

Highs and lows; VAT rate–setting in the European Union

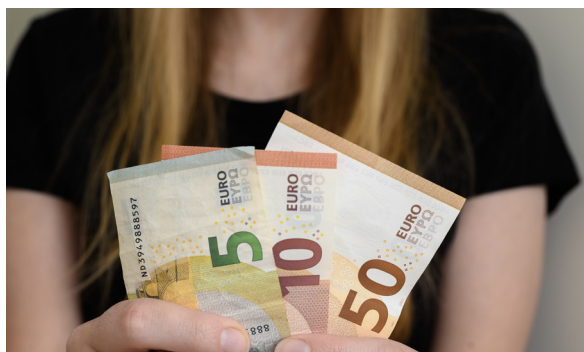
SUMMARY

How value added tax (VAT) rates are levied on various goods and services has wide-ranging implications, including for the fiscal revenues of national and EU budgets and the prices consumers have to pay. This briefing examines how EU legislation shapes Member States' ability to set VAT rates.

EU law establishes the framework within which Member States may apply different VAT rates, including the types of goods and services that can benefit from preferential rates. Such differentiation is used to pursue policy objectives – for example, supporting low-income households or incentivising the consumption of certain 'merit' goods. However, these policy choices can also create legal and administrative complexity and lead to sizeable revenue losses. Moreover, studies have questioned the extent to which lower VAT rates are effectively passed on to consumers by businesses, raising doubts about their efficiency as policy instruments.

The European Parliament has expressed concerns about the legal uncertainty and the complexity arising from the proliferation of different VAT rates, and has called for regular reviews to assess which of the preferential VAT rates remain necessary and effective.

At a time when many EU Member States face high budget deficits and competing spending priorities, a smart approach to VAT rate–setting is essential. Ensuring that VAT rate policy effectively balances social objectives, market efficiency and revenue collection is key to maintaining both fiscal sustainability and fairness within the EU.



IN THIS BRIEFING

- The role of VAT in the EU
- EU VAT rate–setting rules
- Lowering VAT rates – objectives and challenges
- European Parliament position
- Stakeholders



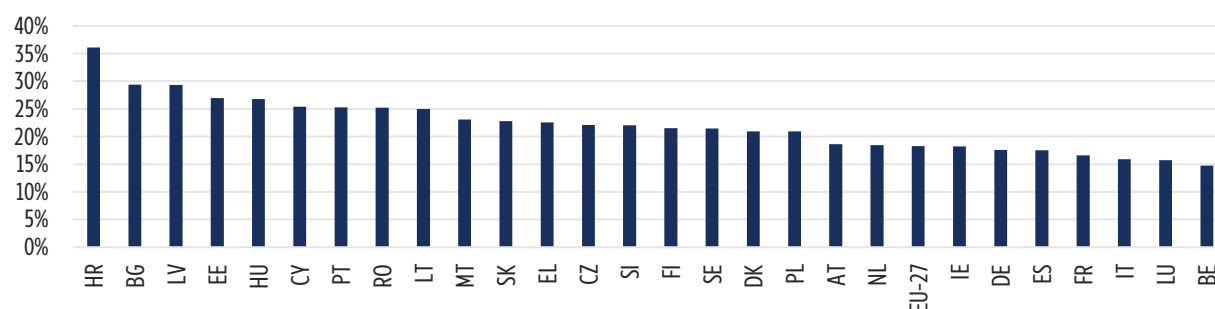
The role of VAT in the EU

Over the past decades, VAT has become one of the most important and widely used instruments for raising government revenue. First introduced in France in 1954, the tax has since been adopted by around [175 countries](#) worldwide, including all EU Member States.

As a broad-based consumption tax, the defining feature of VAT lies in its structure. Unlike a single-stage sales tax, VAT is levied at each step of the production and distribution chain, with the final burden falling exclusively on the end consumer, i.e. private consumption. Businesses¹ charge VAT on their sales ('output VAT') and remit it to the tax authorities, while also paying VAT on their purchases ('input VAT'), which they are entitled to deduct. Through their periodic VAT returns, businesses declare both amounts, with the net VAT owed determined by subtracting input VAT from output VAT. This multi-layered application of VAT ensures neutrality and simplicity and minimises distortions in production and trade.

VAT is a significant contributor to EU Member States' budgets, generating over [€1.2 trillion](#) annually. This is equivalent to 7 % of EU GDP and roughly one-fifth of total government revenues across the EU. However, its relative importance within national revenue mixes varies considerably among Member States (Figure 1). VAT also serves as the basis for one of the EU's [own resources](#), with a share of Member States' VAT revenue allocated to the EU budget. This own resource collected [€23 billion](#) in 2024.²

Figure 1 – VAT revenue as a share of total tax revenue, EU, 2023



Data source: [Data on Taxation Trends](#) (last updated March 2025), European Commission. Total tax revenue includes compulsory social contributions.

EU VAT rate-setting rules

Although the first VAT Directive was adopted in 1967, the first substantive EU rules on VAT rate-setting were only implemented in the early 1990s, as part of establishing the internal market.³ At the time, the European Commission [sought](#) to bring Member States' VAT rates 'sufficiently close' to each other by introducing defined VAT rate bands (14 % to 20 %), and broadening the VAT base by phasing out zero rates (0 %) and limiting the number of product categories eligible for reduced VAT rates. Other than simplifying administration, aligning VAT rates would also reduce incentives for cross-border shopping, thereby promoting fair competition in the internal market and protecting Member States' fiscal revenues. The Council opposed these changes, however, and removed the rate bands, retained zero rates and expanded the number of items eligible for reduced VAT rates. This tension between the Commission, advocating for greater harmonisation and a larger VAT base, and the Council, defending national fiscal autonomy and flexibility, would dominate subsequent attempts for reforms in [1995](#), [1996](#) and [2003](#).

These debates also took place against the broader backdrop of the EU's attempts to move towards an origin-based VAT system, whereby VAT is levied in the jurisdiction where the goods are located when their transport or dispatch begins. Such a system required strong alignment of VAT rates to prevent sellers simply relocating to Member States with the lowest VAT rates. As alignment failed

to materialise, and rates in fact diverged further, the origin-based model was abandoned [in 2012](#) in favour of the destination principle, whereby VAT is levied in the jurisdiction where the goods arrive after transport or dispatch, reducing the need for rate approximation.

After four years of negotiations – highlighting both the continuing complexity and the political sensitivity of VAT rate-setting – the most recent [reform](#) of the EU's VAT rules was adopted in 2022. The reform sought to modernise the system by aligning VAT rate provisions more closely with environmental and social priorities, thereby ensuring greater coherence with the objectives of the European [Green Deal](#).⁴ New possibilities were introduced for Member States to apply preferential VAT rates to items such as solar panels, low-emission heating systems and repairs of household appliances and (e-)bicycles. It also required the gradual phase-out of advantageous VAT rates on fossil fuels by 2030, and on chemical fertilisers and pesticides by 2032.

Following this latest reform, the contemporary VAT rate-setting framework is laid down in Articles 96-129a of the VAT Directive ([Council Directive 2006/112/EC](#)). Whilst the VAT rates themselves are not harmonised at EU level, Member States must operate within this common framework. A central component of this is the directive's Annex III, which lists the categories of goods and services eligible for preferential VAT rates.⁵ Annex III therefore serves as a key reference point throughout this briefing, as it underpins many of the rules, derogations and policy choices discussed below. The text of Annex III is provided at the end of the paper (Table 2).

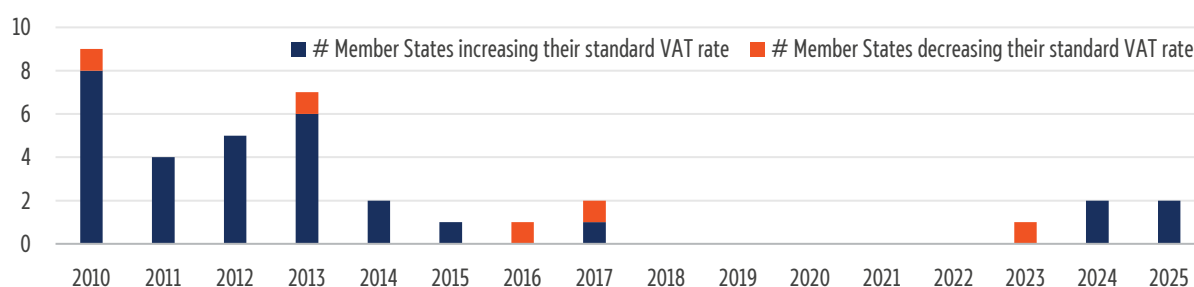
The rules governing VAT rate-setting in the EU can be broadly divided into two main components: a general framework, which sets out the common principles applicable to all Member States, and a set of temporary or permanent derogations, reflecting historical arrangements.

Main framework

Regarding the main framework, the VAT Directive identifies both a standard rate and a range of non-standard VAT rates (reduced, super-reduced and zero rate).

- Standard rate:** Member States must have a standard VAT rate that applies to most goods and services. This is the most recognisable rate – the one that typically comes to mind when people think of VAT. This rate cannot be below 15 %. After a wave of increases following the 2008 financial crisis, VAT standard rates have remained largely stable across the EU in recent years (Figure 2). The standard VAT rates applicable in 2025 are listed at the end of this briefing (Table 3).⁶

Figure 2 – Number of Member States that have changed their standard VAT rates, EU-27, 2010-2025



Data source: [Data on Taxation Trends](#) (last updated March 2025), European Commission. Calculations are based on the rates that applied on 1 July or for more than six months of any given year.

- Reduced rate:** Member States may apply up to two reduced VAT rates, not lower than 5 %. These may be used for up to 24 categories listed in Annex III, which covers a broad range of goods and services reflecting cultural, social, digital and environmental objectives. The list includes, for example, hotel and restaurant services, cultural and sporting events, hairdressing, cleaning, (e-)bikes, children's clothing, internet access,

electricity, etc. The reduced rates currently applicable in the EU are listed at the end of this briefing (Table 3).

- **Super-reduced rate and zero rate:**⁷ Member States may apply a super-reduced VAT rate (below 5 %) or zero rate (0 %) to the Annex III items covered in points (1) to (6) and (10c). These cover basic need items, such as medicine, female sanitary products, food, water and non-alcoholic drinks.

It is important to stress that the use of reduced, super-reduced and zero rates remains optional. Member States are free to apply their regular standard VAT rate to all of the goods and services listed in Annex III if they wish. Where Member States do apply non-standard VAT rates to a listed good or service, they may still further restrict its use to certain types of goods or services within a category.⁸

Table 1 – VAT-rate structure, EU, high-level overview

Rate	Level	Scope	Legal basis
Standard rate	Not lower than 15 %	All goods and services	Art. 96–97
Non-standard rate			
Reduced rate	A maximum of two rates that are not lower than 5 %	Supplies of goods or services covered in a maximum of 24 points in Annex III	Art. 98(1)
Super-reduced rate	Can be below 5 %	Supplies of goods or services covered in points (1) to (6) and (10c) of Annex III	Art. 98(2)
Zero rate (exemption with the right to deduct) ⁹	0 %	Supplies of goods or services covered in points (1) to (6) and (10c) of Annex III	Art. 98(2)

Table source: Author's own work. Please note that this remains a high-level overview, with the table not covering, for example, the provision of electronically supplied services (Article 98(3)), goods imported for disaster victims (Article 101a) or territorial derogations (Article 104).

Permanent and temporary derogations: transitional arrangements

As discussed above, the first impactful VAT rate rules arrived in 1993 with the launch of the internal market. However, to attain the necessary unanimous support at the time, the Council allowed several Member States to continue to apply reduced rates on items not listed in Annex III. Similarly, during the 2004 EU enlargement, some acceding Member States were allowed to continue to apply certain non-standard rates.¹⁰

Many of these historical derogations remain in place today. The Council reform of VAT rates in 2022 sought to find a new balance by ensuring equal treatment between Member States and phasing out other derogations:

- **Super-reduced rate and zero rate (Article 105a(1)):** Member States that in January 2021 were applying super-reduced rates or zero rates to items listed in Annex III – **other than** points (1) to (6) and (10c) – can maintain those measures. To ensure equal treatment, other Member States were also permitted to apply reduced or zero rates to the same goods and services under identical conditions to those already in place. Member States making use of this option had to notify the [VAT Committee](#) by October 2023.¹¹
- **Temporary derogation (Article 105a(2)):** Member States that in January 2021 were applying rates lower than 12 % or zero rates to items **not** listed in Annex III can maintain them until January 2032.

- **Parking rate (Article 105a(3)):** Member States that in January 2021 were applying reduced rates not lower than 12 % to items **not** listed in Annex III can retain them. Other Member States could do the same for the same goods and services under identical conditions, subject to notification to the VAT Committee by October 2023.
- **Derogation related to housing (Article 105b(1)):** Member States that in January 2021 were applying rates not lower than 5 % to transactions relating to housing **not** forming part of a social policy can continue applying those reduced rates. However, by January 2042, the applicable rate must not be lower than 12 %. Other Member States that did not previously apply such reduced rates could apply a rate not lower than 12 % to the same goods and services under identical conditions, provided they had notified the VAT Committee by October 2023.

In October 2025, the European Commission [outlined](#) which Member States had decided to maintain these derogations and which had decided to make use of the provision to 'duplicate' another Member State's derogation.¹² The report noted that just three Member States – Luxembourg, Ireland and Italy – accounted for 75 % of all derogations. Only three Member States – Cyprus, Greece and Malta – had made use of the temporary option to duplicate another Member State's derogation.

VAT exemptions without the right to deduct

As a separate category, the EU VAT Directive also establishes certain exemptions for activities, but without the right for suppliers to deduct input VAT (see contrast with 'zero rates'). These exemptions are in principle mandatory, although there is some room for discretion.¹³ The exemptions fall into two main groups:

- Exemptions for activities in the public interest: hospital care, medical care, dentistry, (physical) education, etc. ([Article 132](#)).
- Exemptions for other activities: applies to activities that are considered difficult to subject to VAT, such as financial services, insurance and gambling ([Article 135](#)).

Legal principles

While the VAT Directive does offer a degree of flexibility to Member States in setting VAT rates, this discretion is constrained by two key legal principles developed through the case law of the Court of Justice of the European Union (CJEU): fiscal neutrality and strict interpretation.

The principle of fiscal neutrality requires that goods and services which are in competition with each other must not be treated differently for VAT purposes.¹⁴ In essence, where goods or services are identical or sufficiently similar, from the consumer's perspective, and satisfy the same consumer needs, they must be subject to the same VAT rate.

The principle of strict interpretation is another key concept in VAT rate-setting. Since exemptions constitute derogations from the general principle of VAT as a broad-based consumption tax, the CJEU has consistently held that such derogations must be interpreted strictly and cannot be simply extended beyond what is necessary to achieve their intended purpose.

Lowering VAT rates – objectives and challenges

This section examines the policy rationale for non-standard VAT rates and the challenges associated with their use.

Non-standard VAT rates are generally introduced for one of [three main purposes](#):

- reducing the regressive nature of the tax;
- promoting the consumption of [merit goods](#) (a good whose consumption the government wants to promote);
- supporting employment in (price-elastic) sectors.¹⁵

These policy objectives are reflected in the list of items set out in Annex III.

The regressivity of VAT is one of the most extensively researched and debated features of the tax; indeed, one study [called](#) it 'the biggest drawback of an otherwise nearly perfect tax'. Because low-income households spend a larger share of their income on consumption, they bear a proportionally heavier VAT burden than high-income households. Applying preferential rates to (basic need) items is therefore intended to mitigate this effect and enhance the fairness of the tax system.¹⁶ Lower rates may also be used to encourage the consumption of goods considered environmentally, educationally or culturally beneficial, such as solar panels, books and newspapers or to support labour-intensive, price-elastic sectors (such as hospitality or personal services) where lower VAT can stimulate demand and thereby sustain employment.

Yet in practice, the operation of non-standard VAT rates proves considerably more complex. Their effect largely depends on how much of the VAT reduction shows up in consumer prices ('pass-through') and how the benefits are distributed. They may also impose sizeable fiscal costs that can outweigh their benefits relative to alternative policy instruments. Moreover, maintaining a multi-rate system adds legal and administrative challenges for both tax authorities and businesses.

Pass-through

While the objectives behind lowering VAT rates may be laudable, their effectiveness depends heavily on the extent to which VAT cuts are passed on by businesses, meaning the extent to which the reduction translates into lower consumer prices. In practice, this is far from guaranteed: [most empirical evidence](#) indicates that VAT reductions are typically not fully reflected in lower consumer prices.¹⁷ Although pass-through rates can vary by sector, market structure and the magnitude of the VAT change, the prevailing pattern is one of under-shifting, meaning that consumer prices fall by less than the reduction in VAT would indicate. Higher pass-through rates can be found in more [competitive market](#) sectors or when the rate reduction is under huge [public scrutiny](#) or is permanent rather than temporary.

Low pass-through rates for VAT reductions can reflect firms' incentives to widen profit margins – which can in turn benefit shareholders or employees – but they may also arise from ['menu costs'](#). When companies want to adjust their prices after a VAT rate change, a range of tasks may be required: updating the company's invoicing software, amending advertisements, revising contracts with distributors and coordinating across marketing, accounting and sales departments.¹⁸ If these costs are perceived as too high, companies may decide not to adjust their price, particularly for small or temporary VAT reductions, thereby limiting the policy's intended effect.

The European Commission has also been explicit – perhaps even more so in recent years – in expressing its cautiousness about the impact of VAT cuts. During the energy cost crisis following the Russian invasion of Ukraine, the then Commissioner for taxation, Paolo Gentiloni, [warned](#) Member States of reductions in VAT rates, stating they had a 'bad track record' in lowering prices for consumers. More recently, in response to a question on lowering VAT on fruit and vegetables, Commissioner Hoekstra [noted](#) that the pass-on rates of VAT cuts were 'relatively low', with consumers benefiting only 'to a limited extent, if at all'.

Distributional aims

Even assuming full pass-through of VAT reductions to consumer prices and setting aside complications such as differing price elasticities for demand, questions remain about whether non-standard rates can truly support distributional goals (to support people on lower incomes).

Compared to, for instance, direct subsidies for low-income households, VAT is a rather ['blunt instrument'](#) when it comes to distribution, as it is charged regardless of a buyer's income level. This means that lower VAT rates – if passed on – benefit all consumers across the income scale. Although lower rates may provide proportionally greater relief to lower-income households, the absolute cash gains tend to be larger for higher-income households, who generally consume more overall.¹⁹

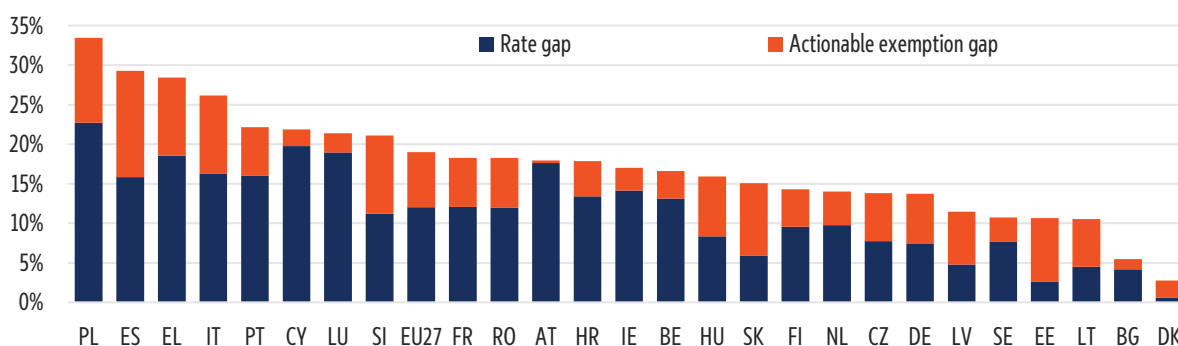
Moreover, the consumption of some goods and services commonly granted lower rates, such as books, cultural activities, restaurants and hotels, may be disproportionately greater among higher-income groups.

Fiscal impacts

Applying lower VAT rates inevitably results in a lower amount of VAT revenue collected. To quantify this effect, the European Commission publishes an annual estimate of the '[actionable policy gap](#)' in Member States' VAT bases. This represents the share of potential VAT revenue that could theoretically be recovered if all reduced and super-reduced ('rate gap') and zero rates ('actionable exemption gap') were discontinued and replaced by the applicable standard rate in each Member State.

In 2022, the actionable VAT policy gap in the EU was estimated at around 19 % of the total theoretical VAT revenue, or €481 billion, underscoring the significant fiscal impact of Member States' VAT rate policies.²⁰ The composition of the VAT policy gap varies widely across Member States.

Figure 3 – Actionable policy gap: Rate gap and actionable exemption gap in the EU, 2022



Data source: European Commission, CASE, Poniatowski, G., Bonch-Osmolovskiy, M., Braniff, L., Harrison, G., Luchetta, G., Neuhoﬀ, J., Śmietanka, A., Zick, H., [VAT gap in the EU – Report 2024](#). Table 4 in the annex presents the estimated VAT revenue lost by each Member State in millions of euros.

The large loss of fiscal revenue due to lower VAT rates can, in turn, constrain governments' ability to finance public services – on which low-income households tend to rely the most – or force governments to increase other, potentially more distortive, taxes.

One reason for the large use of non-standard VAT rates is the phenomenon of 'rate creep':

'By granting a reduced rate to one sector, other sectors will inevitably lobby hard for inclusion. This is an international issue with lobbyists quoting a reduced rate in country A as a means of pressing the government in country B to follow suit.' ([OECD](#), 2010).

Legal complexity

Setting aside complexities regarding pass-through or distributional impacts, the application of non-standard VAT rates requires legislation to clearly distinguish between those items eligible for the lower VAT rate and those remaining subject to the standard rate. In practice, however, drawing these boundaries is often more complex than anticipated. Tax authorities need to issue detailed guidance to clarify how the rules apply in specific situations. New products or technologies may also challenge existing definitions over time.²¹ Meanwhile, businesses have a strong incentive to argue their products qualify for lower rates.

This has led to numerous legal disputes over the correct VAT treatment of specific goods and services. For VAT purposes, courts have been asked whether driving lessons could qualify as tuition services, at what point bread ceases to be 'bread' or whether certain products can genuinely be regarded as 'cakes', amongst other questions.²²

Cake or biscuit?

Arguably one of the most well-known and often-cited VAT cases is [United Biscuits \(LON/91/0160\)](#) – commonly referred to as the Jaffa Cakes case.

In 1991, the United Kingdom authorities had classified Jaffa Cakes – small, sponge-based confectionery items with an orange jam centre and a thin chocolate coating – as 'biscuits'. This classification would have made them subject to the UK's standard rate of VAT rather than the zero-rate applied to cakes. McVitie's, the producer of Jaffa Cakes, contested this classification with the British courts.

The court considered various factors of Jaffa Cakes to come to a judgment, including Jaffa Cakes' size, packaging, material, texture and the way they harden when stale. Ultimately, the court ruled that Jaffa Cakes possessed 'enough characteristics of cakes to be accepted as such', allowing them to benefit from the zero rate.

While such legal disputes may make for amusing headlines, litigation over VAT rate applications entails time and financial costs for tax authorities, businesses and courts, including expenses related to legal representation, administrative proceedings and penalties.

Administrative burden

Next to legal and interpretative costs in borderline cases, a multi-layered VAT rate structure can also result in higher [administrative costs](#) for businesses, as accounting and invoicing systems must be upgraded and adapted to handle the different VAT rates. Additionally, the greater the number of reduced or zero VAT rates, the higher the likelihood that a business will be in a net refund position for VAT, which can increase administrative effort and cash flow challenges. While it is difficult to quantify the exact level of compliance costs associated with managing multiple VAT rates, research suggests a [positive correlation](#) between the number of VAT rates and the total administrative burden faced by businesses. Tax authorities may also face additional administrative costs in verifying compliance in a multi-rated VAT system, rendering tax audits more complex.

A particular challenge for EU businesses is keeping up to date with VAT rates applied in other Member States. Cross-border sales often require the customer's domestic VAT rate to be applied, meaning businesses must constantly monitor differing rates and derogations to avoid applying an incorrect rate and incurring disputes and penalties. This challenge is exacerbated by the fact that VAT rates can change at short notice and at any point in the year.

To improve transparency, the European Commission created the [Taxes in Europe](#) database, which offers an overview of standard and non-standard rates per Member State, searchable by CN codes (for goods) and CPA codes (for services). However, the database is not legally binding and some Member States have not fully completed their CN and CPA listings. As a result, ensuring that traders can rely on accurate and up-to-date information on applicable VAT rates across the EU remains an ongoing administrative challenge.

The way forward

Addressing the challenges associated with non-standard VAT rates is by no means straightforward. Removing such rates, whether selectively or broadly, would itself entail significant difficulties. Whereas VAT rate cuts tend to be under-shifted, evidence [points to](#) increases being more easily passed on, thus having an immediate impact on households. Moreover, withdrawing non-standard rates can trigger strong opposition from [voters and affected sectors](#), as well as concerns about cross-border shopping.

In addition, large-scale withdrawals of preferential rates could temporarily add upward pressure to inflation, with potential implications for monetary policy. In Member States with automatic wage indexation, the resulting VAT-driven price increases may trigger wage adjustments, further amplifying the economic effects.

Looking ahead, several avenues have been proposed to reconcile the policy objectives behind non-standard VAT rates with the need for a simpler, more efficient system. Much of the [literature](#) argues that alternative tax and benefit instruments – such as targeted subsidies or increasing income tax thresholds – are more effective and cost-efficient in supporting low-income households than VAT rate differentiation.²³ These instruments deliver support more precisely, although they may also entail higher administrative costs for governments. Others have also [highlighted](#) the potential of real-time digital technologies to mitigate the regressivity of VAT. Under such proposals, VAT paid could be automatically fully or partially reimbursed to lower-income households in real time.

European Parliament position

While the European Parliament is not a co-legislator on VAT, as VAT legislation follows a special procedure requiring unanimous Council approval, it has adopted several opinions on VAT rates.

In its 2018 [opinion](#) on the latest VAT rate reform, the European Parliament supported granting Member States a degree of flexibility in setting VAT rates to reflect 'local conditions, preferences and traditions'. At the same time, it stressed the importance of a 'greater convergence' in VAT rates across the EU. Unlike the Council and the Commission, the Parliament favoured a cap to the standard VAT rate – set at 25 %. It urged Member States to refrain from applying reduced VAT rates to harmful or luxury products. Parliament also underscored the impact VAT rate changes can have on both the national and EU budget. In October 2025, the European Parliament [stated](#) that reduced VAT rates 'increase[s] legal uncertainty and the complexity of the tax system' and called for 'a periodic review and assessment of which reduced VAT rates remain necessary and effective'.

Questions concerning VAT rates – and whether certain categories of goods or services may benefit from reduced or zero VAT rates – have been frequently raised with the Commission in recent years. These inquiries have covered a wide range of items, including [menstruation products](#), [lowering VAT during sales periods](#), [fruit and vegetables](#), [bottled water](#), [basic foodstuffs](#), [restoration of historic monuments](#), [donated products](#) and [essential goods for disabled persons](#).

Stakeholders

In 2024, [the VAT Expert Group](#) – a group assisting and advising the European Commission on VAT matters – [expressed](#) concern about the growing complexity of the Member States' VAT rate structure.²⁴ The multitude of exemptions, derogations and other exceptions creates significant compliance burdens for businesses operating across borders, the group argued. The Commission was therefore encouraged to consider proposals aimed at simplifying the system by eliminating certain exemptions and derogations. In the group's view, simplification could be pursued gradually, beginning with a system featuring one standard rate and a single reduced rate.

ENDNOTES

- ¹ For simplicity, we will use 'business' throughout this briefing rather than the concept of 'taxable person'.
- ² Member States' contributions are calculated in the following way: first, the total amount of VAT receipts collected by a Member State is divided by that Member State's weighted average VAT rate – this is the overall VAT rate the Member State effectively applies, calculated by weighting each rate by the value of the transactions or consumption it applies to. From this base, 1 % is taken. If that amount exceeds 0.5 % of the Member State's gross national income (GNI), the base for the next step is capped at 0.5 % of GNI. Finally, a uniform call rate of 0.3 % is applied to the (possibly capped) base to determine the Member State's contribution for the VAT own resource. In 2023, the 'capping' measure [applied](#) to Croatia, Cyprus, Luxembourg, Malta, Poland and Slovenia. As part of its [own resources package](#) for the 2028–2034 multi-annual financial framework (MFF), the European Commission has proposed to remove the GNI-capping measure from the VAT own resource calculation.
- ³ For more information on the history of VAT rate-setting rules in the EU, see Cornielje, S. (2022). [The Costly Stalemate of EU VAT Harmonization](#). EC Tax Review, 31(2), 85–96.
- ⁴ The final Council agreement diverged significantly from the Commission's original [proposal](#). The Commission had initially sought to grant Member States considerably greater flexibility in setting VAT rates by replacing Annex III with a negative list, i.e. a list of goods and services to which preferential rates could never be applied (such as tobacco and alcohol).
- ⁵ For the purposes of this briefing, the terms 'lower rate', 'preferential rate' and 'non-standard rate' are used interchangeably as a general designation for any VAT rate lower than the standard rate, i.e. reduced, super-reduced and zero rates.
- ⁶ It is also important to remember that VAT is charged on the '[taxable amount](#)', which represents the total value of the transaction. This amount includes not only the intrinsic value of the good or service but also any additional taxes or duties. Consequently, VAT operates on a cumulative basis alongside other taxes.
- ⁷ While the VAT Directive also refers to this as a 'reduced rate', this type of rate is commonly called 'super-reduced rate', to avoid confusion with the other reduced rate category.
- ⁸ For instance, Annex III allows Member States to apply non-standard VAT rates to food. However, Member States are not required to extend this treatment to all food products; they may instead limit its scope to categories they consider appropriate, such as fruit and vegetables, provided that the principle of fiscal neutrality is respected.
- ⁹ The right of deduction refers to the ability of businesses to recover VAT they paid on their own transactions. Throughout this briefing, the term 'zero rate' is used to describe supplies that are taxable but subject to a 0 % VAT rate, thereby maintaining the right of deduction. Supplies that are exempt without the right of deduction will be referred to as 'exemptions'.
- ¹⁰ In addition, the VAT Directive lists several derogations set out in Articles 371–390c in combination with Annex X, allowing Member States to continue to exempt certain supplies, until the adoption of definitive arrangements, under the conditions as applied in 1978. These 'standstill provisions' will not be covered in this briefing.
- ¹¹ The VAT Committee is an advisory committee composed of VAT representatives from Member States and the European Commission. The Committee provides guidance on the application of the directive and is consulted or notified when Member States make use of the options provided for in the VAT Directive.
- ¹² The report did not cover the temporary derogations of Article 105(a)(2).
- ¹³ See Article 133, 134 and 137. This briefing will not cover the exemptions related to intra-Community transactions (Articles 138–142), imports (Articles 143–145), exports (Articles 146–147, 151–152 and 154–166), international transport (Articles 148–150) and intermediary services (Article 153).
- ¹⁴ Under *Rank Group* ([C-259/10](#)) – a case concerning gambling machines where some types of machines were subject to VAT, while others were not – the CJEU developed a two-step 'neutrality test' to check whether the principle of fiscal neutrality is upheld.
- ¹⁵ Price-elastic sectors are those sectors where demand is very responsive to a price change.
- ¹⁶ [Other studies](#) have assessed the VAT as much less regressive, or even slightly progressive, when it is assessed relative to expenditure.
- ¹⁷ See also Benedek, D., De Mooij, R.A., Keen, M. et al (2020). [Varieties of VAT pass through](#). *Int Tax Public Finance* 27, pp. 890–930.
- ¹⁸ For example, a restaurant which wants to reduce prices in response to a VAT-rate cut on restaurant services may need to pay a layout artist and publisher to produce and print the new menus – hence the term 'menu costs'.
- ¹⁹ The European Commission provides [the example](#) of a lower rate on electricity, which may help with heating homes but could also be used to heat a private swimming pool.
- ²⁰ It is important to note that these figures are estimates and may be influenced by country-specific factors. For example, Spain's relatively high actionable VAT gap is partly explained by the use of indirect taxes other than VAT in the Canary Islands, Ceuta and Melilla.

- ²¹ For example, the VAT Directive permits lower VAT rates for books, but in the 2010s the CJEU had to determine whether this also covered audiobooks and e-books, as seen in cases such as *Commission v France* (C-479/13) and *K Oy* (C-219/13).
- ²² In *A & G Fahrschul-Akademie* (C-449/17), the CJEU was asked whether the scope of Article 132 of the EU VAT Directive, which provides exemptions for educational services, extended to driving school instruction. The Court ruled that it does not. In *Bookfinders Ltd v Revenue Commissioners*, the Irish courts were asked to determine whether the bread used in Subway sandwiches qualified as 'bread' eligible for a zero VAT rate under Irish law. The court ruled that it did not, as the sugar content in the dough exceeded two percent of the weight of the flour, breaching the legal definition of bread for VAT purposes in Ireland.
- ²³ See also Institute for Fiscal Studies (2011). [A retrospective evaluation of elements of the EU VAT system](#). TAXUD/2010/DE/328.
- ²⁴ The group is composed of organisations representing, in particular, business and tax practitioners, as well as individuals appointed in a personal capacity, such as academics.

DISCLAIMER AND COPYRIGHT

This document is prepared for, and addressed to, the Members and staff of the European Parliament as background material to assist them in their parliamentary work. The content of the document is the sole responsibility of its author(s) and any opinions expressed herein should not be taken to represent an official position of the Parliament.

Reproduction and translation for non-commercial purposes are authorised, provided the source is acknowledged and the European Parliament is given prior notice and sent a copy.

© European Union, 2025.

Photo credits: © Paweł Kacperek / Adobe Stock.

eprs@ep.europa.eu (contact)

<https://eprs.in.ep.europa.eu> (intranet)

www.europarl.europa.eu/thinktank (internet)

<http://epthinktank.eu> (blog)

Annex

Table 2 – VAT Directive; Annex III

Please note that certain subcategories or specific details were omitted from the overview below for clarity and ease of reading. For a complete and detailed description, please refer to the official legal text.

Article	Goods and services
(1)	foodstuffs (including beverages but excluding alcoholic beverages) for human and animal consumption;
(2)	supply of water;
(3)	pharmaceutical products used for medical and veterinary purposes, including products used for contraception and female sanitary protection, and absorbent hygiene products;
(4)	medical equipment, appliances, devices, items, aids and protective gear, including health protection masks, goods essential to compensate and overcome disability;
(5)	transport of passengers and the transport of goods accompanying them;
(6)	supply, including on loan by libraries, of books, newspapers and periodicals either on physical means of support or supplied electronically;
(7)	admission to shows, theatres, circuses, fairs, amusement parks, concerts, museums, zoos, cinemas, exhibitions or access to the live-streaming of those events;
(8)	reception of radio and television broadcasting services; internet access services;
(9)	supply of services by writers, composers and performing artists, or of the royalties due to them;
(10)	supply and construction of housing, as part of a social policy, as defined by the Member States; renovation and alteration, including demolition and reconstruction, and repairing of housing and private dwellings; letting of immovable property for residential use;
(10a)	construction and renovation of public and other buildings used for activities in the public interest;
(10b)	window-cleaning and cleaning in private households;
(10c)	supply and installation of solar panels on and adjacent to private dwellings, housing and public and other buildings used for activities in the public interest;
(11)	supply of goods and services of a kind normally intended for use in agricultural production but excluding capital goods such as machinery or buildings; and, until 1 January 2032, supply of chemical pesticides and chemical fertilisers;
(11a)	live equines and the supply of services related to live equines;
(12)	accommodation provided in hotels and similar establishments;
(12a)	restaurant and catering services;
(13)	admission to sporting events or access to the live-streaming of those events or both; use of sporting facilities, and the supply of sport or physical exercise classes;

Article	Goods and services
(15)	supply of goods and services by organisations engaged in welfare or social security work as defined by Member States and recognised as being devoted to social wellbeing by Member States, in so far as those transactions are not exempt pursuant to Articles 132, 135 and 136;
(16)	supply of services by undertakers and cremation services;
(17)	provision of medical and dental care and thermal treatment in so far as those services are not exempt pursuant to of Article 132;
(18)	supply of services provided in connection with sewage, street cleaning, refuse collection and waste treatment or waste recycling;
(19)	supply of repairing services of household appliances, shoes and leather goods, clothing and household linen;
(20)	domestic care services such as home help and care of young, elderly, sick or disabled;
(21)	hairdressing;
(22)	supply of electricity, district heating and district cooling, and biogas, supply and installation of highly efficient low emissions heating systems; and, until 1 January 2030, natural gas and wood used as firewood;
(23)	live plants and other floricultural products;
(24)	children's clothing and footwear; supply of children's car seats;
(25)	supply of bicycles, including electric bicycles; rental and repairing services of such bicycles;
(26)	supply of works of art, collectors' items and antiques listed in Annex IX, Parts A, B and C;
(27)	legal services supplied to people under a work contract and unemployed people in labour court proceedings, and legal services supplied under the legal aid scheme;
(28)	tools and other equipment of a kind normally intended for use in rescue or first aid services when supplied to public bodies or non-profit-making organisations active in civil or community protection;
(29)	supply of services in connection with the operation of lightships, lighthouses or other navigational aids.

Table 3 – VAT rate overview, standard and reduced rates, EU, 1 July 2025

Member State	Standard rate	Reduced rate	Member State	Standard rate	Reduced rate
Austria	20	10/13	Italy	22	5/10
Belgium	21	6/12	Latvia	21	5/12
Bulgaria	20	9	Lithuania	21	5/9
Croatia	25	5/13	Luxembourg	17	8/14
Cyprus	19	5/9	Malta	18	5/7
Czech Republic	21	12	Netherlands	21	9

Member State	Standard rate	Reduced rate	Member State	Standard rate	Reduced rate
Denmark	25	/	Poland	23	5/8
Estonia	24	9/13	Portugal	23	6/13
Finland	25.5	10/14	Romania	19	5/9
France	20	5.5/10	Slovakia	23	5/19
Germany	19	7	Slovenia	22	5/9.5
Greece	24	6/13	Spain	21	10
Hungary	27	5/18	Sweden	25	6/12
Ireland	23	9/13.5			

Data source: [Taxes in Europe database](#) (last updated 1 July 2025). Romania increased its standard rate from 19 % to 21 % on 1 August 2025. Please note that this overview does not list super-reduced or parking rates.

Table 4 – Actionable policy gap, € millions, 2022

Member State	Standard rate	Member State	Standard rate
Austria	12 389	Italy	90 546
Belgium	14 647	Latvia	699
Bulgaria	627	Lithuania	1 040
Croatia	2 818	Luxembourg	1 714
Cyprus	1 020	Malta	50
Czech Republic	5 438	Netherlands	20 806
Denmark	1 723	Poland	39 034
Estonia	555	Portugal	10 615
Finland	7 285	Romania	8 128
France	80 056	Slovakia	2 730
Germany	74 831	Slovenia	2 064
Greece	13 334	Spain	66 232
Hungary	5 229	Sweden	10 197
Ireland	7 080	EU-27	480 932

Data source: European Commission, CASE, Poniatowski, G., Bonch-Osmolovskiy, M., Braniff, L., Harrison, G., Luchetta, G., Neuhoﬀ, J., Śmietanka, A., Zick, H., [VAT gap in the EU – Report 2024](#).