

European Scrutiny Committee

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From: Sir William Cash MP

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The EU VAT threshold for small businesses: potential application in Northern Ireland under the Irish Protocol

Thank you for your letters of 5 November 2019 and 7 January 2020 updating us on the adoption of the EU's new SME VAT Directive (Directive 2020/285/EU).¹ We note that the final legislation, approved by EU Finance Ministers on 18 February 2020, will set a maximum VAT turnover threshold for small businesses across the EU at €5,000 (£74,900) from 1 January 2025. It also allows SMEs from one EU country to benefit from the VAT exemption when selling into another Member State under certain conditions.

I am writing on behalf of the European Scrutiny Committee to seek further clarification from you on the implications of this new Directive, and in particular the maximum VAT threshold it contains, under the Ireland/Northern Ireland Protocol in the Withdrawal Agreement. As you know, Article 8 of the Protocol requires the UK to continue applying EU VAT legislation in Northern Ireland, insofar as those laws 'concern goods'. This includes the relevant provisions of Directive 2006/112/EC, as now amended to introduce the lower turnover limit in five years' time, provided the Northern Irish Assembly gives it support for extension of the Protocol when it is due for renewal in late 2024.

¹ The Directive was considered by the Committee as document (39449), 5334/18, COM(2018) 21.

If the new Directive were to apply to firms in Northern Ireland engaged in the supply of goods under the Protocol, it would result in a substantial reduction of their VAT threshold from the current £85,000 to approximately £74,900. This would mean many more Northern Irish firms would have to start applying VAT rules and pay for the associated administrative costs; it could also potentially distort competition within the UK internal market if small businesses in Northern Ireland must comply with VAT-related administrative obligations at a lower turnover level than their competitors in Great Britain.²

In your letter of 5 November last year, you said the Government did not “consider” that Directive 2020/285/EU would have to be applied in Northern Ireland under the terms of the Protocol. In support of this, the Government appears to rely firstly on the argument that the new legislation is out of the ambit of Protocol altogether because the threshold applies to firms irrespective of whether they sell goods or services (and therefore does not exclusively ‘concern goods’ in the words of Article 8). Secondly, Treasury officials have implied the UK-EU Joint Committee could adopt “appropriate measures”, essentially a waiver, to avoid having to apply the new legislation under the Protocol, an option foreseen by Article 8 to safeguard Northern Ireland’s position within the UK’s internal market.

It is not clear if the EU shares this interpretation of the basic scope of Article 8, or – if it did not – support special waivers for Northern Ireland. There has been no official confirmation that implementation of Article 8 is even to be discussed at the first meeting of the Joint Committee, scheduled for 30 March. However, it seems incongruous for the Government – as you noted in your letter of 5 November – to have unsuccessfully sought to raise the EU-wide VAT threshold under the new Directive to €100,000, which approximates the current UK turnover limit of £85,000, if it was confident the changes had no implications for Northern Ireland under the Protocol.

In light of the above, the Committee would like you to write by 8 April to clarify:

- If it is indeed the Government’s formal position that Directive 2020/285/EU, and in particular the new VAT threshold, is in fact outside the ambit of Article 8 of the Irish Protocol, and confirm that the EU agrees with that interpretation;
- If not, what kind of “appropriate measures” the UK is proposing the Joint Committee adopt with respect to the new VAT threshold if it would

² This effect would be exacerbated if the VAT threshold in Great Britain were to be raised further in the future. We note in this respect that the long-term future of the VAT threshold was the subject of a report by the Office for Tax Simplification (OTS) in November 2017, but that no fundamental change of policy has been announced by the Treasury to date.

otherwise be applicable in Northern Ireland in some form under Article 8 from January 2025; and

- Whether the Government considers that small firms in Northern Ireland will be eligible for the new cross-border arrangements in the VAT Directive to benefit from the SME exemption in one of the EU-27 countries (and vice versa).

Depending on the nature of your reply, and in the context of any relevant discussions at the UK-EU Joint Committee meeting of 30 March, the Committee may follow up with you on the VAT-related implications of Article 8 of the Protocol for Northern Ireland more generally.

I am copying this letter to Simon Hoare MP, Chair of the Northern Ireland Affairs Committee and Margaret McKinnon, Clerk of that Committee; Rachel Reeves MP, Chair of the Business, Energy & Industrial Strategy Committee and Rebecca Davies, Clerk of that Committee; the Rt Hon Mel Stride MP, Chair of the Treasury Committee, and Gosia McBride, Clerk of that Committee; to Lord Kinnoull and Christopher Johnson in the Lords; to Les Saunders at the Cabinet Office; and to Victor Peluola at your Department.

CHAIR