THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

June 2021

MODULE 3.02 – EU VAT OPTION

SUGGESTED SOLUTIONS

PART A

Question 1

Finance Director
Gamma SA
Bordonia
EU

ADIT Student
Anywhere
A Country

12 June 2021

Dear Sir or Madam

VAT aspects of your business

I am pleased to provide a review of the EU VAT aspects of your business and advise you that the VAT treatment of each of your activities is as follows:

Availability of Music recording and production facilities

The place of supply of these facilities is dependent upon the extent to which the professional staff assists users of the equipment in the recording studio. The hire of a recording studio on its own would generally be regarded as a land related supply for which the place of supply is where the studio is located (Art 47 PVD), which is Bordonia in this case. However, it appears that professional staff are provided to assist musicians who have hired the studio and are more than ancillary to it.

Since the use of the recording studio includes availability of professional staff to assist customers, this suggests the supply is not purely a land related service of a studio hire for a defined period of time. The use of sound equipment together with professional engineers is more likely to be a professional service allowing use of recording and editing equipment as well as the provision of a room. As such it could be seen as a mixed supply of which the dominant element, on CPP principles, is the use of the equipment. In this case your supply is one of services of recorded music production for which the place of supply is determined by the status of your customers as well as where your customers belong.

In the case of customers who can provide documentation showing they are in business the place of supply is determined by where they belong.

For those business customers with an establishment in Bordonia you will be required to charge Bordonian VAT as these are business to business (B2B) supplies under Art 44 PVD. In contrast, for business customers established in Theta the place of supply will be Theta and they will be required to account for Theatian VAT under the reverse charge principles outlined in Art 196 PVD. This will require you to issue them with an invoice stating that your supply is subject to the reverse charge in their member state. Supplies to Theta businesses may also require you to make an entry on an EC Sales List (or Recapitulative statement) showing the value and VAT registration number of your customers in each member state. EC Sales Lists can be completed quarterly or monthly if you have values of B2B intra-EU supplies above €50,000 per quarter, and need to be submitted before the end of the month following that in which the transactions took place.

For customers who are not taxable persons, the place of supply is where you are established, Bordonia, and will result in you needing to charge them Bordonia VAT as Business to Consumer (B2C) supplies of services covered by Art 45 PVD. This applies irrespective of whether they belong in Bordonia or Theta. No recapitulative statement entries are required.

It is essential that you are able to accurately determine where your customers belong and whether or not they are taxable persons. Acceptable evidence of their business status may

consist of them providing a valid VAT registration number which you should check on the Europa website, or other evidence such as a bill or headed paper indicating their country of establishment, Art 18 of the Implementing Regulations (282/2011) allows a supplier to rely upon these items in the absence of evidence to the contrary.

In the case of individuals and other non-taxable persons, you may rely upon Art 18(2) IR which says that in the absence of evidence to the contrary you may assume a customer established in the EU to be a non-taxable person where they have not communicated a VAT registration number to you.

To determine whether your customer is a taxable person or alternatively in business you will need to consider Art 9 PVD which defines a taxable person as "any person who independently carries out in any place an economic activity". In the case of musicians this may require you to identify those for whom it is a hobby or interest from those who perform or record for income/professional purposes.

Indoor stage – admission to live performances

Admission charges to your stage to see live music is subject to VAT under Art 53 or Art 54 PVD and Art 32 IR and is due where those activities take place, it will be subject to Bordonia VAT irrespective of where the attendees belong.

Live streaming music channel

I understand the live streaming music channel is provided throughout Europe free of charge – this is a free supply of services for which no VAT is due as there is no consideration. In the case of the premium service for which a charge is raised – this is a supply of electronically supplied services (Art 58 PVD) which will result in an obligation to account for VAT in each member state in which your subscribers are established. This is likely to require many registrations and can be simplified if you apply to account for the VAT due in each member state using the special scheme set out in Arts 369a – 369k PVD (Mini One Stop Shop) which will allow you to submit a single return in Bordonia incorporating the various VAT amounts due from each supply you have made to each subscriber.

To enable you to determine which member state each of your non-business subscribers belongs in you should use the rules in Arts 24b(d) and 24f IR which enable you to refer to 2 non-contradictory pieces of information such as country in which credit/debit card is issued and IP address to determine the country and therefore the rate of VAT that you need to collect.

Please do not hesitate to contact me if I can be of further assistance.

Yours faithfully
ADIT Student

Question 2

Blunden Spa
EU

12 June 2021

Dear Sir or Madam

Report on VAT aspects of your interior design business

Interior design work on immovable property

Any works performed on an existing building will be regarded as land related services (Art 47 PVD) for which the place of supply will be the location of the land. If this is in Theta it follows that Theta VAT will need to be charged whether or not the clients are individuals or corporates. If work is performed in relation to property that is located in the EU but outside Theta there is a likelihood of a registration requirement and a need to account for VAT at the local rate. Some member states allow this to be dealt with under the "tax shift" allowed in Art 194 PVD if your client is VAT registered, but this is not possible for natural persons who are not VAT registered. You may wish to appoint an agent in each territory who can deal with the tax obligations on your behalf.

Interior design work on immoveable property where ultimate location is unknown

Where design services are provided which are not in relation to a specific property the default VAT position will be that you charge VAT at the rate applicable in Theta since that is where you as supplier are established (Art 45 PVD).

However, if your clients are in business and are established outside Theta the place of supply will be the country of their establishment and if that is an EU member state there will be a requirement for them to account for VAT at the recipient's rate in their country using the reverse charge procedure (Art 44 PVD). Where this is the case you will need to endorse your invoice to state that you are making a reverse charge supply. An EC sales list will also need to be made for supplies to EU established business clients. For clients established outside the EU there is no requirement to account for VAT in Theta neither is there a reporting requirement.

Blunden Spa will require an EORI number to identify themselves on Customs documentation and may benefit from duty and VAT deferment if there are large volumes of imports. The VAT payable at import will be recoverable by the business as a cost component of the onward taxable supplies.

When goods are purchased domestically they may incur VAT which can also be recovered by the business as input tax. In the case of goods purchased from suppliers in other EU member states – Blunden will be responsible for acquisition tax if they have provided their VAT registration number to the supplier – the acquisition tax will be calculated using the cost and freight charges of he goods and must be entered on the VAT return as both acquisition tax and input tax if it is to be recovered. If the value of arrivals exceeds the annual value limit used in Theta.

Interior design work in relation to yachts

I understand that all yachts will be in Theta when work is performed on them; this is an important fact as the location of the yacht at the time you physically carry out work onboard is critical to the place of supply. On the assumption that your clients are non-taxable persons (individuals) and not in business, your supplies of design and installed interior items will be subject to VAT in Theta (Art 54(2)b PVD).

However, if the yachts are intending to leave Theta after the installation it will be possible, in certain circumstances, to treat your services as work on goods for export and zero rate your supply. The circumstances are:

- The yachts were bought in the EU or imported into Theta for the purpose of the interior design installation;
- The yachts are owned by non-taxable persons established outside Theta; and
- The yachts sail from Theta and leave the EU after the installation (Art 146 (d) PVD).

It follows that work provided in Theta for EU residents will be subject to Theta VAT.

In the case of works performed in Theta on corporate owned vessels it is necessary to determine whether the vessels are "qualifying ships" or not (Art 148 PVD). In general, a qualifying ship does not include a vessel designed for pleasure use and would therefore exclude most yachts. It is therefore necessary to charge Theta VAT for interior design works provided to yachts whether they are privately or corporately owned.

Importation and purchase of materials for installation

The importation of materials in Theta for subsequent supply as part of the interior design installation will create a liability to VAT which will apply at the same rate as would apply to a supply of goods domestically (Art 70 PVD). The valuation for import VAT will include any Customs duty as well as freight, insurance and ancillary charges that are incurred in importing the goods. The business will be entitled to deduct the import VAT.

Bad debts

When Bad debts are incurred on supplies made to clients' member states have discretion to allow adjustment to the value of the original supply (Art 90 PVD). Whilst the conditions that need to be met differ across member states, common features include the requirement for the original supply to have been subject to VAT, payment must have already been made to the respective tax authority, evidence that the recipient of the supply has encountered financial difficulties or not paid and usually a specified period of time must have elapsed since the original tax point of the supply before adjustment can be made.

Yours faithfully
ADIT Student

PART B

Question 3

Right to deduct – general

The right to deduct input VAT is a fundamental right of taxable persons, it is established under Art 168 PVD which states that VAT will be given as a deduction against the VAT a taxable person is liable to pay where goods and services are used for the purpose of taxed transactions of the taxable person in the member state in which he carries out those transactions. The timing of any deduction is determined by Art 167 PVD

It is significant that to be able to get a deduction under Art 168 the taxable person must be established in the member state in which the VAT was incurred and ordinarily should have VAT due from which the amount can be deducted. It is also essential that the taxable person is making taxed transactions as this eliminates taxable persons making exempt or solely non-business transactions. VAT deduction can also be restricted where special arrangements for Tour Operators and flat rate and second-hand goods schemes are permitted.

In the case of taxable persons who are not established in the member state in which VAT is incurred, there are cross border refund claims and 13th Directive reclaim procedures through which incurred VAT can be claim if conditions are met (Art 170 PVD).

The right to deduct is also extended to taxable persons who make supplies outside their member state which would have been taxable if performed inside – these are known as outside the scope with the right to recover (Art 169 PVD) and include certain supplies made overseas which would have been exempt if made in the EU and supplies made in connection with exports. Under normal domestic arrangements the taxable person must be able to produce an invoice for all amounts claimed showing the taxable person from who the VAT is due, the amount of VAT incurred and the tax point date, VAT is only eligible for recovery within specified time periods which are generally defined in domestic legislation. In limited circumstances member states may accept alternative evidence that VAT has been incurred and paid for example import documents. Similar restrictions are also placed on VAT incurred prior to registration and in advance of making taxable supplies – again these measures are subject to domestic legislation in the member state in which the VAT is incurred and sought to be recovered.

Denial of claims

There is a substantial body of CJEU case law which concerns disputes over the right of deduction, case have ranged from circumstances where the liability of a purchased supply has changed to taxable, time limits, allocation to taxed transactions and most commonly where there is suspected abuse of law or fraudulent transactions are suspected of having taken place in the supply chain.

PART C

Question 4

To: Financial Controller, Non-EU Company
From: ADIT Candidate
Re: VAT refunds
Date: 21 June 2021

Dear Sir or Madam

Thank you for your enquiry concerning the possibility of recovering VAT incurred in Bordonia during the past two years.

Whilst it is possible for a non-EU established business to obtain a refund of VAT there are some rules that you need to consider. Directive 86/560 (13th Directive) allows member states to make refunds, on terms no less favourable than those that apply to businesses established in other member states, where certain conditions are met. These include:

- The company must not have had either its business or a fixed establishment in Bordonia during the period of the claim;
- It must not have supplied any goods or services in Bordonia during that period, except a limited range of services associated with transport or reverse charge services;
- Reciprocal arrangements must exist with the tax authority in your country of establishment for refunds of VAT incurred by Bordonia established businesses;
- Claims must be presented, with invoices where necessary, within time limits that may be prescribed by Bordonia and repayments will be may within timescales determined by the Bordonia tax authority;
- Payments will be made in the local currency;
- The company may be required to appoint a tax representative in Bordonia to prepare the claim;
- Bordonia is able to exclude certain types of expenditure from claims e.g. luxury items; and
- Proof is required that the company was engaged in "economic activities" in its country of establishment during the period of the claim.

This last point may raise an issue since you were not VAT registered in your country until May 2020, although you incurred VAT costs in Bordonia from July 2019. It may be possible, if the company was engaged in economic activities before becoming VAT registered, for it to satisfy the economic activity test by it providing evidence that sales invoices were raised before May 2020. In the event that you can evidence whether economic activities took place continuously from July 2019 (or before) you may be able to make a claim subject to time limits for claims that have been set in Bordonia.

If Bordonia VAT is likely to be incurred in future, I recommend you make claims at the earliest possible opportunity after expenditure has been made although it is likely that Bordonia will specify the frequency e.g. annually that claims can be submitted.

I hope this information is sufficient but please do not hesitate to contact me if I can be of further assistance.

Yours
ADIT Student

Question 5

Fiscal Neutrality

Fiscal neutrality is a concept which has proved difficult to define as it is to a large extent aspirational and imprecise. That said, it refers to the overall approach to VAT which seeks to ensure that VAT is not a charge upon economic operators who are intended not to bear the burden of the tax, provided that their activities are subject to VAT. It is referred to by both the EU and the OECD in their guidelines regarding the application of VAT/GST and is widely regarded as consisting of two principles.

The first principle is that VAT is a tax on consumption and that the deduction of input tax is designed to relieve the burden of the tax, whilst taxing the final consumer – "the First Directive Principle".

The second is that businesses should be treated similarly for tax purposes – "the Parity Principle".

The majority of case law surrounding the First Directive principle has been concerned with the deductibility of input tax in relation to business that make taxable supplies to consumers through a supply chain of several taxable persons, in contrast to where tax is incurred on exempt activities or in circumstances where the supplies have ultimately not been used by the claimant business. A further aspect of this principle is that the amount of tax borne by an ultimate consumer cannot be greater than the amount due on the consideration paid for the final supply to the consumer per Elida Gibbs (C-317/94) which allowed a reduction in the value for VAT purposes for a manufacturer who made promotional payments to consumers of its products.

The overall effect is that VAT should be fully deductible throughout a supply chain where the final supply is subject to tax. The effect of the First Directive principle is that the tax is completely neutral as regards its effect on a taxable person who makes only taxable supplies (other than the administrative costs of accounting for VAT, and subject to specific exclusions).

The second principle is concerned with trying to ensure a level playing field and it precludes treating similar goods and supplies of services, which are thus in competition with each other, differently for VAT purposes, so that those goods or supplies must be subject to a uniform rate. This principle has been applied to:

- The concept of unjust enrichment, which at one time was unjustifiably applied to payment traders but not repayment traders selling the same product (Marks & Spencer plc (C-309/06));

- Financial products, where essentially similar products were treated differently for tax purposes (JP Morgan Fleming Claverhouse (C-363/05));

- Healthcare services, where it has been held that the tax treatment of such services could not be dependent on the legal persona of the taxpayer (Jennifer and Mervyn Gregg (C-216/97));

- Gaming machines, regulated under different gambling legislation (Rank Group plc (C-259/10)); and

- Where car parking facilities are supplied by public bodies and private businesses in competition or potential competition with each other (Isle of Wight Council (C- 288/07)).

[Examiners note – there are many cases that have considered fiscal neutrality which could be quoted in answers to this question. De Voil Indirect tax V1.230B contains a comprehensive list which could include: Purple Parking (C-117/11); K Oy (C-219/13); Belgocodex SA (C381/97) and Card Protection Plan Ltd (C-349/96).]

Direct Effect

Direct effect is the EU law concept that allows the provisions of Treaties and Directives to give rise to rights or obligations which individuals may enforce before the national courts, if the necessary EU provisions have not been implemented or implemented correctly in national legislation.

Direct effect applies to those articles of the Directives, which are i) unconditional and ii) sufficiently precise, and allows them to be relied upon as against any national provision which is incompatible with the Directive, or in the case of individual's rights are assertable against the state.

The most notable VAT case concerning Direct Effect has been *Becker (C- 8/81)*, which remains a leading case. Becker was a self-employed credit negotiator who invoked before her German national court the provision in the 6th VAT Directive which made the granting and negotiation of credit an exempt supply. Germany had not yet implemented the Article into national law. Becker wished to apply the exemption to the period of time from the coming into force of the Directive until the German law changed. The ECJ subsequently held that when a Member State has failed to implement a Directive correctly and not before the end of the period prescribed for implementation, that it had breached Article 189 of the EU Treaty which states that a Directive shall be binding upon each Member State.

The court concluded that it would be incompatible in view of the binding Article to exclude the possibility of the obligations imposed being relied upon by persons affected. Consequently, a Member State which has not adopted the measures required by a Directive in time may not plead, as against individuals, its own failure to perform the obligations that the Directive entails.

Other tax cases in which Direct Effect has been considered include:

- *GMAC (C-589/12)* in which bad debt relief was allowable on the difference between the VAT originally accounted for on a hire purchase vehicle sale and the amount subsequently received from a defaulting customer plus auction sale proceeds for the vehicle, where that was a lower amount. The ECJ rejected the UK position that bad debt relief was not available under UK legislation and applied the principle of direct effect.

- *Linneweber & Akriditis (C-453/02 and C-462/02*) the CJEU found that Article 13B(f) of the Sixth Directive had direct effect and could be relied upon by an operator of games of chance or gaming machines against national rules which were inconsistent. In this case the German government had made the exemption dependent on the identity of the operator.

- In *JP Morgan Fleming Claverhouse Investment Trust (C-363/05)* the ECJ found that Art 13B(d)(6) of the Sixth Directive had direct effect and that the words 'special investment funds' are capable of including close-ended investment funds such as Investment Trust Companies. In exercising the Member State's discretion in defining 'special investment funds' the Court said the UK had to respect the objective of the exemption.

- In *British Film Institute (C-592/15)* the CJEU held that the wording in the VAT Directive was not precise enough for it to have direct effect such that admission to cinemas in the UK should be exempt.

Question 6

Derogations

Derogations can be made under four broad headings:

1. Continuation of treatments applied by member states at 1 January 1978, Articles 370 to 374.

2. Measures granted to member states that acceded to the EU after 1 January 1978, Articles 375 to 390(b).

3. Special measures that were applied by member states before 1 January 1977 and notified to the Commission before 1 January 1978, Article 394.

4. Special measures authorised by the Council under the procedure provided for in Article 395.

Articles 370 to 374

Arts 370 to 374 allow member states which at 1 January 1978 taxed or exempted transactions or applied provisions derogating from principles relating to the right to deduct and agency in Arts 179, 28 and 79, that existed at 1 January 1978, to continue with those tax treatments.

Articles 375 to 390(b)

Arts 375 to 390(b) permit specified member states, which acceded to the EU after 1 January 1978, to retain former tax treatments on particular activities until specified future dates.

Article 391 provides the opportunity for member states to allow taxable persons the right to opt for taxation of transactions covered in some of the Arts 371 to 390(b) which allowed for exemption.

The existence of the Art 370 to 390(b) derogations are kept under review by the EU Commission with a view to facilitating the transition to definitive arrangements. (Art 393).

The EU Commission website publishes a list of all Derogations in force under the various headings. Member states are not obliged to apply the Derogations for which they have received authorisation.

Article 394

In addition to any general derogations allowed under Articles 370-374, member states may be allowed to retain special measures, in existence at 1 January 1977, to simplify the procedure for collecting VAT or to prevent certain forms of tax evasion or avoidance. These are provided that they have notified the Commission accordingly before 1 January 1978 and that such simplification measures comply with the criterion laid down in the second subparagraph of Article 395(1) – not to affect the VAT collected on final consumption except to a negligible extent.

Article 395

Article 395 PVD allows member states to derogate from the Directive's provisions to simplify the procedure for collecting VAT or preventing certain types of evasion or avoidance.

Derogations authorised under Art 395 intending to simplify the procedure for the collection of VAT may not, except to a negligible extent, affect the overall amount of tax revenue of the member state collected at the stage of final consumption.

A member state wishing to introduce a measure covered by Art 395 is required to send an application to the European Commission and provide all necessary information. Once the Commission has all the necessary information it has one month to notify the requesting member state accordingly and to send the request to the other member states. Within three months of giving the notification, the Commission shall present to the Council an appropriate proposal or where appropriate a communication setting out its objections to the derogation request.

The whole procedure detailed in Art 395 should be completed within eight months of the receipt of the application by the Commission, although this is shortened to six months in cases of imperative urgency, covered under Art 199b “Quick Response Mechanism” special measure to combat sudden and massive fraud e.g. measures to tackle MTIC fraud.

Question 7

Sale of Metro and other cards by Athena GmbH

On the understanding that Metro cards are electronic cards that can be credited with proceeds that can be used for travel it would appear that these are single purpose vouchers covered under by Art 30a and 30b PVD which were introduced from 1 January 2019 following the introduction of Directive 2016/1065 regarding the treatment of vouchers.

The fact that Athena GmbH are earning commission on the sale of Metro cards suggests that they are acting as an agent for the transport provider who is also established in Mediterania. Since it appears that the cards can only be used public transport there is a question regarding whether the Directive should apply since it states that "the provision regarding vouchers should not trigger any change in the VAT treatment of transport tickets, although the practical interpretation of this is likely to differ across Member States.

On the understanding that Metro cards are regarded as single purpose vouchers on the grounds that they can only be used in the member state of issue and for a single type of service for which the VAT due is known at the time of issue. It would suggest that any VAT on the commission and underlying transport is chargeable in Mediterania. Further that VAT is due on the full value of the Metro card at the time of sale by Athena under the provisions of Art 30b PVD, but since Athena are acting in the name of the transport provider the supply shall be regarded as being made by the transport provider not Athena.

In the case of the cards sold for use on public transport in Theta, another member state. Subject to the transport tickets exclusion, these would appear to be multi-purpose vouchers as defined in Art 30a PVD which simply says, "other than a single-purpose voucher". The practical effect of this is that the tax due on the eventual supply is not chargeable at the time the card is sold but is due in the member state and at the time of redemption.

The commission charged by Athena which can be identified as being in respect of a distribution service will be subject to VAT. The fact that this is made in respect of a sale on behalf of the Theta transport provider suggests that under Article 44 PVD the place of supply is Theta and that the supply by Athena is B2B and can be subject to the reverse charge. Athena will need to issue an invoice bearing the appropriate statement and enter on their recapitulative statement.