

Date
14 May 2008

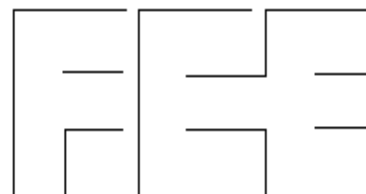
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European Commission's Consultation Paper on the review of existing legislation on VAT reduced rates (TAXUD/D1 D/24232)

FEE (Fédération des Experts Comptables Européens – Federation of European Accountants) represents 43 professional institutes of accountants and auditors from 32 countries, including all of the 27 EU Member States. With a combined membership of more than 500.000 professional accountants, FEE works in the public interest to contribute to a more efficient, transparent, and sustainable European economy.

FEE welcomes the opportunity to comment upon the European Commission's consultation paper on the review of existing legislation on VAT reduced rates (TAXUD/D1 D/24232) and encourages the initiative to review the present system of reduced VAT rates on the grounds of rationalisation, simplification and economic growth.

From this perspective, any extension of Member States' possibility to adopt reduced VAT rates on locally supplied services including labour intensive services, environmentally friendly and energy-saving goods and services as well as energy products should in our view, be carefully considered and for each reduction in rates the primary objective should be clearly indicated (e.g. growth or protection of the environment) as the rationale and the criteria for achieving the rate reductions will not be the same. We would suggest that before any generalised application of reduced rates is implemented that it should be determined on a case by case basis as to whether an alternative approach (e.g. a direct subsidy to the persons concerned) may not be more effective rather than a general reduction in VAT rates (as inevitably a reduction in rates generates a tax loss as high income earners also benefit from the tax reduction).

In particular, the following aspects should to be taken into account:

- Under the present system, the question as to whether a certain supply is subject to a reduced VAT rate or not has generated a number of Court cases at both national and European level, since the definition of such supplies is generally subject to different interpretation. Therefore, to prevent that the introduction of additional types of supplies subject to reduced VAT rates leads to an increased level of litigation and thus contradicts the aim of simplification, the definitions of the services covered and their scope would have to be well designed.
- The implementation of and the compliance with changed VAT rates and new reduced VAT rates may result in additional compliance cost for entrepreneurs. On the other hand cash flow savings (or cash flow costs) arising from reduced VAT rates could offset (or increase) such costs. These possible effects must, in our view, be thoroughly investigated and taken into account within an impact assessment procedure before implementation of any changes.

- The overall benefit from a reduced VAT rate in the end only remains if the reduction continues within the entire supply chain. The benefit ceases, however, in the case where the supply subject to a reduced VAT rate is used subsequently in the making of a standard rated supply because the following supplier can only deduct the reduced input VAT. Therefore, the impact on specific sectors, which should benefit from the additional reduced VAT rates, is a further point to be taken into account within the impact assessment procedure.
- In the case where a supply becomes subject to a reduced VAT rate after having formerly been subject to the standard rate, experience shows that the end-consumer does not generally benefit from the reduction – or perhaps only partially. An impact on increased consumption – and therefore a contribution to economic growth from this side – is, in our view, not obvious and should be further assessed.
- From a European perspective and with a view to completing the internal market and to simplifying compliance with VAT, a further harmonisation of the scope of the relevant VAT rates might be considered appropriate. This aim cannot be achieved by giving Member States the possibility to adopt reduced VAT rates at their discretion. Even if some of the reduced VAT rates would be limited to local supplies, an impact on the internal market may arise, in particular in border regions.
- The extension of reduced rates may lead to a reduction in VAT fraud as the incentives for the fraudsters to defraud the tax authorities of a lower amount of VAT (as the reduced rates are more widely applied) would be reduced. However, great care must be taken in this area as fraudsters are known to use reduced or “zero-rated” supplies of services to hide more complex VAT frauds. As a consequence we are concerned that the application of further reduced rates could increase the administrative burdens on tax authorities and on legitimate taxpayers in the fight against organised VAT fraud.

After due consideration, we believe that the potential economic impact of a modification of the present system of reduced VAT rates should be further assessed on the grounds of rationalisation, simplification and economic growth – by building on the study from Copenhagen Economics. Although we appreciate the rationale and the intended public policy goals behind such proposals, it seems difficult to form an informed view on its merits at this stage. In the case where an extension of the existing reduced VAT rates would be envisaged, the drafting of definitions would have to be carried out with proper care to ensure that the legislation is unambiguous and provides to taxpayers the level of legal certainty that they are entitled to expect. Only at this stage will it be possible to evaluate the possible shortcomings of these definitions and then to assess their impact and balance the pros and cons.

We would be pleased to discuss any aspect of this letter you may wish to raise with us and to contribute to any further work to be carried out by the Commission in this regard.



Jacques Potdevin
President