

European Scrutiny Committee

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From: Sir William Cash MP

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Rt Hon. Lucy Frazer QC MP
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Northern Ireland Protocol: Provisional EU agreement on minimum VAT rates

You will be aware that EU Finance Ministers on 7 December reached a ‘General Approach’ on new EU legislation relating to minimum rates of Value Added Tax (VAT) for goods and services.¹ While the legislation still awaits formal adoption, the endorsement of this draft legal text by all Member States points to a strong possibility that it will become EU law in its current form. We are writing to solicit your views on how this new VAT Directive may impact the UK under the Northern Ireland Protocol, given that its provisions foresee the continued application of EU VAT law ‘concerning goods’ in Northern Ireland.

In that context, we understand the draft legislation foresees significant changes to the permissibility of applying reduced and super-reduced VAT rates, including zero-rates, to particular goods and services within the EU. In particular, it would abolish reduced VAT rates on certain polluting goods, including fertilisers and fossil fuels. The Directive would also appear to set a numerical limit on the different categories of goods and services to which VAT rates below 5% can exceptionally be applied, suggesting that—in countries where the number of such exceptions currently exceeds that limit—existing rates may need to be increased for certain products in due course.

It is not clear to us at present how the changes foreseen by the new Directive, because of the Protocol, might impact on the rates and structures of VAT in Northern Ireland. While the new EU rules on VAT rates are only due to take

¹ EU Council document 14754/21.

effect in 2025, with full applicability in relation to exemptions and super-reduced rates due to be phased in over several years after that, the potential ramifications for the UK are significant. Clarity about its implications for NI at the earliest opportunity would be preferred, not least because the Government itself warned in its Command Paper of July 2021 that problems caused by the VAT provisions of the Protocol “may multiply as UK and EU VAT [...] rules evolve”. We are naturally aware of the Government’s efforts to renegotiate significant tracts of the Protocol, including in relation to Northern Ireland’s obligation to align with EU VAT legislation. However, the precise nature of the UK’s proposals—and what progress, if any, has been made to persuade the EU of their merits to date—is not clear.

As such, as things stand, it remains a possibility that the UK would have to apply any changes to EU rules on VAT rates, insofar as they concern goods, in Northern Ireland (if the new EU legislation takes effect while the Protocol as currently worded is in force). With this in mind, we would be grateful if you could confirm that the Government is undertaking an assessment of the new VAT Directive on rates to ascertain its implications for VAT rates in Northern Ireland under the Protocol, and if so when you expect to be able to share your Department’s initial conclusions with us. We are particularly interested in:

- whether the approach taken by the EU Council would affect the pre-Brexit exemptions from the EU’s minimum VAT rate rules which the UK can still apply in respect of Northern Ireland (for example because the number of categories of goods to which the UK exceptionally applies a rate below the 5% reduced rate would exceed the permitted limits);
- more generally, the extent to which the new legislation may in due course require changes in VAT rates in Northern Ireland or, indeed, would give the UK more flexibility under the Protocol as currently worded to vary such rates; and
- whether the new Directive could lead to different VAT rates on goods between Northern Ireland and Great Britain and, if so, what the implications of this would be for the UK internal market, for example with respect to shifting patterns of consumption, production, evasion and fraud.

Separately, it would also be helpful to hear what progress the Government has made with respect to its efforts to renegotiate the operation of the VAT provisions of the Northern Ireland Protocol in talks with the EU. If the Government’s proposal, based on the Command Paper, was accepted by the EU in full, what impact would it have on the EU’s new legislation on VAT rates.

We appreciate these matters, while political, are also highly technical. We therefore look forward to receiving your initial reply by the end of January, setting out how the Government is taking forward its assessment of the EU proposal and any preliminary conclusions reached by that point.

I am copying this letter to Simon Hoare MP, Chair of the Northern Ireland Affairs Committee and Stephen Habberley, Clerk of that Committee; to Lord Kinnoull, Chair of the House of Lords EU Select Committee, and to Chris Johnson, that Committee's Clerk; and to Les Saunders in the Cabinet Office.

CHAIR