

FILE

VLS

C: /hpdocs/economic/VAT.VLS

(Deb S's)



10 DOWNING STREET
LONDON SW1A 2AA

From the Private Secretary

17 May 1990

VAT Registration Threshold

The Prime Minister was grateful for the Chancellor's minute of 15 May covering a note by Customs and Excise on the VAT registration threshold.

The Prime Minister is content that the Chancellor should pursue a further initiative to remove EC obstacles to setting a higher VAT threshold.

(BARRY H. POTTER)

John Gieve, Esq.,
H.M. Treasury.

RESTRICTED

A handwritten signature in dark ink, appearing to be "Pm", is located in the bottom right corner of the page.

RESTRICTED



Treasury Chambers, Parliament Street, SW1P 3AG
071-270 3000

Prime Minister

The Chancellor proposes a
further initiative to remove
EC obstacles to setting a higher
VAT threshold.

Content to proceed
as he suggests?

BHP
16/5

PRIME MINISTER

VAT REGISTRATION THRESHOLD

At my party at No.11 on Budget evening you asked the Chairman of Customs & Excise, Brian Unwin, whether we could make a substantial further increase in the VAT registration threshold. Although he explained the constraints, he undertook to have another look at this.

... 2. The attached note by Customs summarises the current position and recommends a further political initiative on the threshold. I fear that it looks as if the prospect of agreement on flexibility to fix a higher threshold is pretty remote. But if we could achieve it, it would have considerable advantages. Not only would it enable us to increase our own threshold in real terms, with benefits both for small businesses and our own costs of administering VAT; but it would also end the threat of infraction proceedings that were initiated back in 1984 against our current threshold - a course which the Commission are currently showing renewed interest in pursuing.

3. I therefore agree that we should consider a new political initiative. Since our immediate priority must be to concentrate on settling the technical arrangements for the post 1992 VAT regime, I also agree that, on the question of timing, it would be better to pursue the matter later this year during the Italian Presidency. If you are content, I will consider the best options for an initiative.

RESTRICTED



4. Finally, I should add briefly that the technical proposals for the VAT and trade statistics regime for the post 1992 period presented by the Commission last week are generally very acceptable to us. Although there is an unwelcome proposal to change to an 'origin' system of collection in 1997 - which we shall seek to modify in negotiation - the proposed arrangements are very much on the lines we have been consistently advocating and should mean much less burden and bureaucracy for businesses.

[J.M.]

15 May 1990

RESTRICTED

VAT REGISTRATION THRESHOLD

Note by HM CUSTOMS AND EXCISE

Background

A VAT registration threshold has operated since 1973; its purpose was to limit the administrative costs for both traders and Customs. When the VAT 6th Directive was adopted in 1977, Article 24 permitted Member States whose threshold exceeded 5,000 ECUs to increase it only to maintain its value in real terms. This facility has been exploited in successive Budgets but the Commission have challenged our method of indexation and in 1984 issued a warning letter under Article 169 of the Treaty as the first step in infraction proceedings.

2. The basis of the Commission's claim is that indexation should be based on the threshold in force on the date of the Directive's adoption (17.5.77), whereas we have used the date of the introduction of the tax in the UK (1.4.73). We are thus already under threat of proceedings for our current threshold, and it follows that any increase beyond the annual budget revalorisation would be regarded as a clear breach of our Treaty obligations. Indeed, the Commission have already made warning noises about the simplifications in this year's Budget and we understand their lawyers are again looking at the possibility of pursuing infraction proceedings.

RESTRICTED

The Draft Small and Medium-Sized Enterprises Directive (SMED)

3. It is the existence of this draft directive that has probably caused the Commission to stay their hand so far. Following the Prime Minister's initiative in 1985 it was submitted to the Council in September 1986; it incorporates a minimum threshold of 10,000 ECUs with an optional higher threshold of 35,000 ECUs. Although it has been discussed several times at official level in Brussels, it has not been on the agenda since December 1988 and has remained dormant since then. It has singularly failed to attract the support of other Member States, all of whom except the UK and Ireland regard the optional higher threshold as too high.

4. We had hoped that the Irish might provide new impetus during their current Presidency but, despite pressure at official level, they have no plans to discuss SMED. They believe there is little prospect of agreement; and indeed the Brussels timetable is so heavily committed to Single Market issues that it is unlikely in any case that SMED would command any priority.

The UK threshold and 35,000 ECUs

5. Last year's threshold of £23,600 moved within and outside the 35,000 ECUs limit during the course of the year so we can expect the 1990-91 revalorised limit of £25,400, although currently (in our view) within, to be more vulnerable if and when the exchange rate improves. As and when discussions begin again in Brussels we shall, of course, argue strongly for revalorisation of the 35,000 ECUs proposal which is now out of date.

The way forward

6. We shall, as a matter of course, maintain strong pressure in Brussels and seek any opportunity of either reviving interest in the SMED itself or of using the forthcoming Commission VAT Single Market proposals as a vehicle for re-opening discussion on VAT

thresholds and small business measures generally. The Single Market proposals have now been unveiled and generally follow the line we have been advocating on the need to reduce burdens on business. The Commission has proposed high thresholds in at least two areas (statistics and mail order) and we should be able to build on this foundation. This suggests that the best routine way forward is to use our present (relatively high by Community standards) threshold to demonstrate our commitment in the Single Market to the least burdensome and bureaucratic system, and to show our partners that this system works perfectly well.

7. The question is, however, whether we can accelerate or short circuit this by a high level intervention either by the Chancellor (eg at ECOFIN) or by the Prime Minister. Although there is always a danger of it being used as a trade off against other negotiating points, a substantial further increase in the SMED threshold would provide the flexibility we currently lack in fixing the UK limit and would bring the infraction proceedings to an end. At official level it is doubtful whether we shall make any progress - at any rate for a long time to come - by continuing on the present path.

8. The timing of a political initiative is critical. For the reasons referred to above, progress is unlikely under the Irish Presidency and in any case our first priority must be to concentrate on settling the technical details of the new Single Market VAT and trade statistics systems. This suggests that, subject to developments, it would be best for the issue to be raised by the Chancellor or the Prime Minister during the Italian Presidency towards the end of the year.