

# MERIDIAN

## *VAT trends*

*November/December 07*



### **THIS ISSUE:**

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# MESSAGE FROM MERIDIAN'S CEO

2007 has been an eventful year in international VAT, with many significant developments effecting business, tax administrations and ultimately the consumer.



This highlights the ongoing complexity and uncertainty faced by business in a rapidly changing Single Market, which must deal with scenarios not envisaged when the legislation was initially drafted.

The year started with Romania and Bulgaria acceding to the European Union on January 1<sup>st</sup>, increasing the population of the Single Market by 8% and bringing the total number of Member States up to 27. This has created the leading global market with a combined population of 483 million, nearly twice the population of the United States. Ongoing discussions are in progress with Turkey, Serbia and Montenegro, Albania, Bosnia Herzegovina, and The Ukraine for future EU Membership.

The New Year also saw the single biggest tax rise in modern Germany, with an increase in the standard rate of VAT from 16% to 19%. This move highlights a more general trend among the developed world to reduce the levels of direct taxation with corresponding increases in indirect taxation.

From a legislative perspective, 2007 will be remembered as the year in which the European Council of Finance Ministers finally reached consensus and achieved political agreement on a package of VAT reforms that were tabled and had been under discussion since December 2003.

Much work lies ahead for both taxpayers and administration, who will have to remodel existing systems and processes to facilitate implementation of the constituent parts of the VAT package, which comes into force on a piecemeal basis starting from 2010 through to 2015.

The past year has also produced some interesting jurisprudence handed down by the Court of Justice of the European Communities, as well as the national Courts of the Member States. Many of these cases, which have been covered in VATtrends, have had far reaching implications concerning the application and interpretation of European VAT.

2007 has also been a busy year for our VATtrends editorial team, who have been working hard to provide relevant, up to date and innovative content to our readers:

- In addition to our core English circulation, VATtrends is now translated and published in French, German, and Japanese;
- In 2007, we commenced publishing exclusive lead articles written by VAT directors from some of the world's leading multinational companies, providing our readers with a practical insight to specific international VAT topics;
- We are proud to have grown our circulation list to over 25,000, with readers spread across the globe including Azerbaijan, Malaysia, Russia, Croatia, Australia, New Zealand and South Africa;
- Our subscriber-base now includes readers from the European Commission and tax Administrations.

We hope that over the past year, you have enjoyed receiving VATtrends and have benefited from the content provided. We appreciate the continuous feedback that we receive from our readers, which helps us to continually improve both content and design, for the benefit of all our readers.

I would like to thank our editorial team and most importantly our readers, who have helped to make VATtrends one of the leading international VAT periodicals. We would like to wish you all a happy, healthy and prosperous Christmas and New Year.

**Mark O'Riordan**  
Chief Executive Officer



## BELGIUM

### Clarification of terms affecting 'Credit Notes' and 'Unit Prices'

In a question and answers session held on 3 Nov 2007 in the Belgian Senate, the representative of the Belgian Minister for Finance provided useful clarification on the definition of "document" and "unit price" as stipulated within Belgian VAT legislation.

#### 1. Credit notes and Corrective Documents

Q: Does the term "document" as mentioned in Art. 53 (2)(3) of the Belgian VAT Code, which relates to the creation and issue of documents, include credit notes? What is the corresponding Article. of the Sixth Directive? Are corrective documents to be included in local VAT returns?

A: A 'corrective document' may be a credit note, a debit note (invoice), a rectified credit note or debit note (Art. 28 of the Belgian Vat Code) or any document other than a credit note that cancels the transaction in specific circumstances. Therefore, a "document" can mean any of the above mentioned documents. This corresponds to Art. 22(3)(a) of the former Sixth Directive 77/388/EEC.

Those documents should only be included in a local VAT return if they affect the returns, i.e. if they are effectively credit or debit notes. They need to be included in the period in which they were issued. The recipient is only required to include the correction document if they had already closed and accounted for the previous transaction and as such, must make the necessary changes so that their VAT return corresponds with the issuer's VAT return.

An administrative bulletin will be published by the Belgian administration to confirm this treatment.

#### 2. On unit prices as a mandatory invoicing requirement

Q: Is there an obligation to mention the unit price on an invoice as per Art. 5 (1) (8) of the Royal Decree?

A: In accordance with Art. 5 (1) (8) of the Royal Decree N° 1 dated 29 December 1992, mentioning a unit price on an invoice is a mandatory requirement for the supply of both goods and services.

It is up to the supplier who issues an invoice to ensure that the relevant unit price is shown on the invoice.

For the delivery of goods, the price must be given according to the type of item, per unit. For the supply of services, the price payable may be determined according different criteria, depending on the agreement between the parties and the agreed contractual terms. If the total price of a service is not determined before the services took place, the unit price is determined by the party issuing the invoice (i.e. hourly rate applicable). On the other hand, if the total price of a service is determined in advance, the price can be considered as the unit price.

For example the services of an accountant may be invoiced with a unit of hourly rates (unit price) or by quoting a fixed pre-agreed price (unit price).

As a result of the above, the recovery of Belgian input VAT may be denied if the unit price is not quoted.

An administrative bulletin will be published by the Belgian Authorities in relation to this.



## IRELAND

### 2008 Budget

On 5 December 2007 the Irish Minister of Finance presented his financial statement in regards to the budget for 2008. In terms of support afforded to small and medium enterprises, the budget increased the VAT registration threshold from €35,000 to €37,500 per annum for services and from €70,000 to €75,000 per annum for goods. The thresholds will come into force from 1 May 2008.



## IRELAND (cont)

### 2008 Budget (cont)

It has been estimated that, as a result of this decision, almost 3000 businesses might be taken out of the VAT system.

The Irish Government also intends to reduce the VAT on certain seeds and bulbs for bio-fuels.



## ROMANIA

### Amendments to the rules regarding export exemptions

The Minister of Economy and Finance has published order no. 1503/5.10.2007 in the Official Gazette of Romania in October 2007, amending the instructions for applying VAT exemptions for exports, similar operations and intra-community supplies of goods.

Firstly, the documentation supporting the exempt supply can, in certain cases, be presented to the Tax authorities within 90 days of the invoice being issued. Should, during an audit, the proof of dispatch or export not be available, and hence an assessment of output VAT is issued, a trader may request a reconsideration if he obtains the proofs within a specific period of time, the duration of which will be determined on a case by case basis.

Secondly, with the introduction of electronic export procedures, the electronic certificate issued by the custom's office where the goods leave Community territory substitute any manual paper documents.

Other measures in relation to the supply of goods for the construction of sea-going vessels and aircraft, as well as measures concerning inward processing of goods which commenced prior to EU accession of 01 January 2007 have been implemented.

Should you wish to learn more about compliance in Romania, please contact your Meridian client services manager.



## AUSTRIA

### Strict rules for VAT reclaim applications

This update is important for non-established business wishing to recover Austrian VAT under the provisions of the EU 8th or 13th VAT Directives.

The new rules apply for claims submitted for invoices dated 2007 and onwards.

In summary, all original invoices and claim documents (including tax certificates and signed claim forms) concerning the relevant claim period have to be submitted to the Austrian VAT authority by 30 June following the invoice date.

Claims submitted without all of the necessary invoice and document formalities, will automatically be rejected **without the possibility to provide the original invoices or documents after the June 30 deadline.**

Claimants who have previously filed 'protective' claims while waiting for documents to be finalized and original invoices to be sought, can no longer rely on the ability to supplement these claims post-deadline. All formalities must be in place at the time of the annual June deadline submission.



## CROATIA

### Reduced rate on Newspapers / Magazines

In August 2007 the Croatian Parliament approved the application of the reduced VAT rates on daily and periodic newspapers and magazines. This is a healthy reduction of the price of such items, cutting the rate from the standard rate of 20% to only 10%.

Croatia has only recently introduced the reduced rate on accommodation services, such as bed and breakfast type accommodation, as well as on agent's commissions providing hotel and catering services.

If you require further information on VAT in Croatia, and possible refund opportunities there, please contact your Meridian Client Services Manager.



## CANADA

### Reduction of GST rate to 5%

On 30 October 2007, the Government of Canada announced that its Goods and Services Tax ("GST") would be reduced from 6% to 5% with effect from 1 January 2008.

This is the second 1% GST rate reduction in less than two years.

It is important to note that, under the general transitional rule, the 5% rate will apply for GST that becomes payable on or after 1 January 2008. GST that is paid or becomes payable before 1 January 2008 will be due at the current rate. For instance, the 6% rate will still apply to:

- Prepayments made before 1 January 2008 for goods to be delivered after 31 December 2007;
- Airline tickets purchased before 1 January 2008, even if the travel will take place after 31 December 2007.

In some cases, the applicable rate will be 5%. This is in relation to services rendered before 1 January 2008, but paid for after this date.

For example:

- Fees for professional services rendered before January 1, 2008 will be taxed at 5% if the invoice is issued after December 31, 2007.

With regards to imported goods, they will be taxed at the rate in effect on the day the goods are released from Customs control (Canada Border Services Agency).



## CZECH REPUBLIC

### VAT and Commissionaire structures

In August 2007, the Ministry of Finance issued an official statement that summarizes the basic VAT aspects of services provided by commissionaires acting as undisclosed agents.

For VAT purposes, a transaction carried out through a commissionaire ("agent") constitutes a supply made to and, subsequently, by the agent, under a sale or purchase commission contract.

If the tax base of the supply between the agent and the customer is different from the tax base for a supply between the principal and the agent, the difference is the remuneration of the agent. In this case the agent does not need to issue a separate VAT invoice to the principal. This 'remuneration' is effectively accounted for via the margin between the two separate supplies for VAT purposes.

However, if the tax base of the supply to the customer is the same as the tax base of the supply between the principal and the agent, and the commissionaire receives payment from his principal in form of a commission, this commission is treated under Czech VAT law as consideration for a separate service rendered by the commissionaire to his principal. In this respect, the commissionaire must issue a separate invoice and must apply Czech VAT at the standard rate.



## HUNGARY

### Important Changes to Hungarian VAT Act – Effective from 01 January 2008

On 12 November 2007 the Hungarian Parliament adopted a new VAT Act, which will radically change VAT legislation in Hungary upon its introduction on 1 January 2008. The text of the new Act represents a significant departure from the current legislation. The new Act is the product of three years of review and preparation and will bring the Hungarian VAT code in line with the Principal EU VAT Directive.

While the changes may create some short-term difficulties for business registered for VAT in Hungary, as they adjust to some of the new requirements, ultimately it will reduce administrative burdens, simplify the VAT refund process and extend the scope of the VAT group system in Hungary.



## HUNGARY (cont)

### Important Changes to Hungarian VAT Act – Effective from 01 January 2008 (cont)

The key changes relate to the following subjects:

- VAT groups
- Use and enjoyment provisions
- Tax point
- VAT treatment of discounts
- Input VAT recovery
- Extended reverse charge mechanism
- Rules in relation to issuing invoices
- VAT registration

#### Retrospective VAT Registration

The provisions of the new Act on the rules of taxation concerning the registration of taxpayers have been amended with a view to introducing retrospective VAT registration. Meridian will keep its readers updated in relation to this.

For a full version of the article, please click on this link <http://www.meridianp2p.com/uploads/hungvatactdec07.pdf>



## EUROPEAN UNION

### ECOFIN adopts VAT Package

The European Council of Finance Ministers (ECOFIN) reached their long anticipated political agreement to change the way that VAT is applied to services.

The new rules will mean that the supply of services between businesses (B2B supplies) will be taxed where the recipient is established as a general rule, rather than the exception. The general rule change comes into effect from 2010.

The supplies of electronic, broadcasting and telecommunication services provided to individuals (B2C supplies) will shift from the place of establishment of the supplier, to the place where the consumer resides. This element comes into effect only from 2015.

The long implementation timeframe behind the B2C element of the VAT Package was as a result of Luxembourg's political bartering, as they stand to lose significant revenues as a result of the changes.

### EU Council adopts Fiscalis 2013 Programme

The Fiscalis programme, which was introduced by the European Council with effect from 2003 (which replaced the Matthaues-Tax programme), aims to assist traders in combating VAT fraud and to reduce compliance costs in order to promote and further the Single Market and its businesses.

The Fiscalis 2013 Programme will continue its work on the main issues already focused on in the 2007 programme. These include:

- Reducing administrative burden on both traders and administration;
- Strengthening the fight against VAT fraud, particularly against carousel or missing trader fraud;

- Promote exchange of information between administrations through international tax IT systems.

The Commission released press update IP/07/1748 on 22 November 2007. If you wish to access this, please follow this link:

<http://europa.eu/rapid/pressReleasesAction.do?reference=IP/07/1748&format=HTML&aged=0&language=en&guiLanguage=en>

### Commission communication to improve fight against VAT fraud

The EU Commission published its communication (COM (2007) 758) on ways to improve intra-EU cooperation to tackle VAT fraud.

With the key elements having been put forward, the Council is now asked to provide the necessary political guidance, such as legal frameworks, to ensure that there is a common legal basis in order to implement the necessary measures, which include:

- Need to improve accuracy of the information provided and exchanged on intra-EU trade;
- Central management of EU VAT receipts to protect VAT revenues not only at national level;
- Common approach for registration and deregistration process for in EU;
- Enhancement of tax administrations' capacity to collect VAT receipts in cases of VAT fraud

If you wish to review the complete communication, please follow this link:

[http://ec.europa.eu/taxation\\_customs/taxation/tax\\_cooperation/reports/index\\_en.htm](http://ec.europa.eu/taxation_customs/taxation/tax_cooperation/reports/index_en.htm)

## **Extension of reduced rates on certain supplies granted until 2010 to all Member States**

In accordance with Art. 96 of the EU VAT Directive, Member States must apply VAT at standard rate of at least 15 percent. According to Art. 98, Member States may apply either one or two reduced rates, which may only apply to supplies of goods or services listed in Annex III of the Directive.

Art. 106 of the EU VAT Directive introduces scope for temporary provisions for particular labour-intensive services. This means that services listed in Annex IV of the Directive may be taxed at the reduced rate until 31 December 2010, on **no more than two of the services listed in said Annex.**

On accession, some Member States, such as the Czech Republic, Cyprus, Hungary, Poland, Slovenia and Slovakia, were allowed individual derogations to levy a five per cent tax rate on certain goods and services, such as printed material, restaurant services and care for the elderly, only until 31 December 2007 as per Art. 123 of the EU Directive.

The EU finance ministers meeting on 13 November 2007 failed to agree on the extensions, however, ministers endorsed an extension of the derogations for three years in their meeting on 4 December 2007.

The three-year extension will avoid a politically sensitive situation in which the Member States would have to raise the reduced five per cent VAT rates to at least the minimum 15 per cent, while consumers in other Member States would continue to enjoy the lower rates until 2010.



## Legality of bank guarantee / security deposits for refund of credit balance

Preliminary hearing in case C-25/07: Alicja Sosnowska v Izba Skarbowa we Wrocławiu Ośrodek Zamiejscowy w Wałbrzychu

### Introduction

Under Polish VAT legislation, a taxpayer cannot receive a repayment of VAT from the Polish administration without lodging a security deposit. A similar rule exists in Italy, where businesses in a regular credit balance position are required to establish a bank guarantee as security.

Under Polish VAT law, if a business files a claim for a VAT repayment within twelve months of registering for VAT, the tax authorities are allowed a period of 180 days in which to make the repayment. However, if the taxable person provides the authorities with a 'security deposit' of 250,000 zlotys (€ 70,000), established with the National Bank of Poland, the 180-day rule does not apply. In this case, the repayment must be made within 60-days.

Therefore, tax payers who are in a refund position find themselves in the situation where they either have to wait for 180 days for their refund, or pay for the right payment to obtain a refund more quickly. It should also be noted that any deposits held in the National Bank of Poland do not earn any interest.

The Polish Supreme Administrative Court has referred the following question to the European Court of Justice:

*"Is the provision in Polish VAT law that requires certain businesses to lodge a 'security deposit', as a condition of being eligible to receive a VAT repayment compatible with Art. 183 of Directive 2006/112/EC?"*

This article allows Member States to make the repayment of VAT credits subject to "conditions which they shall determine". Furthermore, the ECJ was asked whether the Polish regulation constitutes a "special measure to prevent certain types of tax evasion and avoidance", for which a Member State must obtain a derogation under Art. 395 of the EU Principal VAT Directive.

In relation to the Italian rule of having to lodge deposits in order to avail of a refund, the ECJ's findings may have an impact on Italian taxpayers currently suffering from this "payment-for-repayment" situation.

This case has significant implications for Member States such as Poland, Italy and others who make repayment claims very costly and difficult for businesses to achieve.

Meridian will keep its readers informed of any updates on this case.



## Accounting for imported consulting services in partially exempt businesses:

ECJ referral, Sweden – Case C-291/07 [*enter reference*]

Introduction:

The outcome of this case will be relevant to any partially-exempt business that buys reverse-charged professional consulting services from outside their country of establishment, where the purchase fully relates to non-taxable activities.

Furthermore, some Member States currently only require that VAT is accounted for if such services are received for the purpose of the taxable business element, as the purchase for the exempt part of their business would be outside the scope of both the output and the input VAT element.

Only in cases where the purchase of reverse charged services cannot be attributed to any of the two business elements would the purchase have to be apportioned in accordance with the business' partial exemption method to be applied to any residual input VAT.

However, Art. 196 of the Directive states that "VAT shall be payable by any taxable person to whom the services referred to [in Art. 56] are supplied."

This article could be interpreted that – regardless of the question of attribution - reverse charged services purchased should be accounted for by any business, even if only part of their activities are taxable.

The case:

The Collective Agreement Foundation, a partially exempt Swedish organisation, purchased consultancy advice from an advisor established in Denmark, for the purpose of their fully exempt activities. The Swedish administration ruled that, because the appellant also provides taxable services, they must account for VAT on the purchase, but the input VAT would be denied.

The administration's ruling was appealed to the Swedish Supreme Administrative Court, who referred the following question to the ECJ:

Are Articles 56(1)(c) and 196 of the Principal VAT Directive "to be interpreted as meaning that a person who purchases consultancy services from a person liable to tax in another EC country and carries out both economic activity and also activity which falls outside the scope of the Directives is to be regarded as a taxable person/person liable to tax where those articles are applied, even though the purchase was made solely in respect of the latter activity?"



## **AG opines that Italian tax amnesty violates EU law**

Case reference: C-132/06) – Commission vs Italy

In the Finance Act 2004, the Italian Government extended retrospective tax amnesty (known as "the *condono*") adopted under Finance Act 2003, to the fiscal year 2002.

Effectively, this amnesty allows taxpayers to regularise matters in terms of unpaid taxes, including VAT. According to these fiscal arrangements, if a taxable person makes use of the amnesty for a certain taxable year, he may correct his VAT position permanently, simply by paying a fixed sum to the Italian authorities - if no return was filed - or a percentage (2%) of the VAT due in respect of supplies in each taxable year.

In return for the payment, the Italian administration waives its right to audit the affected periods. The waiver of further controls on unpaid VAT applies even if it is

proven that irregularities existed. This means that many traders can deliberately avoid paying VAT and that the Italian tax administration renounces its right to legally prosecute them.

The European Commission considers that this scheme is in breach of the EU VAT legislation, and has brought an action against the Republic of Italy before the European Court of Justice on 06 May 2006. The Commission claims that the Directive requires taxing all goods and services supplied within the country and it obliges Member States to ensure that taxable persons fulfil their obligation to declare and pay VAT.

On 27 October 2007, Advocate General Sharpston opined that the measures adopted by Italy go beyond the margin of discretion that Member States enjoy for adjusting their controls on the basis of human and technical resources available. Italy's action appears to be an overt renunciation of controls for the collection of VAT, thus being in breach of the obligations it has assumed with regard to the application of Community law.

Meridian will keep readers informed as soon as the final judgment of the Court is delivered, expected early 2008.

## **Infringement procedure – 8th and 13th Directive VAT refunds – Case reference 2003/4648**

The Italian legislation stipulates that taxable persons established and VAT registered in Italy, with their main place of establishment outside Italy, must recover VAT paid or due in Italy using the 8<sup>th</sup> and 13<sup>th</sup> Directives mechanisms.

The Commission pointed out that the above-mentioned national legislation is incompatible with the purpose of the 8<sup>th</sup> and 13<sup>th</sup> VAT Directives, and the relevant provisions defining their scope of application.

The Commission's point of view is that taxable persons established in Italy must be able to recover input VAT through deduction on their local Vat return and not by way of the VAT refund procedure exceptionally applicable to non-established taxable business.

## **Infringement procedure – 8th and 13th Directive VAT refunds – Case reference 2003/4648 (cont)**

The European Commission has decided to turn to the European Court of Justice because Italy failed to introduce the necessary amendments within the prescribed deadline of two months. The case was referred in July 2007 under reference 2003/4648 and was announced in press release no. IP/07/1031.



### **Infringement procedure against France<sup>1</sup> – reduced rate of VAT applied to services provided by lawyers**

France was issued with a reasoned opinion in December 2006 (see VATtrends March/April 2007) for its application of the reduced rate of 5.5% to services provided by lawyers within the framework of legal aid. Since France has not yet complied with the opinion, the Commission has referred the case to the European Court of Justice in July 2007, which was announced in Press Release IP/07/1164.

According to the Principal VAT Directive, a reduced VAT rate may only be applied to a closed list of goods and services provided in the Directive. As this list does not comprise the services rendered by lawyers, the Commission sent a reasoned opinion to the French Government advising that a normal rate of VAT<sup>2</sup> should be applied to those services. The referral to the ECJ is the last step in the legal proceedings against France, and may be followed by sanctions if the French Authorities do not comply.

This procedure is another example of the determination of individual Member States to extend the list of services to which a reduced rate could be applied to other services with a high social impact when the Commission is aiming at a strict application of the text.

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<sup>1</sup> Reference no. 2005/2277

<sup>2</sup> The standard rate of VAT in France is 19.6%

# Coming Soon

**UK: Treatment of fund management for VAT purposes**

**Europe: The Vat Package**



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