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EUROPEAN COMMISSION

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Proposal for a

COUNCIL DIRECTIVE

amending Directive 2006/112/EC on the common system of value added tax, with regard to the duration of the obligation to respect a minimum standard rate

(presented by the Commission)

EXPLANATORY MEMORANDUM

1. CONTEXT OF THE PROPOSAL

1. Article 97(1) of Directive 2006/112/EC of 28 November 2006 on the common system of value added tax[1] (hereinafter "the VAT Directive") provides that from 1 January 2006 until 31 December 2010 the standard rate may not be less than 15% and Article 97(2) stipulates that the Council shall decide, in accordance with Article 93 of the Treaty, on the level of the standard rate of value added tax (VAT) to be applied after 31 December 2010.

2. This provision was based on Article 93 of the Treaty establishing the European Community (the EC Treaty). As from 1 December 2009, Article 93 of the EC Treaty is replaced by Article 113 of the Treaty on the Functioning of the European Union (TFEU). Article 113 TFEU stipulates that 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 to the extent that such harmonisation is necessary to ensure the establishment and functioning of the internal market and to avoid distortion of competition.

3. With a view to establishing the internal market on 1 January 1993, the Commission presented proposals intended to set up a definitive system of tax harmonisation.

4. However, when it became clear that it would be impossible to adopt the Commission's proposals before 1 January 1993, the Council decided to adopt a transitional system. With regard to VAT rates, it adopted Directive 92/77/EEC[2].

5. That Directive introduced a system of minimum rates. It stipulated that from 1 January 1993 to 31 December 1996, the standard rate could not be set lower than 15%. This provision has been extended four times and applies until 31 December 2010.

6. To maintain the degree of harmonisation of rates already achieved, the Commission has twice presented proposals providing for a standard rate band with a minimum rate of 15% and a maximum rate of 25%[3]. The band was derived from the rates applied in practice in Member States, where standard rates have always varied between 15% and 25%.

7. In both cases, the proposals to approximate rates were amended by the Council,[4] which kept only the principle of a minimum rate, referring to a 15% minimum rate comparable to the system introduced by the 1992 Directive.

8. However, these Council Directives were adopted with a statement for the Council minutes mentioning Member States' efforts to avoid widening the 10 percentage point span between the lowest and highest rates applied. This demonstrates the continued concerns of Member States about distortions between high and low rate countries and the possible budgetary effects of different levels of VAT rates. In the light of the current economic crisis, there are

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[1] OJ L 347, 11.12.2006, p. 1.
[2] OJ L 316, 31.10.1992, p. 1.
[3] COM(95) 731 (OJ C 73, 13.3.1996, p. 22) and COM(98) 693 (OJ C 409, 30.12.1998, p. 13).
[4] Council Directive 96/95/EC of 20 December 1996 (OJ L 338, 28.12.1996, p. 89) and Council Directive 1999/49/EC of 25 May 1999 (OJ L 139, 2.6.1999, p. 27).

further arguments for keeping a minimum standard rate to be laid down in the VAT Directive.

9. Despite various improvements to the common VAT system based on the Commission's pragmatic, phased VAT strategy launched in 2000[5] and updated in 2003[6], the VAT system continues to suffer from shortcomings and high administrative burdens. This means it needs to be fundamentally reassessed. New economic realities, technological processes, fraud patterns etc. also give rise to new challenges. That is why the Commission plans to publish a consultative green paper soon on a new VAT strategy. This will launch a consultation on future tax harmonisation. Only in the light of the outcome of that process can an appropriate decision be taken on the level of standard rates of VAT in the EU.

10. Moreover, recent modifications to the VAT Directive[7] have favoured taxation at the place of consumption, as this results in fewer possibilities for cross-border transactions seeking lower VAT rates, leading to distortions of competition. However, it remains important to prevent growing divergence in standard VAT rates applied by Member States from leading to structural imbalances in the EU and distortions of competition in some sectors of activity. To this end, it is common practice in the field of indirect taxes, both for excise duties and VAT, to set minimum rates. Although no maximum rate is proposed, the span between the standard rates applied in the Member States can – as is currently the case – be expected to ensure the proper functioning of the internal market while acknowledging the possible need for new budgetary resources from consumption taxes.

11. The accession of new Member States on 1 May 2004 and on 1 January 2007 did not alter the situation regarding the standard rate. That still ranges from 15% to 25% in 27 Member States. Two Member States (Cyprus and Luxembourg) apply a 15% rate and three a 25% rate (Denmark, Hungary and Sweden).

12. In these circumstances, it therefore appears appropriate to maintain the principle of a minimum standard VAT rate of 15%, and to propose that the current arrangements be extended.

13. To give businesses necessary legal certainty, and allow further evaluation of the appropriate level of the standard VAT rate at EU level, it seems appropriate to extend the provision for another five years, while the Commission reflects on a new VAT strategy and re-examines the standard VAT rate appropriate for a common approach.

14. Since the application of the minimum standard rate under Article 97(1) of Directive 2006/112/EC expires on 31 December 2010, the object of this proposal is to enable the Council to extend the period during which this rate applies. The minimum standard VAT rate is therefore set at 15% for five years from 1 January 2011 to 31 December 2015. The Commission would also expect the Council to renew the statement for the minutes agreed earlier on the span between the lowest and highest rates applied for that same period.

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5 COM(2000) 348 final of 7.6.2000.

6 COM(2003) 614 final of 20.10.2003.

7 Council Directive 2008/8/EC of 12 February 2008 amending Directive 2006/112/EC as regards the place of supply of services (OJ L 44, 20.2.2008, p.11)

2. RESULTS OF CONSULTATIONS WITH THE INTERESTED PARTIES AND IMPACT ASSESSMENTS

Considering that no specific complaint was reported to the Commission concerning the rules on applying the standard VAT rate, there has been no need for consultation or external expertise.

The measure concerned purely aims to prolong the temporary provision concerning the length of time during which the current minimum standard VAT rate is to be applied. Such an extension simply maintains the current satisfactory situation concerning the standard VAT rate. It has a technical nature and thus does not require an impact assessment.

3. LEGAL ELEMENTS OF THE PROPOSAL

The Directive amends the VAT Directive. The legal basis is Article 113 of the Treaty on the Functioning of the European Union (TFEU).

- **Subsidiarity principle**

The subsidiarity principle applies insofar as the proposal does not fall under the exclusive competence of the European Union. The objectives of the proposal cannot be sufficiently achieved by the Member States for the following reasons:

The European Union has already laid down harmonised provisions on the application of VAT rates, in the VAT Directive. These provisions may only be amended or extended by a European Union act and Member State legislation cannot deviate from the harmonised rules.

Therefore, only European Union action can achieve the objectives of the proposal and ensure equal treatment of citizens in the European Union. The proposal therefore complies with the subsidiarity principle.

- **Proportionality principle**

The proposal complies with the proportionality principle for the following reasons:

The present proposal maintains the current situation, whereby Member States apply a standard VAT rate at a minimum of 15%.

Given that the proposal merely extends the period during which an existing provision applies, the measure is proportionate to the aim pursued. The proposal involves no financial cost to the European Union and no new financial burden is placed on businesses or on consumers.

- **Choice of instruments**

The proposed instrument is a Directive. No other means would be adequate, as this proposal modifies provisions concerning VAT rates already enacted in a Directive.

4. BUDGETARY IMPLICATION

The proposal has no implication for the European Union budget.

5. OPTIONAL ELEMENTS

Notes on the Articles

Article 1

Article 1 proposes that the current minimum standard rate of VAT in Member States, set at 15%, be extended from 1 January 2011 to 31 December 2015.

Articles 2 to 4

These Articles provide for the entry into force of the Directive.

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THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 113 thereof,

Having regard to the proposal from the European Commission,

After transmission of the draft legislative act to the national Parliaments,

Having regard to the opinion of the European Parliament[8],

Having regard to the opinion of the European Economic and Social Committee[9],

Acting in accordance with a special legislative procedure,

Whereas:

(1) Article 97 (1) of Directive 2006/112/EC of 28 November 2006 on the common system of value added tax[10] provides that from 1 January 2006 until 31 December 2010 the standard rate may not be less than 15%.

(2) The standard rate of value added tax (VAT) currently in force in Member States, combined with the mechanism of the transitional system has ensured that this system has functioned to an acceptable degree. With new rules on the place of supply of services which favour taxation at the place of consumption, the possibilities for exploiting differences in VAT rates through relocation have been limited further and potential distortions of competition reduced.

(3) To prevent growing divergence in standard VAT rates applied by Member States from leading to structural imbalances in the European Union and distortions of competition in some sectors of activity, it is common practice in the field of indirect taxes to set minimum rates. It is still necessary to do so for VAT.

(4) Pending the outcome of consultations on a new VAT strategy which is expected to address future arrangements and corresponding levels of harmonisation, it would be

8 OJ C […], […], p. […].
9 OJ C […], […], p. […].
10 OJ L 347, 11.12.2006, p. 1.

premature to set a permanent standard rate level or to consider changing the minimum rate level.

(5) It is therefore appropriate to maintain the current minimum standard rate at 15% for a further period long enough to ensure legal certainty, while allowing further review.

(6) This does not preclude a further revision of VAT legislation before 31 December 2015 to address the outcome of the new VAT strategy.

(7) Directive 2006/112/EC should therefore be amended accordingly,

HAS ADOPTED THIS DIRECTIVE:

Article 1

Article 97 of Directive 2006/112/EC is replaced by the following:

"Article 97

From 1 January 2011 until 31 December 2015, the standard rate may not be lower than 15 %."

Article 2

Transposition

1. Member States shall bring into force the laws, regulations and administrative provisions necessary to comply with this Directive by 1 January 2011 at the latest. They shall forthwith communicate to the Commission the text of those provisions and a correlation table between those provisions and this Directive.

When Member States adopt those provisions, they shall contain a reference to this Directive or be accompanied by such a reference on the occasion of their official publication. Member States shall determine how such reference is to be made.

2. Member States shall communicate to the Commission the text of the main provisions of national law which they adopt in the field covered by this Directive.

Article 3

Entry into force

This Directive shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

Article 4

Addressees

This Directive is addressed to the Member States.

Done at Brussels,

For the Council
The President