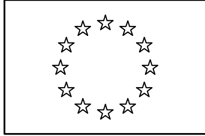

COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 14.12.2006
COM(2006) 802 final

Proposal for a

COUNCIL DECISION

authorising Estonia, Slovenia, Sweden and the United Kingdom to apply a special measure derogating from Article 17(1) of the Sixth Council Directive 77/388/EEC on the harmonization of the laws of the Member States relating to turnover taxes

(presented by the Commission)

EXPLANATORY MEMORANDUM

1) CONTEXT OF THE PROPOSAL

- **Grounds for and objectives of the proposal**

Pursuant to Article 27(1) of the Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes - Common system of value added tax: uniform basis of assessment, the Council, acting unanimously on a proposal from the Commission, may authorise any Member State to apply special measures for derogation from that Directive in order to simplify the procedure for charging the tax.

By letter registered with the Secretariat-General of the Commission on 26 January 2006, the United Kingdom requested an extension of an existing derogation from Article 17(1) of Directive 77/388/EEC. The derogation authorised the United Kingdom, to postpone the right of VAT deduction until it had been paid to the supplier.

By letters registered with the Secretariat-General of the Commission on 31 August 2006 from Estonia, on 27 June 2006 from Slovenia and on 6 April 2006 from Sweden, requests were made for a derogation from Article 17(1) of Directive 77/388/EEC to postpone the right of VAT deduction until it has been paid to the supplier.

In accordance with Article 27(2) of Directive 77/388/EEC, the Commission informed the other Member States by letter dated 6 October 2006 of the request made by Estonia, by letter dated 6 October 2006 of the request made by Slovenia, by letter dated 4 October 2006 of the request made by Sweden and by letter dated 6 October 2006 of the request made by the United Kingdom. By letter dated 6 October 2006 the Commission notified Sweden and by letter dated 9 October 2006 the Commission notified Estonia, Slovenia and the United Kingdom, that it had all the information it considered necessary for the appraisal of their request.

- **General context**

The United Kingdom has an optional simplified scheme (cash accounting) for taxable persons whose turnover does not exceed GBP 660 000 (approximately €964 000). Under this scheme, eligible taxable persons are permitted, pursuant to the third subparagraph of Article 10(2) of Directive 77/388/EEC, to defer payment of tax until receipt of payment. At the same time, and by way of derogation from Article 17(1) of Directive 77/388/EEC, input tax may not be deducted by the taxable persons that have opted for the simplified scheme until it has been paid to the supplier.

The United Kingdom obtained the authorisation to derogate from Article 17(1) of Directive 77/388/EEC on the basis of Council Decision 87/400/EEC. This Decision limited the use of the cash accounting scheme only to taxable persons of which the annual turnover was less than ECU 340 000. As the derogation was extended with Council Decisions 90/497/EEC, 93/111/EEC, 97/375/EC, 2000/435/EC and 2003/909/EC, also the turnover limit was gradually increased up to its current amount of GBP 660 000.

In the current request for derogation, the United Kingdom requested that the turnover

limit for the cash accounting scheme would be increased to GBP 1 350 000 (approximately €2 000 000). This would double the existing turnover limit.

According to the United Kingdom, the cash accounting scheme is part of a series of simplification measures which aim to aid small and medium sized businesses. The potential number of businesses entitled to use the cash accounting scheme is around 1 million and the number of companies who could derive benefit from the scheme is around 750 000. Of these businesses, 159 000 are actually using the scheme. The increase in the turnover limit would make an additional 57 000 companies eligible to use the scheme.

The current derogation is valid until 31 December 2006. The United Kingdom requested that an extension of the derogation be permitted until 31 December 2009.

The Commission considers that the request of the United Kingdom is acceptable both as to the increase of the turnover limit as well as to the duration of the derogation. The optional cash accounting scheme has been in use in the United Kingdom since 1 October 1987. The requested increase in the turnover limit does not bring any changes to the scheme.

Estonia, Slovenia and Sweden are also requesting a derogation from Article 17(1) of Directive 77/388/EEC for use with an optional simplified scheme (cash accounting). Like the United Kingdom scheme, eligible taxable persons would be permitted, pursuant to the third subparagraph of Article 10(2) of Directive 77/388/EEC, to defer payment of the tax until the receipt of payment. At the same time, and by way of derogation from Article 17(1) of Directive 77/388/EEC, input tax would not be deducted by the taxable persons that have opted for the simplified scheme until it has been paid to the supplier. The details of the scheme including the rules for admission and withdrawal, and the specific accounting requirements will be set by the Member States themselves.

For Slovenia the threshold would be set at 50 000 000 tolars (approximately €208 000). Of the 62 000 businesses that could opt to use the scheme, it is expected that about 1 000 would do so.

In the case of Sweden, the threshold would be set at SEK 3 000 000 (approximately €300 000). This would allow about 630 000 businesses to opt to use the scheme of which an estimated 60%, or 400 000 businesses, are likely to opt to use the scheme.

Both the Slovenian and Swedish derogation requests follow the existing United Kingdom derogation and its proposed renewal. As such, the Commission can support the derogation requests which aim to simplify the procedures for small businesses.

The rules for the optional simplified scheme (cash accounting) are not limited by a turnover threshold for Estonia. Its use is instead restricted to taxable persons classified under Estonian law as sole proprietors, of which there are approximately 5 700 registered for VAT. These businesses are allowed to declare their income for direct tax purposes under cash based accounting rules. It would, therefore, simplify accounting obligations for these businesses to be allowed to declare VAT on a cash basis as well. Given the small number of businesses to which the scheme will apply and the simplification benefits that it offers, the Commission can support this derogation

request.

- **Existing provisions in the area of the proposal**

Council Decision 97/375/EC of 9 June 1997 authorising the United Kingdom to apply an optional measure derogating from Article 17(1) of the Sixth Council Directive (77/388/EEC) on the harmonization of the laws of the Member States relating to turnover taxes. The Council Decision has been amended by Council Decisions 2000/435/EC of 29 June 2000 and 2003/909/EC of 22 December 2003 and expires on 31 December 2006.

- **Consistency with the other policies and objectives of the Union**

Not applicable.

2) CONSULTATION OF INTERESTED PARTIES AND IMPACT ASSESSMENT

- **Consultation of interested parties**

Not relevant.

- **Collection and use of expertise**

There was no need for external expertise.

- **Impact assessment**

The proposed Decision relates to simplification measures for the charging of VAT for small and medium sized businesses and will potentially improve the cash flow situation of the businesses concerned.

Impact will in any case be limited because of the narrow scope of the derogation.

3) LEGAL ELEMENTS OF THE PROPOSAL

- **Summary of the proposed action**

Authorisation for the United Kingdom to continue to derogate, and for Estonia, Slovenia and Sweden to be allowed to derogate, from Article 17(1) of the Sixth Council Directive 77/388/EEC in order to apply an optional cash accounting scheme under which a taxable person must postpone the VAT deduction until the goods or services have actually been paid to the supplier.

- **Legal basis**

Article 27(1) of the Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes - Common system of value added tax: uniform basis of assessment.

- **Subsidiarity principle**

The proposal falls under the exclusive competence of the Community. The subsidiarity

principle therefore does not apply.

- **Proportionality principle**

The proposal complies with the proportionality principle for the following reason(s).

This Decision concerns an authorisation granted to a Member State on their own request and does not constitute an obligation.

Given the limited scope of the derogation, the special measure is proportionate to the aim pursued.

- **Choice of instruments**

Proposed instruments: other.

Other means would not be adequate for the following reason(s).

Under Article 27 of the Sixth Council Directive 77/388/EEC on the harmonization of the laws of the Member States relating to turnover taxes, derogating from the common VAT rules is only possible on the authority of the Council acting unanimously on a proposal from the Commission. A Council Decision is the only suitable instrument since it can be addressed to an individual Member State.

4) BUDGETARY IMPLICATION

The proposal has no implication for the Community budget.

5) ADDITIONAL INFORMATION

- **Repeal of existing legislation**

The adoption of the proposal will lead to the repeal of existing legislation.

- **Review/revision/sunset clause**

The proposal includes a sunset clause.

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THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community,

Having regard to the Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment[1], and in particular Article 27(1) thereof,

Having regard to the proposal from the Commission[2],

Whereas:

(1) Council Decision 97/375/EC[3] authorises the United Kingdom, in accordance with the procedure laid down in Article 27 of Directive 77/388/EEC, to apply a special measure derogating from Article 17(1) of the said Directive in order to operate an optional scheme in which tax is accounted for on the basis of cash paid and received (cash accounting). Under that cash accounting scheme, the right of deduction of input VAT of taxable persons, who account for the output VAT for their supplies when they have received the payment of the price from their customers, pursuant to the second indent of the third subparagraph of Article 10(2) of the said Directive, may be postponed by the UK, by way of derogation from Article 17(1) of the said Directive, until the input VAT has been paid to the supplier.

(2) By letter registered by the Secretariat-General of the Commission on 26 January 2006, the United Kingdom requested an extension of three years of that derogation from Article 17(1) of Directive 77/388/EEC. The United Kingdom also requested for the turnover limit for the simplified cash accounting scheme to be increased from GBP 660 000 to GBP 1 350 000.

(3) By letter registered by the Secretariat-General of the Commission on 31 August 2006, Estonia requested a derogation from Article 17(1) of Directive 77/388/EEC to allow

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[1] OJ L 145, 13.6.1977, p. 1. Directive as last amended by Directive 2006/69/EC (OJ L 221, 12.8.2006, p. 9).

[2] OJ C , , p. .

[3] OJ L 158, 17.6.1997, p. 43. Decision as last amended by Decision 2003/909/EC (OJ L 342, 30.12.2003, p. 49)

the VAT to become deductible by the taxable person when the supplier is paid. This postponement of deduction will apply only under a simplified cash accounting scheme under which taxable persons account for the output VAT for their supplies when they have received payment from their customers, pursuant to the second indent of the third subparagraph of Article 10(2) of the said Directive. Estonia requested that the cash accounting scheme be limited to taxable persons classified as sole proprietors under Estonian law.

(4) By letter registered by the Secretariat-General of the Commission on 27 June 2006, Slovenia requested a derogation from Article 17(1) of Directive 77/388/EEC to allow the VAT to become deductible by the taxable person when the supplier is paid. This postponement of deduction will apply only under a simplified cash accounting scheme under which taxable persons account for the output VAT for their supplies when they have received payment from their customers, pursuant to the second indent of the third subparagraph of Article 10(2) of the said Directive. Slovenia requested that the turnover limit for their simplified cash accounting scheme be set at SIT 50 000 000.

(5) By letter registered by the Secretariat-General of the Commission on 6 April 2006, Sweden requested a derogation from Article 17(1) of Directive 77/388/EEC to allow the VAT to become deductible by the taxable person when the supplier is paid. This postponement of deduction will apply only under a simplified cash accounting scheme under which taxable persons account for the output VAT for their supplies when they have received payment from their customers, pursuant to the second indent of the third subparagraph of Article 10(2) of the said Directive. Sweden requested that the turnover limit for their simplified cash accounting scheme be set at SEK 3 000 000.

(6) In accordance with Article 27(2) of Directive 77/388/EEC, the Commission informed the other Member States by letter dated 6 October 2006 of the request made by Estonia, by letter dated 6 October 2006 of the request made by Slovenia, by letter dated 4 October 2006 of the request made by Sweden and by letter dated 6 October 2006 of the request made by the United Kingdom. By letter dated 6 October 2006 the Commission notified Sweden and by letters dated 9 October 2006 the Commission notified Estonia, Slovenia and the United Kingdom, that it had all the information it considered necessary for the appraisal of their request.

(7) The cash accounting scheme is a simplification measure for small and medium sized businesses. Regarding the United Kingdom, raising the ceiling for the simplified scheme will allow a greater number of firms to opt for the scheme. The increase of the turnover limit would extend the scheme to a potential additional 57 000 businesses. The derogation requested by Estonia will allow 5 700 businesses to use the cash accounting scheme. In the case of Slovenia, 62 000 businesses will be able to opt for the use of the cash accounting scheme. As for Sweden, the scheme will be available to 630 000 businesses.

(8) The Estonian, Slovenian, Swedish and United Kingdom derogations can be accepted in view of the percentage of eligible businesses that could opt for this simplified scheme and the limited duration.

(9) The derogation in question does not affect the overall amount of the tax revenue of the Member States collected at the stage of final consumption and as a consequence does

not have a negative effect on the own resources of the European Communities accruing from VAT.

HAS ADOPTED THIS DECISION:

Article 1

By way of derogation from Article 17(1) of the Sixth Council Directive (77/388/EEC), Estonia, Slovenia, Sweden and the United Kingdom are authorised to postpone the right of deduction of the input tax of the taxable persons, as defined in the second paragraph, until the input tax has been paid to their suppliers.

The taxable persons concerned must use a scheme whereby they account for the output VAT for their supplies when they have received the payments from their customers. They must have an annual turnover not higher than SIT 50 000 000 for Slovenia, SEK 3 000 000 for Sweden and GBP 1 350 000 for the United Kingdom, or, in the case of Estonia, must be registered as a sole proprietor.

Article 2

Decision 97/375/EC is repealed.

Article 3

This Decision shall expire on 31 December 2009.

Article 4

This Decision is addressed to the Republic of Estonia, the Republic of Slovenia, the Kingdom of Sweden and the United Kingdom of Great Britain and Northern Ireland.

Done at Brussels,

For the Council
The President