables is assumed, in the 2015 EY study, to be dependent on the magnitude of these indicators from the past four quarters. The choice has been influenced by the quarterly frequency of the data and validated using statistical measures[270].

As regards the changes in the consumption price and export price levels, the results of the primary data analysis were used as the input.

[270] See Annex E of the 2015 EY Study for more details.

In particular, the link between the policy options and the macroeconomic variables is translated into the econometric model via:

- the effect of the compliance cost savings on the export prices, and
- the effect of the VAT fraud reduction on the VAT rate.

In this respect, it is assumed that:

- the savings made by business from the reduction in the intra-EU B2B compliance costs due to the implementation of the policy options will improve the competitiveness of the suppliers and would be passed on to the intra-EU B2B exports as price reductions; and
- the additional VAT collected resulting from the reduction of the scale of VAT fraud will be returned to the consumers in the form of a tax rate cut, decreasing therefore the overall price levels in the future.

The above two assumptions provide one of a number of plausible scenarios for how governments and businesses will react to increased VAT revenues and reduced compliance costs respectively.

In this respect, a **VAR model**, unlike a general equilibrium model, allows the savings from the VAT compliance costs to be passed solely onto intra-EU trade activities and the proceeds from the fraud reduction to be used to fund a VAT rate reduction. For these reasons, the VAR modelling approach has been adopted. The model adopted in the study has also been designed to compare the different policy options.

The econometric modelling approach consisted of three stages. A brief summary overview of the process is presented below[271].

In order to estimate the likely impact of the proposed policy options, several economic variables are forecast using the VAR model to outline a baseline scenario. The baseline forecasts are calculated for a 3-year period (2014-2016) and indicate the cumulative growth of the macroeconomic indicators. Subsequently, new scenarios are run for each policy option which produces forecasts of the same variables. Finally, a comparison is made of the scenarios for each proposed policy option with the baseline, which establishes the magnitude of the impact of these policy options on the selected macroeconomic variables over 12 quarters.

Table 14 below shows the estimated forecasts for the macroeconomic variables under the baseline. Table 15 shows by how much the 3-year cumulative growth of the macroeconomic variables under each of the five policy options differ from the baseline. According to the VAR forecasts, the EU 28 per capita real GDP is estimated to grow at a cumulative rate of 4.465% over the 3-year period. This estimate is higher than the estimated growth of real consumption in the same period (3.5%), but lower than the estimated real exports growth at 13.4%. In absolute terms, the baseline real EU GDP at 2005 prices in 2013 was EUR 11 768 billion[272.] It is worth mentioning that **the baseline forecast of GDP growth 4.465% produced by the VAR model is not substantially**

[271] Full details are available in Annex E of the 2015 EY Study.
[272] Eurostat.

different from the European Commission's spring 2015 forecasts which indicates a cumulative growth of 5.3% during the 2014-2016 periods[273].

Table 14: Forecasts of the macroeconomic variables under the baseline (3-year cumulative growth)

Macroeconomic variables	Baseline
Per capita real GDP	4.465%
Per capita real consumption	3.536%
Per capita real exports	13.455%
Employment rate	1.897%

Source: EY, 2015.

Table 15: Difference in % of the 3-year cumulative growth of the macroeconomic variables under each of the five policy options differ from the baseline

.

Macroeconomic variables	Option 1	Option 2	Option 3	Option 4	Option 5
Real GDP growth	0.004%	0.157%	0.005%	0.017%	0.158%
Real consumption growth	0.003%	0.130%	0.004%	0.014%	0.130%
Real exports growth	0.000%	0.010%	0.000%	0.001%	0.010%
Real employment growth	0.002%	0.101%	0.003%	0.011%	0.101%

Source: EY, 2015.

Macroeconomic data and approach to addressing data issues

In addition to the results from the primary data analysis which inform the policy inputs, the analysis relies on the secondary data about the historical levels of the macroeconomic variables (per capita real GDP growth, per capita real consumption growth, per capita real exports growth and employment growth). The econometric method requires quarter-on-quarter growth rate of these variables as input. Also, two intermediary variables through which the policy inputs affect macroeconomic indicators, namely, aggregate inflation (GDP deflator inflation) and the export price inflation were needed.

The quarterly data was collected over the 2000-2013 period from Eurostat. Reliable EU-28 data on employment for periods earlier than 2000 was imprecise as some Member States have not been EU members long enough to provide data or data was not collected at the required frequency. Deseasonalised data on GDP, exports and consumption for period beyond 2013 for a number of Member States, hence EU 28 in aggregate, was not yet available. Due to the limited number of data points for several Member States, the economic analysis has not been carried out for individual Member States as the results may have been influenced by these data limitations. However, based on the hypothesis that the effect of aggregation is likely to overcome these challenges, the economic analysis was carried out for the EU 28 as a single entity[274].

The complete list of the data used in the economic analysis, along with Eurostat codes and descriptions, is given in Table 49 in Annex E of the 2015 EY Study.

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273 http://ec.europa.eu/economy_finance/eu/forecasts/2015_spring/eu.html

274 See Annex E of the 2015 EY Study for further details on the modelling approach.

The dataset used in the study covers the 2008-2009 period, during which the economic indicators showed significant drops. In particular, the interval between 2008 Q3 and 2009 Q2 constitutes the period during which the growth rates deviated most significantly from their long term averages (0.4%, 0.1% and 0.1% for GDP deflator inflation, real GDP growth rate and the real consumption rate respectively). To prevent bias in the estimates due to outliers, it has been assumed that during this period pre-2008 Q3 trend continued to hold. Thus, the growth rates for the 4 quarters from 2008 Q3 to 2009 Q2 were obtained by extrapolating the data from pre-2008 Q3 period, using the same VAR methodology.

Modelling strategy: Compliance costs reduction

During the primary data analysis stage, a reduction of business VAT compliance costs related to intra-EU B2B trade has been identified as one of the two main impacts of the proposed policy options.

The assumption made in this respect is that any savings made by businesses on intra-EU VAT compliance would be passed on to export price reductions. It is assumed that the discount over intra-EU B2B export prices driven by a compliance cost reduction comes into effect gradually. The pass- through occurs initially at a rate of 25% in the first quarter (which was assumed to occur at the end of 2013 Q4, the last period in the historical data sample) to 100% in the Q4 and beyond.

The modified data facilitated an analysis of the impact of the resulting competitiveness gain on macroeconomic indicators. The export price index is a composite of intra- and extra-EU exports. In order to evaluate the effect of the proposed policy options, only the intra-EU proportion of the index was adjusted. This was done using the share of intra-EU VAT compliance costs within aggregate export prices as the scaling factor. Then, using Member States' 2013 real GDP as weights, a weighted average of the index was calculated to represent the competitiveness gain for the EU 28.

To determine the percentage change in ongoing costs of businesses in response to the policy option changes, a combination of the responses from the Business Survey and Eurostat data was used to calculate the change in the export price deflator.

Step 1: The proportion of net sales of the surveyed businesses that were related to B2B intra-EU trade for each Member State was calculated.

Step 2: The VAT labour and non-labour costs that related to intra-EU B2B compliance within the business sample were calculated. Average hours spent on VAT activities per year, average hourly wage rate, the business split of B2B and B2C activities, the business split of domestic and intra-EU activities and third party costs were used. Third party costs were assumed to be attributed to wage costs elsewhere in the economy.

Step 3: The proportion of intra-EU B2B VAT compliance costs to intra-EU B2B net sales of the businesses

$$A = \frac{Hours\ spent\ on\ B2B\ intra\ EU\ VAT\ compliance\ activities * Wage\ rate + 3rd\ party\ costs}{Net\ sales * Percentage\ of\ intra\ EU\ B2B\ sales}$$

was calculated for each respondent business. The number of respondents was not sufficient to calculate this number individually for each Member State. Therefore, the

responses were collated across the EU 28. Within the sample of EU-wide aggregate responses that was received, the intra-EU VAT compliance cost for businesses is calculated to be 0.62% of intra-EU trade.

Step 4: The percentage reductions in compliance costs were obtained from the tax experts' survey for each business type (SME Type 1, SME Type 2 and Large Business), for each policy option and each Member State. The aggregate costs reduction percentage implied by each policy option for each Member State was then calculated as the weighted average of the percentage costs reductions of each business type, using the Gross Value Added of the business types as weights.

Step 5: The percentage cost reduction obtained in step 4 were translated into percentage export price changes for each Member State and policy option by multiplying them with the factor obtained in step 3.

Step 6: The percentage export price change from step 5 was averaged across Member States using the real GDP from 2013 of each Member State as weights. This is done for each policy option.

Step 7: Finally, for each policy option the export price changes were downscaled to reflect the share of intra-EU exports within total exports of the Member States.

Modelling Strategy: VAT Fraud Gap

The other model component that would be impacted under two of the proposed policy options (option 2 and option 5) is the VAT fraud gap. The impact of these options on the magnitude of VAT fraud in the EU was analysed.

The assumption is that the government is revenue neutral. Thus, the increase in the VAT collection arising from reducing the VAT gap is compensated by a proportional reduction of the VAT levied on consumers. The reduction in the VAT rate is the consumer prices, leading to an overall decrease in the consumer price deflator (inflation).

The approach that was adopted can be summarised in the following steps:

Step 1: The change in the magnitude of VAT fraud in intra-EU B2B transactions is calculated for each policy option. It is assumed that the size of intra-EU B2B transactions is equivalent to the level of intra-EU exports.

$$\%\text{ decrease in VAT gap} = \%\text{ Share of VAT gap within VTTL (VAT Total Liability)} \times \%\text{ Share of MTIC fraud gap within VAT gap} \times \%\text{ Decrease in Fraud}$$

Step 2: The approach was based on the VAT baseline gap estimates from the EC study "2012 Update Report to the Study to quantify and analyse the VAT Gap in the EU-27 Member States" and the standard VAT rates from each Member State as at the end of 2013. The revenue neutrality assumption implies that:

$$(1 - \%\text{ VAT baseline gap}) * \text{Pre — policy Standard VAT rate} = (1 - \%\text{ VAT post — policy gap}) * \text{Post — policy standard VAT rate}$$

Step 3: A weighted average post-policy VAT rate is calculated by applying 2013 real GDP for each Member State as weights.

Step 4: Lastly, the consumer price deflator (inflation) trend identified was modified from the VAR (4) analysis at the rate of change implied by the new tax rate.

$$\text{New deflator} = \text{Old deflator} * \frac{\text{Post — policy Standard VAT rate}}{\text{Pre — policy Standard VAT rate}}$$

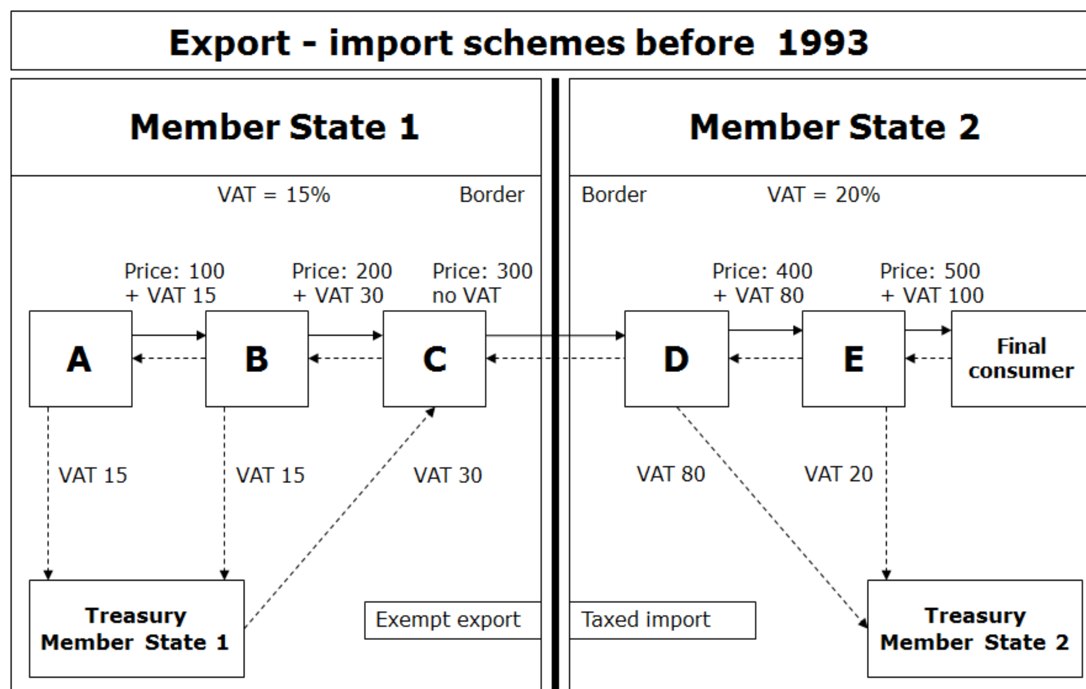
It is assumed that this impact is felt gradually, that is at a rate of 25% in the first quarter following implementation to 100% in the 4th quarter and beyond.

Finally, it has to be noted that **a caveat to the results** is that the compliance cost savings and the reduction in VAT fraud could well be higher; this is because the compliance cost estimates do not consider further cost savings that may occur in subsequent years due to increased compliance efficiencies while the VAT fraud reduction estimates do not include reduction in diversion fraud. As a result, **the economic impact is estimated to be conservative**.

ANNEX 5: BACKGROUND INFORMATION ON VAT

1. VAT treatment of intra-EU supplies of goods before 1993

Box 8: VAT system before 1993



Before 1993, intra-EU cross-border transactions in goods were subject to customs procedures and controls meaning that the payment of the VAT due was controlled at the time of import of the goods. Intra-EU cross-border supplies of goods (in the figure the transaction between C and D) were exempt (in Member State 1, which is the Member State of origin) because they gave rise to an export. The introduction of the goods (in Member State 2 that is the Member State of destination) gave rise to an import and was taxed (either at the border or via deferred payment in the VAT return). Preceding supplies (A-B and B-C) and subsequent supplies (D-E) were taxed with VAT. Both the VAT charged on the supply made by A to B, by B to C and by D to E and the VAT paid by D at import were as a rule deductible (as regards C through a refund since there would be no output VAT on the supply made by C against which the deductible VAT of 30 could be offset). To prove import/export, customs documentation was required and checked by the customs administration.

2. Destination-based versus origin-based VAT system

A "destination-based" VAT system means that goods traded across borders are taxed in the country where they are consumed (the destination country) rather than where they are produced (the origin country), and at the destination country's tax rate. This is consistent with VAT being conceived of as a tax on consumption, rather than on production. It helps ensuring that households and firms face the same tax rate on their purchases regardless of where they buy the goods, and therefore should not distort trade patterns. But applying the destination principle can be problematic, leading to distortions in trade (e.g. because of deduction limitations in the country of origin) and potentially higher compliance costs. An "origin-based" system is in principle more in line with a common market functioning as a domestic market.

3. Historical background of the reform: from the Green Paper to the Action Plan

Since the basic requirements for an origin-based system proved not to be achievable, despite several attempts, the Commission decided in 2010 to focus on this issue in the framework of its broad public consultation based on the "Green Paper on the future of VAT[275]" (hereinafter "2010 Green Paper").

This consultation[276] showed that many businesses consider that the complexity, additional compliance costs and legal uncertainty generated by the current VAT rules governing cross-border intra-EU supplies of goods often prevent them from engaging in cross-border activities and reaping the benefits of the single market. Stakeholders also expressed the need for MTIC fraud to be tackled through specific remedies targeting fraudulent taxpayers rather than measures that could affect indirectly compliant taxpayers, creating a disadvantage to them.

The European Parliament[277], the European Economic and Social Committee[278] and stakeholders such as businesses, tax practitioners and academics also recognised the deadlock[279]. They therefore favoured a new system based on the principle of taxation at destination as a realistic solution. On this basis, the Commission adopted on 6 December 2011 a communication "On the future of VAT – Towards a simpler, more robust and efficient VAT system tailored to the single market[280]" (hereinafter "2011 Communication").

Discussions with Member States confirmed that the objective to implement a definitive VAT regime for intra-EU trade in goods based on the principle of taxation in the Member State of origin was still politically unachievable given in particular the approximation of rates it would require. This was confirmed by the Council in May 2012[281].

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[275] COM(2010) 695, Commission Staff Working Document, SEC(2010) 1455, 1.12.2010

[276] To note that the Commission received 1,726 replies from businesses, academics, citizens and tax authorities, a record response to a tax consultation (see for more information in Annex 2).

[277] European Parliament Resolution of 13 October 2011 on the future of VAT (P7_TA(2011)0436): http://www.europarl.europa.eu/sides/getDoc.do?type=TA&language=EN&reference=P7-TA-2011-0436

[278] European Economic and Social Committee Opinion of 14 July 2011 on the 'Green Paper on the future of VAT – Towards a simpler, more robust and efficient VAT system': http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:52011AE1168

[279] On 6 May 2011, the European Commission (Directorate General for Taxation and Customs Union) organised a one day conference in Milan on the Green Paper on the future of VAT - Towards a simpler, more robust and efficient VAT system (see Annex 2). This conference was an important part of the consultation process associated with the 2010 Green Paper. It brought together policy makers, experts, businesses and other stakeholders and the general public from all over Europe, and beyond. See for more information on: https://ec.europa.eu/taxation_customs/business/vat/action-plan-vat/communication-future-vat/green-paper_en

[280] Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee on the future of VAT - Towards a simpler, more robust and efficient VAT system tailored to the single market (COM(2011) 851, 6.12.2011): http://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/taxation/vat/key_documents/communications/com_2011_851_en.pdf

[281] Council conclusions on the future of VAT - 3167th Economic and Financial affairs Council meeting, Brussels, 15 May 2012 (see in particular point B 4): http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/130257.pdf

After the adoption of the 2011 Communication, the Commission services entered into a broad-based and transparent dialogue with Member States and with stakeholders to examine in detail different possible ways of implementing the destination principle. This took place in particular via the GFV and the VEG.

Following intense and in-depth analytical work[282] five options, each one with their own merits and shortcomings, have been identified[283] (further details on the selection of these options are available in Section 9 "Selection of options" below). In order to assess the impact of each of those five options in comparison with the current situation, a study was commissioned and finalised by mid-2015[284]. The results of this study were discussed in a Fiscalis seminar[285] which brought together both the GFV and the VEG.

On 7 April 2016, the Commission adopted the Action Plan which sets out the measures envisaged in order to modernise the EU VAT system. In this context, the Commission announced its intention to adopt in 2017 four VAT-related proposals:

- a definitive VAT regime for intra-EU cross-border trade based on the principle of taxation in the Member State of destination of the goods in order to create a robust single European VAT area;
- a modernised VAT rates policy so as to allow Member States greater autonomy on setting the VAT rates;
- a comprehensive simplification VAT package for SMEs;
- a proposal to enhance VAT administrative cooperation and EUROFISC.

4. Sources attesting to the existence of the problems

4.1. The 2010 Green Paper

The contributions received from stakeholders during the public consultation on the 2010 Green Paper allowed a first identification of the shortcomings of the current transitional VAT system (see Annex 2). Stakeholders mentioned problems such as disproportionate compliance costs, legal uncertainty, cash flow disadvantages and distortions of competition.

The causes of the shortcomings were found to be the lack of harmonisation of the VAT rules in the EU, the complexity of the rules applicable to intra-EU activities and the additional VAT administrative obligations and risks associated with intra-EU activities. Stakeholders pointed out that these shortcomings can constitute an obstacle, in particular for small businesses, preventing them from engaging in intra-EU trade. They further underlined that the current transitional VAT system is not suitable for the single market

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[282] See details in Annex 1.

[283] Commission staff working document on the implementation of the definitive VAT regime for intra-EU trade (SWD2014) 338, 29.10.2014): http://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/taxation/vat/swd_2014_338.pdf

[284] Implementing the 'destination principle' to intra-EU B2B supplies of goods - Feasibility and economic evaluation study – Final report – 30 June 2015: http://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/common/publications/studies/ey_study_destination_principle.pdf

[285] Organised in June 2015 in Vienna (see for further details in Annex 1).

and prevents them from fully benefiting from its advantages. For these reasons most of them were against the idea of making the current rules the definitive VAT system[286].

4.2. The work in the GFV and in the VEG

On the basis of this first analysis of the shortcomings of the current transitional VAT system and their causes, the Commission services engaged into in-depth discussions with the Member States[287] and expert stakeholders[288] in order to identify more precisely the problems caused by the current transitional VAT system.

At the VEG the expert stakeholders widely agreed that the list of shortcomings and their causes outlined by the Commission was complete and correctly reflected the problems faced by businesses. They emphasised that problems are linked both to legal uncertainty (in particular regarding the means of proof of the intra-EU transport of the goods to be provided in order for the supplier to justify the exemption of an intra-EU supply) and to compliance costs due notably to the complexity of the current rules, the fact that the rules are not adapted to all current business models and the divergent application of the rules by the Member States.

At the GFV the Member States also generally confirmed the list of shortcomings and their causes as described by the Commission. Most Member States generally reiterated the need for greater harmonisation and simplification of the existing rules and some also stressed the importance of the problems related to fraud and tax evasion.

4.3. The evaluation of the current system

A comprehensive retrospective evaluation of the EU VAT system[289] has been carried out. That evaluation made it possible to conclude that the current transitional VAT system is too complex. This results in higher compliance costs for businesses trading across the EU as compared with those operating only at domestic level and in legal uncertainty for both businesses and tax administrations. As a consequence, intra-EU cross-border trade and the functioning of the internal market as a whole are disrupted. Further, the evaluation also mentioned that the current transitional VAT system has generated a significant level of cross-border fraud that hampers the functioning of the internal market.

5. VAT fraud schemes

Box 9: Basic schemes

MTIC fraud example involving two Member States

The customer of a cross-border transaction purchases goods VAT-free and in the subsequent domestic sale charges VAT to his customer without remitting it to the

[286] The contributions are available together with a report summarising their main elements at http://ec.europa.eu/taxation_customs/common/consultations/tax/2010_11_future_vat_en.htm. More detailed information can be found in Annex 2.

[287] As of the 5th meeting of the GFV which took place on 29 November 2012. See further information in Annex 1.

[288] As of the 1st meeting of the VEG which took place on 24 October 2012. See further information in Annex 1.

[289] IFS et al., 2011. The key elements of this evaluation have been integrated into the different parts of this impact assessment.

Treasury. The rules applicable to intra-EU supplies are not abused but allow the acquirer (the "missing trader") to commit MTIC fraud in the subsequent domestic supply.

In this case, the acquirer in Member State 1 purchases goods VAT-free from a supplier in Member State 2 and charges VAT to his customer in Member State 1 without remitting it to the Treasury. Before the tax administration is able to audit the acquirer he would have disappeared. The customer might not be aware of this fraud and when he is a business he might also be able to deduct the VAT charged to him (as he received a valid invoice he remains in principle entitled to a tax deduction).

Diversion fraud example involving a single Member State

The supplier pretends to have transported the goods to another Member State but the goods are in fact consumed locally (goods are diverted from cross-border to domestic trade). The rules applicable to intra-EU supplies are abused by the supplier.

In this case, the supplier in Member State 1 charges and collects VAT from his customer in Member State 1 but reports this supply in his VAT return as an exempt intra-EU supply of goods and therefore does not transfer the VAT collected to the Treasury. Before the tax administration can hold up information received from the tax administration of the Member State where the goods are supposed to have been transported to with information obtained during an audit of the supplier, this supplier would have disappeared. The customer might not be aware of this fraud and when he is a business he might also be able to deduct the VAT charged to him by the supplier (as he received a valid invoice he remains in principle entitled to a tax deduction).

6. VAT notions

Box 10: VAT notions

VAT identification number

The VAT identification number serves several purposes, both with regard to the declaration/payment of VAT and for audit/statistical reasons.

Declaration/payment

As a rule, businesses making taxable transactions within the EU must register for VAT purposes and be allocated a VAT identification number in each Member State in which they are liable to pay the VAT. Thus:

- when making supplies of goods taxable in a particular Member State, the supplier is liable to VAT in that Member State and must register and pay the VAT there;

- when acquiring goods from another Member State, the acquirer is liable to pay the VAT due on the intra-EU acquisition to the tax authorities of the Member State in which the goods are acquired and must obtain a VAT identification number there.

Through this VAT registration, businesses will comply with all their VAT obligations (e.g. the VAT identification number will have to be mentioned in the invoices issued, in the VAT returns submitted to declare VAT, as well as in the recapitulative statements submitted – see details below).

Businesses might need to be registered not only in the Member State where they are established (and where they carry out habitually their activities) but also in any other Member States where they are liable to VAT even without having a fixed establishment there.

Audit/statistical reasons: proof of the status of the acquirer to whom an intra-EU supply of goods is made

In case of an intra-EU supply of goods, the supplier must provide sufficient evidence that the goods have been supplied to a "taxable person acting as such in a Member State other than that in which transport of the goods began"[290] in order to justify, before the tax authorities of the Member State of origin, the VAT exemption and therefore the fact that he did not charge VAT on such supply. This is because only where the intra-EU supply is made to an acquirer having that status the intra-EU supply will be exempt; in any other case the supply will be taxed and the supplier will have to charge the VAT of the Member State of origin to the acquirer.

In order for the intra-EU supplier to determine whether his customer is a business or a final consumer (only in the first case the exemption will apply and the business customer will be liable to pay the VAT due on the intra-EU acquisition of goods) he needs to obtain the customer's VAT registration details and check the status in the VIES system[291].

Further in the recapitulative statements (see below) an intra-EU supplier should mention the VAT identification number of his intra-EU acquirer. By cross-checking the information contained in these listings, Member States are informed of goods circulating (VAT free, since the intra-EU supply is exempt from the tax) from one Member State to another. This allows for the administrative follow-up of the goods necessary in order to ensure that VAT is paid in the Member State of destination of the goods.

Liability rules for non-established businesses[292]

As a rule, suppliers of goods are liable to pay VAT to the tax authorities of the Member State where the tax is due. However, when they make supplies of goods in a Member State in which they are not established, there are cases in which the person liable for the payment of VAT will be the customer[293] (reverse charge for supplies made by non-established businesses).

Consignment and call-off stocks

Consignment stock refers to the situation where a trader transfers business goods to a Member State where he is not established, in order to sell them there at a later stage and in any case after arrival. Call-off stock is a specific category within the general notion of consignment stock and refers to the situation where at the time the goods are transferred

[290] Article 138 of the VAT Directive.

[291] VIES (the VAT Information Exchange System) is an electronic mean of validating VAT-identification numbers of economic operators registered in the European Union for cross-border transactions on goods or services. See more info on: http://ec.europa.eu/taxation_customs/vies/

[292] A non-established business refers to a "non-resident" business with regard to a particular Member State, thus a business established in one Member State which trades with another Member State where it does not have any fixed establishment will be considered to be a "non-established business" in this later Member State.

[293] See Article 194 of the VAT Directive.

the trader already knows the identity of the buyer to whom the goods will later be supplied.

According to EU rules, the transfer of the goods entails

(i) a deemed intra-EU supply of goods in the Member State of origin made by the transferor;

(ii) a deemed intra-EU acquisition of goods made in the Member State of destination also by the transferor, who will have to get registered for VAT purposes and declare the intra-EU acquisition there;

(iii) a subsequent domestic supply made in the Member State of destination by the transferor to his customer.

To be exempt from VAT, the deemed supply of goods needs to fulfil the conditions of any intra-EU supply of goods in the Member State of origin. The transferor will have to be registered and declare the transfer in the VAT return submitted in the Member State of origin and will further have to furnish the proof of the intra-EU transport of the goods to the tax authorities of that Member State.

In the Member State of destination, the deemed intra-EU acquisition of goods entails a number of obligations on the transferor (e.g. registration, declaration of the intra-EU acquisition). Further obligations will be imposed on him on account of the subsequent domestic supply (e.g. declaration and payment of VAT unless reverse charge applies).

Cross-border chain transactions

This refers to the case where multiple parties are involved in successive sales of the same goods which are the object of a single transport: A sells to B, who sells to C, who sells to D and the goods are transported directly from A to D, so B and C are just intermediaries.

When this situation happens, according to the case-law of the CJEU[294], the intra-EU movement of the goods can only be ascribed to one of the supplies, and only that supply will benefit from the VAT exemption provided for an intra-EU supply. All the other supplies in the chain will be domestic supplies, taxed and not exempt.

Proof of transport of intra-EU supplies of goods

In case of an intra-EU supply of goods, the supplier must provide sufficient evidence that the goods have been transported from one Member State (Member State of origin) to another (Member State of destination) in order to justify, before the tax authorities of the Member State of origin, the VAT exemption and therefore the fact that he did not charge VAT on that supply.

VAT returns

[294] Judgment of the CJEU of 6 April 2006 in case C-245/04, Emag Handel.

Businesses registered for VAT purposes must periodically[295] submit VAT returns to declare the value of their transactions and the corresponding VAT due. Through this VAT return businesses also exercise their right to deduct the VAT due on their acquisitions (see below).

Businesses might need to submit VAT returns in more than one Member State, meaning having to comply with rules of Member States other than that in which they have established their business.

Recapitulative statements

This refers to an obligation specifically linked to intra-EU cross-border trade that requires businesses to report periodically[296] the value of their intra-EU supplies and the identity of their intra-EU customers.

Businesses supplying goods to other Member States must submit periodical recapitulative statements (and add a special mention in their VAT return) of their exempted intra-EU supplies of goods. Those supplies will in the Member State of destination give rise to taxable intra-EU acquisitions of goods for which the customer is the person liable to VAT.

Further the VAT Directive gives the option to the Member States to also require a recapitulative statement for intra-EU acquisitions of goods made by businesses on their territory.

Dealing with VAT audits

Businesses registered for VAT purposes or liable to pay the VAT due in Member States other than the Member State in which they are established are also subject to VAT audits in these Member States.

VAT treatment/qualification of certain transactions

The VAT Directive makes a distinction between supplies of goods[297] and supplies of services[298]. The VAT treatment of intra-EU supplies of goods and intra-EU supplies of services is different and therefore the delimitation between both concepts is crucial to avoid double or non-taxation.

Input tax deduction

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[295] EU rules allow for time frames (tax period and deadline for submission of the VAT return) to be set by the Member States. Tax periods may be set at one month to a maximum of one year and deadline may not be more than two months after the end of each tax period. Member States have implemented different rules. Most require monthly returns although for some it is quarterly reporting. Nearly all Member States allow micro enterprises to file at longer periods than monthly (quarterly, half-yearly or yearly). In most Member States the VAT return should be submitted with a deadline of the end of the month following the tax period. See PWC, 2013.

[296] EU rules allow for time frames to be set by the Member States at one month or a quarter. Periodicity depends in each Member States upon a certain amount of intra-EU supplies.

[297] According to Article 14 of the VAT Directive ‘Supply of goods’ shall mean the transfer of the right to dispose of tangible property as owner.

[298] According to Article 24 of the VAT Directive ‘Supply of services’ shall mean any transaction which does not constitute a supply of goods.

As a rule[299], a business carrying out VAT taxable transactions has the right, in the Member State in which it carries out these transactions, to deduct the VAT which it is liable to pay upon its purchases of goods and services. This is done by subtracting the deductible amount from the VAT due (the VAT collected from his customer) in the regular VAT return submitted to the tax authorities.

However, when a business acquires goods and services in a Member State in which it is neither established nor registered, the right of deduction has to be exercised, not through compensation with any VAT due by the business but through a refund procedure. To this end the refund request will have to be submitted to the Member State of acquisition of the goods and services[300]. Such refund procedure has a cash flow impact on businesses since VAT will only be refundable after several months[301].

7. The additional VAT obligations associated with the current transitional VAT system (driver 1)

Box 11: Additional VAT obligations

Depending on whether a business acts as a supplier or as an acquirer and depending on the supply chain (transaction involving one, two or more parties), it might have to comply with the following main additional obligations when trading in another Member State.

VAT identification number

To ensure that his intra-EU supply of goods is exempt from VAT, the supplier needs to validate the status of his customer. This means checking in the VIES system that the VAT identification number is valid and collecting information about the customer's compliance. Businesses have to prove that they have acted in good faith and exercised *due diligence (because of the 'knowledge test'*[302]). They must keep written records to this end.

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[299] See Articles 168 of the VAT Directive.

[300] See Articles 170-171 of the VAT Directive and Directives 2008/9/EC (refund to EU traders) and 86/560/EEC (refund to non-EU traders). Further details on http://ec.europa.eu/taxation_customs/business/vat/eu-vat-rules-topic/vat-refunds_en

[301] According to Directive 2008/9/EC, refunds of the approved amount shall be paid by the Member State of refund at the latest within ten working days of the expiry of the deadline for refund (either within four months of receipt of the refund application by that Member State where no additional information is requested, or within six months where additional information is requested, but in any case at the latest within eight months from receiving the refund application). In 2015 for EU-25 (as information is not available for three Member States), an average of 65% (about EUR 2 billion) of total handled cross-border refund applications were refunded within the four month deadline, an average of 18% (about EUR 663 million) of total handled cross-border refund applications were queried and refunded within six or eight months; and an average of 3% (about EUR 139 million) were refunded after more than 8 months (the remaining 14% are rejected applications). It has to be noted though, that the above figures are average figures and differences exist between Member States, with a number of Member States refunding more that 90% of all applications within 4 months, whilst others refund more than 50% of the total applications within 6 or 8 months,

[302] The "knowledge test" refers to the reiterated criterion of the CJEU according to which, if the tax administration can prove that a taxable person knew or should have known that he was participating in a transaction linked to VAT evasion, the tax administration can refuse the right to deduct VAT or the right to exempt from VAT an intra-Community supply, to that taxable person. See for instance the judgment of the CJEU in case C-439/04, Axel Kittel.

When trading in other Member States businesses acting either as suppliers or as customers might be required to ask for a VAT identification number to report their transactions and possibly pay the VAT due. This could mean obtaining additional VAT registrations in Member States in which these businesses are not established.

There is an obligation to be registered in a Member State for exports, domestic supplies, intra-EU supplies or transfers of own goods even if the supply is exempted there. Registration is required although in those cases there is no VAT to be paid to the tax authorities.

Liability rules for non-established businesses

In case a Member State does not provide for a reverse charge (i.e. the customer is liable for payment of the VAT due) for supplies made by non-established businesses[303] these businesses might be obliged to charge VAT to their customers and pay it to the tax authorities of the Member State where they are not established.

Consignment and call-off stocks

Businesses transferring own goods from one Member State to another might have to fulfil specific declaration obligations in the Member State of arrival of the goods even if those goods are call-off or consignment stocks (i.e. later on giving rise to a taxable supply). A VAT registration and related reporting obligations in the Member State of arrival of the goods might be required.

Cross-border chain transactions

The VAT Directive provides a simplification for triangular transactions but this does not cater for all chain transactions, in particular not for situations involving more than three parties or non-EU intermediaries.

The absence of simplification measures leads to the need for multiple VAT registrations of non-established businesses and related reporting obligations.

Proof of transport of intra-EU supplies of goods

To be able to prove the transport of goods to another Member State, the supplier must, in addition to normal commercial documentation, keep appropriate records and details on the transport.

In particular for businesses which are not directly responsible for the transport, additional investigations would be needed and permanent resources allocated to obtain sufficient proof of transport from transporters and/or customers.

VAT returns

When acting either as the supplier or as a customer, businesses might be required to report their transactions in a VAT return and pay the VAT due in Member States in which they are not established. This will be in addition to the VAT return they have to submit periodically in their Member State of establishment.

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[303] Article 194 of the VAT Directive provides for an option for Member States to apply reverse charge to supplies made in their territory by non-established taxable persons.

In some cases (transfers of own goods across the EU) there is a need to report movements of goods although similar domestic transfers are not reported. Further for statistical purposes[304], businesses might also be required to add a special mention in their VAT return concerning the intra-EU movement of goods (either when supplied to another Member State or, in some Member States, when acquired from another Member State). This means having to complete a box with the value of these supplies/acquisitions.

Recapitulative statements

For intra-EU supplies of goods

Businesses supplying goods to other Member States must submit periodical recapitulative statements of their exempted intra-EU supplies of goods (which will give rise to a taxable intra-EU acquisition of goods in the Member State of destination).

For intra-EU acquisitions of goods in some Member States

In some Member States, businesses acquiring goods from other Member States must submit periodical recapitulative statements of their intra-EU acquisitions of goods. Filling in those statements does not fit well with normal commercial and accounting practices as reporting only covers certain transactions, that is intra-EU acquisitions.

Dealing with VAT audits

Businesses registered or liable to pay the VAT due in a Member State other than that in which they are established are subject to tax audits also in any such Member State. This might necessitate the appointment of a fiscal representative who knows the procedure and language of the Member State.

VAT treatment/qualification of certain transactions

In case of different interpretation of one and the same transaction by different Member States, businesses might face double taxation. This can result in administrative (or even judicial) claims against the business.

Input tax deduction

Businesses incurring input VAT in a Member State in which they are neither established nor registered can only exercise their right to deduct that VAT by means of a refund request to be submitted to this Member State. To this end, they must make use of a specific electronic refund procedure.

8. Divergent application of EU VAT rules across the Member States (driver 2)

Box 12: Divergences in obligations and procedures

VAT identification number

The process for attributing VAT identification numbers, the amount of information that operators must make available to the tax authorities in order to have such a number assigned, the reasons for which a tax authority may refuse to register or decide to de-

[304] Intrastat requirement statistics.

register a business and the date from which registration or de-registration will produce effect are all matters which vary across the EU.

Liability rules for non-established businesses

There is no consistent application of the option under which Member States may provide for special liability rules for non-established businesses. Therefore, depending on the Member State, reverse charge or registration apply for businesses making supplies in a Member State in which they are not established with considerable divergences on how the rules are applied across the EU. This has an impact on how deduction of input VAT can be exercised: in some Member States (where registration applies) VAT is recovered through local VAT returns yet in others (which apply reverse charge) VAT can only be recovered through a claim under the refund procedure. The latter has the potential to put the non-established supplier at a competitive disadvantage compared to domestic suppliers[305].

Proof of transport of intra-EU supplies of goods

There are no clear and uniform rules regarding the evidence to be provided by the supplier to justify the exemption of the intra-EU supply of goods. Documentation requirements instead depend on and vary within each Member State. The requirement for the supplier to provide proof where an intra-EU supply of goods is made under Ex-Works delivery terms[306], or where no third-party transport carrier is involved, can be particularly problematic.

The period throughout which businesses must ensure the storage of the VAT documentation attesting the transport also depends on each Member State which adds extra complexity.

VAT returns

The format, content and level of data to be included in the VAT returns diverge from one Member State to the other. For audit and/or statistical reasons, some Member States require extremely detailed VAT return content[307].

There are also differences in the time frame (tax period can be set by the Member States from one month up to a maximum of one year) and filing deadline[308].

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[305] Despite a recent comprehensive reform regarding cross-border VAT refunds for EU businesses (Directive 2008/9/EC and Implementing Regulation 79/2012), refund procedures are slow (and formalistic (input VAT incurred can be lost when certain formal requirements are not met) and can trigger audits by the tax authorities. This results in cash flow disadvantage due to refund situation when paying VAT on purchases and selling to customers in other Member States. There can also be problems with reclaiming pre-registration input VAT in a Member State where the business is not established. See for more information on https://ec.europa.eu/taxation_customs/business/vat/eu-vat-rules-topic/vat-refunds_en

[306] Ex Works (EXW) is an international trade term that describes an agreement under which the seller is required to make goods ready for pickup at his or her own place of business. All other transportation costs and risks are assumed by the buyer. In that case the supplier is not in charge of the transport and to prove the transport, he therefore has to rely on items of evidence provided to him by the buyer.

[307] The proposal for a standard VAT return (COM(2013) 721, 23.10.2013) represented an important area for simplification for businesses. However it did not meet unanimous agreement in Council by the Member States and was therefore withdrawn by the Commission.

[308] See box 6 above.

Recapitulative statements

The format, procedure and filing deadlines of these listings diverge from one Member State to the other[309].

Since the obligation to also submit a recapitulative statement for intra-EU acquisitions of goods results from an option left by EU legislation for the Member States to apply, there is no uniform application across the EU.

VAT audits

Audit is a matter that rest entirely in the hand of each individual Member State. This might imply the need for businesses to have a local tax representative.

Box 13: Divergences in the qualification of certain transactions and their VAT treatment

Consignment and call-off stocks

Some Member States provide simplification measures by which non-established businesses holding a stock of goods are allowed not to register for VAT purposes and not to declare any intra-EU acquisition in their territory.

This situation may give rise to problems where a trader established in a Member State which applies the simplification transfers goods to another Member State where no such simplification is applied. The trader, thinking in good faith that the simplification also applies in this later Member State, will neither get registered nor declare any intra-EU acquisition there, thus risking heavy penalties in that Member State.

Cross-border chain transactions

The problem with cross-border chain transactions is determining to which supply the intra-EU transport of the goods should be attributed.

The VAT Directive provides a simplification for certain cross-border chain transactions (known as "triangular transactions")[310] but the simplification is applied unevenly by Member States in particular in terms of assumptions made as to who is transporting the goods. In some Member States, the simplification can also be applied when more than three parties are involved. Further some Member States allow for the simplification to apply where the intermediate party is already registered in the Member State of the final customer while others do not.

VAT treatment/qualification of certain transactions

Some Member States treat supplies involving the installation of goods as a supply of goods, others as a supply of services. Such a divergence in the qualification of the transaction leads to differences in VAT treatment as the rules governing goods and

[309] See box 6 above.

[310] While as a rule businesses making taxable transactions in a Member State in which they are not established should register in this Member State and declare their transactions (and possibly pay VAT which could however be deducted), simplification measures aim at avoiding such registration.

services are not the same (e.g. different place of supply, VAT rates). This may lead to double or non-taxation. In case of double taxation, businesses might need to have recourse to local tax experts.

Another example of this type of situation is leasing, which is treated by some Member States as a supply of services and by others as a supply of goods. The result is double or non-taxation and such inconsistent treatment can be used for tax planning purposes[311].

Input tax deduction

Different rules on input tax deduction apply in the Member States (e.g. restrictions of the right to deduct, calculation of recoverable VAT for companies engaged both in transactions opening the right to deduct input VAT and in transactions which do not).

9. Selection of options

After the adoption of the 2011 Communication, the Commission services started technical discussions with Member States in the GFV and with other stakeholders in the VEG to identify possible options to achieve a simpler and more robust VAT system based on the principle of taxation at destination for B2B intra-EU supplies of goods.

When looking at possible options to tax B2B transactions at destination, two fundamental issues had to be considered, namely:

- the place of taxation (whether it will be based on the physical flow of the goods or not); and
- the person liable for payment of VAT (whether the supplier charges the VAT of the Member State of destination and pays the VAT via the One-Stop-Shop or if instead the customer accounts for the VAT through the reverse charge).

The various combinations of these two issues would lead to substantially different taxation regimes for intra-EU trade.

To carry out the work, the Commission services proposed a three-step working methodology which was adopted by both the GFV and the VEG. In particular:

The first step of this work was to make an inventory of the various options for taxation at destination, to identify their main possible advantages and disadvantages and to determine the criteria for a future comprehensive assessment of these options. To this end, the Commission services established a non-exhaustive preliminary list of eleven possible options each with their main features, advantages and disadvantages[312]. The following qualitative assessment criteria were suggested and agreed: (i) equality and simplicity; (ii) budgetary impact; (iii) ease of administration and cost of collection; and (iv) prevention of fraud and abuse.

311 Judgment of the CJEU of 22 December 2010 in case C-277/09 RBS Deutschland Holding.

312 Seven main options, four of which each has two variants, full details are available in working documents GFV N° 14 and VEG N° 4 B2B supplies of goods – Taxation at destination – Identifying options and criteria for a qualitative assessment, available here.

Two rounds of discussions took place in the GFV and the VEG during this phase. It was suggested that two other options be added to the initial list, resulting in an inventory of thirteen possible options[313] (Table 16 below).

[313] See working documents GFV N° 16 and VEG N° 5 B2B supplies of goods – Taxation at destination – Options – Examining how they work, and their pros and cons, and GFV N° 22 and VEG N° 13 B2B supplies of goods – Taxation at destination – Additional Option –Improvement of current rules for the option 13 improving the current rules without modifying them fundamentally.

Table 16: Inventory of possible options

Initial options	
No 1	Maintaining the status quo
No 2	Adapting current rules whilst still following the flow of the goods with the supplier charging the VAT of the Member State of destination
No 3	Adapting current rules whilst still following the flow of the goods with the reverse charge mechanism
No 4	Aligning with the rules governing B2C sales with the supplier charging the VAT of the Member State of destination
No 5	Aligning with the rules governing B2C sales with the reverse charge mechanism
No 6	Aligning with the rules governing the place of supply of services[314] with the supplier charging the VAT of the Member State of destination
No 7	Aligning with the rules governing the place of supply of services with the reverse charge mechanism
No 8	Aligning with the contractual flows with the supplier charging the VAT of the Member State of destination
No 9	Aligning with the contractual flows with the reverse charge mechanism
No 10	Viable Integrated VAT (VIVAT)
No 11	Compensating VAT (CVAT)
Additional options	
No 12	The Single European VAT Area (SEVA)
No 13	Improving the current rules without modifying them fundamentally

The second step of the working methodology consisted in refining the workings of the thirteen options identified during the first step and in further analysing their pros and cons with a view to preparing a selection of some of those options which deserved further analysis and for which the Commission would launch an external study to provide sufficient material for an impact assessment.

At the end of this phase, the Commission services asked both the GFV and the VEG to indicate the options which could already be put aside and the options which would merit further analysis. At that stage, the following first conclusions were drawn[315]:

- As regards the possible place of taxation at destination: following the physical flow of the goods remains a valid criterion to be used for determining the place of taxation for intra-EU B2B supplies of goods[316]. Nevertheless, in both groups there was sufficient interest in further exploring systems for which a different criterion would be used;
- As regards the person liable for the payment of VAT on intra-EU supplies: strong reservations were expressed about the charging of VAT by the supplier on intra-

[314] As well as with the place of supply of gas, electricity and heat or cooling to a taxable dealer (Article 38).

[315] See GFV N° 21 and VEG N°12: B2B supplies of goods – Taxation at destination – State of play of the discussions on the options.

[316] The physical flow of the goods remains a determining factor with options 1, 2, 3, 4, 5, 10, 11, 12 and 13. With options 6, 7, 8 and 9, the physical flow of the goods is no longer the driving force for determining the place of taxation for B2B supplies of goods.

EU supplies. However, a number of members expressed an interest in further pursuing options including this element. The Commission services took the view that it would be premature to put completely aside at this stage the idea of the supplier being the person liable for the tax given the restoration of the integrity of the EU VAT system and the consistency between cross-border and domestic transactions it could achieve;

- Options 4 and 5 could be discarded as they add further complexity to the current rules;
- Options 10, 11 and 12 could also be discarded[317].

During the third step, further technical discussions were held looking at the options where liability for the payment of the VAT would fall on the supplier, examining in particular the issues related to the functioning of a large One-Stop-Shop[318] and possible mitigation measures[319] to tackle some of the difficulties which could occur with these options.

In addition, the areas of priority where improvements of the current rules could be made were also identified, namely the (i) proof to justify the exemption of intra-EU supplies, (ii) the VAT treatment of chain transactions and (iii) the VAT treatment of consignment stocks. Following the request of many members in GFV and VEG, the Commission services created two sub-groups, composed of members from the VEG and the GFV, to examine the VAT treatment of consignment stocks and chain transactions. As regards the burden of proof to exempt intra-EU supplies, the EU VAT Forum[320] decided to create a mixed sub-group to examine that issue. All three sub-groups reported back with their recommendations to both the VEG and GFV[321].

On the basis of the outcome of these discussions, the Commission services proposed to put aside options 4, 5, 10, 11 and 12. This was agreed by the members of both the GFV and the VEG.

As regards the final selection of the options to be assessed in-depth in an external study, in addition to option 1 Maintaining the status quo, the following five options were selected:

[317] In the GFV there was no support for options 10 and 11 mainly because (i) they require the existence of a clearing mechanism as the VAT will be paid to the Member State of origin and deducted in the Member State of destination and (ii) also because adjustments will be needed in the Member State of destination where the VIVAT/CVAT rate, which will be common for all Member States to apply to intra-EU B2B supplies of goods, differs from the national rate of the Member State of destination. Option 12 was considered politically unacceptable as it will require the application of a harmonised set of tax rates in all 28 EU Member States. In the VEG, a large number of stakeholders took the view that these options should not be further examined, given that they are not politically acceptable for the Member States.

[318] See GFV N° 023 and VEG N° 14: B2B supplies of goods – Taxation at destination – One-Stop-Shop – Functioning & Possible issues.

[319] See GFV N° 028 and VEG N° 017: B2B supplies of goods – Taxation at destination – Options based on VAT being charged by the supplier – Mitigation measures.

[320] See Glossary.

[321] All these documents are publically available in CIRCABC, see
GFV N° 041 and VEG N° 027 Sub-Groups report – Proof of intra-EU supplies
GFV N° 039 and VEG N° 028 Sub-Groups report – Consignment stocks
GFV N° 040and VEG N° 029 Sub-Groups report – Chain transactions

- Option 2 – Adapting current rules whilst still following the flow of the goods with the supplier charging the VAT of the Member State of destination
- Option 3 – Adapting current rules whilst still following the flow of the goods with the reverse charge mechanism
- Option 7 – Aligning with the rules governing the place of supply of services with the reverse charge mechanism
- Option 8 – Aligning with the contractual flow with the supplier charging the VAT of the Member State of destination
- Option 13 – Improving the current rules without modifying them fundamentally

In the view of the Commission services, these options broadly cover the range of combinations resulting from the two fundamental issues that need to be addressed: the place of taxation (based on following the physical flow of the goods or not) and the person liable for payment of VAT (the supplier charges VAT or the customer accounts for it via reverse charge).

Moreover, the chosen options reflected to the extent possible the different views of the members of the GFV and the VEG and the need to concentrate on the most ambitious and promising options given the limited time and resources at hand. The requirement of continuing to follow the flow of the goods, an approach prioritised by most Member States, was met with options 1, 2, 3 and 13.

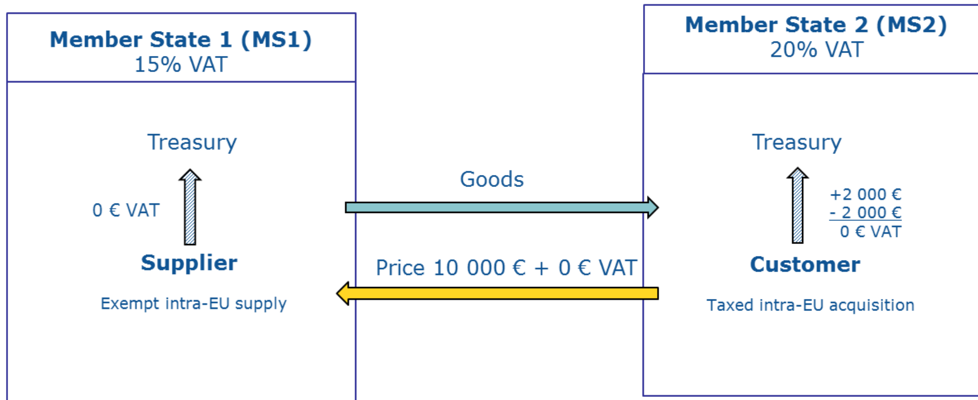
The possible extension of existing digital solutions (for instance by extending the current MOSS[322]) has in particular been taken into account.

In the selection of the options, care has been taken to ensure that simplification measures also target SMEs.

10. Diagrams of the options

[322] Since 2015, a mini One Stop Shop (MOSS) allows businesses supplying telecommunication services, television and radio broadcasting services and electronically supplied services to non-taxable persons in Member States in which they do not have an establishment to account for the VAT due on those supplies via a web-portal in the Member State in which they are identified. See further developments under Box 5 of the main report.

Diagram 1: Option 1 – ***Limited improvements of the current rules***

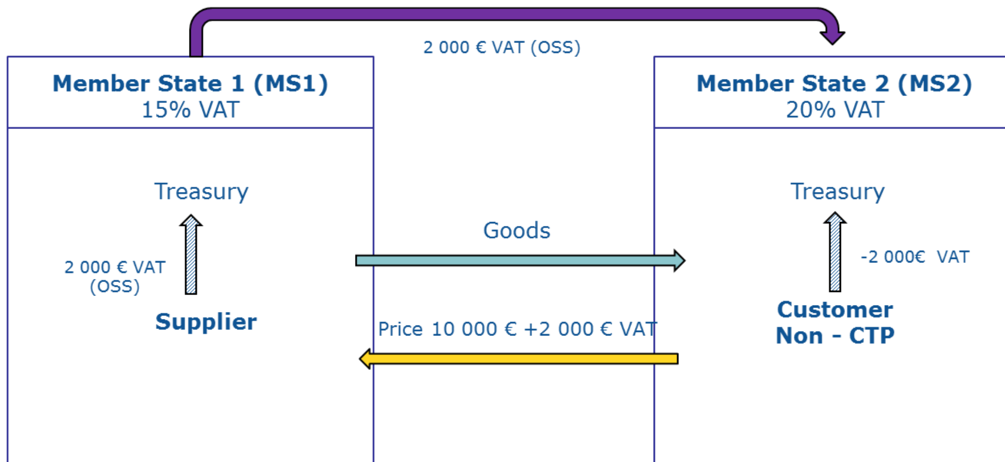


(1)Intra-EU supply in MS1
Place of taxation: Member State of departure of the goods = MS1
Person liable: Supplier, but no VAT is due because intra-EU supply is exempt (proof of transport necessary)

(2) Intra-EU acquisition in MS2
Place of taxation: Member State of arrival of the goods = MS2
Person liable for the payment of VAT: Customer via reverse charge in MS2. The VAT due (+2 000 €) is paid to Treasury of MS2 and simultaneously deducted (-2 000 €) using traditional VAT return

Diagram 2: Option 2 - ***Taxation following the flow of the goods***

Where the customer is NOT a Certified Taxable Person

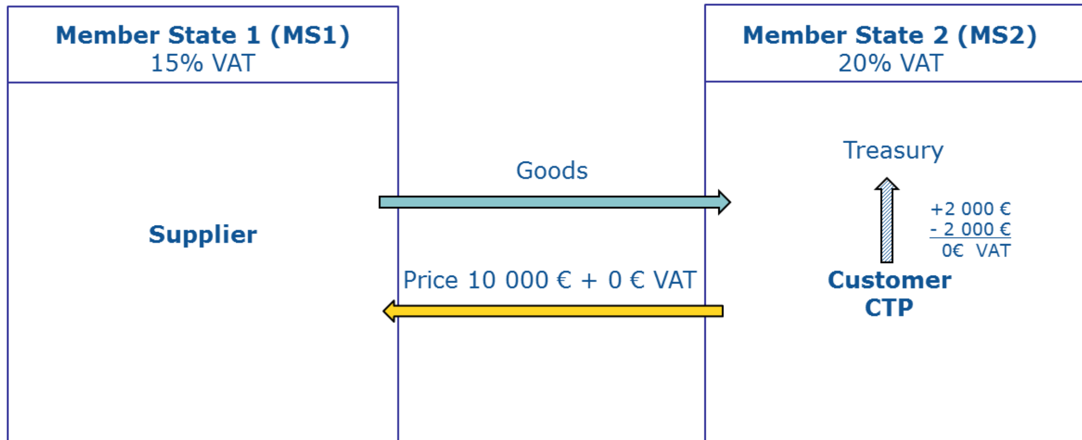


Place of taxation: Member State of arrival of the goods = MS2

Person liable for the payment of VAT: Supplier via OSS. The VAT due (+ 2 000 €) is paid to Treasury of MS1 and Treasury of MS1 remits the VAT due (+ 2 000 €) to Treasury of MS2. Customer deducts in MS2 (-2 000 €) using traditional VAT return

Diagram 3: Option 2 - *Taxation following the flow of the goods*

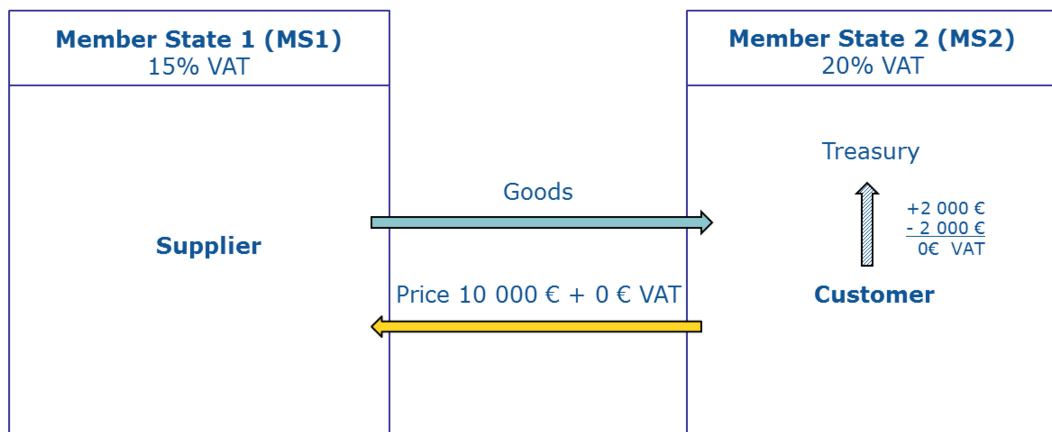
Where the customer is a Certified Taxable Person (CTP)



Place of taxation: Member State of arrival of the goods = MS2

Person liable for the payment of VAT: Customer CTP via reverse charge in MS2. The VAT due (+2 000 €) is paid to Treasury of MS2 and simultaneously deducted (- 2 000 €) using traditional VAT return

Diagram 4: Option 3 – *Reverse charge following the flow of goods*

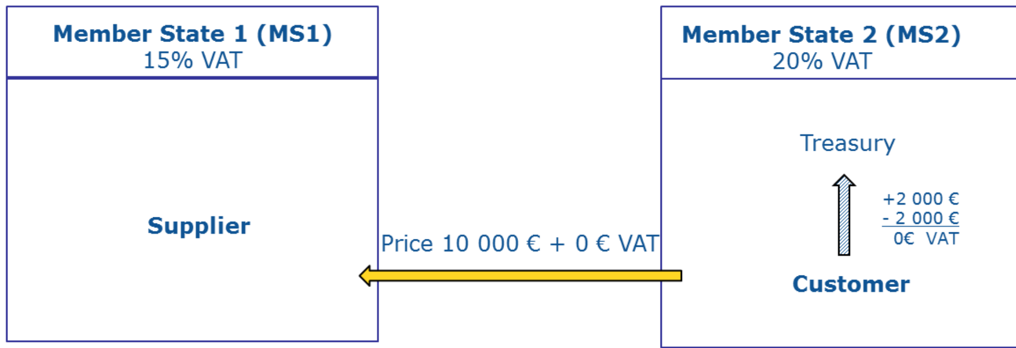


Place of taxation: Member State of arrival of the goods = MS2

Person liable for the payment of VAT: Customer via reverse charge in MS2. The VAT due (+2 000 €) is paid to Treasury of MS2 and simultaneously deducted (- 2 000 €) using traditional VAT return

Diagram 5: **Option 4 – *Alignment with the place of supply of services***

Where the goods are provided for the main place of business of the Customer

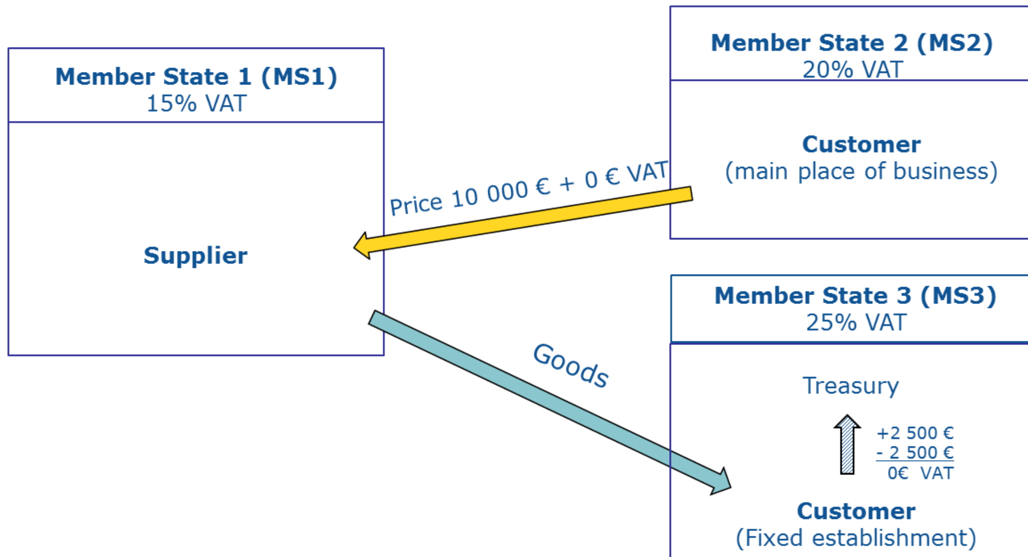


Place of taxation: Member State of main place of business of the Customer (whether or not goods are transported outside MS1) = MS2

Person liable for the payment of VAT: Customer via reverse charge in MS2. The VAT due (+2 000 €) is paid to Treasury of MS2 and simultaneously deducted (- 2 000 €) using traditional VAT return

Diagram 6: **Option 4 - *Alignment with the place of supply of services***

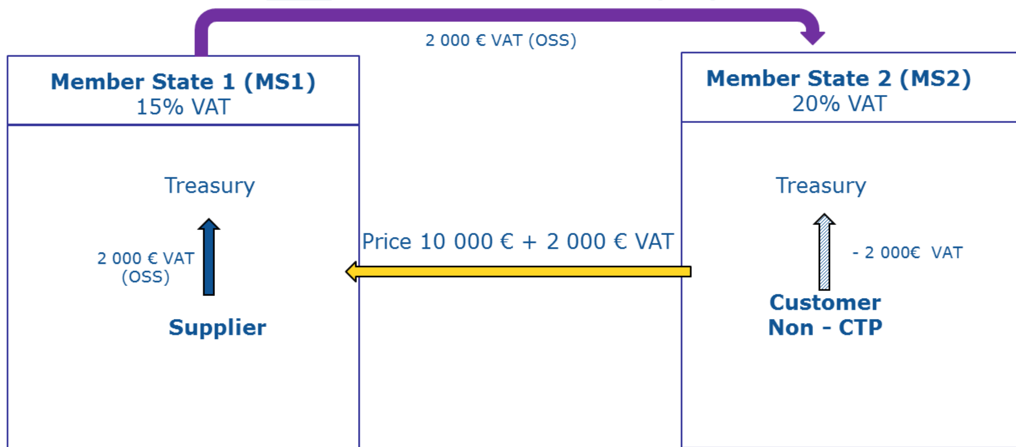
Where the goods are provided for the fixed establishment of the Customer



Place of taxation: Member State of fixed establishment of the Customer (whether or not goods are transported outside MS1) = MS3
Person liable for the payment of VAT: Customer via reverse charge in MS3. The VAT due (+2 500 €) is paid to Treasury of MS3 and simultaneously deducted (- 2 500 €) using traditional VAT return

Diagram 7: Option 5 – *Taxation following the contractual flow*

Where the customer is not a Certified Taxable Person (CTP)

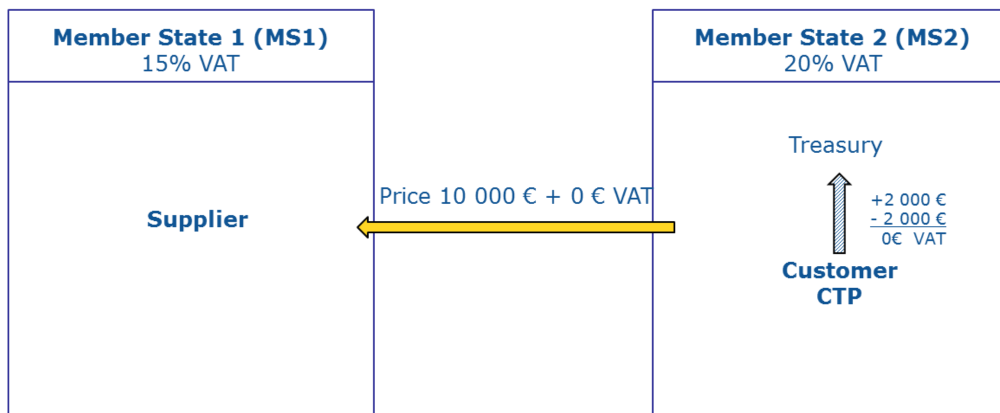


Place of taxation: Member State of Customer which has contracted the supply (whether or not goods are transported outside MS1) = MS2

Person liable for the payment of VAT: Supplier via OSS in MS1. The VAT due (+ 2 000 €) is paid to Treasury of MS1 and Treasury of MS1 remits the VAT due (+ 2 000 €) to Treasury of MS2. Customer deducts in MS2 (-2 000 €) using traditional VAT return

Diagram 8: Option 5 – *Taxation following the contractual flow*

Where the customer is a Certified Taxable Person (CTP)



Place of taxation: Member State of Customer which has contracted the supply (whether or not goods are transported outside MS1) = MS2

Person liable for the payment of VAT: Customer CTP via reverse charge in MS2, the VAT due (+2 000 €) is paid to Treasury of MS2 and simultaneously deducted (- 2 000 €) using traditional VAT return

11. Additional information on percentages of replies to public consultation per stakeholder group

Below information relates to the percentage of replies received from groups of stakeholders to questions from the public consultation (which took place between 20 December 2016 and 20 March 2017) that were referred to under Section 7.1 and Annex 2 (stakeholder consultation) of the impact assessment.

Information on all replies received from the groups of stakeholders are available publicly under the following https://ec.europa.eu/taxation_customs/consultations-get-involved/tax-consultations_en.

Question 15: Currently, domestic and intra-EU supplies of goods are treated differently for VAT purposes. Could this situation be discouraging/ encouraging for some businesses **to supply** goods cross-border?

Replies to Question 15 "the current situation is discouraging": 43% - SMEs, 43% - large businesses, 46% - business associations, 65% - tax advisors and academics, 80% - members of the public and 50%- public authority.

Question 17: Are there any additional compliance costs for business linked with the application of the VAT rules to intra-EU supplies of goods, as compared with domestic supplies of goods?

Replies "there are additional costs" to Question 17 : 95% - the whole business, 86% - SMEs, 100% - large businesses, 89% - business associations, 100% - tax advisors and academics, 100% - members of the public and 100%- public authority.

Question 19: Are small companies deterred from doing business cross-border because of additional compliance costs, if any, linked with the application of the VAT rules?

Replies to Question 19 confirming that small companies are currently deterred from doing business cross-border: 71% - the whole business, 71% - SMEs, 71% - large businesses , 78% - business associations, 94% - tax advisors and academics, 80% - members of the public and 100%- public authority.

Question 20: Do you agree that the current taxation system is not sufficiently resistant to VAT fraud within the EU?

Replies "strongly agree or agree" to Question 20: 67% - the whole business, 79% - SMEs, 64% - large businesses , 68% - business associations, tax advisors and academics - 94%, members of the public – 100% and 100% - public authority.

Question 21: Under the current system, VAT is normally charged by any taxable person making a taxable supply. There are, however, situations in certain sectors (or in relation to specific goods and services) where it is the customer who is obliged to account for and to pay the VAT (domestic reverse charge). Has the application of a reverse charge in certain sectors increased or reduced compliance costs for businesses operating in those sectors?

Replies "costs are reduced" to Question 21: 21% - the whole business, 14% - SMEs, 29% - large businesses, 38% - business associations, 24% - tax advisors and academics, 60% - members of the public, 50% - Member States.

Replies "costs are increased" to Question 21: 60% - the whole business, 50% - SMEs, 61% - large businesses, 51% - business associations, 53% - tax advisors and academics, 20% - members of the public, 50% - Member States.

Question 22: Is a reverse charge, as it has been used until now in certain sectors, an effective measure to combat tax fraud?

Replies "yes it is at least to certain extent" to Question 22: 60% - the whole business, 64% - SMEs, 68% - large businesses, 70% - business associations, 88% - tax advisors and academics 60% - members of the public, 100% - Member States.

Question 23: Is a VAT identification number provided by the customer in the context of an intra-EU supply, a reliable proof of his status as a taxable person?

Replies "yes the VAT number is a reliable proof" to Question 23: 92% - the whole business, 87% - SMEs, 93% - large businesses, 95% - business associations, 94% - tax advisors and academics, 80% - members of the public, 100% - Member States.

Question 24: Do you agree that in the case of an intra-EU supply, a lack of a valid VAT identification number of the customer should imply that the intra-EU supply should not be exempt in the Member State of departure?

Replies "strongly agree or agree" to Question 24: 63%, - the whole business, 86% - SMEs, 54% - large businesses, 32% - business associations, 76% - tax advisors and academics, 80% - members of the public, 50% - Member States.

Question 25: In general, the term "chain transactions" refers to the situation where the goods are supplied via intermediary suppliers and the goods are dispatched or transported directly form the first supplier to the final purchaser. Should the legislative improvements to the current transitional rules address VAT issues linked with chain transactions?

Replies "yes" to Question 25: 90% - the whole business, 79% - SMEs, 93% - large businesses, 68% - business association, 88% - tax advisors and academics, 88%, 80% - members of the public, 100% - Member States.

Question 26: Should the legislative improvements to the current transitional rules address issues linked with the proof required to demonstrate that the goods were moved from one Member State to another?

Replies "yes" to Question 26: 90% - the whole business, 79% - SMEs, 93% - large businesses, 68% - business associations, 82% - tax advisors and academics, 80% - members of the public, 50% - Member States.

Question 27: In general, the term "call-off stock" refers to the situation where the supplier moves his own goods from one Member State to another Member State where they are kept in a warehouse from which the (already known) customer may take them when he needs them. Should the legislative improvements to the current transitional rules address issues linked with call-off stock?

Replies "yes" to Question 27: 88% - the whole business, 71% - SMEs, 93% - large businesses, 54% - business associations, 82% - tax advisors and academics, 40% - members of the public, 100% - Member States.

Question 28: Under the reverse charge mechanism it is the customer who is obliged to account for and to pay the VAT. Do you think that an optional application by Member States of a generalised reverse charge on domestic transactions above a certain threshold per invoice would help in fighting tax fraud?

Replies "strongly agree or agree" to Question 28: 50% - the whole business, 64% - SMEs, 43% - large businesses, 24% - business associations, 41% - tax advisors and academics, 40% - members of the public, 0% - Member States.

Replies "strongly disagree or disagree" to Question 28: 38% - the whole business, 21% - SMEs, 46% - large businesses, 41% - business associations, 59% - tax advisors and academics, 40% - members of the public, 100% - Member States.

Question 29: Would the optional application by Member States of a generalised reverse charge on domestic transactions increase or reduce compliance costs to businesses?

Replies "costs will increase" to Question 29: 67% - the whole business, 43% - SMEs, 75% - large businesses, 54% - business associations, 53% - tax advisors and academics, 60% - members of the public, 100% - Member States.

Question 31: Currently, under the transitional VAT arrangements, intra-EU supplies of goods are, as a rule, exempt and intra-EU acquisitions are taxable. Do you agree that, under the definitive system, there should be only one taxed transaction i.e. a taxed intra-EU supply of goods as it is currently the case with the domestic supplies?

Replies "strongly agree or agree" to Question 31: 69% - the whole business, 64% - SMEs, 68% - large businesses, 62% - business associations, 94% - tax advisors and academics, 80% - members of the public, 50% - Member States.

Replies "strongly disagree or disagree" to Question 31: 23% - the whole business, 21% - SMEs, 25% - large businesses, 24% - business associations, 6% - tax advisors and academics, 20% - members of the public, 0% - Member States.

Question 32: Should the B2B intra-EU supplies of goods be taxed in the Member State where the goods arrive?

Replies "yes" to Question 32: 46% - the whole business, 64% - SMEs, 36% - large businesses, 54% - business associations, 76% - tax advisors and academics, 60% - members of the public, 50% - Member States.

Question 33: Should the B2B intra-EU supplies of goods be taxed in the Member State where the customer is located?

Replies "yes" to Question 33: 62% - the whole business, 57% - SMEs, 68% - large businesses, 32% - business associations, 35% - tax advisors and academics, 40% - members of the public, 50% - Member States.

Question 34: Who should be liable for the payment of the VAT due on B2B intra-EU supplies of goods?

Replies "the supplier" to Question 34: 43% - SMEs, 14% - large businesses, 11%, - business associations, 53% - tax advisors and academics, 4 0% - members of the public and 50% - public authority.

Replies "the customer" to Question 34: 50% - SMEs, 79% - large businesses, 54%, - business associations, 41% - tax advisors and academics, 60% - members of the public and 50% - public authority.

Question 35: Currently intra-EU supplies of goods are exempt in the Member State of departure and intra-EU acquisitions are taxable in the Member State of arrival. Will business compliance costs increase or be reduced as a result of the replacement of these two (separate from a legal point of view) transactions by only one taxable supply?

Replies "costs will be reduced" to Question 35: 64% - SMEs, 32% - large businesses , 30% - business associations, 94% - tax advisors and academics, 40% - members of the public and 50% - public authority.

Replies "costs will increase" to Question 35: 21% - SMEs, 29% - large businesses , 14% - business associations, 6% - tax advisors and academics, 0% - members of the public and 50% - public authority.

Replies "costs will not be affected" to Question 35: 14% - SMEs, 14% - large businesses , 24% - business associations, 0% - tax advisors and academics, 60% - members of the public and 0% - public authority.

No opinion on Question 35: 0% - SMEs, 25% - large businesses , 32% - business associations, 0% - tax advisors and academics, 0% - members of the public and 0% - public authority.

Question 36: Currently intra-EU supplies of goods are exempt in the Member State of departure and intra-EU acquisitions are taxable in the Member State of arrival. Will administrative/ procedural/ budgetary costs (burdens) increase or be reduced for Member States' tax administration as a result of taxation of intra-EU supplies?

Replies "costs will be reduced" to Question 36: 19% - the whole business, 21% - SMEs, 21% - large businesses, 14% - business associations, 59% - tax advisors and academics, 40% 0 members of the public, 0% - Member States.

No opinion on Question 36: 48% - the whole business, 50% - SMEs, 54% - large businesses, 73% - business associations, 29% - tax advisors and academics, 20% - members of the public, 100% - Member States.

Question 37: Do you think that taxation of B2B intra-EU supplies (which are currently exempt in the Member State of departure of the goods) will help fighting VAT fraud?

Replies "strongly agree or agree" to Question 37: 43% - SMEs, 39% - large businesses , 43% - business associations, 94% - tax advisors and academics, 80% - members of the public and 50% - public authority.

Replies "strongly disagree or disagree" to Question 37: 33% - the whole business, 21% - SMEs, 36% - large businesses, 24% - business associations, 6% - tax advisors and academics, 0% - members of the public, 50% - Member States.

Question 39: Do you think that under the definitive VAT system the MOSS should be extended to taxable intra-EU B2B supplies of goods (and in this way become a One Stop Shop (OSS), thus avoiding the need for the supplier to register in Member States where he is not established)?

Replies "strongly agree or agree" to Question 39: 64% - SMEs, 89% - large businesses , 70% - business associations, 88% - tax advisors and academics, 60% - members of the public and 100% - public authority.

Question 40: Do you think that if the OSS is extended to taxable intra-EU B2B supplies of goods it should allow not only for the payment of output VAT but also for the deduction of input VAT?

Replies "strongly agree or agree" to Question 40: 79% - SMEs, 100% - large businesses , 84%, - business associations, 82% - tax advisors and academics, 80% - members of the public and 50% - public authority.

Question 43: Would the introduction of the concept of CTP reduce or increase the compliance costs of suppliers?

Replies "costs will be reduced" to Question 43: 14% - SMEs, 32% - large businesses , 27% - business associations, 53% - tax advisors and academics, 20% - members of the public and 0% - public authority.

Replies "costs will increase" to Question 43: 43% - SMEs, 54% - large businesses , 51% - business associations, 41% - tax advisors and academics, 40% - members of the public and 0% - public authority.

Question 44: Do you think that the criteria for obtaining the CTP status should be laid down by each Member State or harmonized at EU level?

Replies "harmonized at EU level" to Question 44: 94% - the whole business, 93% - SMEs, 93% - large businesses, 68% - business associations, 76% - tax advisors and academics, 100% - members of the public, 100% - Member States.

Question 47: If CTP provisions were adopted, would you be interested in applying for CTP status?

Replies to Question 47 "I would be interested in applying for CTP status, regardless of the difficulty of the criteria that would have to be met": 7% - SMEs, 11% - large businesses, No answer 68%, - business associations, 12% - tax advisors and academics, 0% - members of the public and 0% - public authority.

Replies to Question 47" I would be interested in applying for CTP status if the criteria were not too burdensome": 71% - SMEs, 86% - large businesses , – No answer for 68%, - business associations, 35% - tax advisors and academics, 20% - members of the public and 0% - public authority.

Replies to Question 47 "I would not be interested in applying for CTP status, regardless of the difficulty of the criteria that would have to be met": 8% - the whole business, 21% - SMEs, 4% - large businesses, No answer 68% - business associations, 24% - tax advisors and academics, 40% - members of the public, 50% - Member States.

ANNEX 6: EVALUATION AND STUDIES TO SUPPORT THE IMPACT ASSESSMENT

6.1 Evaluation

A retrospective evaluation of the key elements of the EU VAT system was conducted by an external consultant in 2011 and its findings have been used as a starting point for the examination of the current VAT system. This evaluation was a comprehensive exercise that covered all important aspects for the design of an improved VAT system as identified in the Green Paper that launched a broad based consultation process with stakeholders on the functioning of the current EU VAT system and how it should be reframed in the future. The evaluation had been carried out before the Better Regulation Guidelines were put in place. This means in practice that the structure of the 2011 evaluation was not organized around the five evaluation criteria that became mandatory later on. Nevertheless, the evaluation provided solid analysis of the problems underlying the current transitional VAT system, the results of which have been confirmed by further consultation of stakeholders (see Annex 2) as well as recent studies (see below). It looked in particular into the design and implementation of the most important elements of the current VAT system, including the functioning of the transitional VAT arrangements, and assessed their effectiveness and efficiency in terms of results (meeting objectives they were serving) and impacts (direct, indirect, expected and unexpected) they had created. It also examined their relevance and coherence with the smooth functioning of the single market and the requirement to avoid distortion of competition specified in Article 113 of the Treaty on the Functioning of the European Union. The findings of the evaluation are therefore still valid and relevant for use in this impact assessment.

In addition to this, the Commission engaged an independent consultant to conduct a study of the five policy options designed to enable the implementation of a destination-based VAT system across the EU which was finalised in 2015. The purpose of this study was to assess the impacts of the five policy options from both a qualitative and a quantitative perspective. This study also looked at the baseline situation in order to facilitate comparison to the policy options, thus providing valuable information of the existing problems with the current system.

However, in order to facilitate the reading and understanding of the analysis of the 2011 evaluation report as well as the 2015 study, this annex sums up the main relevant findings and conclusions, in accordance with the main evaluation criteria defined by the Better Regulation Guidelines.

A. Relevance

VAT is a central plank of fiscal policy at both EU and national levels. All EU Member States must operate a VAT as a requirement for membership, and it raises large amounts of revenue in all of them. VAT is one of the main sources of government revenue in all EU Member States.

In 2009 it raised EUR 784 billion annually, 6.6% of the EU's GDP and 17.3% of all taxes raised. Across the EU as a whole, in 2015 VAT brought in EUR 1.032 billion of revenue, 7% of the EU's GDP and 17.6% of all taxes raised[323]. This increase alone shows that VAT continues to remain as relevant for the budget of EU Member States and the EU today as it was at the moment of the evaluation study.

[323] See Eurostat – Tax Revenue Statistics for a more detailed breakdown.

Uniquely among the major taxes, the framework rules for how VAT works are set out in common at the EU level in Council Directive 2006/112/EC of 28 November 2006 on the Common System of Value Added Tax – often known simply as 'the VAT Directive'– although some derogations from the common rules are in place for individual Member States, and many aspects of policy are left to Member States' discretion.

The external evaluators concluded that VAT has many desirable properties in principle and that these desirable properties are mostly displayed by the EU VAT system in practice as well. Despite the fact that there is much to be said in its favour, the common VAT system also has a number of weaknesses.

According to the evaluators this is, in part, because the economic environment in which VAT operates has changed a great deal since the main features of the regime were put in place (1967). The nature of business activities has evolved. International trade has expanded dramatically and internal frontiers within the single European market were abolished in January 1993. Technology has changed both how taxes can be operated and the nature of what is to be taxed. Over the last two decades, piecemeal policy responses have sought to improve the functioning of the VAT system in the face of these developments but have left many fundamental problems unaddressed. A more radical remodelling of the VAT system could address the significant limitations of the current system and allow VAT to fulfil its potential as the economically efficient tax it can, in principle, be.

B. Effectiveness

Broadly speaking, a destination-based VAT – one in which the VAT levied on goods and services depends on the country in which they are consumed – should not distort trade patterns within the single market, since goods are taxed at the same rate regardless of their origin. The original objective of the VAT Directive was to create an EU VAT system that ensures the highest degree of simplicity and neutrality. The evaluators analysed to what extent the objective has been met. Their conclusion was that there are 3 reasons which limit the extent to which the current VAT system can ensure the highest degree of simplicity and neutrality:

- There are exceptions to the application of the destination principle in the VAT system. These are a particular problem for B2C (business-to-consumer) trade in both goods and services, where (with certain exceptions such as for new motor vehicles) cross-border shopping, distance selling below the relevant distance selling thresholds, and some B2C services are taxed in the supplier's location rather than (as the destination principle demands) in the customer's location. However, such B2C trade is a relatively small part of trade, so the magnitude of the problem is not necessarily that large. Moreover, since 1 January 2015, the place of taxation of certain B2C transactions (telecommunications, television and radio broadcasting, and electronically supplied services) has been moved to the Member State of the customer and a recent proposal by the Commission[324] will further extend the destination principle to online supplies of goods.

[324] See further details here: https://ec.europa.eu/taxation_customs/business/vat/digital-single-market-modernising-vat-cross-border-ecommerce_en

- The costs to firms of complying with VAT obligations are higher when trading across borders than when trading domestically, creating a bias against cross-border trade. The evaluators' assessment is that this is likely to be a fairly significant problem, and that there could be potentially significant gains in trade and GDP if costs could be reduced, although research in this area is still at an early stage (partly because estimates of how compliance costs vary between domestic and cross-border transactions are limited). As an indicative example, the evaluators estimated how much trade would increase if costs equivalent to 1% of cross-border sales were abolished: intra-EU trade would increase by 4.3%, GDP by 0.4% and consumption by 0.3%. They also estimated how reductions in differences in VAT rules and procedures and VAT rates would affect cross-border trade and GDP. For instance, a 10% reduction in dissimilarities of rules and procedures ('obligations') is estimated to increase intra-EU trade by 3.7%, GDP by 0.4% and consumption by 0.3%.

- Where VAT paid on inputs is not recoverable, it will be built into the prices of traded goods, creating an incentive to source goods from one country rather than another

Available data do not generally allow for the quantification of the magnitude of these non-neutralities directly and reliably but the evaluators have strived to account for their effects on trade by estimating directly the relationship between VAT policy and trade patterns.

C. Efficiency

The analysis of this criterion has focused on two components of the VAT architecture: on the one hand the administrative and compliance costs that the system of collection entails on tax administrations and economic operators and on the other hand the types and levels of fraud which such a system can give rise to.

Administrative burden and compliance costs

There is a strong consensus in the literature that the costs to firms of complying with VAT obligations are higher when trading across borders than when trading domestically – though some of the reporting requirements associated with trade would be needed even in the absence of VAT itself. To date there is little convincing quantification of the compliance costs of doing business across borders, though indirect estimates of their effects on trade were discussed above.

The compliance costs of VAT are substantial according to most studies, but the range of estimates is extremely wide. Studies for the UK, Australia and New Zealand in the 1980s and 1990s reported compliance costs between 2 and 9 percent of VAT collected; more recent ones, applying the Standard Cost Model methodology, ranged from the low of 0.3 percent reported in a study of Denmark, to as high as 8 or even 25 percent of VAT collected, as shown in studies of Croatia and Slovenia. According to the 2015 study, the cost of compliance relating to cross border trade was 11% higher than the compliance costs associated with domestic transactions.

According to the 2011 report, the current arrangements for operating tax adjustments on transactions between Member States are more complex, and significantly different from VAT rules for purely internal transactions which opens up the possibility that the current

VAT system could act as a barrier to participation in the internal market, by smaller firms in particular. Differences in rules about how VAT is collected in different areas of cross-border trade (e.g. whether the origin or destination country's VAT rates should be used, and whether the seller or buyer should remit the tax) also increase complexity and compliance costs, and the simplifications in this regard are therefore welcome.

Fraud

Most VAT fraud is domestic, but cross-border trade is associated with particular forms of fraud, notably Missing Trader Intra-Community (MTIC) fraud. This arises because of the break in the VAT 'chain' (the collection of VAT in parts from traders throughout the supply chain) that occurs when supplies of goods from one Member State to another are zero-rated, combined with the abolition of fiscal border controls at which VAT was before 1993 levied on imports and now just self-assessed by the customer (without sufficient cooperation between revenue authorities in enforcement and audit procedures to substitute effectively the previous customs controls).

The complexity and variation in rules and procedures across Member States may also increase the risk of infringements or fraud when trading across borders: mistakes are more likely to be made when firms have to deal with multiple, potentially quite different sets of procedures, and the additional compliance costs involved may encourage non-compliance. The differences in the administration of VAT, a result of the subsidiarity principle, create opportunities for skilled evaders and makes cooperation between tax authorities more difficult.

While there are estimates of overall VAT gaps across the EU (in 2014 it amounted to 14,3 % or EUR 160 billion[325]), it is very difficult to estimate fraud associated with cross-border trade at the EU level. According to the 2015 study, based on a limited number of replies from Member States Tax Administrations, on average 20% of the overall VAT gap was considered to be due to MTIC fraud, while the weighted average (based on overall VAT gap proportion) is 24%. The rest of the VAT gap is attributed to losses of revenue due to domestic fraud and evasion, tax avoidance, bankruptcies, financial insolvencies, as well as miscalculations.

D. Coherence

The internal coherence of the VAT system is affected by the difference of treatment between that of services and that of goods. The VAT system was originally set up to deal with a traditional model of trade in physical goods, for which the notion of a trade transaction can generally be defined clearly in terms of the physical movement of the taxed commodities. Yet international trade in services has grown much more rapidly than trade in goods in recent decades, placing increasing strain on some aspects of current consumption tax legislation and procedures in the EU and elsewhere. Many of the problems that arose in the VAT treatment of traded services were solved by a change of their place of taxation according to the destination principle, i.e. from the place of the supplier to the place of consumption. However, the current taxation model for goods remains based on the logic of an origin-based VAT system, although taxing de facto at destination.

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As the VAT treatment of services is outside the scope of the current impact assessment report, the difference is not further addressed in the analysis.

As regards the coherence of the tax treatment between domestic and cross-border transactions, the 2015 study showed that the dissimilarity between one and the other is the main cause of the higher compliance costs for businesses trading cross-border compared to businesses trading only domestically (11% higher).

Further, as regards the coherence between the EU VAT rules and national rules, according to the 2015 study, the VAT experts in all 28 Member States considered that, in general, there were no significant differences between the EU Directive and the local VAT legislation. There were however certain areas where the Tax Authorities have applied the rules differently across the EU.

These principally relate to the following areas:

- the documents required in order to evidence a B2B (business-to-business) intra EU supply;
- the conditions that are required to be met in order for the simplified triangulation rule to apply;
- the treatment of chain transactions;
- the treatment of call-off and consignment stock.

The 2015 study analysed the solutions that would address the problems that stem from a dissimilar treatment of each of these areas. The current impact assessment report has integrated the results of this analysis into its conclusions.

E. EU added value

Although the EU-added value is a complex criterion to pin down, the external evaluators identified 3 main features of the current VAT system which have an impact on the efficiency, effectiveness and robustness of the current method of collecting VAT, in comparison with conceivable alternatives:

- **neutrality in relation to business purchasing decisions:** with the main exception of the financial services sector, the current method of collecting VAT ensures that businesses are indifferent to the rate of VAT on purchased inputs. As a result rather few resources are expended on contesting VAT on purchased inputs (for example through complex tax planning to minimise input VAT), and the VAT system does not distort business sourcing in the internal market.

- **certainty of revenue collection**: the principal issues have to do with the exposure of different VAT systems to opportunities for fraud, evasion and other forms of non-compliance. These opportunities will depend on the particular VAT mechanism - so that, for example, different arrangements for the taxation of transactions between Member States would be exposed to very different forms of fraud - and in the absence of detailed study of alternatives it is impossible to assess the relative vulnerability of the current system. One problem with the existing system of collection is the large volume of VAT refunds: it can exceed 40% of gross collection in many countries. The fact that firms can receive VAT refunds means that VAT fraud can lead to not only zero revenues from

transactions on which taxes are due: there may in fact be negative revenues. Whilst any invoice-based system of VAT will involve refunds (because there will always be some firms selling goods at a loss), two other features of the existing VAT system influence the number of refunds: the zero-rating of intra-EU supplies and exports and the reduced rates of VAT. This emphasises the link between the way VAT is collected (e.g. with many refunds) and the overall structure and operation of VAT: the issues are interrelated.

- **simplicity**. The EU VAT system offers Member States the scope to operate with relatively simple procedures, which limit the burden placed on taxpaying firms, and the costs of tax administration. For example, the current system allows non-collection from the smallest firms: issues of compliance are removed from these through the registration threshold which exempts smaller firms, for which the costs of operation may be out of proportion to the revenue raised. Other features of collection methods that simplify compliance for firms are for instance, allowing online filing and payments, and requiring less frequent returns.

National differences in VAT regimes can affect trade in the internal market by increasing the costs of border-crossing trade flows relative to domestic sales, e.g. through the need to familiarise and comply with different procedures by country. Such costs are likely to bear relatively heavily on small and medium-sized businesses which may only be trading small volumes, creating a real market-entry barrier and anti-SME bias in intra-European trade. They may also distort and complicate firms' decisions of whether to supply cross border or set up local subsidiaries, which is likely to be a particular problem for firms that organise complex trade networks in intermediate goods. Finally, VAT regime differences can affect consumers' decisions. Cross-border shopping and distance-selling mean that consumers can take advantage of lower rates of VAT in other countries, especially in border regions. And, more generally, exemptions and variation in VAT rates can affect what consumers buy by changing relative prices differently in different countries.

VAT policy could potentially have quite significant effects on trade patterns and the wider economy. The conclusion of the external evaluators was that harmonising procedures and limiting differences in VAT rates, and more generally reducing compliance costs, are goals that should be aimed at.

6.2. Studies

In the impact assessment, reference is made to the above evaluation and study as follows:

IFS et al., 2011, A retrospective evaluation of elements of the EU VAT system

EY, 2015, Implementing the 'destination principle' to intra-EU B2B supplies of goods

In addition to these two reports, the impact assessment draws on the following studies which have provided detailed analysis of the problems at stake and the possible ways forward. Reference is made to these studies in the impact assessment as follows:

PWC, 2012, Study on applying the current principle for the place of supply of B2B services to B2B supplies of goods, see link:

http://ec.europa.eu/taxation_customs/business/vat/vat-reports-published_en

CPB, 2013, Economic study on charging VAT on intra-EU supplies of goods and services, see link:

https://circabc.europa.eu/sd/a/60e05641-2653-4ac3-aca2-3060896aa6e3/33-ANN%20-%20Final%20report%20-%20Study%20on%20charging%20VAT%20on%20intra-EU%20supplies%20of%20goods%20and%20services%5B1%5D.pdf

PWC, 2013, Study on the feasibility and impact of a common EU standard VAT return
http://ec.europa.eu/taxation_customs/publications/studies-made-commission_en

CASE, 2013, Study to quantify and analyse the VAT Gap in the EU-27 Member States
http://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/common/publications/studies/vat-gap.pdf

CASE, 2016, Study and Reports on the VAT Gap in the EU-28 Member States
https://ec.europa.eu/taxation_customs/sites/taxation/files/2016-09_vat-gap-report_final.pdf