

VAT: Constant change marks global headlines

September 2012

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

Global Indirect Taxes

In brief: Among many other developments this month, of particular importance to US multinationals is the introduction of a new UK VAT law for cost sharing agreements as well as further guidance on the Chinese VAT Pilot Program. The new UK VAT law offers guidance for independent businesses and organizations with VAT exempt and/or non-business activities that may wish to set up cost sharing arrangements to mitigate irrecoverable VAT costs. The guidance from China explains how the Pilot Program applies to international transportation services, certain services of qualified animation enterprises, shipping agency services, and operating lease services.

EUROPEAN UNION

European Court of Justice

ECJ hears arguments against infringement proceedings: The ECJ heard arguments against the European Commission's infringement action on Member States which permit 'non-taxable persons' (e.g., pure holding companies) to join VAT groups.

The Commission's position is that national legislation in the UK, Ireland, Finland, Denmark and Czech Republic is incompatible with EU legislation that, in the Commission's opinion, requires each VAT group member to be a taxable person in its own right. At the hearing, the Member States defended their position. Their principal arguments were:



- the single taxable person created by the VAT group must carry on an economic activity, not each individual group member;
- the Directive permits grouping of 'persons', not 'taxable persons' and this was the intention of the legislature;
- there is no risk that groups will be composed solely of non-taxable persons;
- inclusion of holding companies achieves the Directive's objective of simplifying VAT and may be necessary in some cases for the prevention of avoidance;
- exclusion of particular entities could breach neutrality and equal treatment;

Businesses which currently have non-taxable companies (e.g., passive holding companies) inserted into VAT groups in the affected jurisdictions should monitor the outcome of these proceedings. In the event that the EU Commission is successful in their arguments, domestic laws are likely to be changed such that non-taxable companies can no longer be included in VAT groups. This would have a direct effect on the VAT recovery position of the removed entities and is likely to create irrecoverable VAT costs.

Belgium

Repeal of the guarantee payment required to obtain an ET 14000 license (import VAT deferment license): Section 5, §3 of Belgian Royal Decree no. 7 establishes a system whereby the payment of VAT due on importation of goods can be shifted to the periodic VAT return rather than being paid to the Customs Authorities. In order to benefit from the deferral, taxable persons have to request an import

deferral license and pay a 'guarantee' amount of 1/24th of the annual import VAT due.

As of October 1, 2012, the payment of this 'guarantee' will no longer be required. The Government is still working on the exact details of this repeal as well as on transitional measures for refunds of outstanding guarantee amounts. Further information is expected to be available in due course.

Businesses currently engaging in the import VAT deferral scheme should prepare to seek recovery of the guarantee amount. Businesses who have not historically operated under the deferral license should consider obtaining the new guarantee-free license as a means to improve their cash flow position.

France

VAT rate increase cancelled: As reported in the [January VAT Alert](#), the French Parliament has now confirmed that the increase in the standard VAT rate from 19.6% to 21.2%, which was due to take effect from October 1, 2012, has been cancelled. However, future rate changes cannot be ruled out.

It has also been confirmed that all books (both hard copy and electronic) will be subject to the 5.5% reduced rate from January 1, 2013 rather than the current 7% reduced rate. However, this measure could be subject to change, as the European Commission is currently challenging Member States' application of reduced rates to e-books.

Germany

Sale of shares as sale of business: The sale of a self-contained business unit from one business to another is treated as being outside the scope of VAT in Germany (i.e., is not a taxable supply within the meaning of the German VAT Act). In January 2011, the Supreme Tax

Court held that this treatment could also apply to the sale of the shares in a subsidiary forming part of a VAT group. The condition was that either the entire share capital was sold, or that a majority holding was sold and that the acquirer purchased the shares with the intention of bringing the new subsidiary into a VAT group.

The finance ministry has now amended its VAT implementation decree to reflect this judgment such that the sale of shares now qualifies as a non-VAT-able sale of a business where the acquirer is able to assume the position of the seller as a lead company in a VAT group comprising the subsidiary acquired. This condition is deemed to be met if the newly acquired business is integrated into that of its new parent, that is, the subsidiary supports or complements the operation of the parent. It is not essential that the new subsidiary actually joins the VAT group.

The benefit of this treatment, as opposed to a VAT-exempt sale of shares, is that a deduction of the input tax incurred on costs associated with the sale (in this case, legal and consultancy) can be claimed in line with the business's overall VAT recovery position (in contrast, costs related to an exempt share sale are generally irrecoverable). Businesses should review their position to ensure that VAT recovery is maximized in connection with subsidiary disposals.

VAT-free business transfer despite only short-term lease of premises: The owner of a shop in Germany sold her business to a successor free of VAT under the exemption for a transfer of a going concern business. The assets transferred consisted of the stocks and shop fittings at an agreed value, with the premises being transferred under a lease cancellable at will at three months notice. The German Tax Authorities refused to accept that the sale was

exempt from VAT as the transfer of a going concern business, as the premises, which were necessary for the business operation, were not transferred for any significant length of time. The seller disagreed that a lease cancellable at will indicated only a short-term business transfer where there was no actual intention to give notice on the lease, and further claimed that official insistence on a long-term lease in order for VAT exemption to apply went beyond the requirements of the EU VAT Directive.

Following referral to the ECJ, the Supreme Tax Court (*Supreme Tax Court judgment XI R 27/08* of January 18, 2012, published on March 7, 2012) held that the VAT-exemption applied since the assets transferred were sufficient to enable the purchaser to carry on the business operation and that, whilst a shop needed premises, it was not necessarily tied to any specific location. It was noted that the business operated under the new owner for the following 23 months (until the shop was finally closed) demonstrating there was no immediate intention of winding it up the business at the moment of transfer.

Hotel voucher subject to VAT as a prepayment: A ticket agency ran a hotel voucher promotion entitling purchasers to a three-night stay at one of various hotels located in Germany and abroad. The hotel did not charge the guest or agency for the accommodation, but did require a minimum consumption in the hotel restaurant, such that this amount would be charged to the guest, regardless of whether they ate there or not. The agency sold each voucher for €49.90 and claimed that the amount was not a charge for a taxable service, as the service had not yet been, and likely never would be, performed.

Vouchers lapsed after a year and only about 14% were actually redeemed.

The Supreme Tax Court held that the sale of each voucher should be regarded as an advance payment for the anticipated services of the accommodation agent. The payment is therefore taxable at the standard rate hotel accommodation in Germany and exempt from German VAT in respect of accommodation located abroad. Further, given that the use of the voucher is unknown at the time of sale, the sale should be taxed at the standard rate, which may be subsequently reversed should the voucher be redeemed abroad. If the voucher is not redeemed at all, the taxation becomes absolute on the basis that the service of offering accommodation was performed in Germany, the country of the agency. (*Supreme Tax Court judgment* of September 8, 2011, published on January 11, 2012).

This case further demonstrates the complexity involved with supplies of vouchers for VAT purposes. Businesses providing vouchers should ensure comfort is obtained over the VAT liability of their supplies in order to avoid unexpected VAT costs or penalties for non-compliance.

Poland

Losses from sale of tax deductible debts may include VAT: On June 11, 2012, the Supreme Administrative Court issued *Case no I FPS 3/11*, stating that losses from the sale of receivables which were previously included in taxable revenue can now be treated as income tax deductible **together** with any VAT included in the receivables.

This resolution allows for substantial additional income tax deductions of up to 23% (i.e. the VAT rate) when receivables are sold. Businesses incurring losses from the sale of bad

debts stand to benefit significantly from this new position.

Portugal

Tax incentive for public to request VAT invoices: Effective from January 1, 2013, individuals will be allowed an income tax deduction of 5% of VAT incurred (subject to an upper limit of €250.00) in respect of the purchase of the following services:

- maintenance and repair of motor vehicles;
- maintenance and repair of motorcycles, related spare parts and accessories;
- accommodation, restaurants and similar; and
- hairdressing salons and beauty parlors.

Persons that intend to benefit from the incentive should ensure that the service provider issues a valid VAT invoice and includes their tax identification number on that invoice. Such invoices should then be kept by the individual for a four-year period. The provisions have been implemented to encourage individuals to request VAT invoices in an effort to counter tax evasion by businesses that provide the above services. Business operating in these areas should ensure that their systems and process are set up to issue compliant VAT invoices to individuals on request.

New invoicing rules: Decree Law no. 197/2012 dated August 24, 2012, introduces a number of VAT related changes, including:

- changes to the place of supply rules for long-term hiring of a means of transport by a non taxable person;
- changes to the tax point and chargeability of VAT on intra-

Community supplies of goods and services; and

- updates to invoicing rules.

In respect of the invoicing changes (effective from October 10, 2012), the following will apply:

- issuing valid VAT invoices will become mandatory (the concept of issuing "equivalent documents" disappears);
- mandatory language requirements for self-billing and reverse charge supplies;
- a simplified regime for invoicing will be introduced to replace the current regime of invoicing exemption and mandatory issuing of sales receipts; and
- e-invoicing rules will become more flexible, making it possible to choose means other than EDI and advanced electronic signature to guarantee the authenticity and integrity of the invoice.

Decree Law no. 198/2012, also dated August 24, 2012, further provides that, from January 1, 2013, taxable persons will have to notify the tax authorities of the data contained in invoices issued, by the eighth day of the following month of their issue (similar notification requirements are also being introduced in respect of transport documentation).

Compliance with the new invoicing and transport documentation rules will require procedural and systematic changes for businesses. Businesses should ensure that they are familiar with the new rules and are equipped to deal with the changes prior to implementation in 2013.

United Kingdom

Tax authority guidance on VAT cost sharing exemption: On August 24, 2012, Her Majesty's Revenue & Customs (HMRC) issued Brief 23/12 providing guidance on the newly introduced Cost Share Group Exemption - Group 16, Schedule 9 of the VAT Act 1994. The guidance follows the receipt of royal assent of the new law in the Finance Bill on July 17, 2012.

The cost sharing exemption applies when two or more organizations (whether businesses or otherwise) with exempt and/or non-business activities join together on a cooperative basis to form a separate, independent entity, a so-called cost sharing group (CSG), to supply certain services at cost between themselves. The exemption applies to supplies of certain qualifying services that are made by the representative member of the CSG to other members of the CSG. These supplies must be 'directly necessary' for the exempt and/or non-business supplies made by the members.

This policy applies to all independent businesses and organizations which have VAT exempt and/or non-business activities. Business such as charities, banks, education institutions can benefit greatly from the use of CSG arrangements by removing or mitigating the irrecoverable VAT cost incurred on services received.

MIDDLE EAST

Israel

VAT rate increase announced: The standard VAT rate increased from 16% to 17% with effect from September 1, 2012.

ASIA/PACIFIC

China

Additional VAT Pilot Program guidance: On June 29, 2012, the Ministry of Finance (MOF) and the State Administration of Taxation (SAT) have jointly issued a new circular

Caishui [2012] No 53, which provides additional policies relating to the VAT Pilot Program in the Pilot Regions. The circular covers international transportation services, certain services of qualified animation enterprises, shipping agency services, and operating lease services. The additional policies have retrospective effect from January 1, 2012, except in relation to operating lease services, which are effective July 1, 2012. The main points include:

- a provisional VAT rate of 3% will apply to international transportation services provided by transportation service providers from non-treaty countries/ regions;
- a transitional 3% VAT rate will apply to certain services provided by qualified animation enterprises (from January 1, 2012 until December 31, 2012);
- it has been clarified that shipping agency services are subject to the port services rate of 6% from January 1, 2012; and
- the VAT "Simplified Tax Calculation Method" applies to certain qualified operating leases that were in place prior to January 1, 2012.

As the expansion of the Pilot Program continues and the specific policies and regulations become clearer, additional changes and adaptation may be required. Businesses operating in China should continually review their position to determine the impact of the Pilot Program and ensure compliance with the revised laws.

Vietnam

Ruling on VAT treatment of interest paid to foreign lenders: The Ho Chi Minh City Tax Department recently

issued Official Letter 4927/CT-TTHT dated June 27, 2012, stating that interest paid to a foreign lender is liable to 5% VAT withholding, in addition to the 5% FCWT (Foreign Contractor Withholding Tax).

The Official Letter does not make it clear whether this will only apply to interest paid to a non-bank lender or will also catch loans from foreign banks. The basis for the 5% VAT rate is also unclear. Nevertheless, lenders providing loans to Vietnamese companies should be aware that VAT withholding is likely to be applicable going forward. Appropriate "gross up" provisions may be recommended for inclusion in loan agreements to ensure that lenders are able to increase their interest charges accordingly.

AFRICA

Tanzania

New VAT rate of 10%: The Minister of Finance has proposed to introduce a new VAT rate of 10% (in addition to the current rate of 18%). This new rate will apply to selected businesses that are currently enjoying special relief under the Third Schedule of the Value Added Tax Act.

This new VAT rate (in conjunction with changes to the special relief schemes) is expected to cause an increase in the number of taxpayers that are frequently in a net VAT refund position. Refunds of VAT in Tanzania can take over a year to process and the new VAT rules are expected to exacerbate this problem. For this reason, businesses operating in Tanzania should review the likely impact of the new VAT rate and associated changes on their overall VAT position.

In addition to the new VAT rate, the following new exemptions have also been introduced:

- electronic fiscal devices (EFDs) will now be exempt from VAT. This is a measure intended to make the EFDs affordable to the business community and encourage their use for improved tax compliance; and
- various equipment that will be used for the storage, transportation, and distribution of compressed natural gas and piped natural gas will also be exempt from VAT.

AMERICAS

Mexico

Application of 'pro homine' principle when interpreting VAT law: A tax court decision has established that the pro homine principle (a principle included in many international treaties covering the basis of human rights) should not apply to article 32, section VIII of the VAT Law, which sets out certain reporting obligations for taxpayers. This means that such reporting obligations have been found to not limit, suppress or exclude the fundamental rights of the individual taxpayers.

Article 32, section VIII, of the Value Added Tax Law establishes a formal obligation on certain taxpayers to report on a monthly basis, via electronic media and forms specified by the Revenue Administration Service, information pertaining to the payment, withholding, crediting and charging of VAT on operations conducted with suppliers. Failure to provide this information, or providing incomplete or erroneous information, constitutes a violation of the rules for filing tax returns and is subject to a fine.

The court ruled that it is not possible to interpret section VIII of Article 32 on the basis of the pro homine principle, since doing so would allow the taxpayer, merely as a result of claiming a violation of his fundamental rights, to violate the rules regulating compliance with tax obligations. The court found that the relevant Article does not regulate any protected rights of taxpayers, neither does it limit, suppress or exclude any of those rights. Businesses required to report under Article 32 should continue to do so in light of this ruling.

PwC has a global network of 1,900 indirect tax professionals in 130 countries worldwide, including a dedicated VAT team located in the U.S. who is available to provide real-time VAT advice. This News Alert does not provide a comprehensive or complete statement of the taxation law of the countries concerned. It is intended only to highlight general issues, which may be of interest to our clients. For issues relating to this News Alert, please contact your local Indirect Tax Practice advisor or the specialists listed at the end of this article.

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Global VAT Online Service

Many of the developments above are described in more detail on Global VAT Online (referred by many as "GVO") -- PwC's online subscription service which provides up-to-date business critical information on VAT/GST rates, rules and requirements around the world. This information will help you maintain control, mitigate risk, and improve the overall effectiveness of your VAT/GST function. For further information, please speak to your usual PwC advisor or a member of the U.S. VAT Team above. [GVO Website](#)

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SOLICITATION

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