
EUROPEAN COMMISSION COMMUNICATION ON VAT FOCUSES ON FISCAL CONSOLIDATION EFFORTS

On 6 December 2011 the European Commission published the long awaited Communication on the future of VAT (COM 2011 851/3). While the Communication clearly recognises that non-profit organisations face a significant VAT burden, it does not propose any (new) solution to remedy this, other than calling on Member States to make use of existing options to alleviate the VAT burden on non-profit making organisations and to consider VAT refund schemes at the national level.

In concrete terms, with regard to irrevocable VAT costs paid on acquisitions the Communication suggests that Member States could draft targeted compensation mechanisms outside the VAT system. While such national mechanisms are among the potential solutions that the EFC has advocated for, the inclusion of this suggestion in the latest EC Communication clearly signals that the development of any EU level compensation mechanism through which foundations could recover input VAT, is off the table although this had been considered in the past by the Council of Ministers.

More worrying is the suggestion that Member States could generate more income by limiting the use of VAT reduced rates, which would imply that public-benefit foundations may have to provide services at a higher price. The Communication suggests that existing exemptions would /should be examined with the aim of broadening the tax base.

Current proposals do not worsen the situation of foundations, but the EFC and its members must remain vigilant in the coming months about the possible review of current reduced rates and exemptions granted to non-profit organisations and public bodies.

Summary of the Communication

The European Commission sees the review of VAT as part of its pro-business pro-growth strategy for Europe. " VAT is paid for by citizens, collected by businesses and accounts for over 20% of national revenues. It therefore has a significant impact on every single EU citizen. However, it is now 40 years since the EU VAT system was first set up, and the regime no longer fits with our service-driven, technology-based economy. The time has come for an ambitious VAT reform." said Algirdas Šemeta, Commissioner for Taxation, Customs, Anti-fraud and Audit. On this basis, the Commission has adopted the Communication on the future of VAT. The Communication sets out the fundamental characteristics that must form the basis of the new VAT regime, and priority actions needed to create a simpler, more efficient and more robust VAT system in the EU.

The Communication suggests three overriding objectives for the new VAT system:

- First, VAT should be made more workable for businesses. A simpler, more transparent VAT system would relieve businesses of considerable administrative burdens and encourage greater cross-border trade. Among the measures envisaged for a more business-friendly VAT are expanding the one-stop-shop approach for cross border transactions; standardising VAT declarations; and providing clear and easy access to the details of all national VAT regimes through a central web-portal.
- Second, VAT should be made more efficient in supporting Member States' fiscal consolidation efforts and sustainable economic growth. Broadening tax bases and limiting the use of reduced rates could generate new revenue for Member States without the need for rate increases. The standard VAT rate could even be reduced in some Member States, without any impact on revenue, if exemptions and reductions were removed. The Communication sets out the principles that should guide the review of exemptions and reduced rates. The Commission will also be analysing Member States' use of reduced rates and exemptions when reviewing their fiscal policies in the context of the European Semester (see [MEMO/11/11](#)).

- Third, the huge revenue losses that occur today due to uncollected VAT and fraud need to be stopped. It is estimated that around 12% of the total VAT which should be collected is not (the so-called “VAT Gap”). In 2012 the Commission will propose a quick reaction mechanism to ensure Member States can respond better to suspected fraud schemes. Furthermore, the Commission will see whether current anti-fraud mechanisms, such as Eurofisc, need to be strengthened and will explore the possibility of a cross-border audit team to facilitate multilateral controls.

Finally, the Commission has concluded that the long-standing question of changing to a VAT system based on taxation at origin is no longer relevant. Therefore, VAT will continue to be collected in the country of destination (i.e. where the customer is located).

Impact of suggested measures for public benefit foundations and EFC comments

As Action 10, the *“Communication calls on Member States to make use of existing options to alleviate VAT burden on non-profit making organisations”*. While this Action Point clearly recognises the existence of the VAT burden for public-benefit organisations including foundations, it puts the ball into the court of Member States and it does not suggest new solutions. The Communication suggests that *“those organisations already benefit from an exemption which covers their activities in the general interest. The residual activities not covered by this exemption are the only cause of concern. However, these activities could be covered by the general exemption scheme for small businesses that have a turnover below a certain threshold and through further simplification measures and procedures which Member States can introduce.”*

With regard to irrevocable VAT costs paid on acquisitions the Communication suggests that Member States could draft targeted compensation mechanisms outside the VAT system. While such national mechanisms are among the potential solutions that the EFC has advocated for, the inclusion of this suggestion in the latest EC Communication clearly signals that the development of any EU level compensation mechanism through which foundations could recover input VAT, is off the table.

At the same time, the European Commission is suggesting that Member States should limit the use of reduced rates and that existing exemptions will be reviewed with the overall aim of broadening the tax base, which would have a negative effect on those foundations currently providing services at lower than market rates or in exempt areas. The Communication suggests that *“exemptions which act as restrictions in the tax base and which might create distortions will be examined to see whether the economic, social or technical reasons for them are still valid and whether the way they are applied can be improved. In seeking to broaden the tax base, no options should be discarded at this stage.”* The EFC is concerned that the Communication could gradually lead to a withdrawal of existing exemptions and reduced rates, which would worsen the case for many public-benefit foundations. A removal of existing reduced rates and exemptions could signal a move in the direction of a full taxation model. The EFC would only support the idea of public-benefit foundations entering the VAT system, if it was optional for foundations to do so.

Background

On 1 December 2010, the Commission adopted a Green Paper on "The future of VAT – Towards a simpler, more robust and efficient VAT system". This Green Paper was followed by a six month public consultation in which the Commission received some 1,700 contributions from businesses, academics, citizens and tax authorities. The consultation ran until 31 May 2011 and the EFC and Donors and Foundations Networks in Europe (DAFNE) network, as well as the European Charities' Committee on VAT (ECCVAT), contributed to the consultation:

http://www.efc.be/EUAdvocacy/EFC%20Statements/2011_EFC_DAFNE_VATConsultationResponse.pdf

The Communication on the future of VAT itself can be found here:

http://ec.europa.eu/taxation_customs/resources/documents/taxation/vat/key_documents/communications/com_2011_851_en.pdf

A link to frequently asked questions is here:

<http://europa.eu/rapid/pressReleasesAction.do?reference=MEMO/11/874&format=HTML&aged=0&language=en&guiLanguage=en>

The link to the accompanying press release is:

<http://europa.eu/rapid/pressReleasesAction.do?reference=IP/11/1508&format=HTML&aged=0&language=en&guiLanguage=en>

Way forward

The EFC will continue to work closely with other public-benefit organisations across Europe through the European Charities' Committee on VAT (ECCVAT) to highlight the concerns of foundations about the current VAT regime and the suggested revisions to the system. Public-benefit organisations including foundations need to monitor carefully any developments that will make more goods and services VAT applicable. When it comes to overcoming input VAT costs, the ball is in the court of national governments to consider compensation schemes for public-benefit organisations.