European Commission’s New Package of Proposals on E-Commerce: A Critical Assessment

It is with great enthusiasm that the European Commission released a new package of proposals towards a modernization of VAT for e-commerce. The European Commission announced nothing less than a astronomical revenue for the Member States and a major drop in compliance and administrative costs. Against this background, the author in this article proposes a systematic analysis of the new proposals and concludes that the reality might be much different from the “success story” being told by the European Commission.

1. Introduction

On 1 December 2016 the European Commission released three new proposals towards a “modernisation of VAT for cross-border B2C e-commerce”. The first proposes amendments to the VAT Directive¹ (Proposal 2016/757);² the second proposes amendments to the Implementing Regulation 282/2011 (Proposal 2016/756)³ and the third proposes amendments to the amending Regulation 904/2010 on administrative cooperation and combating fraud in the field of VAT (Proposal 2016/755).⁴ This package of proposals (altogether “the proposal”) covers e-commerce in a wide sense, including electronically supplied services (see section 2.), distance sales (see section 3.) and imports of low-value goods up to EUR 150 (see section 4.).

This article seeks to offer a critical analysis of the proposal, which comes less than 2 years after the entry into effect of the new rules for business to consumer (B2C) supplies of electronically supplied services. It concludes, on the one hand, that what the European Commission proposes regarding electronically supplied services and distance sales would constitute positive developments for businesses, albeit that it would represent a risk for the Member States and would not settle the efficiency and effectiveness flaws of the current legislation of concern to non-EU businesses. On the other hand, it also concludes that the proposals made in relation to imports of low-value goods, first, create discrimination between EU and non-EU taxable persons, and also between small and large non-EU taxable persons; second, again raise major questions of efficiency and effectiveness and; third, put a major additional burden on the transport sector with potentially detrimental consequences for consumers and businesses alike (see section 5.).

2. Electronically Supplied Services

2.1. The current situation

2.1.1. The 2003 rules: A mix of origin and destination-based taxation and a Mini One-Stop Shop to streamline compliance by non-EU taxable persons

Electronically supplied services have been the focus of the e-commerce VAT policy of the European Union since the early 2000s. As early as in 2003, the European Union acted as a pioneer by adopting specific rules for these supplies in line with the 1998 OECD Ottawa Framework for e-commerce transactions.⁵ In a nutshell, the 2003 rules provided for the taxation of B2C intra-EU supplies at origin while all other supplies, i.e. intra-EU business to business (B2B) and both B2B and B2C inbound supplies,⁶ became taxable at destination.

As regards tax collection, a reverse charge system became applicable for intra-EU B2B supplies while a One-Stop Shop was introduced allowing non-EU taxable persons to register once in the European Union (in the so-called “Member State of identification”) and to declare and pay the VAT related to all their supplies of electronically supplied services made to EU final customers through the Member State of identification via “single” periodical returns. The Member State of identification was then required to redistribute the revenue among the different “Member States of consumption”.⁷ Unfortunately, the

⁶. That is, provided by a non-EU taxable person to an EU taxable or non-taxable customer.

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number of registration has been extremely low: only 539 businesses were registered under the One-Stop Shop in January 2014 (thus 11 years after the scheme had been put into place). This was a slight increase as compared to the end of 2011, when 453 businesses had registered. It is striking, however, that the total amount of VAT collected through the One-Stop Shop scheme for the period January-December 2011 was EUR 96,965,304.04 which went down to EUR 92,450,909.07 for the period January-December 2014. The main reason for these low figures is that EU Member States have no enforcement jurisdiction beyond their borders and therefore cannot verify the declarations made by non-EU taxable persons. These figures, which are thus the outcome of a 12 years real life test of the One-Stop Shop system, show that a vendor registration system for electronically supplied services scores quite poorly in terms of effectiveness in an inbound scenario. In fact, the only way to increase effectiveness would be to adopt instruments of international cooperation in the form of both exchange of information and assistance in tax recovery with all countries around the world, which does not seem very realistic.

2.1.2. The 2015 rules: Destination-based rules for all with new guidelines for customer location and identification and a MOSS for EU and non-EU taxable persons

All supplies taxed at destination

In 2008, the EU Member States decided to tax all supplies of electronically supplied services at destination as of 2015. This decision was meant to level the playing field between EU and non-EU taxable persons (subject to different compliance burdens because an origin-based taxation means applying home country rules while a destination-based taxation means dealing with many different rules depending on the state of destination) but also to remove the distortions that the origin-based taxation of intra-EU B2C supplies had created (because under these rules, businesses located in a low VAT Member State were able to offer lower prices to EU final customers. This created an incentive for businesses to get established in such low VAT Member States and for customers to buy from taxable persons located in these low VAT Member States). Since 2015, EU taxable persons thus also have to charge and collect VAT at destination.

An EU and a non-EU MOSS

EU taxable persons were also offered the possibility of a single registration through a One-Stop Shop procedure. A “Union Scheme” and a “Non-Union Scheme” is now available (altogether referred to as the “Mini One-Stop Shop” or MOSS which also covers telecommunications and broadcasting services), respectively for EU and non-EU taxable persons. Current figures show that the number of registrations of EU taxable persons is much higher than it is for non-EU taxable persons: 12,900 registrations in the EU scheme and slightly below 1,100 in the non-EU scheme by the middle of 2016 (where an increase in the number of registrations is thus also occurring). This difference in the number of registrations by EU and non-EU taxable persons can be explained by the greater possibility for Member States to enforce the registration requirement over EU taxable persons, in view of the existence of instruments of cooperation between the Member States. EU taxable persons are therefore more likely to be compliant. Moreover, for EU taxable persons, the MOSS registration is made in their Member State of establishment, which is always simpler than to register in a foreign country. In contrast, and if a vendor registration system may thus prove effective in a domestic or in an intra-EU scenario, the still quite low number of registrations by non-EU taxable persons (even after the massive information campaign carried out by the European Commission) confirms the ineffectiveness of a vendor registration system in an inbound scenario. This creates an unlevel playing field between EU and non-EU taxable persons. This is why the European Commission on page 2 of Proposal 2016/757 clearly states that:

There are in essence three reasons to act: (…) the current system is not neutral as EU businesses are at a clear disadvantage to non-EU businesses which can legitimately and through high levels of non-compliance make VAT-free supplies into the EU. Given that VAT rates can be as high as 27%, there is a substantial distortion in favour of non-EU business if VAT is not applied (…).

High setting up costs probably also have an impact on compliance (in particular for non-EU taxable persons, which are outside jurisdictional reach of the EU Member States). The final version of the impact assessment accompanying Proposal 2016/757 (the Impact Assessment) does not seem very realistic.

8. Most of them in the United Kingdom (266), the Netherlands (111), Germany (43), Ireland (43) and Luxembourg (28). Only 15 had registered in France, 14 in Italy, 8 in Sweden, 4 in Malta, 3 in Denmark, 2 in Spain, 1 in Belgium, Bulgaria, Cyprus and Greece, and none in Austria, the Czech Republic, Croatia, Estonia, Finland, Hungary, Latvia, Lithuania, Poland, Portugal, Romania, and Slovakia (figures communicated by the UK Treasury in Mar. 2012).
9. Most of them in the United Kingdom (207), the Netherlands (83), Luxembourg (65), Germany (36), Ireland (25) and Italy (14). There were only 8 registrations in France, 5 in Sweden and 3 in Denmark, 2 in Spain, 1 in Belgium, Bulgaria, Cyprus, Greece and Malta and none in Austria, the Czech Republic, Estonia, Finland, Hungary, Latvia, Lithuania, Poland, Portugal, Romania, and Slovakia (figures communicated by the UK Treasury in Jan. 2014).
New rules for customers’ identification and location

With effect from 2015, the Member States also adopted new rules for the identification and location of EU customers. A destination-based system indeed implies that taxable persons are able to identify (i.e. confirm the taxable or non-taxable status) and locate (i.e. identify the taxing jurisdiction) their customers on a transaction basis. The fact is that this requirement is often difficult to achieve in the case of electronically supplied services, which are made remotely, in a fully automated way and 24/7. The system in application since 2015 is based on “presumptions for customer location”. A number of presumptions could in principle apply but in practice the presumption that is most likely to apply requires from the taxable person that he collects two pieces of non-contradictory evidence to determine the location of the customer (including, for example, an IP address, a billing address, a credit card number or any other element that would allow determination of the residence of the customer). As to customer identification, the absence of a verifiable VAT registration number is sufficient to conclude that the customer is a non-taxable person. In spite of their apparent simplicity, these rules actually raise all sorts of difficulties so that the European Commission felt the need to publish 92 pages of explanatory notes. However, these notes are not binding and still do not offer the legal certainty to which taxable persons are entitled, essentially because the location rules assume that taxable persons are able to proceed to real time verifications and arbitrages (e.g. taking a decision if the IP address and the billing address are different. It also appeared that payment details may not always be available to the taxable person before the payment has been made, i.e. at the moment he needs them to calculate the tax). As regards identification rules, it may sound simple to offer the possibility to deny taxable status to a customer in the absence of a real-time verifiable VAT number. However, in practice it is inconvenient for the taxable person who will undoubtedly lose the client if unable to prove its taxable status for any reason such as the absence of its VAT number in the VIES database (which for some Member States only contains VAT numbers of those making intra-Community supplies). A taxable customer would be entitled to a VAT-free supply (with VAT to be paid by the customer under the reverse charge mechanism) and would not be able to recover the VAT he would be charged if treated as a non-taxable person. Another major flaw is that providing a valid VAT number is not difficult, however, the question arises as to how the taxable persons can verify that the VAT number actually belongs to the customer (cross-verification may not always be possible, either because the VIES does not always show an address or because the name may appear differently and verifications must be automated). In view of the above, it is not surprising that the European Commission itself acknowledges on page 5 of Proposal 2016/757 that: “the concerns raised during the consultation process by businesses and business associations, including small and medium enterprises, mainly relate to the 2015 place of supply rules and application of the MOSS for the services concerned”. A last element is that the Member States of consumption remain competent to audit the taxable persons (and not the Member States of identification). Therefore, taxable persons may be confronted with different expectations in terms of compliance. The Commission tried but failed to convince the Member States to adopt a standard audit file, potentially further increasing compliance costs and legal uncertainty for businesses.

2.2. The proposal

2.2.1. A first threshold of EUR 10,000

With effect from 2018, the proposal made by the European Commission is to introduce a threshold of EUR 10,000 below which the place of supply of B2C supplies of electronically supplied services for intra-EU B2C supplies remains in the Member State of the taxable person. The European Commission thus proposes a return to the origin principle for intra-EU B2C supplies, at least in the case of small taxable persons. As the Impact Assessment holds that SMEs, including micro-businesses, account for more than 99% of businesses in the European Union, it is expected that this threshold would have a substantial impact.

As noted above, the origin-based taxation of these supplies as of 2015 had been decided in 2008. It thus took less than two years for the European Commission to propose a backward step on that question. Moreover, this move goes at odds with the OECD VAT/GST guidelines that services and intangibles should be taxed at destination

16. A provisional figure of EUR 2.5 million setting up cost per business and an average annual administrative burden estimated at EUR 2,172 for EU taxable persons and EUR 41,623 for non-EU taxable persons had been communicated in February 2016 but has apparently been removed from the final version of the report.


23. This was confirmed in the explanatory notes.

24. See M. Lamensch, supra n. 22.


26. Paras. 2-5 to be added to art. 58 VAT Directive.

in order to ensure neutrality in cross-border trade. If this threshold is adopted, distortions of competition will again arise in favour of taxable persons located in low-VAT Member States (and if we combine this with the proposal made by the European Commission to give more leeway to the Member States regarding the setting of rates, it means that some Member States will have the possibility to attract SMEs to their territory. It goes without saying that tax competition between the Member States should be avoided and not encouraged in such a way). In addition, it reintroduces discrimination towards non-EU businesses that would be required to collect the tax at destination (with the related compliance burden) irrespective of the volume of sales to the European Union.

From a business perspective, the threshold is likely to be a relief for small (EU) taxable persons. Moreover, origin taxation should remain optional. In other words, SMEs should be “allowed to use the MOSS anyhow, e.g. if during a calendar year their turnover is exceptionally below the threshold”. In fact, the real question is rather the other way around: whether, if during a calendar year a business under the threshold exceptionally has a higher turnover, it should register to the MOSS, for how long, and with or without retroactive effect. This situation actually contains a risk for the Member States that SMEs underdeclare VAT in order to remain under the threshold (which they would not do if the consequences of exceeding the threshold were not that substantial).

2.2.2. Home country rules for invoicing and record keeping, and new rules regarding auditing

Also with effect as of 2018, the European Commission proposes that the invoicing rules of the Member State of identification apply. In other words, while the Member States of consumption have the taxing rights, they should accept having to audit taxable persons on the basis of invoices drawn up in accordance with other Member States’ rules. This would be a major relief for businesses. However, it looks like a rather far-reaching proposal to make to the Member States who failed to reach an agreement on a standard audit file for the MOSS (which would at least have offered them standard invoices to audit and not country-specific invoices). It remains to be seen whether the European Commission will convince the Member States to accept having to audit taxable persons on the basis of invoices of a very different format (and potentially in different languages).

The European Commission further proposes that the period for keeping records in the non-Union scheme and Union scheme respectively, is the period defined by the Member State of identification of the taxable person instead of the current period of 10 years, which largely exceeds the record-keeping requirements of most Member States. This would be a positive change for businesses.

Finally, the European Commission also proposes that requests for records and other administrative inquiries should be coordinated by the Member State of identification (instead of other Member States having direct contact with the taxable person) so as to avoid uncoordinated requests for records or administrative inquiries by several Member States of consumption. In the case of refusal to act by the Member State of identification, the Member State of consumption could “take any appropriate actions according to its national law”. The question is to what extent this would allow Member States of consumption to intervene and audit the taxable persons in an efficient manner if a Member State of identification failed to act. In any case, on completion of an administrative enquiry, a Member State of consumption may decide to issue, according to its national law, a new tax assessment, including possible interest and penalties to be paid. In that case, it will request the Member State of identification to notify this assessment to the taxable person or, if applicable, his intermediary, and to collect the amount due from this assessment. It should be noted that the Member States of identification will obtain a 5% collection fee on the amounts of VAT that they collect for the other Member States in order to compensate them for the costs linked to the collection and control of VAT under the MOSS. The Member States of identification should, as a consequence, be attentive to collecting as much VAT as possible (the European Commission even suggests that “the coordination of audits together with the incentive of the administrative fee should result in risk based audits”). However, it should be kept in mind that the efforts and resources that would need to be put into verifications are likely to exceed the expected revenue, so that the incentive effect may be rather limited in practice (keeping in mind that the 5% collection fee will also apply to those amounts collected after an administrative enquiry has been carried out by the Member State of consumption itself).

30. To be amended art. 219a VAT Directive.
32. To be amended art. 369(2) and 369(2) VAT Directive.
33. Art. 471 and 472 to be inserted in amending Regulation (EU) 904/2010. The proposal that is made is as follows: if the Member State of consumption decides that an administrative enquiry is required, it shall first consult with the Member State of identification on the need for such an enquiry. In cases where the need for an administrative enquiry is agreed, the Member State of identification shall inform the other Member States. In cases where the Member State of identification does not agree on the need for an administrative enquiry, it shall inform the other Member States of consumption concerned outlining its reasons. If at least two Member States consider that an administrative enquiry is required, the Member State of identification shall be required to undertake an administrative enquiry in coordination with those Member States. If only one Member State of consumption considers that such an enquiry is needed, that Member State of consumption may take any appropriate actions according to its national law. See sec. 3, proposed subsec. 3 Proposal 2016/755. See also sec. 3, subsec. 4 (art. 47) which provides for the payment of a fee of 5%, to be paid by the Member States of consumption to the Member State of identification in order to compensate the latter Member State for the costs linked to the collection and control of VAT under the special schemes.
34. Art. 47k to be inserted in amending Regulation (EU) 904/2010.
35. Sec. 3, subsec. 4 (art. 47) to be inserted in amending Regulation (EU) 904/2010.
2.2.3. Relaxed customer identification requirement below a second threshold of EUR 100,000

The European Commission also proposes to relax, as of 2018, the requirements regarding customer location in the case of electronically supplied services. The European Commission proposes that a single piece of evidence will be sufficient (instead of two as mentioned above) where the total annual value of intra-EU B2C supplies, exclusive of VAT, does not exceed EUR 100,000. This threshold thus again only applies to intra-EU supplies (in the same way as the first threshold of EUR 10,000 discussed above). Accordingly, it again provides for less favourable treatment of non-EU businesses. The question which then arises is: how are small non-EU taxable persons supposed to comply with the two pieces of evidence requirement when it is clearly acknowledged that small EU taxable persons cannot?

Furthermore, in general, it seems that only requiring one piece of evidence means that it will be very easy for fraudulent customers to obtain VAT-free supplies (for example, by changing their IP address or by providing a false billing address). For the sake of clarity, and as already stated elsewhere, the author believes that the two pieces of evidence requirement was difficult to fulfill by SMEs. However, in the author’s view, the solution does not lie in relaxing this requirement but rather in the design of an alternative method of assessing and collecting VAT on electronically supplied services.

2.2.4. No proposal to fix the effectiveness flaw of the current legislation

As noted in section 2.1.2., the European Commission clearly states on page 2 of Proposal 2016/757 that:

There are in essence three reasons to act: (…) the current system is not neutral as EU businesses are at a clear disadvantage to non-EU businesses which can legitimately and through high levels of non-compliance make VAT-free supplies into the EU. Given that VAT rates can be as high as 27%, there is a substantial distortion in favour of non-EU business if VAT is not applied (…).

The European Commission does make new proposals to tentatively address that issue in respect of imports of low-value goods (see section 4.). However, it does not propose anything to address the low level of compliance by non-EU taxable persons providing electronically supplied services to EU final customers (as reflected in the very low number of (M)OSS registrations by non-EU taxable persons).

As noted, one of the reasons for non-compliance is probably the high setting up and compliance costs. However, the main reason is most likely the absence of a means to enforce compliance on non-EU taxable persons (in particular in this sector where supplies are intangible and therefore do not physically cross borders). In this context, it is regrettably that difficult and costly verification requirements are being maintained on non-EU taxable persons regarding customer location (while they are being softened for EU taxable persons because the European Commission itself acknowledges that the current requirements are difficult to comply with). This will certainly not help to increase the level of compliance from non-EU taxable persons. Consequently, the EU Member States will continue to lose substantial VAT revenue. Moreover, the playing field will still not be levelled between EU and non-EU businesses in the area of electronically supplied services (since below the EUR 10,000 threshold, EU taxable persons will have to charge VAT in their Member State of establishment, which means that audits will be even more efficient than if performed by another Member State).

3. Distance Sales

3.1. The current situation

“Distance sales” in EU language means the B2C intra-EU supplies of goods with transport, typically those made to final consumers via the Internet. Special rules were adopted to address these supplies: taxable persons with a turnover above a certain threshold charge and collect the VAT at destination while taxable persons with a turnover below the threshold may charge and collect VAT at origin. The objective of this dual rule is to put all taxable persons on a level playing field by applying the destination principle as an exception to the general rule of article 32 of the VAT Directive, which provides for taxation at the point of departure of the transport operation (as the remote access to a wider customer base offered by the Internet creates distortions of competition under this general provision, in favour of sellers located in low-VAT Member States), while at the same time sparing heavy compliance burdens to small businesses making a few cross-border sales.

3.2. The proposal

With effect from 2021, the European Commission proposes an extension of the MOSS to distance sales. Complying with the MOSS is much easier in the case of distance sales than in the case of electronically supplied services because customer identification and location is more straightforward, given that the customer needs to provide an address for delivery (frauds remain possible but would be marginal) and there is more time for potential verifications regarding status (as the customer does not expect instantaneous delivery as in the case of electronically supplied services).

Still on the positive side, taxable persons carrying out both supplies of services and distance sales of goods under this special scheme should be able to declare both types of supplies in the same VAT return.
Another positive development for businesses is an extension of the deadline to submit the VAT return from 20 to 30 days following the end of the tax period and that corrections to previous VAT returns can be made in a subsequent return instead of in the returns of the tax periods to which the corrections relate. These changes will also apply with respect to electronically supplied services.

On the downside, and if tax assessment is easier in the case of distance sales as noted above, high compliance costs to comply with the practical requirements of the MOSS (in particular setting up costs) remain an issue for smaller taxable persons. This is why the EUR 10,000 threshold discussed above (under which VAT may be charged at origin) will also apply to distance suppliers. In practice therefore, this EUR 10,000 threshold should apply as of 1 January 2018 for supplies of electronic services only, but as of 2021 this threshold should become a global threshold applying to electronic services and distance sales. In the same way as for electronically supplied services, however, the risk exists that small businesses under declare VAT in order to remain under the threshold.

4. Imports

4.1. The current situation

B2C imports of goods from third countries are taxed at import. Since 1983, a VAT exemption applies in most Member States for imports of goods below a certain amount (the “de minimis exemption”, from EUR 10 up to EUR 22) simply because the cost of handling VAT collection would outweigh the expected revenue in the case of such low-value supplies. However, with the development of the Internet, the number of imports has rocketed up (in 2015 it is estimated that 144 million consignments benefited from the exemption, which is a 300% increase over the last 15 years) and the amount of VAT that the Member States give up collecting is growing accordingly. What is more, it is widely acknowledged that a large number of goods declared as “low value” actually have a value that exceeds the de minimis threshold. However, as customs authorities do not have the resources to verify each parcel (and again because this would result in excessive administrative costs), the loss in VAT revenue due to undervaluations (fraud) is dramatic. It is estimated that between VAT foregone and non-compliance in cross-border e-commerce, such losses are currently as high as EUR 5 billion annually. In addition, this puts EU taxable persons at a disadvantage as they have to charge VAT even on low-value goods while their competitors established outside of the European Union do not (and, moreover, have the possibility to reduce VAT liability by making undervaluations and with very little risk of being caught).

Like most jurisdictions currently applying an exemption for low-value goods, the EU Member States are therefore willing to remove the exemption. The question, however, is how to avoid a situation where the administrative costs related to the monitoring of the tax would exceed the expected revenue (which is the rationale for the exemption).

The BEPS Action 1 Report on the challenges of the digital economy identifies four possible approaches to streamline the collection of VAT/GST on imports of goods with a view to reducing the exemption threshold. Options include (i) enhancing the traditional procedure, (ii) a vendor registration system, (iii) a third-party collection system, and (iv) a customer collection system. It should be noted that the OECD international VAT/GST guidelines do not yet cover these supplies (under their current state they remain focused on services and intangibles).

4.2. The Commission’s proposal

A combination of a vendor collection and a third-party collection model

The solution proposed by the European Commission as an accompanying measure to the suppression of the de minimis threshold is twofold. It is a combination of a vendor registration system and a third-party collection system.

First, the European Commission again proposes to broaden the MOSS (meant to become an OSS in view of its much wider scope) to also cover imports of low-value goods, i.e. vendor registration. No threshold for smaller businesses is foreseen, which means that registration is mandatory from the first EUR 0.01. The OSS would apply for all parcels of an intrinsic value not exceeding EUR 150 and taxable persons not established in the European Union should designate an intermediary, except in the case where they would be duly authorized by the Member State of identification or where they would be established in a country with which the European Union has concluded an agreement on mutual assistance. As no VAT should be payable anymore upon importation of the goods, an exemption should be inserted into the VAT Directive.

In practice, the Member State of importation should verify the validity of the VAT identification number to be provided to the customs authorities upon importation before providing the exemption.

Second, and because the European Commission does not expect all non-EU taxable persons to register under the OSS, a fallback is proposed in the case of failure to regis-

44. To be inserted art. 369f VAT Directive for the EU scheme and art. 364 VAT Directive for the non-EU scheme.
45. To be amended art. 365 VAT Directive for the non-EU scheme and art. 369g(4) VAT Directive for the EU scheme.
46. Art. 60 VAT Directive.
47. Impact assessment, p. 15.
ter: Member States should allow the person presenting the goods to customs in the Community (i.e. the postal operators or express couriers) to report and pay import VAT due on these consignments electronically on the basis of a monthly declaration, on behalf of the person for whom the goods are destined – a third-party collection. To further simplify the declaration, these goods should systematically be subject to the standard VAT rate, unless the person for whom the goods are destined specifically requests the application of a reduced rate. In this case however, a standard customs declaration would be required. It should be noted that, at the moment, transporters already collect the VAT on imports whose value exceeds the de minimis, at an estimated cost of between EUR 0 and EUR 22 for postal companies and EUR 9 on average for express carriers, which translates into a fee for the customer that is often much higher than these figures.

This is the part of the proposal that, in the author’s view, is the most problematic.

Different treatment for EU and non-EU businesses

First of all, the solution proposed by the European Commission creates discrimination between EU and non-EU taxable persons. Firstly, because the former may benefit from the EUR 10,000 threshold discussed above (under which VAT is to be charged at origin and not at destination, which results in a different compliance burden and may lead to distortions of competition within the European Union) while the latter may not. Secondly, because supplies made by non-EU taxable persons would be taxed at the standard rate even if a reduced rate would apply if the same product were sold domestically. This second aspect may actually contravene GATT non-discrimination rules. More precisely, if the possibility for the customer to request the application of a reduced rate through a special procedure probably means that the proposal is compliant with article III:2 of the GATT (which prohibits the levy, directly or indirectly, of internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to similar domestic products), it may contravene article III:4 of the GATT, which provides that imported products cannot be accorded a less favourable treatment than that accorded to similar products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use.

In the author’s view, the obligation for the customer to submit a customs declaration in order to benefit from a reduced rate rather than to let the supplier or the transporter do the declaration does indeed amount to a less favourable treatment of imported products in the sense of article III:4 of the GATT (‘keeping in mind that most customers are likely to not make the effort of making the import declaration themselves and that, de facto, most products that would benefit from a reduced rate if sold intra-EU will be taxed more heavily when imported). In fact, it introduces a de facto different treatment of non-EU businesses depending on their size, since the costs related to the registration under the OSS and the requirement to appoint a fiscal representative means that only the big players will be able to register. In practice, a customer buying from a taxable person registered under the OSS will be able to benefit from a reduced rate without further formalities, while a customer buying from a smaller taxable person having to rely on the fallback will have to make a customs declaration to benefit from the reduced rate.

Efficiency?

Second, the very reason for adopting a de minimis threshold was the administrative cost related to the collection of taxes on small parcels, at a time when Internet sales were already at an embryonic state. Now that they have reached a peak, the proposal that is made by the European Commission is to remove the exemption and to ask the customs authorities to verify that all incoming parcels declared as “coming from a registered taxable person” are effectively shipped by a registered business. An initial question is: how should the verification of VAT registration numbers be done in practice? As noted above, the Member State of importation should verify the VAT number of the taxable person. However, the practicalities from a supplier’s perspective have not yet been defined. Non-EU taxable persons may have to issue and paste a barcode onto their parcels to allow customs authorities to make the verifications, which is an additional compliance cost that does not seem to have been taken into account in the Impact Assessment.

A second question relates to administrative costs, since, at the moment, thousands of parcels declared as low value cross the EU border every day without being handled individually as a result of the VAT exemption. If we remove the exemption and a systematic scanning of parcels by customs officers becomes necessary, it may require much higher resources than are available at the moment. (The bar coding is just a hypothetical solution but is there any viable alternative? Could customs officers be required to manually enter the VAT numbers in the VIES database? This would be even more disastrous from an efficiency perspective.)

Effectiveness?

Third, even when a parcel is identified as being shipped by a registered taxable person, it will not be possible to ensure that this taxable person eventually correctly declares the related VAT. As a matter of fact, with the OSS system, tax collection will no longer be performed at the moment of import, but via periodical returns. This means that the Member States have to trust that non-EU taxable persons registered in the OSS will duly declare and pay the VAT due after the delivery has been completed (i.e. at the end of the period of importation). This is the part of the proposal that, in the author’s view, is the most problematic.

54. To be inserted art. 369y et seq
55. To be inserted art. 369ya.
56. Impact Assessment, p. 16.
of the taxable period). Accordingly, and contrary to what the European Commission seems to infer, the provision of a valid VAT identification number will not amount to proof that VAT is declared under the special scheme because payment will occur later (goods are sent immediately after purchase and it cannot be expected that taxable persons declare and pay the VAT before the goods reach the EU borders). The problem, however, is that it cannot be assumed that the many businesses currently making false value declarations will not continue to do so. And as noted above, a major source of concern with the vendor model in the case of an import scenario is that the Member States do not really have the means to enforce compliance on non-EU businesses in the absence of effective international cooperation and assistance agreements (with all states around the world). Even when such agreement exists, or if the taxable person voluntarily submits itself to an audit, tax administrations will operate less freely than they would in the case of a domestic audit. To a certain extent, they will always have to rely on the documents that the non-EU taxable persons will be willing to communicate.

The proposal includes the requirement to appoint a fiscal representative, which is admittedly not a trade facilitator (despite the fact that the European Commission claims that the OSS will offer a “simplified procedure”). Moreover, it will come at a cost for taxable persons, and confirms that only large businesses will register (and that the others will opt for the fallback). The proposal moreover foresees that this requirement can be waived if the taxable person is duly authorized by the Member State of identification where the following criteria are complied with:  
- the absence of any serious infringement or repeated infringements of customs legislation and taxation rules, including no record of serious criminal offences relating to the economic activity of the taxable person;  
- demonstration by the taxable person of a high level of control over its operations and of the flow of goods, by means of a system managing commercial and, where appropriate, transport records, which allow appropriate customs and tax controls; and  
- financial solvency, which shall be deemed to be proven where the taxable person has good financial standing, which enables it to fulfil its commitments, with due regard to the characteristics of the type of business activity concerned.

Even if these conditions seem to constitute robust safeguards, at the end of the day the verification that these conditions have been satisfied will still be in the hands of the Member State of identification, which may not constitute a sufficient guarantee for the Member State of consumption.

This means that random verifications by the customs authority would still be most welcome to avoid underdeclarations, but would again result in administrative costs that the Member States are not willing to bear (and that were the reason for the exemption in the first place).

A tsunami for the transport sector

Fourth, the fallback imposes new obligations on express carriers and postal companies that are hardly insignificant. In practice, this implies that transporters assess the tax on the basis of data provided by taxable persons and that they eventually collect it on a much higher number of parcels than they do now, and with a cost that will often exceed the collected VAT revenue (which is exactly the reason why an exemption applies at the moment). The Impact Assessment estimates that an additional 150 million parcels will be subject to a VAT declaration if the exemption is removed.

Whether tax collection occurs before delivery or at delivery, it will also result in major disruptions in the delivery process (because transporters will have to warehouse a high number of parcels until payment is made). It may also be expected that national postal companies are not equipped to handle these new obligations, including the obligation to segregate commercial shipments from gifts and handle potential fraudulent gift declarations.

Another question is: who will pay for it? Should the non-EU taxable persons pay for the service? Should it be the customer? Or should the transporter integrate the cost in its price? The European Commission unfortunately did not provide any figure on the possible impact of the proposed measures on the transport sector. In fact, the Impact Assessment holds that it is difficult to provide an estimate because it may vary depending on the operator, which is somewhat too simplistic in the author’s view (in particular when the report has no difficulty in providing figures regarding compliance costs for businesses whose infrastructure towards compliance may also vary greatly). A study run by the Cross-border Research Association, in collaboration with the University of Lausanne and the University of Bamberg concluded that the VAT de minimis should actually be raised to EUR 80 from the current EUR 22 to avoid a situation where the total cost of collection faced by customs administrations and the private sector exceeds the revenues collected. This is obviously not an acceptable solution for Member States. However, removing the threshold and expecting the transport sector to absorb the shock is not a solution either.

The Impact Assessment does not provide estimates of the possible impact on consumers’ choices if the compliance were to be passed onto them in the case of purchases from

59. See Proposal 2016/757, p. 10: “Where VAT is declared under this special scheme, no VAT should be payable anymore upon importation of the goods. It is therefore necessary to provide for an exemption for such imports. This exemption is inserted in Article 143(1) of the VAT Directive. To allow customs to identify these consignments upon importation, a valid VAT identification number proving that VAT is declared under the special scheme should be provided to customs at the latest upon lodging of the import declaration (point 7).” The italic part should rather read: “that the supplier is registered under the MOSS”.

61. J. Hintza et al., The import VAT and duty de minimis in the European Union – Where should they be and what will be the impact? (Cross-border Research Association, Lausanne, Switzerland – in cooperation with HEC University of Lausanne and University of Bamberg 2014).
small businesses relying on the transporter and not on larger businesses able to rely on the OSS.

**A major flaw of the current situation remains completely unaddressed**

Last but not least, transporters, and in particular postal companies, will still not be able to verify the data provided by taxable persons as regards value. Express carriers do have risk assessment procedures in place. In contrast, postal companies are not so equipped and certainly will not be once the volume of parcels to assess has increased as a result of the removal of the exemption. A study by Copenhagen economics reports that 65% of consignments from non-EU taxable persons sent through the postal channel are not compliant. 62 UK HMRC estimates that non-EU taxable persons selling online to UK customers have evaded GBP 1.1.5 billion of VAT in 2015. 63 In the author’s view, too little attention is given to what is a major flaw in the proposed system. It is indeed unlikely that those who currently make false value declarations will suddenly start acting differently. This means that if this proposal is adopted, transporters, and in particular postal companies, will not only have to increase their capacity in terms of volume, they will at the same time have to improve their risk assessment procedures in order to tackle the issue of fraud. There is no indication by the European Commission of how much these measures will cost and whether this proposal is at all realistic in terms of capacity (again, in particular for EU postal companies).

Regarding that question, the Impact Assessment simply suggests that the system developments that will result from the recent changes to the Union Customs Code, which have put security-related obligations onto both postal operators and couriers (i.e. they will all need to provide advance information by 2021 to EU customs administrations), may be an opportunity to also improve the postal operators’ and couriers’ risk assessment regarding false declarations. The reference to the new obligations imposed on the transport sector regarding security and surety is very relevant as it means that the sector will already be facing major additional compliance to be able to guarantee a higher degree of surety and security (which everyone agrees is essential). In this context, the option to impose additional VAT obligations on the sector (and in particular on postal companies) should be more carefully evaluated.

### 4.3. Intermediate conclusion

Based on the above, the author suggests that the dual system proposed by the European Commission as regards imports of low-value goods (i.e. a combination of a vendor collection and a third-party collection model) will result in the following situation.

First, most MNEs will probably register under the OSS. As long as it is used by trustworthy businesses, it may offer a satisfactory level of (voluntary) compliance. However, while most non-EU large businesses are trustworthy and willing to comply with the rules, it should be acknowledged that the EU Member States will have very little means to verify this. In practice, verifying registration numbers is also likely to be costly (for both taxable persons and the customs authorities) and will moreover not be sufficient, because what matters at the end of the day is that the declarations made in the periodical returns are correct. Even where these taxable persons appoint a tax representative and subject themselves to audits, the EU tax administrations will not be able to run these audits with the same effectiveness as domestic audits. Where applicable, the Member States of consumption will moreover have to trust that the Member States of identification effect good implementation of the safeguarding measures.

Second, it should be acknowledged that all smaller businesses directly selling to final consumers will have to choose the fallback. This is likely to include those businesses selling through platforms acting as marketplaces (e.g. Alibaba, eBay and even Amazon for a part of their activity) because under the marketplace model, the platforms simply offer “space” to businesses and do not intervene in the sales. Accordingly, the platforms have little to no control over the goods that are being sold there (which, inter alia, means that they would not be able to comply with the hypothetical requirement to paste a barcode onto their parcels; 64 it also means that if they became liable under EU law to collect VAT they would have to trust the information provided by the business). As most of the taxable persons selling through these platforms would not be willing to register under the OSS themselves, in practice, this means that express carriers and postal companies will be required to assess and collect the VAT on a huge number of parcels at their own cost. It is thus very unfortunate (to say the least) that the Impact Assessment released together with the proposal does not offer any figure regarding the expected impact of the proposal on the transport sector. A particular source of concern is that transporters will have to run risk assessments in order to verify, as much as possible, that the values declared by the taxable persons are correct. Since VAT will be due on each parcel even with a value of EUR 1, this will result in major compliance costs for the sector. Moreover, it may also be expected that in spite of all the efforts that transporters will be able to make, controls will remain insufficient to address the issue of undervaluations (in particular for the postal sector which at the moment is completely ill-equipped to carry out these investigations).


64. Again, the bar coding is just a hypothetical solution but it seems to be the only viable way to allow for verifications at the border.
5. Conclusions

There is an urgent need to modernize the VAT system for cross-border B2C commerce. Indeed, the VAT system was created more than half a century ago, in an economy dominated by domestic transactions between parties that physically interacted with each other at an identifiable geographic location. It is not surprising that it cannot cope with an economy that has become global and digital.

Tribute should be paid to the European Commission for having spent the last 15 years working on several proposals to modernize the VAT system in the wake of the digital economy, the Commission’s explanatory notes and also its major contribution to the coordination effort launched by the OECD with the international VAT/GST guidelines. Unfortunately, however, there is only so much that the European Commission can do to address the paradigm shift that has occurred in the way business is being done. The Proposal released in December 2016 is unfortunately not up to the challenge. Its implementation would not solve the major issue of frauds based on undervaluations and the low level of enforceability on non-EU taxable persons. It would, moreover, result in major compliance costs for the transport sector with unavoidable repercussions for customers.

This is a key moment. Action is needed but precipitation to adopt inappropriate measures would be disastrous since undoing those measures would require the unanimous agreement of Member States.

In the author’s view, technology is the key. It offers unprecedented opportunities that have not yet been investigated (an online registration system and a VAT number database being a very basic use of technology!). Only this approach will allow for a genuine modernization of the VAT system. What the European Commission proposes to do is to improve a system that was designed in – and for – another era. What is needed instead is a fundamental rethink of the system on the basis of available or – to be created – technology. To quote Professor Harari: “Edison’s electric light did not come about from the continuous improvement of the candle”. 65

It undoubtedly implies some investment by the Member States. However, that is always the case with innovation. And in this case the potential return is enormous.

65. Oren Harari was a business professor at the University of San Francisco.