VAT: Transaction tax guidance to assist global businesses

October 2012

Keeping US multinational companies informed of key indirect tax developments across the globe.

Global Indirect Taxes

In brief: Among other developments this month, of particular importance to US multinationals is the new UK legislation that implements a nil registration threshold for non-established suppliers, the continued developments of the Pilot VAT Program in China and potential changes to the VAT refund procedure in Germany.

In the UK, the introduction of the nil registration threshold will increase the likelihood of non-residents creating UK VAT obligations. In addition to the nil registration threshold, the UK has also implemented revisions to electronic notification procedures and changes to the rules for self storage supplies.

In China, the continued expansion of the Pilot VAT Program is expected to bring challenges as businesses transition to the new rules, particularly in the regions which are expected to implement the Pilot Program before the end of the year.

In Germany, infringement proceedings from the EU Commission attempt to streamline the process for non-residents to submit VAT refund requests.

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EUROPEAN UNION

European Court of Justice

Judgment in Case C-587/10 (VSTR): On September 27, 2012, the European Court of Justice (ECJ) delivered its judgment in the above mentioned case, holding that the granting of exemption (i.e., zero rating) for an intra-community supply of goods cannot be refused solely on the basis that the supplier did not obtain the purchaser's EU VAT registration number.

In summary, the ECJ held that where the supplier acts in good faith and takes all the measures which can reasonably be required of him, but still is unable to provide the VAT ID number of their customer, then the supply should still be eligible for exemption, provided that the supplier obtains other information to sufficiently demonstrate that the customer is a taxable person acting as such in respect of the purchase.

While the impact of the judgment is yet to be tested in each Member State, it appears that the ECJ's ruling may prove useful for businesses in the context of supporting exemption, particularly in cases where all reasonable measures for obtaining a customer's VAT number have been exhausted. Businesses should be mindful that this judgment is unlikely to be relevant in cases where reasonable measures have not been taken to obtain the VAT registration number of the customer, and that the application of exemption in such a scenario is still likely to be denied.

ECJ judgment on VAT recovery by holding companies: In a case concerning costs recharged by an active holding company to its subsidiary, the ECJ has held that input VAT incurred by the holding company is creditable if it has a direct and immediate link with the taxable supplies made by the holding company(*Portugal Telecom SGPS, SA*: C-496/11).

The taxpayer in this case was an active holding company providing technical, administrative and management services to its subsidiaries. The taxpayer bought services from consultants and recharged those services, plus VAT, to its subsidiaries. The taxpayer deducted all of the input VAT incurred in relation to the purchase of the services. However, the tax authority took the view that the taxpayer should only be entitled to recover a pro-rated amount, subject to its overall VAT recovery position. In this case, the appropriate percentage was set at 25%, determined on the basis that the primary activity of the holding company was to hold shares in its subsidiaries, an activity which does not facilitate VAT recovery in its own right. The Taxpayer appealed and ultimately the second tier court in Portugal referred the case to the ECJ.

The ECJ restated its historical case law and reaffirmed that, if inputs have a direct and immediate link with wholly taxable output transactions, the taxpayer should be entitled to full VAT credit in respect of those inputs. It was also stated that VAT credit could not be limited simply because domestic legislation treated the taxable transactions as being ancillary to the main activity of the holding company (the activity of holding the shares in the subsidiaries).

While this judgment appears to provide clarity with regard to the VAT recovery of certain costs incurred by holding companies, there continues to be significant complexities in this area. Businesses incurring VAT at the holding company level should review their position in light of this judgment and determine whether there may be scope for increased VAT recovery.

Austria

Place of supply and invoicing changes effective January 1, 2013: The Austrian

Tax Amendment Act 2012 introduces a number of important VAT measures. Included in the measure are changes to the place of supply rules for Business to Consumer (B2C) long-term hiring of transport, which will now become taxable at the place where the private individual customer is (i) established, (ii) has his permanent address, or (iii) usually resides.

Other key changes effective January 1, 2013 are set out below:

- in order to prevent tax evasion, the market value (i.e., arm's length value), rather than the invoice value will be viewed as the taxable amount in respect of certain related party transactions
- the VAT invoicing rules of Directive 2010/45/EC, which include certain simplifications for e-invoicing and provide clarity on invoice language requirements, have been transposed into national law.

Germany

The European Commission requests that Germany amend its rules on VAT refunds to non-EU businesses: The European Commission has requested that Germany amend its legislation which requires that VAT refund applications filed by non-EU businesses be personally signed by the applicant. The Commission considers that this German rule goes against the basic EU law principles of effectiveness, proportionality and equivalence and can make it excessively difficult for those not established in the EU to obtain a VAT refund. The Commission considers that Germany's objective with this requirement, namely combating tax evasion and ensuring a proper refund procedure, could be achieved through other means, such as the appointment of a tax representative.

The request takes the form of a Reasoned Opinion (the second stage of an infringement procedure). If the legislation is not brought into compliance with EU Law within two months, the Commission may refer the matter to the ECJ.

Businesses currently submitting (or expecting to submit) 13th Directive claims to Germany should be mindful of these proceedings to be sure that any procedural changes for submitting such claims are enacted as appropriate.

Hungary

New financial transactions tax effective January 1, 2013:
On July 23, 2012, the Hungarian Parliament adopted a new act which introduces a duty on financial transactions, commonly known as the tax on 'yellow cheques' (postal money orders). The tax will enter into force on January 1, 2013.

The new act applies to payment service providers with a registered address or branch office in Hungary and, in certain cases stipulated by law, to the National Bank of Hungary (NBH). Generally affected transactions include money transfers, direct debit, cash in and out payments and cash transfers. In most cases, the tax rate will be 0.1% of the amount of the transaction but should be no more than HUF 6,000 per transaction. This cap will, however, not apply to transactions in which the tax is payable by the NBH, the State Treasury, or the institution that operates the Posta Elszámoló Központ (Postal Clearing Centre), i.e. Magyar Posta Zrt.

Businesses conducting or utilizing financial services within Hungary should determine the impact of the new tax on their transactions and, if necessary, ensure procedures and systems are updated before January to comply with the associated compliance requirements.

Latvia

Work on recast VAT law nearly complete: The Latvian VAT Act, which has been amended more than 30 times since its adoption in 1995, is to be superseded by a recast VAT Act next year. Work on the new version of the legislation started back in 2007 and is now approaching the final stages prior to implementation.

The Bill features a rearranged structure, with certain terms and their definitions being superseded and/or clarified. Clarifications have also been made to the sections which determine the tax point (time of supply) for domestic and intra-Community supplies of goods, and for intra-Community acquisitions of goods. In addition to the changes/ clarifications, the bill improves the wording of existing clauses, tidies up the structure of the law and brings the terminology into line with Directive 2006/112/EC.

The recast law is expected to come into force on January 1, 2013 and aims to promote the administration of VAT and simplify taxpayers' duties and administrative expenses. Businesses operating in Latvia should familiarize themselves with the key additions and revisions to ensure compliance and efficiency under the new law.

United Kingdom

Nil registration threshold for non-established suppliers: The Value Added Tax (Amendment) (No. 2) Regulations 2012 SI 2012/1899 implements the following changes to the UK VAT legislation:

- establishment of a nil registration threshold for non-established taxable persons, effective December 1, 2012
- introduction of electronic applications and notifications relating to group registration, VAT registration, transfers of going concerns, VAT representatives, annual accounting and flat-rate schemes
- introduction of invoicing rules in relation to the anti-forestalling rules for supplies of self storage and alterations to protected buildings
- adoption of a new regulation, which will enable suppliers of self storage to opt to include capital items with a value below the current threshold of £250k in the VAT capital goods scheme when their supplies change from exempt to standard-rated on October 1, 2012.

The removal of the registration threshold for non-established businesses (i.e., introduction of the nil threshold) will be of particular importance to US businesses. For example, under the new rules, even low value supplies of goods made in the UK by non-established entities should now trigger a VAT registration obligation.

EUROPE

Serbia

VAT rate increase to 20% effective October 1, 2012: As part of a package of measures to tackle the budget deficit, the standard VAT rate was increased from 18% to 20%, effective October 1, 2012.

In addition, the Ministry of Finance is planning to introduce a number of other VAT measures with a likely effective date of January 1, 2013. The changes are expected to affect, among others, free of charge supplies of services, immovable property, distribution of marketing material, VAT registration, place of supply rules, and refunds of VAT to non-residents. The Ministry will also legislate for a number of rules that have not to date been covered in the VAT legislation, but were applied either as a result of practice or based on non-binding opinions.

US companies operating in Serbia should be aware of the upcoming changes and prepare for operation under the new rules. Further information will be provided in this respect once the changes are finalized.

Extended scope of VAT exemption for asset transfers: The Minister of Finance and Economy has issued amendments to the VAT Rulebook dealing with the transfer of all or part of the goods forming part of a business or business unit. The new rules are effective August 4, 2012.

Under the amendments, the transfer of assets which represent a 'functional business unit' should be treated as falling outside the scope of Serbian VAT. Under the previous rules, such a treatment only applied if the part of the business being transferred represented a complete 'technical-technological unit' (e.g., production plant, production line, etc.).

The previous rule had given rise to difficulties in interpretation and the change intends to bring clarity and extension to the scope of the business transfer rules.

ASIA/PACIFIC

China

Potential impact of extended VAT Pilot Program: As reported in previous issues, following the success of the program in Shanghai, the Chinese State Council announced that the VAT Pilot Program would be implemented in another 10 Chinese provinces by the end of 2012 (Beijing, Tianjin, Jiangsu, Zhejiang, Anhui, Fujian, Hubei, Guangdong, Xiamen and Shenzhen). The operation of the Pilot Program in these regions should be in line with the scheme currently implemented in Shanghai, with the various circulars and guidance issued for Shanghai being technically applicable to the new Pilot Regions.

It is expected that introduction of the Pilot Program in the new regions may raise additional complexities due to the existence of separate State Tax Bureaus and Local Tax Bureaus for the administration of VAT and BT respectively (as opposed to a unified Tax Bureau in Shanghai). More specifically, it is possible that the different Tax Bureaus may interpret the impact and scope of the Pilot Program differently, particularly in the case of services which are not well defined under the current measures. Any such complications are likely present increased challenges for taxpayers in these new regions, particularly during the transitional period.

Meanwhile, it is expected that further guidelines are to be issued to clarify certain practical issues associated with the Pilot Program in Shanghai. These may include:

- whether certain consulting services fall within the scope of Pilot Services and, therefore, are eligible for VAT exemption when provided to a foreign party
- clarity over the implementation of the 'exempt, credit and refund' treatment for exports by qualified Pilot Enterprises.

The significant changes in China continue to warrant careful attention to the developing rules and procedures. In particular, businesses operating within the new pilot regions should ensure they are prepared to operate under the new rules at the date of implementation which should be before the end of the year.

Vietnam

Update on VAT invoices issued in foreign currency: The Ho Chi Minh City Tax Department recently issued an

Official Letter (Letter 4380) reconfirming that VAT invoices denominated in foreign currency issued by unauthorized sellers will be considered illegal. Businesses receiving such invoices from their suppliers are likely to be denied input VAT credit and corporate income tax deduction.

Businesses operating in Vietnam should be mindful of the risk involved in receiving invoices in foreign currency and implement processes to ensure that non local currency invoices are accepted from specifically authorized suppliers.

AFRICA

South Africa

VAT treatment of allowances and discounts: The second version of Binding General Ruling 6 (BGR 6(2)) which deals with the VAT treatment of allowances and discounts, appears to eliminate the practical problems created by the original version, but does not address all the issues experienced by businesses.

By way of background, differences in the classification of allowances (including discounts, rebates and incentives) in the retail industry have resulted in VAT difficulties and risks for suppliers (e.g., manufacturers) and retailers. Often, when a discount is allowed, suppliers and retailers will disagree on whether the supplier has to issue a credit note for a price reduction or whether the retailer must issue a tax invoice for a separate taxable supply.

In an attempt to address this issue, the South African Revenue Service (SARS) issued Binding General Ruling 6 (BGR 6(1)) dated March 25, 2011, to provide a legal framework for the VAT treatment of allowances in the Fast Moving Consumable Goods industry. However, because the ruling was not enacted into law, practical problems were created due to inconsistent compliance from vendors. The second version, BGR 6(2) issued on June 19, 2012 aims to eliminate these practical problems by allowing the parties to agree on the most preferred VAT treatment of an allowance. However, BGR 6(2) does not clarify the extent to which the parties' classification of the allowance will be accepted by the tax authorities. Additionally, it does not provide a solution where the parties do not agree on the reason for the allowance, which can often be the case.

This latest development is a timely reminder of the complexities associated with rebates and incentive programs. Businesses operating in affected industries should examine their discount and rebate programs to ensure they meet their global VAT obligations.

AMERICAS

Mexico

Tax authority provides service for e-invoicing: In order to promote electronic invoicing, the Mexican Tax Administration Service (SAT) has created and launched a service to generate electronic invoices, which is primarily aimed at taxpayers with low invoicing volumes. The service is targeted at the leasing industry, individuals performing business activities, and independent fee earning professionals (among others).

The main features of the new service include:

- compatibility with various platforms and browsers
- certification by SAT is performed online
- allowance for users to look up and recover electronic invoices
- generation of XML format and hard copy invoices.

In order to use the new service, taxpayers must have an electronic signature, be able to issue at least one digital stamp certificate, and accept the terms and conditions of use of the service.

For more information, please do not hesitate to contact your U.S. VAT Team:

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Global VAT Online Service

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