
Submitted by HM Treasury on February 2018

SUBJECT MATTER

1. The Commission’s aim in this proposal is to help alleviate the VAT compliance cost borne by small businesses, update the small business exemption for destination based taxation, and reduce non-compliance and fraud.

2. The current small business exemption (the VAT registration threshold) only exempts businesses from VAT in the Member State in which they are established. For example, in the UK, only businesses established in the UK benefit from the small business exemption for businesses turning over £85,000 or under. Under the new proposal, the small business exemption thresholds that Member States apply will be extended to EU businesses that are supplying goods and services in that Member State, but are not established in that Member State.

3. Member States will be allowed to set their own national threshold, up to a new common upper limit of €85,000 (£75,415). Currently Member States are restricted by “stand still” provisions or by the terms of their accession treaty. The UK threshold is currently £85,000. Each Member State must enforce their own threshold, including for businesses established in other Member States. The proposal also allows for varying the threshold for registration for different business sectors based on objective criteria.

4. Under the proposal, businesses will be allowed to continue to benefit from the exemption if their turnover exceeds the relevant national threshold by 50% or less during a single calendar year. For example, in a Member State where the threshold is €40,000, a business would not be required to register in the first calendar year in which they exceed the threshold, providing in that calendar year their turnover remains at or below €60,000.

5. As well as these national thresholds, the proposal sets out a €100,000 (£88,723) registration threshold for Union turnover (i.e. for those businesses that make supplies in several Member States and exceed a total EU turnover of €100,000). Enforcing this threshold will be the obligation of the Member State in which the business is established.

6. This proposal introduces the concept of ‘small enterprises’, defined as businesses with a turnover up to €2,000,000 (£1,774,460). Small enterprises that do not benefit from the SME exemption will be able to benefit from simplification measures such as the option of filing of VAT returns covering a calendar year, not having to make interim payments, and simplified obligations relating to the storage of invoices. UK businesses can currently use the annual accounting scheme, which requires interim payments, if their turnover is below £1.35m.
7. Under this proposal Member States will no longer be allowed to offer graduated relief to small businesses.

8. The proposal will also mean that small enterprises that are exempt should have access to simplified registration, invoicing, accounting and reporting obligations. These are already available for exempt UK small enterprises.

SCRUTINY HISTORY

9. This proposal is referred to in the VAT action plan – ‘Towards a single EU VAT area – Time to decide’ (7687/16, COM(2016) 148 final), which was the subject of EM 37648. This was cleared from scrutiny by the EU Select Committee on 25/05/2016, and by the European Scrutiny Committee after a debate was held on 21/02/2016. It is also referred to in the follow up to the VAT action plan – ‘Towards a single EU VAT area – Time to act’ (COM(2017) 566 final), for which an EM was issued on 24/10/2017 and remains held under scrutiny by both committees.

MINISTERIAL RESPONSIBILITY

10. The Chancellor of the Exchequer has responsibility for United Kingdom policy on European Union monetary and economic issues. The Foreign and Commonwealth Secretary and the Secretary of State for Exiting the EU are responsible for overall United Kingdom policy towards the European Union.

INTEREST OF DEVOLVED ADMINISTRATIONS

11. VAT policy is a reserved matter under the UK’s devolution settlements and no devolved administration interests arise. The devolved administrations have therefore not been consulted in the preparation of this EM.

LEGAL AND PROCEDURAL ISSUES

i. Legal basis

12. Article 113 of the Treaty on the Functioning of the EU (TFEU)

13. The Justice and Home Affairs (SHA) opt-in is not a consideration.

   ii. European Parliament Procedure
14. The Special Legislative procedure applies.

   iii. Voting procedure

15. Unanimity
iv. Impact on United Kingdom Law

16. When agreed, the directive will need to be transposed into UK law

v. Application to Gibraltar

17. The directive does not apply to Gibraltar.

vi. Fundamental Rights analysis

18. None identified.

APPLICATION TO THE EUROPEAN ECONOMIC AREA

19. N/A

SUBSIDIARITY

20. The proposal makes changes relating to cross border transactions and which also ensure domestic and non-established EU businesses are subject to the same rules. The Government agrees that consistency of treatment is more likely to be achieved through action at EU level and that the proposal is accordingly justified under the principle of subsidiarity.

POLICY IMPLICATIONS

21. On 23 June, the EU referendum took place and the people of the United Kingdom voted to leave the European Union. Until exit negotiations are concluded, the UK remains a full member of the European Union and all the rights and obligations of EU membership remain in force. During this period the Government will continue to negotiate, implement and apply EU legislation. The outcome of these negotiations will determine what arrangements apply in relation to EU legislation in future once the UK has left the EU.

22. The Government welcomes proposals that reduce the burden placed on SMEs by the administration of VAT and that lessens any VAT threshold-related distortions. However, the Government is mindful of the interactions between EU legislation and the consultation on the design of the VAT registration threshold which the Chancellor announced at Autumn Budget 2017.

23. The Government understands that the proposal to allow non-established businesses also to benefit from the UK’s SME exemption should reduce the burden of VAT on small businesses. The Government sees the logic in the Commission’s suggestion that in a destination based EU VAT system a national SME exemption should apply to non-established businesses as well. Equally, the proposal would require changes to the Annual Accounting Scheme, and would require the UK to introduce simplified invoice storage for small enterprises. Whilst the Government recognises the merits of simplifying the VAT
obligations of small businesses, more work is needed to review the benefits of such changes.

24. There are compliance obligations placed on Member States by this proposal to monitor the level of supplies that businesses established in that Member State, make in other Member States. We also need to better understand the way Member States plan to operate some of the easements in this proposal.

25. The Government will also explore the principle of an EU wide threshold and will look at whether €100,000 (£88,723) is an appropriate amount.

26. On removing graduated relief in favour of a 50% 1 year buffer above the threshold, the UK does not apply a graduated relief currently. The Government's final view on this matter will once again be informed by the upcoming consultation.

CONSULTATION

27. The Commission conducted a public consultation between December 2016 and March 2017 which covered SMEs. The UK provided input to this consultation.

28. The Chancellor announced at Autumn Budget 2017 that the Government would consult on the design of the threshold.

IMPACT ASSESSMENT

29. The Commission has produced an impact assessment for this proposal. In it, they describe the benefits of the proposal as reducing compliance costs by up to 18%, increasing SME's cross border trading activity by about 13%, and having a long term positive revenue impact because of SME growth and increased voluntary compliance.

FINANCIAL IMPLICATIONS

30. The government is still considering the financial implications of this proposal which will inform its views in due course.

TIMETABLE

31. This proposal is not one identified by the Bulgarian presidency as one of their priorities and therefore it is likely to make slow progress.
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