

Financial Services VAT Alert*

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Indirect Taxes

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EUROPEAN UNION

1. Developments regarding the proposed reforms in respect of the VAT treatment of financial and insurance services

Whilst there is still no final draft of a proposed Directive and Regulation, businesses should follow the progress of the expected changes and consider the impact.

Background

In November 2007 the EU Commission submitted a proposed Council Directive and Regulation regarding the VAT treatment of financial and insurance services. The proposals included three sets of measures:

1. Modernisation of the definitions and rules governing exemption from VAT for financial and insurance services;
2. More general application of an option for taxation available to economic operators covering all financial and insurance services;
3. Introduction of a cross-border cost-sharing scheme for providers of insurance and financial services.

Since then, there have been a number of amended versions of the proposed Directive and Regulation. The most recent document to be published in this respect is the Czech Presidency Progress Report (10219/1/09) of 28 May 2009, which outlines the progress made by the Presidency in respect of the last published proposal for a Council Directive (7889/09 FISC 36) of 20 March 2009. We have outlined below some important developments.

1. Definitions

- Guaranteeing of debts – Export Credit Guarantees have been excluded from the exemption
- Financial transfers – payments made via mobile phone are now included in the exemption
- Transactions in financial derivatives – although member States are closer to agreement, the debate regarding the wording of the definition is ongoing.

- Management of investment funds – the purpose of the amendments to the definition of investment funds is to reflect the fact there should be no difference in the VAT treatment between direct investment in securities and collective investments. A paper from the Presidency is expected in relation to the position for pension funds.
- Outsourcing – there is no agreement on the definition of outsourcing and it seems likely that discussions will be put on hold until the core exemptions are agreed, i.e. financial and insurance services.

2. Option to Tax

This is the subject of ongoing discussion and a report on this from the European Banking Federation is expected shortly.

3. Cost Sharing

Member States have responded negatively to the Cost Sharing proposals, mainly in respect of the scope (i.e. industry specific) and its alignment with the existing exemption for independent groups (Article 132 of the VAT Directive) and with VAT grouping (currently allowed in 16 Member States).

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FRANCE

2. Change in the VAT treatment of carbon credits trading

Business involved in carbon credit trading should immediately assess the impact of the change in VAT treatment.

The French tax authorities (FTA) issued an administrative doctrine on 10th June 2009, whereby, with effect from 11th June 2009, the transfer of carbon credits and the supply of related negotiation services are exempt from VAT.

The FTA have taken the decision to VAT-exempt carbon credit trading to prevent VAT fraud and to avoid the distortions of competition between the French and the UK exchanges.

The exemption, based on the assimilation of the carbon credits to "securities", applies on transfers of carbon credits and the related supplies of negotiation services. The new doctrine does not deal with the VAT treatment of any other related services, which should in principle benefit from the option to tax. However, considering the specific context of the decision, the applicability of the option to tax is not yet clear.

Although the doctrine deals explicitly with the European Union Allowances, (EUA - Directive 2003/87/EC) and the Certified Emissions Reductions (CER - Kyoto Protocol), the exemption should apply to all carbon credits.

This new VAT exemption will generate VAT-exempt turnover and could, therefore, impact the VAT recovery position of the transferor/seller and, accordingly, increase the cost of French payroll tax (or, as the case may be, make them liable to payroll tax).

However, it is expected that this will not be the case as the treatment will effectively be the same as if zero-rating is applied, i.e. exempt with credit. In this case, there should be no loss of VAT recovery and the tax payer should not be liable to payroll tax on the basis of this exemption.

France is in the process of addressing a request for derogation to the EU Commission under the provisions of Article 395 of the Directive.

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THE NETHERLANDS

3. A Dutch Court confirms the applicability of the VAT exemption to fund management and administration services

Businesses operating under similar contracts should check the VAT treatment of fund management services, as this decision confirms the applicability of the exemption.

In this particular case, the taxpayer provided management services to several funds. The services included the management of immovable properties and liquid assets, as well as administrative services. The funds were regarded as special investment funds under Dutch VAT law, the management of which qualifies for VAT exemption.

Under the management agreements in respect of the funds, services were separately identified and priced. The Court decided that all services provided by the taxpayer under the agreements are VAT exempt as the management of collective investment funds.

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SWITZERLAND

4. New Value Added Tax Law – impacts for financial sector

Businesses operating in the financial services sector should consider the cost saving opportunities, as indicated below.

As announced in the last FS VAT Alert (2009/5), Switzerland will implement a new Value Added Tax Law on 1 January 2010. The law aims to simplify the administrative handling of Swiss VAT. Furthermore, it creates opportunities for businesses (particularly those in the in the financial sector) to save some of the irrecoverable VAT cost.

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The following issues highlight the opportunities most relevant for the financial sector:

- Dividend income will no longer be included in the pro rata and so will not lead to a reduction in VAT recovery (although the impact to the bank flat rate method is not yet clear).
- VAT grouping requirements have been restricted as well as the scope of joint liability.
- Assigning input VAT credits will be possible. This will allow banks to offer new investment models for companies with large VAT credits.
- The practice of the Swiss Federal Tax Administration regarding the flat rate VAT recovery method should be followed closely. It is expected that the calculation can be optimised in future to optimise the amount of VAT recoverable.

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UNITED KINGDOM

5. Questions referred to ECJ on VAT treatment of payment processing: Axa UK plc (C-175/09)

[Businesses which effect payments and transfers for \(or on behalf of\) their customers or others should monitor the progress of this case and any potential impact on their existing arrangements.](#)

The case concerns the applicability of the VAT exemption in respect of monthly fees charged to dentists for operating a payment plan for the dentists' clients and whether the fees should be apportioned between taxable services and exempt payment processing.

The decision of the High Court, which is being appealed by the tax authorities, found in favour of the taxpayer that consideration in the form of monthly fees charged to dentists for operating a payment plan

arrangement should be apportioned between exempt payment handling services and other taxable services. The tax authorities argue that the fees are consideration for a single taxable supply.

The Court of Appeal has referred questions to the ECJ for a preliminary ruling in this case.

The questions referred deal only with the scope of the exemption and not the single versus multiple supplies issue in the case.

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6. VAT Tribunal applies 'abuse' principle: Lower Mill Estate Ltd [2009] UKFTT 00016 (TC)

[This decision will be of interest to all businesses engaged in any form of VAT planning and, in particular, those operating through arrangements under which two separate \(but connected\) entities make supplies \(with differing VAT treatments\) to a single customer at the same time.](#)

The VAT Tribunal has held that a trading structure, under which purchasers of holiday homes received separate supplies of land (standard-rated) and construction services (zero-rated) from two associated legal entities, constitutes an 'abusive practice'. The transactions were therefore redefined by the Tribunal to remove the VAT advantage.

In applying the Halifax test, the Tribunal held that the Taxpayers' contractual arrangements created a market distortion which was "against the objective of the Directive in guaranteeing uniformity of the taxable amount". In addition, the Tribunal held that the evidence indicating that the essential aim of the transaction was to obtain a tax advantage was strong when compared to the "weaker and limited evidence of commerciality".

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7. High Court allows Taxpayer's appeal in IPT 'unbundling' case: Homeserve Membership Ltd [2009] EWHC 1311 (Ch)

Insurers and insurance intermediaries should consider the benefits of having a separate contract which may not be subject to IPT.

The High Court has handed down its decision in the Homeserve case, which concerns an arrangement designed to reduce the insurance premium tax (IPT) payable on the sale of assistance insurance products to homeowners. The Court held that the Taxpayer's services of 'arranging and administering insurance' were provided under a "separate" contract from the insurance policy, such that the fees charged and retained by the Taxpayer were not liable to IPT.

It is not yet known whether this decision will be subject to an appeal but, even if the tax authorities are ultimately successful in this case, arrangements that reduce the IPT charge in a similar way may still be possible.

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