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# ***Financial Services VAT Alert***

## **Tracking EU VAT Developments**

*January 2012  
Edition 2012/1*



**pwc**

## **Editorial**

Dear readers,

Hereby we present to you the first FS VAT Alert for the year 2012. In this January edition you will find the most important VAT developments that have occurred over the past month.

Enjoy reading!

Frans Oomen

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## **EUROPEAN UNION**

### **1. Polish Presidency Progress report regarding the VAT treatment of insurance and financial services**

*On 14 December 2011, the Working Party on Tax Questions (Indirect Taxation) discussed the draft Presidency progress report on the Proposals for a Council Directive and a Regulation as regards the VAT treatment of insurance and financial services and agreed on a text for the report. Please find below a brief summary of the report.*

For the meeting of the High Level Working Party (HLWP) on 26 October 2011 the Polish Presidency identified two possible solutions:

1. To continue the work on the basis of the package of guidelines that would form a future compromise; or
2. To postpone further work on the dossier until examination of the VAT strategy and proposals on the financial sector taxation, this may lead to a new impulse in this file.

During the discussion in the HLWP the vast majority of Member States supported continuation of the work and have shown openness towards the efforts to achieve a compromise as soon as possible.

Some other issues that came up from the report include:

- Working towards a guideline concerning transfer of insurance and reinsurance contract portfolios, assuming that transfer of insurance and reinsurance contract portfolios and transfer of credit contract portfolios

should be treated equally for VAT purposes, which would mean that both types of transfers should be exempt from VAT;

- The majority supported a narrow scope of the definition “outsourcing”, accepting that exemption within outsourcing should be granted only for services of financial or insurance nature;
- The majority of Member States supported equal treatment of investment funds and pension funds, by application of exemption to management of funds, irrespective of their legal form and business structure, in order to avoid possible distortions of competition and not to create artificial burdens in the area of the management of those funds. However, a few Member States argued that certain types of pension funds were by their nature different from investment funds and, in their view, should not be exempt. Some Member States are of the opinion that the exemption should be limited to investment funds collecting savings of small investors;
- In the opinion of the majority of Member States exemption of financial derivatives should only apply to those of a financial nature, while transactions in commodities should be recognized as taxable. Nevertheless, further work should be undertaken to investigate the VAT treatment of derivatives and, in this context, the merits of the simplification for exchange traded commodities.

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## **2. Summary of main EU VAT changes in 2012**

### **2012 Rate changes**

- Belgium - abolished VAT exemption for Notary and Bailiff fees and abolished 12% reduced rate for digital TV subscriptions effective 1 January 2012;
- Czech Republic - reduced rate increase from 10% to 14% effective 1 January 2012;
- Finland - subscriptions to publications 0% to 9% effective 1 January 2012;
- France - reduced rate increase from 5.5% to 7% effective 1 January 2012 (including e-books; increase from 5.5% to 7% on hard copy books postponed to 1 April 2012);
- Hungary - standard rate increase from 25% to 27% effective 1 January 2012;
- Ireland - standard rate increase from 21% to 23% effective 1 January 2012
- Italy - proposed increase in standard rate from 21% to 23% and reduced rate from 10% to 12% from September 2012;
- Luxembourg - e-books taxable at 3% rate (from 15%) effective 1 January 2012;
- [Norway - intermediate VAT rate increased from 14% to 15% effective 1 January 2012];
- Poland - children's clothing liable to 23% VAT (from 8%) effective 1 January 2012;
- Portugal - changes to supplies liable to intermediate and reduced VAT rates effective 1 January 2012; and
- Portugal - standard VAT rate in Madeira will increase from 16% to 22% in April 2012; reduced rates of 4% and 9% will also increase to 5% and 12% respectively.

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## **DENMARK**

### **3. The Danish tax authorities' interpretation of the ECJ case AB SKF**

*In recently published guidelines, the Danish tax authorities have described to what extent the ECJ case AB SKF will change or define Danish practice for VAT deductibility in connection with parent companies selling shares etc. in subsidiaries.*

The Danish tax authorities state that whether a transfer of shares is comparable with a transfer of business (TOGC) must be assessed in each individual case. However, the Danish tax authorities do not find that a business' transfer of shares in subsidiaries is in general comparable with a transfer of business, as the sale of shares does not involve a transfer of the company's (the legal entity of which the shares are sold) assets and liabilities.

On the other hand, the Danish tax authorities state that costs defrayed in connection with a transfer of shares as part of a transfer of business, is deductible. This changes Danish practice.

Finally, the Danish tax authorities define the criteria for when the purchased expenses are considered as used in VAT exempt transactions which is not VAT deductible. It should thus be taken into account whether the defrayed expenses are included in the price of the sold shares, or are solely part of the cost elements in the remaining activities of the taxable person and thus VAT deductible. The Danish tax authorities notice that if the purpose of the expense is to influence the price of the

shares in a positive direction, including to promote the demand for the shares, the expense will be considered as included in the price of the sold shares and is therefore not deductible.

So far Danish practice has not accepted VAT deductibility on costs in relation to the sale of shares, and as we understand the new guidelines, there is no indication that this will change in the future. It also seems that the Danish tax authorities will not consider even a 100 % transfer of shares in a subsidiary as being a VAT exempt transfer of business (TOGC). However, they have stated that an assessment in each case is needed, and that such assessment could lead a different point of view in the specific situation.

Thus the only alteration in Denmark as a result of ECJ case AB SKF is that if a transfer of the assets of a fully VAT liable business includes a block of shares, the costs in connection with the transfer of the block of shares is also VAT deductible.

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#### **DID YOU KNOW? DENMARK**

##### **Special payroll tax**

As of 1 January 2012 share payments to employees are subject to the special payroll tax. This means that the financial sector must also pay 10.5 % in special payroll tax of share payments. The tax base will be defined similar to the rules regarding personal income tax.

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## **GERMANY**

### **4. Termination of a VAT group in case of insolvency**

*An organizational link is required in order for taxable persons to be able to be part of a VAT group. The question is what the effect of insolvency is in respect of the organizational integration.*

Based on a ruling of the Bundesfinanzhof, the organizational integration ends if - as a matter of fact, even though not to the full extent in legal terms - the authority to dispose as well as administrative power is transferred to a temporary liquidator in terms of the remaining operative business units.

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### **5. Share deal as transfer of going concern**

The Federal Ministry of Finance (FMoF) has, by reference to a decision of the Supreme Tax Court, amended the VAT Application Guidelines with comments about transfers of going concern (TOGC) in case of a share deal. The transfer of shares is only considered to be a TOGC if the acquirer enters in the legal relationships of the transferor to the sold company which cause that the shares are considered to be held for business purposes. In case of a VAT group, this may be the case if the acquirer enters into the legal relationships which led to economical integration of the concerned affiliate in the transferor's business. In such

cases, a TOGC may also be present if the acquirer does not meet the other conditions for VAT grouping with respect to the affiliate company.

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## **6. Input VAT deduction and correction: changes in position of fiscal authority**

With circular letter dated 2 January 2012 the Federal Ministry of Finance (FMoF) followed the outcome of several decisions as made by the Federal Court of Finance (BFH, judgment of 9 December 2010, VR1710; 12 January 2011, XIR908; 13 January 2011, VR1208; 27 January 2011, VR3809; 3 March 2011, VR2310) in terms of input VAT deduction and correction.

This led to several changes in the authorities' view and thus in the German VAT Application Decree. In this circular letter the FMoF explained in detail when an input VAT deduction is possible and also gave information on the requirements for potential corrections. One of the major changes is that input VAT deduction is not given if an acquisition was made solely for the private sphere of the taxable person. This also applies where the taxable person generally intends to use the acquired goods to make a supply free of charge. In this case the right to deduct input VAT is not given and the private use is not taxable. The FMoF differentiates in the sector of private sphere between non-entrepreneurial activities and private use, which does not form part of the company's core business activities. Where an asset is used only partly entrepreneurial, a full input VAT deduction is only possible where the other part of the

use is a private use, which is then taxable as supply free of charge. Where the other part of the use is only a non-entrepreneurial activity, a full input VAT deduction is not possible. What the non-entrepreneurial activity is, is defined in the circular letter. Besides others, the sale of shares under company law falls under this term, provided that the shares are not held in the entrepreneurial sphere of the company.

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## **ITALY**

### **7. No limit for the supplier to charge assessed VAT to its customers and right to deduct it by the latter**

Art. 93 of a Decree (so called "*Decreto Liberalizzazione*"), published on 25 January 2012 in the Official Gazette and effective as of 25 January 2012 has replaced Article 60, paragraph 7, Presidential Decree 633/1972.

According to the former Article 60, paragraph 7, Presidential Decree 633/1972, in case of higher VAT due resulting from a tax assessment by the Italian Tax Authorities, the taxpayer had no right to charge the assessed VAT to its customers.

According to Circular letter no. 131/12058 of 12 September 1986, the taxpayer was entitled to charge VAT to his customers only until the issuance of the final assessment by the Italian Tax Authorities.

According to the new text of Article 60, paragraph 7:

1. the taxpayer is only entitled to charge VAT or additional VAT resulting from tax assessments to the recipients of goods and services after the payment of VAT or additional VAT, penalties and interests;
2. in this case, the recipients of goods and services may exercise the right to deduct, at the latest, in the VAT return related to the second year following the one in which they have paid the VAT or additional VAT charged based on the conditions existing when the original operation takes place.

The above represents an important change for taxpayers in Italy, by reducing costs in case VAT is definitively assessed.

Moreover, as currently no guidelines from the Italian Tax Authorities are available it might be worth pointing out the following:

- The last part of the above provision would represent a derogation to the limitation period provided by the Italian Law (Article 19, Presidential Decree 633/1972), which usually starts when VAT becomes chargeable;
- By doing so, the principle of tax neutrality would be met for both the assessed taxpayer and its customers;
- The amended provision does not seem to provide for any time limit for the taxpayer to charge the assessed VAT to its customers and it is not clear whether it can be retrospectively applied;

- Even if official guidelines are not available so far, documental evidences of the actual payments is required;
- Based on the wording of the new text, it is unclear whether a foreign customer is entitled to recover the VAT charged “to late” by the taxpayer via the procedure provided for by the Directive 2008/9/EC and the EC Thirteenth VAT Directive or if they have to be VAT registered in Italy (the current wording refers to the submission of the VAT return).

In the end, this new provision could also be seen as a prompt reply by the Ministry of Finance to the infringement proceeding against Italy that the European Commission opened on November 24, 2011, with reference to the former text of Article 60, paragraph 7, Presidential Decree 633/1972.

The previous law provision seemed to breach Article 1 of the VAT Directive 2006/112/EC and the tax neutrality principle.

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## **THE NETHERLANDS**

### **8. New Decree on deduction of input VAT**

*On 6 December 2011 a new Decree on deduction of input VAT was published. This Decree elaborates on the consequences of the implementation of the technical revision of the VAT Directive as of 1 January 2011. The Decree contains a number of (policy) directions.*

Below we give a brief summary of the key issues in the Decree for the FS practice:

In the Decree a description is given of the general principles that apply in determining whether there are economic or non-economic activities. It also indicates that if there is such close connection between economic and non-economic activities, that overall these activities can be regarded as economic activities;

The Decree also addresses the right to deduct VAT on costs directly attributable to economic and non-economic activities;

A description is given on how to deal with costs that are not directly attributable to economic or non-economic activities. For the deduction of VAT, these costs must be divided into a deductible and non-deductible portion. When this split is made, you have to take into consideration the key criteria which objectively show what part of the costs are attributable to economic activities and which part to non-economic activities;

The Decree indicates to what extent there is a right to deduct VAT on costs relating to the transfer of a totality of assets or part thereof (TOGC). The right to deduct VAT is

determined on the basis of economic activities (taxable or exempt) that occur in that part of the company;

The Decree discusses the doctrine of the costs of joint accounts and the right to deduct VAT for the taxable person who acts as cost sharing party towards the other participating taxable persons.

The key change is that the Dutch revenue now takes the view that cost sharing arrangements in principle cannot be changed over time. This does not seem in line with Dutch case law. Financial institutions should review the cost sharing arrangements they have in place.

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#### **DID YOU KNOW? LUXEMBOURG**

##### **eVAT mandatory as from 1 January 2013**

Taxpayers in Luxembourg filing periodic VAT returns (i.e. monthly or quarterly), will have to file their returns electronically for the period starting 1 January 2013. To do so, taxpayers will need to apply for a LuxTrust Smartcard or Signing stick to electronically sign their VAT returns and get registered for electronic filing with the Luxembourg VAT authorities. Do not hesitate to contact your usual PwC contact or go to <http://www.aed.public.lu/etva/index.html> for more information on electronic filing.

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## ROMANIA

### 9. Tax authorities to cancel VAT registration of dormant companies

*On 5 December 2011, a draft emergency ordinance amending the Fiscal Code was published announcing plans by the tax authorities to cancel the VAT registration of companies that do not carry out economic activities or do not submit VAT returns for a specified period.*

The Ministry of Finance has established drastic measures to cancel the VAT registration of businesses that do not carry out economic activities, do not submit VAT returns for a certain period, or commit tax evasion. The measures could potentially affect many thousands of taxpayers.

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## UNITED KINGDOM

### 10. Court of Appeal allows HMRC's appeal in payment handling case: Axa UK plc.

This case returned to the Court of Appeal (CA) after the ECJ's ruling that VAT exemption did not extend to a service of transferring payments between patients and dentists because the service went beyond payment processing and encompassed debt collection. The tax payer

sought to persuade the CA that the ECJ had mischaracterised the transaction as debt collection rather than payment handling and/or that the case should be referred back to the ECJ for clarification. However, the CA considered that the ECJ's judgment was correct and allowed HMRC's appeal, holding that the UK law on exemption could be interpreted in accordance with the EU law even though the exclusion of debt collection had not been transposed into UK law.

It remains to be seen whether the case will proceed to the Supreme Court. Clearly, businesses which are involved in supplying services of this nature will need to consider the VAT treatment carefully, as it appears that there is a fine dividing line between those which are to be regarded as exempt transactions concerning payments and those which constitute debt collection.

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#### **DID YOU KNOW? LUXEMBOURG**

##### **Proposal for cancellation of VAT registrations by the authorities**

A recent law proposal foresees the introduction in Luxembourg VAT law of provisions whereby the Luxembourg tax authorities may cancel a VAT registration if they have sufficient proof that the VAT registered person does no longer carry out economic activities. The proposal is foreseen to be voted end of January 2012.

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