



**European Commission: Green Paper on the future of VAT
Towards a simpler, more robust and efficient VAT system**

Response by the Low Incomes Tax Reform Group

1. Introduction

1.1. *About us*

- 1.1.1. The Low Incomes Tax Reform Group (LITRG) is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998 LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes.
- 1.1.2. The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT's primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

1.2. *General comments*

- 1.2.1. This short submission is supplementary to the response from our CIOT colleagues. We wish to highlight just two issues which impact on:
- low-income or vulnerable (for example, disabled or elderly) consumers – reforming VAT to remove or minimise reduced rates in favour of a single, standard rate

- certain individuals running businesses who might struggle with what could be considered unreasonable VAT compliance burdens imposed in individual Member States.

2. VAT reforms – impacts on consumers

- 2.1. There is a need for a holistic approach to the issue of reform. It is not sufficient to look only at the impact on taxable persons – one needs to look at the impact on consumers. In so doing, it is necessary to remember that VAT is a particularly regressive tax and it therefore impacts most on people with low, fixed incomes such as many pensioners and those living on state benefits. It is in this context that we look at question 20:

Q20. Would you prefer to have no reduced rates (or a very short list), which might enable Member States to apply a lower standard VAT rate? Or would you support a compulsory and uniformly applied reduced VAT rates list in the EU notably in order to address specific policy objectives as laid out in particular in 'Europe 2020'?

- 2.2. Moves to abolish both Member States' derogations from the main scheme of VAT and reduced rates in favour of standard-rating across most supplies of goods and services are likely to impact most on low-income households.
- 2.3. For example, the UK's domestic VAT law allows for zero-rating of basic foods and children's clothes and reduced rating of domestic fuel – all items which consume a large proportion of such households' budget. Furthermore, it currently allows disabled and elderly people to access certain goods or services at a zero or reduced rate. In our report published in 2007 '*VAT and disabled people – the case for removing the barriers*'¹, we examined some of the differences in VAT reliefs for disabled people in the UK in comparison with other selected Member States.
- 2.4. It could be argued that these examples and similar provisions in other Member States add to complexity in terms of the wider market. Moreover, because the same provisions are not available in every Member State, they could be said to create distortions and unfairness when viewed on a pan-European basis.
- 2.5. It could in fact be argued that there could be a better means of targeting aid to those who need it as problems arise in the current structure. For example, in the case of UK VAT reliefs for disabled people, the consumer is reliant on the trader applying the correct VAT treatment and is unable to obtain a refund from HM Revenue and Customs if the correct treatment is not given.

¹ See <http://www.litrg.org.uk/reports/2007/vat-and-disabled-people-the-case-for-removing-the-barriers>

- 2.6. Nevertheless, we would recommend that the existing systems are preserved until such time as detailed analysis and assessment of the impact of any move to remove or restrict such provisions has been carried out in Member States. We would further recommend that Member States compensate those groups of consumers most affected, through ring-fencing the estimated increase in VAT collected and redistributing those funds. One way of compensating would be via the benefits systems in each country.
- 2.7. We note that one potential impact of changing from the current system of exemptions to one of applying reduced rates of VAT would be to increase the number of persons required to be registered for VAT. That might result in a greater VAT take but it would potentially increase compliance costs both among the new taxpayers and the revenue authorities who would then need to have greater systems capacity to deal with the additional registrations.
- 2.8. Further, to the extent that any suppliers were entitled to claim exemption as a small business, for example a person providing care services, there would be no change in overall impact at all.

3. Reducing 'red tape' – administrative burdens

- 3.1. The Green Paper asks the following questions:

Q21. What are the main problems you have experienced with the current rules on VAT obligations?

Q22. What should be done at EU level to overcome these problems?

- 3.2. On compliance issues, the key issue is that Member States have just about *carte blanche* to do as they wish. Most of the problems reported are not a matter of EU law but domestic law.
- 3.3. One example of what we would regard as a disproportionate measure in the UK is what is called 'VAT Mandation'. This imposes a liability for all VAT taxable persons to submit electronic returns.
- 3.4. There is an exception for persons who have religious objections to using computers but none for others who find it difficult or even impossible to meet this requirement – for example people who have disabilities which prevent their doing so, and those who run businesses from remote areas or at low profit margins meaning that a reliable broadband internet connection is either unavailable or prohibitively expensive. While the provision is nominally permitted by article 250(1) of the Directive, we consider it is disproportionate to impose this requirement on such persons.
- 3.5. Indeed, we are aware of cases where this requirement has left individuals struggling to comply and even having to consider closing down otherwise viable businesses or services essential to rural communities. We also note that in his 'High Level Group of Independent Stakeholders on Administrative burdens' presentation entitled 'Implementation of the

sectoral reduction plan in the field of VAT', Rolf Diemer (Head of Unit 'VAT and other turnover taxes', DG TAXUD, European Commission) noted in relation to electronic invoicing that there needed to be a technology neutral approach – ie that Member States can not prescribe the use of any particular technology¹. While that was in the context of electronic invoicing, we believe the principle underlying the statement is that of proportionality. To prescribe the means by which a person must account for VAT, without taking into account the person's existing resources and capabilities, imposes an undue burden on the taxable person that detracts from the neutrality of the tax.

- 3.6. These issues need considering at European level, particularly as the Green Paper suggests that in future there could be increased reliance on such technology for VAT compliance, and particularly if contemplating standardising systems across Europe (see para 5.4.1 'Reviewing the way VAT is collected' referring to e-invoicing and centralised databases, for example).
- 3.7. Whilst the Green Paper says that, across Europe, 60% of people use the internet regularly and its usage is expected to increase, no figure is given for how many businesses across Europe use the internet for trading purposes and compliance with government regulations, including direct and indirect taxes. *Prima facie*, there could be at least 40% who do not use the internet at all, for whom it would be very difficult to keep up with such new proposals. Moreover, the statistics in each Member State could vary widely depending on their state of technological advancement. Further, it is necessary to distinguish between people who use the internet in a passive manner for basic browsing or social networking and people who have set up systems secure enough to be used to exchange sensitive data. If that is taken into account, we believe that the 60% would be very much reduced.
- 3.8. We therefore recommend that detailed consideration is given to these issues at European level before any advancements in the general scheme of VAT become reliant on electronic transactions. Also, the Commission should consider adopt more policies such as it did on invoicing, setting boundaries to prevent Members States going beyond what is strictly necessary to collect taxes.

LITRG

31 May 2011

¹ See page 6, http://ec.europa.eu/enterprise/policies/better-regulation/administrative-burdens/high-level-group/files/2010_05_20_presentation_vat_en.pdf