Common system of value added tax: special scheme for small enterprises

2018/0006(CNS) - 18/01/2018 - Legislative proposal

PURPOSE: to amend the current VAT rules with a view to reducing VAT costs for small businesses (SMEs).

PROPOSED ACT: Council Directive.

ROLE OF THE EUROPEAN PARLIAMENT: the Council adopts the act after consulting the European Parliament but without being obliged to follow the opinion of the European Parliament.

BACKGROUND: small businesses (SMEs) face proportionately higher VAT compliance costs than larger businesses. The VAT Directive (Council Directive 2006/112/EC) therefore lays down a number of provisions aimed at reducing the burden on SMEs dealing with VAT matters. In particular, it allows Member States to grant a VAT exemption to small businesses provided that they do not exceed a certain annual turnover, which varies from one country to another.

Despite the fact that Member States may exempt SMEs from VAT an option that is widely used SMEs continue to suffer from disproportionate VAT compliance costs due to how the SME exemption is designed. In particular, SMEs involved in cross-border trade cannot benefit from the SME exemption in Member States other than the one in which they are established

The current system has distortive effects on competition on both domestic and EU markets. This issue is set to worsen with the shift towards destination-based taxation under the proposed definitive VAT system; many SMEs may have to charge their customers VAT that differs from that of the Member State in which they are established.

As a follow-up to the 2016 VAT Action Plan, this review aims to create a modern, simplified SME scheme by reducing VAT compliance costs for SMEs both domestically and at EU level and reducing distortions of competition both domestically and at EU level.

IMPACT ASSESSMENT: the impact assessment for the proposal was considered by the Regulatory Scrutiny Board on 13 September 2017. The Board issued a positive opinion on the proposal together with some recommendations, which have been taken into account. The Commission considers that compliance costs for SMEs are expected to be reduced by 18 % under this initiative compared to the baseline scenario outlined in the impact assessment (EUR 56.1 billion per year, compared to EUR 68 billion per year at present). Cross-border trading activities by SMEs within the EU are also expected to increase by 13.5 %. It should also have a positive impact on both voluntary compliance and on business competitiveness.

CONTENT: the main provisions of the proposed amendment to the VAT Directive are as follows:

- define various concepts necessary for applying the provisions of the special scheme: the definition of "small enterprises" would cover all enterprises whose Union annual turnover in the single market is no higher than EUR 2 million;
- the possibility for Member States that decide to implement the SME exemption to set their threshold at the level that best reflects to their particular economic and legal context. The exemption will be available to all EU eligible businesses, whether or not established in the Member State where they carry out supplies subject to VAT;
- for any small enterprise able to avail itself of the exemption in a Member State where it is not established, two conditions must be met: (i) the enterprises annual turnover in that Member State should be below the exemption threshold applicable there; and (ii) its overall turnover in the single market (Union annual turnover) should not be higher than EUR 100 000;
- introducing a transition period for small enterprises making use of the SME exemption whose turnover exceeds the exemption threshold in a given year;
- define a set of simplified VAT obligations for non-exempt small enterprises. Such a set should include simplified registration, simplified record keeping and longer tax periods, which would result in less frequent filing of VAT returns. Non-exempt small enterprises should also be able to opt for the application of normal tax periods.

The amendments will only take effect once the definitive VAT system has been introduced.