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Prime Minister
I will take a
copy to Luxembourg

CDP
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PRIME MINISTER

VAT REGISTRATION THRESHOLD INFRACTION PROCEEDINGS

I think it would be helpful for you to raise with M. Delors when you see him at the European Council next week the question of the infraction proceedings which the Commission are proposing to take against the United Kingdom over what they consider the excessive level of our VAT registration threshold. I discussed the question with Arthur Cockfield last week, but he claims that he has no longer any power to hold the proceedings up.

If you do have the opportunity to speak to M. Delors in Luxembourg, you may like to draw on the following arguments:

- glad that we are to have the opportunity at this Council to discuss again the question of deregulation. Know that we both attach great importance to the question of reducing the administrative burdens on small and medium sized businesses.
- but on one point in particular affecting the United Kingdom, Commission is pursuing policy that would actually increase burden on large number of businesses. This concerns the maximum permitted VAT registration threshold.
- Commission have launched infraction proceedings against UK because they claim we have indexed our threshold (as we are entitled to do) from too high a base.

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Commission formula would leave UK with threshold of around £14,500, rather than £19,500 as at present.

- Keeping threshold high is way UK has chosen to deal with problem of minimizing burden on small businesses. Other member states use different methods, but most recognise that some special treatment is needed. One way is no more 'communautaire' than another. Member states should have the flexibility to tailor their regimes to their individual circumstances.
- Want to ask you, in the light of the work now being done on deregulation, to at least suspend these infraction proceedings until deregulation policy is fully formulated. Unless you do so they will continue of their own momentum.
- Would not be any danger of this being seen as a climbdown by the Commission. More a pragmatic recognition that you are dealing with re-assessed priorities for business in the light of your own deregulation report.
- For Commission to press proceedings in these new circumstances would certainly leave very bad impression in UK. Risks making them look both legalistic and vindictive.

The Commission are also thinking about changes to the Community legislation governing VAT thresholds. Their proposals would also be very unwelcome to the UK. If time permits, therefore, you might like to raise this point as well, on the following lines:



- Also understand that Commission are considering new proposals on VAT registration threshold which would remove the possibility of further indexation of those thresholds above the new limit, which itself would be very much lower than the UK's present threshold.

- Hope that, if this is the case, you will feel able to reconsider. Important that this flexibility should be retained, to allow member states to tailor regimes to their own circumstances.

- Issue has no effect on Community's own resources, nor does it distort international competition.

BACKGROUND

Present VAT registration threshold and infraction proceedings

Under the 1977 Sixth VAT directive, the maximum VAT registration threshold is fixed at 5,000 ecus (c £3,000), except for those member states who already had a larger threshold in 1977. They are allowed to retain and to index their thresholds. On the basis of this, the UK threshold has been progressively increased to £19500.

The particular point on which the Commission have instituted infraction proceedings is the base year from which that indexation has taken place. The UK has indexed its threshold from the £5,000 it was first set at in 1973, whereas the Commission claim it should be indexed from a later year. Their formula would result in a threshold of about £14500. Arthur Cockfield has stalled proceedings for some time, partly by citing the work being done on deregulation, but he now says that he cannot delay things any further.



Deregulation

Following your initiative at last March's European Council and the discussion at Milan, deregulation is to be discussed again in Luxembourg. The Commission have not been making as much progress with setting up a monitoring system as the member states, especially the UK, would like. Delors, however, shares our concern that the administrative burden on small and medium businesses should be reduced wherever possible. So far as VAT is concerned, our policy is to take as many as possible out of the VAT net altogether. Other member states have different methods of dealing with the problem, such as special accounting or collection regimes, but almost all have special arrangements of some sort.

New Commission proposals

Separately, the Commission have proposed that the EEC maximum VAT threshold should be raised. Indexing the present figure would produce about 12000 ecus. The Commission have not yet made a formal proposal, but Arthur Cockfield tells me that he could certainly not get support for a figure above 20000 ecus, and would probably find it difficult to go above 15000 ecus. In addition, the indexation provision from which we have benefitted in the past would be dropped or very severely restricted. (The present UK threshold is equivalent to about 35000 ecus).

A handwritten signature in dark ink, appearing to be 'N.L.' with a flourish.

N.L.

28 November 1985