ViDA as a Future Approach to VAT

Kateřina Hlavatá[1]

Abstract: Digitalization currently affects several aspects of fiscal policy, and financial administration must figure out how to deal with modern and progressive strategies to ensure their effectiveness in collecting tax revenues. The paper deals with the progress of digitalization in the context of value added tax (VAT). For EU Member States, the revenues from VAT influence the prosperity of their economy since it represents a significant part of their tax mix. A few years ago, the European Commission started discussing the modernization of VAT's approach in the context of digitalization. This resulted in the proposal of a new directive called ViDA (VAT in the Digital Age). The approach focuses mainly on e-invoicing, making reporting transactions easier and quicker. Furthermore, the proposal of the ViDA Directive represents a single VAT registration and regulation of digital platforms. The aim of the article is to introduce the reader to the ViDA Directive and highlight that each EU Member State needs to start preparing for the new EU legislation.

Keywords: digitalization, ViDA, e-invoicing
JEL Classification: H20, H21

1 Introduction

One of the key taxes, fundamental to the European Union's functioning, is value added tax (VAT). VAT sophistication, harmonization, and coordination within the EU are unmatched by any other taxes. For several states (such as the Czech Republic, Poland, and Hungary), VAT represents one of the most significant tax revenues for the national budget (OECD, 2020). The correct determination of VAT and following tax levy to state and VAT compliance is crucial for planning national calculation.

The following graph represents the proportion of VAT on tax mix in the EU Member States from 2020 to 2022. Since there are currently 27 EU Member States, the graph is divided into three groups[2] for better illustration. Each column represents the group's average of VAT on tax revenues. VAT increases its significance every year, which is in line with research saying that states should focus more on indirect taxes than direct taxes to support economic growth (Johansson et al., 2008; Arnold et al., 2011).

[1] Prague University of Economics and Business, Department of Public Finance, W. Churchill Sq. 4, 130 67 Prague 3, Czech Republic; katerina.hlavata@vse.cz. The paper was prepared as one of the outputs of a research project of the Faculty of Finance and Accounting at the University of Economics and Business „Public finance in globalized world“ registered by the Internal Grant Agency of University of Economics and Business under the registration number F1/39/2022.

[2] In the first group, the following countries are included: Austria, Belgium, France, Germany, Ireland, Italy, Luxembourg, and the Netherlands. The second group consists of: Czechia, Denmark, Finland, Greece, Malta, Poland, Portugal, Romania, Slovakia, Slovenia, and Sweden. The third group comprises: Bulgaria, Croatia, Cyprus, Estonia, Hungary, Latvia, and Lithuania.

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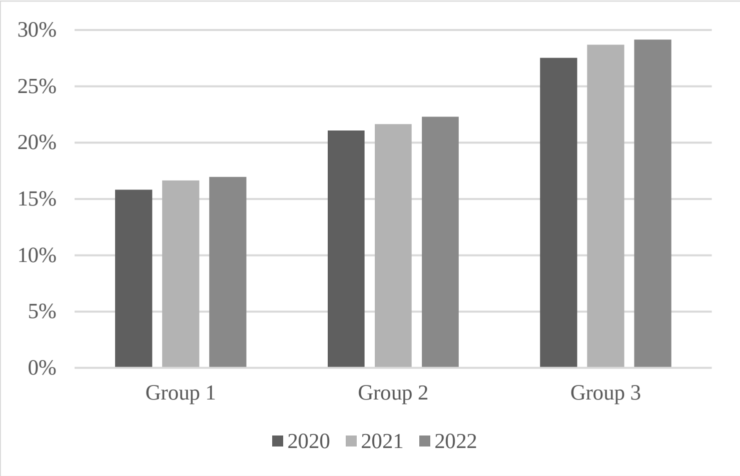
Graph 1 The proportion of VAT on tax mix (the list of countries in each group is stated in the footer)



Source Eurostat (2023)

VAT is susceptible to tax evasion. One of the most prominent forms of VAT fraud is the so-called carousel fraud, a scheme in which goods are traded across multiple borders within the EU, allowing fraudsters to repeatedly claim VAT refunds on the same transaction without remitting the tax (Keen & Smith, 2007; Sergiour, 2012; Sato, 2015).

The determination and calculation of tax evasion is generally quite complex, with several methods available. Regarding VAT, the most commonly established way to express tax evasion is the so-called VAT Gap, which the European Commission regularly publishes. The VAT Gap represents the difference between the theoretical duty pay VAT and the actually collected VAT. According to the last VAT Gap Report, the EU Member States lost approximately EUR 61 billion in VAT revenue for 2021. Compared to 2020, the VAT Gap decreased by EUR 38 billion, mainly attributed to more effective measures in the fight against tax evasion, digitization of tax systems, and e-invoicing (European Commission, 2023).

To eliminate VAT evasion, the European Commission (2024) focuses on three initiatives:

- Improved administrative cooperation (using modern technology such as Eurofics, which helps share information between national tax authorities);
- Centralization of payment information on online sales (working on creating a centralized system for collection of payment data from online sales, which will lead to following cross-border transactions between EU and identify mismatches);
- EU Directive VAT in the Digital Age (ViDA), which is described in the text below.

2 Methods

Digitalization has its own place in the modern world and represents an indispensable part of the public and private sectors. The aim of the article is to present the vision and future of VAT that lies in the ViDA Directive, which is built on the principles of digitalization. The article introduces the reader to the overview of the topic of the ViDA Directive and formulates the ideas and goals.

To achieve the set goal, the descriptive method is applied based on the literature review of the question of digitalization, primary source data, and national and EU legislation. The auxiliary methods are methods of analysis, comparison, and generalization.

3 Digitalization

Generally, the digitalization trend is significantly growing in several aspects of people's lives. The public sector and financial administration are aware that they cannot fight with progress and must adapt their procedures and systems.

Digitalization positively contributes to the tax system, which is fairer, more sustainable, and has higher productivity and transparency (Baldwin, 2016; Barbone et al., 2012). Financial administration processes data more effectively, which leads to a better overview of the economic activities of tax subjects (Kitsios et al., 2020; Heinemann & Stiller, 2023).

Digitalization lowers administrative costs for tax subjects and aims to improve communication between tax subjects and authorities. It is also seen as a helpful instrument that helps to eliminate tax evasion (Slemrod & Gillitzer, 2013; Holá et al., 2022; Zídková et al., 2024).

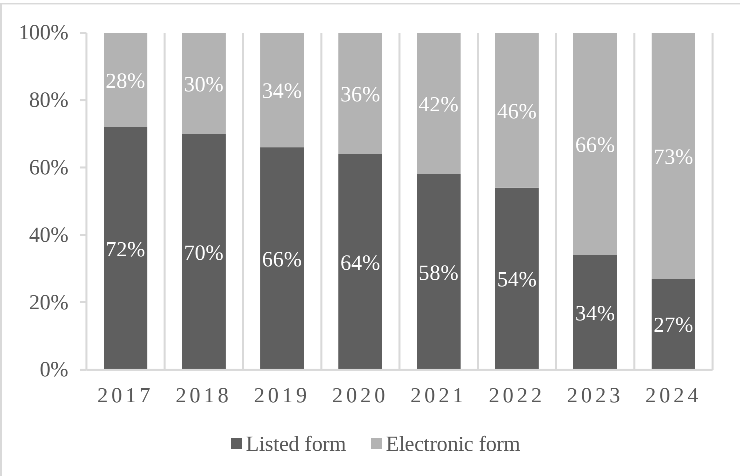
According to Keen & Smith (2007), the digitalization of tax administration represents not only a challenge from the technology aspect but also changes the whole approach to tax subjects. Digitalization brings up questions of how to stand up to data protection. They suggest that the tax administration invests in cyber security and adequately train its employees.

There are several indicators that determine the level of digitalization; the most common are the following:

- E-Government Development Index (EGDI) published by the United Nations, which focused on online services, telecommunication infrastructure, and human capital (UN, 2022);
- The Digital Economy and Society Index (DESI) published by the EU which focuses on using digital services and the integration of technology (European Commission, 2021);
- The Future Orientation Index (FOI) published by the World Economic Forum shows how states can respond to long-term challenges such as technological progress (WEF, 2020).

Alternatively, the proportion of electronic tax returns can be examined. The Czech Financial Administration published its statistics from 2017 up to 2024.[3] Besides the digitalization and improvements of Czech tax portals, the decrease in paper tax returns is related to amendments in tax laws, such as extending the deadline when submitting tax returns of income taxes electronically. In 2024, more than 70% of tax returns are expected to be filed electronically.

Graph 2 The proportion of electronic tax returns in the Czech Republic



Source Czech Financial Administration (2024)

4 Directive ViDA

Besides reducing the VAT Gap, the ViDA Directive should respond to the development of digitalization and lead to a more efficient VAT system. The main areas are e-invoicing, single VAT registration, and platform economy.

From the legal perspective, the European Commission presented amendments in Directive 2006/112/EC, Regulation (EU) No. 904/2010, and Implementing Regulation (EU) No. 282/2011 regarding the information requirements applicable to specific VAT schemes.

The new approach promises:

[3] For 2024, the proportion of electronic tax return is an estimate, as of April 2024, the share of electronic filings was 63%.

- Acceleration of the digital transformation;
- Reduction of tax compliance costs (EUR 4,3 million);
- Increased efficiency of tax control;
- Increased tax collection (EUR 135–177 billion);
- Improved cross-border trade;
- Reduction of tax evasions, etc. (Edicom Group, 2021)

E-invoicing

The EU would like to implement standardized digital reporting and e-invoicing for transactions between the EU Member States (intra-EU transactions). E-invoices will be obliged to be issued in line with the European Standard EN 16931 currently used for B2G transactions.

Whether the recipient agrees with e-invoicing or not will be irrelevant. This will also eliminate the possibility of issuing summary invoices. The e-invoicing process should lead to real-time digital reporting for cross-border B2B transactions. The EU Member States will have information from cross-border trades, which will help them fight VAT fraud in time. According to the European Commission (2023), this will help reduce VAT fraud by up to EUR 11 billion yearly.

In the end, e-invoicing is beneficial from the efficiency perspective (Bellon et al., 2022), reduce administrative errors (Poel et al., 2016), reduce costs (Fairchild, 2004) and lower CO_2 emissions (Koch, 2019; Hagsten & Falk, 2020).

Single VAT registration

Nowadays, taxpayers are obligated to register in multiple EU Member States in which they perform taxable supplies and are liable to pay VAT. It relates to monitoring national legislation, fulfilling national obligations as submitting regular VAT Reports, often hiring tax and law specialists and other administrative and non-administrative burdens associated with additional costs. Costs related to VAT registration were approximately EUR 1,200 per EU Member State, followed by EUR 8,000 annually for VAT compliance in each EU Member State from an average business perspective (EUR 2,400 for Small and Medium-sized Enterprises) (Madeleine et al., 2023).

Since 2015, simplification mechanism called One Stop Shop (OSS) has existed. Currently, OSS primarily applies to remote B2C sales and digital services. Via OSS, the taxpayers register only in one EU Member State. Following that, the taxpayers fill only one VAT Return (so-called single VAT Return) for each quartal, which declares all cross-border transactions to final customers in the EU. The ViDA initiative plans to use this approach more widely. Specifically, the OSS should apply also to:

- Transfers of own goods between the EU Members States;
- B2C sales of goods with installation or assembly; sales of goods on board ships, aircraft, or trains; and sales of gas, electricity, heating, and cooling by taxpayers not established in the EU Member State of consumption.
- Domestic B2C sales of goods by taxpayers not established in the EU Member State of consumption.
- Certain zero-rated transactions (e.g., sales of goods and services, among other things under diplomatic). (KPMG, 2024)

Platform economy

The platform economy is a quickly developed area of online platforms (such as Airbnb, eBay, and Uber) that mediate services and producers.

Since the European Commission is aware of the imbalance in the digital platform market due to the non-registration of online platforms, the ViDA Directive represents the "deemed supplier" concept. The intermediaries shall be considered from a VAT perspective as the supplier, even though they do not provide any goods or services but only mediate. This will lead to taxing the mediated services and the intermediary fee. The new concept will ensure equal conditions for traditional providers and online platforms (European Commission, 2023).

The ViDA Directive amends the definition of the short-term lease by considering it as a taxable supply of up to 45 days. Following that, online platforms will be required to upgrade their systems to track and store detailed information on suppliers, transaction flows, and customers. This data shall be archived for ten years. According to EU estimations, the new regulations on platform economy will increase the EU budget by EUR 6,6 billion within the decade (KPMG CR, 2023).

Current situation

In June 2024, the third proposal of the ViDA Directive was discussed. However, the EU Member States still have not reached a unified opinion on that, especially regarding the platform economy (Estonia vetoed the concept of putative provider since it is not in line with the principle of VAT neutrality). Therefore, the fourth version of the ViDA Directive is expected, and regarding the timing, the current expectations are talking about the year 2030[4].

However, more and more EU Member States have started to or already implement e-invoicing in some way into their national legislation as shows Table 1.

Table 5 E-invoicing

State	E-invoicing
Germany	As of the beginning of 2025, e-invoicing will be mandatory for national B2B transactions, meaning that businesses must be prepared to receive e-invoices. However, certain companies (total turnover of up to EUR 800,000) will be allowed to issue invoices on paper with the recipient's consent until January 2027.
Italy	From 2019, business entities must use the national system (Sistema di Interscambie) for sending and receiving invoices.
Poland	Poland started a system for issuing and receiving electronic invoices in January 2022 (so called KSef). The mandatory obligation for businesses with sales exceeding PLN 200 million is currently postponed to February 2026 and for the rest to April 2026.
Romania	As of the beginning of 2025, Romania extends the mandatory e-invoicing obligations to resident entities for B2C supplies.
Slovenia	A proposal for a new Act on exchanging electronic invoices and other electronic documents is currently discussed. The proposal suggests that from 1 June 2026, business entities will be issuing only e-invoices to other entities. Regarding the final customers, the e-invoice might be issued if both parties agree. However, the final customer can request a paper invoice at any time. All e-invoices shall be transmitted to the tax authority within eight days of the issue or receipt of the e-invoice.
Spain	E-invoicing has been obligatory for business entities with an annual turnover exceeding EUR 8 million from July 2024. For the rest of the entities, the mandatory e-invoicing will be effective in 2025.

Source: Germany (2024), AGID (2024), Edicom Group (2024), Global VAT Compliance (2024), RTC Suite (2024), Quaderno (2024)

From the Czech Republic's perspective, businesses are currently not obliged to issue e-invoices. The only area where the e-invoices are used is for public procurement (from 2016, the Czech authorities must be capable of processing e-invoices). The Czech Republic should be inspired by other EU Member States. It should collaborate with technology providers and create a national system for sending and receiving e-invoices. Furthermore, the Czech Republic should slowly implement the obligation of issuing e-invoices, starting with businesses with high turnover. It cannot underestimate a lengthy legislative process; therefore, it should take some steps soon. Lastly, training for employees of the Czech authorities should be considered so the newly established processes are effective.

5 Conclusions

VAT is quite a vulnerable tax in terms of tax evasion. Due to digitalization, tax subjects have discovered new ways to avoid paying taxes. Generally, tax evasion schemes are becoming increasingly complex and, therefore, are challenging to detect. Hence, the EU Member States and their financial administrations need to respond adequately, which means adapting legislative measurements, investing, and updating their systems to handle the volume of data.

[4] At the time this article is published, the fourth draft of the ViDA Directive has been approved by all EU Member States.

Digitalization of the VAT system is an inevitable step toward a more transparent and effective tax environment in the EU. The step represents the ViDA Directive proposal, which is currently being discussed at the EU level. Even though there are still a few reservations, it is obvious that its implementation will take only a matter of time.

The article summarises topics of the proposal of the ViDA Directive, which promises lower tax evasions via e-invoicing, reporting in real-time, a more straightforward registration process, and higher requirements on digital platforms.

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