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EGYPT
VAT INTRODUCED IN EGYPT

VAT was introduced in Egypt with effect from 8 September 2016, replacing sales tax, its previous indirect tax regime. The new tax law is part of an economic reform programme package aimed at reducing the country's budget deficit and is expected to increase tax revenue by around EGP 30 billion.

In principle, VAT applies to all provisions of goods and services, other than some goods and services that are listed in an exemption table. This article highlights key provisions of the new VAT in Egypt.

Tax rates

The VAT rates are as follows:

- A 13% standard rate applies to most supplies of goods or services. This rate is set to increase to 14% on 1 July 2017.
- A schedule to the VAT Act lists goods and services that are subject to special rates in addition to the standard rate.
- A schedule to the VAT Act also lists goods and services that are subject only to special rates. (continued on page 3)

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EDITOR'S LETTER

Dear Readers,

Welcome to the latest edition of BDO's Indirect Tax News.

As mentioned in the introductory note to our last publication, the introduction of a VAT regime in the Gulf States is fast approaching and BDO International is working closely with the Managing Partners of our Member Firms in the United Arab Emirates, Qatar, Bahrain, Oman, and Saudi Arabia to ensure our firm takes a strong leadership role in assisting our clients and contacts in the region.

As part of this initiative, I presented at VAT-focussed seminars in each of the Gulf States between 25 September 2016 and 3 October 2016. You may also be aware that Egypt has recently introduced a VAT system, that took effect almost immediately, with a headline VAT rate of 13%, that is significantly higher than the 5% VAT rate expected to be imposed in the Gulf.

Furthermore, a few years later than originally anticipated, a Goods & Services Tax (GST) is also in the cards for India, so there are quite a number of Indirect Tax developments across the globe. In the circumstances, please ensure that you take the necessary advice when doing business in any new geographies.

Here in Ireland, we are expecting that the "Brexit" decision by our near neighbours and closest trading partner – the United Kingdom – will have significant implications for our economy and that this will create risks, as well as opportunities, for us.

As part of BDO Ireland's strategy to assist our clients, we are acquiring a Customs & International Trade Advisory Practice, as there will likely be a significant increase in the demand for customs-related advice both in the run up to – and after – the UK's exit from the European Union. This issue will also affect our colleagues in other European Union countries so our customs expertise in Ireland, the UK, and various other countries inside and outside the EU will be well placed to work together to assist our clients as necessary.

Many thanks for reading our publication and please email me (ifeerick@bdo.ie) with suggestions for future articles.

Kind regards from sunny Dublin!

IVOR FEERICK
Chair –
BDO International VAT Centre of Excellence
Ireland – Dublin
ifeerick@bdo.ie

(continued from cover page)

Scope of the tax

VAT applies to the following transactions:

- The supply of taxable goods and services with turnover that has exceeded the registration threshold;
- Importation of taxable goods into Egypt, regardless of the status of the importer;
- Imported services that are performed for customers and clients in Egypt.

Registration threshold

Any individual or legal person who sold taxable goods or services with turnover of at least EGP 500,000 during the 12 months before 7 September 2016 must register for VAT. Individuals whose turnover is below the VAT registration threshold may register voluntarily.

The registration threshold for importers of taxable goods or services is zero, which means all importers must register.

Non-recoverable input tax

No input tax credit is allowed in the following situations:

- With respect to specific taxes imposed by the schedules attached to the VAT law;
- Where input tax is recorded as a cost;
- On exempted goods and services.

Exports of goods and services

Export of goods out of Egypt is zero rated. Subject to certain conditions, a taxable person can claim a refund of VAT paid on inputs used to produce exported goods/services.

Imported goods

VAT is payable on all imported goods at the time the goods are declared to Customs.

Vat returns and payments

- Generally, a VAT return must be filed within two months of the end of a tax period in which VAT is due. However, a VAT registrant's April VAT return must be filed before 15 June;
- Remittances of VAT are due at the same time VAT returns are filed;
- A VAT return must be filed even if there are no sales in that period.

Penalty regime

The VAT legislation provides for penalties for non-compliance. The penalties depend on the reason for, and duration of, the non-compliance, and the amount of tax involved. Simple interest is charged at a rate of 1.5% per month, or part of a month, during which an amount remains unpaid.

In addition to financial penalties, criminal penalties can also be applied for failure to comply with the tax obligations.

Examples of exempted goods and services

Here are examples of some goods and services that are exempt from VAT in Egypt:

- Baby milk, milk, and dairy products;
- Tea, sugar, and coffee;
- Crude oil;
- Natural gas and butane;
- Natural resources, including mining and quarrying products;
- Raw gold and silver;
- Selling and lease of vacant land, agricultural land, buildings, residential and non-residential units;
- Production, sale, and transport of electricity;
- Oil, gas, and mineral resources to the extent that they have not been processed;
- Paper intended to be used for printing purposes;
- Banking services supplied exclusively by banks;
- Insurance services;
- Postal services and non-banking financial services, that are under the supervision of the Egyptian Financial Supervisory Authority (EFSA);
- Non-commercial services rendered by not-for-profit organisations;
- Pharmaceuticals and active substances used for pharmaceutical production.

Non-residents and reverse charge mechanism

A non-established business (non-resident in Egypt and not registered with the tax authority) that makes supplies of taxable goods or services to a resident individual/ entity that is not registered for VAT must appoint a VAT representative to register for VAT if it is liable to account for Egyptian VAT on supplies. The VAT representative must be resident in Egypt, may act on behalf of the taxable person for all purposes related to VAT, and is jointly responsible for compliance with all VAT obligations.

The resident individual/entity should make sure that such non-established business has appointed a VAT representative in Egypt, and if not, the resident individual/entity should settle the tax due as per the law.

Tax refunds

VAT is refunded as per the conditions and procedures prescribed in the executive regulations of the VAT law (which is expected to be issued soon), within 45 days of submitting a "Request for Refund" and supported by documents, in the following cases:

- Input tax on exported goods and services, on condition that the value of exported goods and services has been settled in a bank subject to supervision of Central Bank of Egypt (CBE);
- According to CBE regulations, or as per payment/settlement methods prescribed in the executive regulations of the VAT law, with further condition that the value of exports are not less than inputs;
- Tax collected in error;
- The presence of a VAT credit balance for six consecutive VAT tax periods (6 months/ returns);
- VAT on machinery and equipment used in producing taxable goods or providing taxable services will be refunded in the first sales tax return, except for buses and passenger cars, unless such vehicles and cars are used for carrying out the licensed activity of the business.

One of the refund requirements/procedures is a certificate from a Public Accountant that the registrant is entitled to a tax refund.

Statute of limitation

The statute of limitations is five years and is extended to six years in case of tax evasion.

Tax appeal rules

The taxpayer/registrant has the right to appeal against a VAT claim from the tax authority within 30 days of the date of receipt of such claim.

The law has set up appeal forums at two levels – the Internal Committee and the Appeal Committee. The Appeal Committee's decision is final and taxes should be paid according to that decision. The case may be further appealed by either the tax authority or taxpayers to the court within 60 days of receiving the Appeal Committee's decision.

MOHANAD KHALED
MOSTAFA MAKRAM
Egypt – Cairo
m.khaled@bdo.com.eg
m.makram@bdo.com.eg

ARGENTINA

TAX BENEFITS FOR MICRO, SMALL AND MEDIUM-SIZE BUSINESSES

To promote the growth of micro, small, and medium-size businesses, the Argentine government has decided to grant them certain tax benefits, including on consumption taxes.

The measures adopted include, among others, the deferral of the monthly payment of Value Added Tax (VAT) and the promotion of investments in depreciable goods (new or used), excluding automobiles. This last benefit amounts to allowing such businesses to transform VAT tax credits into non-transferable fiscal credit bonds that can be used to cancel their national taxes, including customs duties. Therefore, companies that benefit from these provisions avoid carrying VAT credit balances that could amount to tax losses when there is inflation.

Such businesses also qualify for benefits on other taxes (for example, the exemption from the Minimum Presumed Income Tax), as well as being able to take advantage of facilities to obtain financial credits that offer greater guarantees and discounts on interest rates, for example.

It should be noted that companies whose main activities are financial or insurance services or services related to gambling and betting, among other excluded activities, cannot qualify as micro, small, and medium-size businesses. As a result, such companies, even if they meet the sales parameters and other applicable requirements, are not allowed to take advantage of the benefits.

GUILLERMO JAIME POCH
ALBERTO FABIÁN MASTANDREA
Argentina – Buenos Aires
gpoch@bdoargentina.com
amastandrea@bdoargentina.com

BELGIUM

SIMPLIFICATION MEASURE FOR PROOF OF INTRA-COMMUNITY TRANSPORT

The Belgian VAT Authorities have published an administrative decision (Decision nr. 129.460 of 1 July 2016), in which they have announced more flexible conditions for the application of the VAT exemption for intra-Community supplies of goods. More specifically, a so-called "document of destination" has been introduced, as an alternative to the CMR document. The purpose of this document is to make it easier to prove that goods have been dispatched from Belgium and received by the buyer.

Document of destination as an alternative for CMR document

Goods supplied by or on behalf of the supplier or customer from Belgium to another EU Member State, where the customer has to perform an intra-Community acquisition of those goods, are exempt from VAT in Belgium. Consequently three conditions need to be fulfilled in order to apply the VAT exemption:

- A supply of goods is made by a VAT taxable person;
- The goods are supplied from Belgium to another EU Member State;
- The customer is required to perform an acquisition of goods in the EU Member State of arrival.

The supplier must therefore be able to prove that the goods have been transported from Belgium to another EU Member State. A crucial piece of evidence in this respect is a CMR document, signed by the recipient of the goods. According to the recently published Decision, the Belgian VAT Administration authorises the use of a "document of destination" as an alternative to the CMR document.

Formalities

In order for the document of destination to be valid proof of transport, it needs to mention:

- The full identity of the supplier and customer (including the VAT identification numbers);
- The statement: "Confirmation of the arrival of an intra-Community supply of goods, in the sense of article 138 of the Council Directive 2006/112/EC";
- The place of arrival of the goods;
- A description of the goods, quantity, and price.

One single document of destination can make reference to multiple invoices issued to the same customer, on condition that the period concerned does not exceed three months. The document of destination must also be signed by the customer in order to confirm receipt of the goods. The person signing the document must be appointed by the customer based on his/her administrative function within the company, and deemed knowledge of the purchases performed by the company (for example, the head of accounting).

Documents of destination may be sent and confirmed via email or another electronic method, so long as that the authenticity of the signatures is guaranteed.

Also, global VAT representatives may use the document of destination to reduce their administrative burden.

Some examples of documents of destination can be found in the above-mentioned Decision.

The new rules took effect on 1 July 2016, by means of trial. The Belgian VAT Authorities, however, reserved the right to revoke the Decision entirely, or refuse its use by individual taxpayers if inappropriate use is established.

ERWIN BOUMANS
Belgium – Brussels Airport
erwin.boumans@bdo.be

CANADA

SALES TAX RATE INCREASES IN THREE MARITIME PROVINCES

The goods and services tax (GST) or harmonised sales tax (HST) generally applies to all taxable supplies made in Canada, other than zero-rated supplies. In the provinces of New Brunswick, Newfoundland and Labrador, Nova Scotia, Ontario, and Prince Edward Island, HST applies. The HST rate is made up of a federal component (currently 5% GST) and a provincial component that is set by each province.

Effective 1 July 2016, the provincial component of HST increased from 8% to 10% in the provinces of Newfoundland and Labrador, and New Brunswick. As a result, the combined HST rate in those provinces increased from 13% to 15%. Effective 1 October 2016 the Prince Edward Island provincial component of HST increased from 9% to 10%, bringing the combined rate in that province to 15%. Nova Scotia, the other maritime province, had previously increased the rate to 15% on 1 July 2010. Ontario's combined HST rate remains unchanged at 13%.

These rate increases will affect any GST/HST registrant doing business in these provinces. Specific transitional rules were released that deal with the application of the HST rate increase for transactions that straddle the respective effective dates.

Newfoundland and Labrador

In addition to the increase in the provincial component of HST, in its 2016 provincial budget, Newfoundland and Labrador announced that the point-of-sale rebate on the provincial component of HST would be eliminated on the sale of books to individuals effective 1 January 2017.

The budget also reintroduced a 15% Retail Sales Tax (RST) on insurance premiums covering property and casualty risks in the province effective 1 July 2016. (Since 1 January 2008 these insurance premiums were not subject to RST.) HST registrants should be aware that the RST paid on insurance premiums cannot be recovered as an input tax credit. Note that where a taxable contract of insurance is purchased from an out-of-province vendor not registered to collect RST, the insured is required to self-assess and remit the tax directly to the provincial Department of Finance.

The RST rate applicable to the sale of used vehicles in Newfoundland and Labrador also increased from 14% to 15% effective 1 July 2016.

Conclusion

In summary, businesses operating in Canada should review their processes, and sales and accounting systems, to ensure transactions are recorded and sales tax is remitted at the appropriate rates.

LINDA MCCRACKEN
Canada – Burlington
lmccracken@bdo.ca

CHILE

VAT ON REAL ESTATE SALES

According to the tax reform introduced by Law No. 20,780 and Law No. 20,899, since 1 January 2016 a modification to the Chilean VAT Law related to the 19% VAT imposed on the sale of real estate sold by a "regular seller" is now in force.

Before this change, VAT was only applicable to sales made by "construction companies" that built all or part of the construction. Now VAT is levied on the sale of real property, whether new or used, regardless of who the property is owned by, if the sale is through someone whose ordinary business is the sale of real estate.

Whether a seller is in the ordinary business of real estate sales is determined by the nature, quantity, and frequency of its real estate sales and relates to whether the particular purchase is for their own use or for resale. The VAT Regulation establishes a presumption of regularity on all operations made by a taxpayer in its line of business.

As well, if the time between the acquisition or construction of real property and its sale is less than one year, there is a presumption that the sale was part of the seller's ordinary business and is subject to VAT.

To determine the taxable base for VAT purposes for new construction, the land value (which can be up to twice its tax value) is deducted from the sale price. The taxable base for VAT purposes on the sale of used property is the difference between the sale and purchase price, less the value of the land.

CATALINA BELLINGHAUSEN A.
RODRIGO BENÍTEZ C.
Chile – Santiago
cbellinghausen@bdo.cl
rbenitez@bdo.cl

GERMANY

INPUT VAT DEDUCTION AT RISK?

One of the formal criteria that must be met to qualify for an input VAT deduction is currently unsettled in Germany. The uncertainty revolves around the meaning of the requirement that a VAT invoice must include an "address of the taxable person" (seller) in order to claim the input VAT deduction.

The uncertainty started as a result of a judgment of the German Federal Fiscal Court (BFH) in decision V R 23/14 dated 22 July 2015. The issue in that case was whether a taxpayer was entitled to an input VAT deduction where the address provided on the invoice was a mere postal address (in other words, a letterbox address). The tax authorities denied the input VAT deduction. The BFH concluded that it is not sufficient for the invoice to have just a postal address stated. The court was of the view that the invoice must include the place of the economic activity of the taxable person.

In contrast to the decision of the BFH, the Financial Court of Cologne was of the opinion in a similar case that the BFH's interpretation of "place of economic activity" is out-dated, given technical developments and changes in business practices. As a result, the Financial Court of Cologne ruled that the taxpayer was entitled to an input VAT deduction if a postal address is provided on the invoice and the other conditions for an input deduction are met.

The Financial Court of Cologne's decision was then referred back to the BFH to decide what "address of the taxable person" means. The BFH's 5th senate asked the European Court of Justice (CJEU) for a preliminary ruling of how the criterion "address of the taxable person" should be interpreted, especially in light of the CJEU decision in the PPUH case dated 22 October 2015. At the same time, the BFH's 11th senate referred a similar case to the CJEU, so it is likely that the CJEU will combine the cases in a joint decision.

So, at the moment, the question remains unsettled and taxpayers are not sure what to do if the German Tax Authorities deny them the input VAT deduction based on their belief that an invoice does not satisfy the formal requirements related to the "address of the taxable person". While the preliminary rulings of the CJEU are outstanding, we suggest taxpayers in this situation file an appeal and ask for a stay of the proceeding until the preliminary ruling of the CJEU is provided.

ANNETTE POGODDA-GRÜNWALD
DANIEL AUER
Germany – Berlin
annette.pogodda@bdo.de
daniel.auer@bdo.de

HUNGARY

VAT CHANGES AS OF 2017

With passage of the 2017 amendments to the tax law, Hungary's tax legislation for the coming year is now finalised. In this article we describe the main VAT changes that will apply next year in Hungary.

Compulsory data content of invoices

With effect from 1 January 2017, the tax ID number of the domestic taxable customer must be shown on any invoice where the amount of VAT charged on the invoice exceeds HUF 100,000.

Domestic sales and purchase listing report

Related to the changes in the information that will have to be included in invoices, the threshold applicable to the requirement to make a summary declaration of domestic sales subject to VAT will drop from HUF 1 million to HUF 100,000 effective 1 January 2017.

Also effective from 1 January 2017, so-called domestic listing reports, which are part of the VAT reporting obligations for domestic transactions in Hungary, will have to list all the invoices and suppliers where the amount of the VAT charged exceeds HUF 100,000 or where the total amount of the VAT charged on the basis of the goods and services purchased from the same supplier and deducted during a given period exceeds HUF 100,000.

Changes to the VAT rates

The following changes to VAT rates will apply beginning 1 January 2017:

- VAT on Internet subscription services and VAT on food served and non-alcoholic drinks prepared and sold at catering establishments will decrease to 18% from 27%. The VAT Act will provide an unambiguous definition of Internet subscription services based on definitions set out in EU regulations.
- VAT on poultry and eggs will drop from 27% to 5%
- VAT on raw milk (excluding UHT and ESL milk) will drop from 18% to 5%.

Electronic reporting obligation and the content of invoices

Similar to the rules that already apply to suppliers on their on-line sales, taxpayers will have to provide the Hungarian Tax Authority with real-time data on the content of their invoices. The details of this provision have not yet been provided, but the new reporting obligation is expected to be fulfilled by a separate function that will be required to be installed in all invoicing software. So, this new obligation will mean that invoicing programs will have to be developed. There will be a separate statutory regulation specifying the scope and format of data to be reported. The new reporting obligation will apply from 1 July 2017.

VAT refund agreement between Hungary and Norway

A VAT refund agreement between Hungary and the Kingdom of Norway will enter into force 1 January 2017. Under a provision in the agreement, retroactive to 2014, Hungarian companies will be entitled to reclaim VAT charged in the territory of Norway and non-established Norwegian companies will be entitled to reclaim VAT on their transactions in Hungary. Taxpayers must file their claims in respect of 2014 and 2015 by 30 September 2016.

ANGÉLA SZŐKE
Hungary – Budapest
angela.szoke@bdo.hu

IRELAND

VAT REGISTRATION

Ireland's Revenue Commissioners have implemented a strict approach in the allocation of VAT Registrations (VAT IDs) in an attempt to reduce what they see as spurious or invalid registration applications.

In soon-to-be-issued guidance, the Revenue Commissioners have identified certain documentation that is required to substantiate a registration application. The Revenue has re-iterated, however, that the substantiation process does not represent a change in practice and is fully in line with the decision in the Rompelman's case, which was a CJEU decision.

The following are some of the documents the Revenue Commissioners expect with an application:

- Copies of any contracts entered into;
- Copies of sales or purchase invoices issued or received;
- Details of customers and/or suppliers;
- Copies of any market research/business plans/feasibility studies prepared or carried out;
- Details of stock or capital expenditure records;
- Details of business premises such as lease, agreement for lease, and so on.

The Revenue Commissioners have stated that if none of this information is available or provided to them by an applicant, the registration application will not be processed.

We have no doubt that the approach being adopted is going to result in additional correspondence between the applicant/agent and the Revenue Commissioners and further delays in what is already a slow process.

JIMMY RYNHART
Ireland – Dublin
jrynhart@bdo.ie

ITALY

OPINION OF THE ADVOCATE GENERAL OF THE EUROPEAN COURT ON VAT INPUT TAX RECOVERY IN THE MERCEDES BENZ ITALY CASE

For fiscal year 2004, Mercedes Benz Italy was assessed by the Italian Tax Authorities for VAT of EUR 1,755,882 (plus penalties and interest) that the tax authorities claimed the company owed as a result of how it calculated its input VAT deduction. Mercedes Benz excluded interest on loans incurred in the year from the pro-rata calculation, because it considered these transactions as ancillary to its main activity.

Mercedes Benz appealed the Tax Authorities' decision (first to the Provincial Tax Court and then to the Regional Tax Court). The Regional Tax Court of Rome requested an opinion from the Advocate General of the European Court about whether the Italian VAT pro-rata rules, as interpreted by the Italian Tax Authorities, are in line with the EU Directive.

Conclusions of the Advocate General

The Advocate General published its opinion on 29 June 2016 (C-378/15). The Advocate General concluded:

- Application of a pro-rata calculation to all purchases of goods and services is contrary to the EU VAT Directive.
- According to the EU Directive, the VAT pro-rata calculation is applicable ONLY on mixed use goods and services.
- For goods or services sold by the company that are subject to VAT, 100% of the input VAT is deductible.
- For goods or services sold by the company that are VAT exempt, the amount of input VAT that is deductible is zero.
- The Italian provision and the interpretation of the Italian Tax Authorities is incompatible with the proportionality, effectiveness, and neutrality principles stated in the EU Directive.

If the Advocate General's conclusions are confirmed by the European Court of Justice (CJEU), these conclusions will mean a very significant change in Italy for all businesses that calculate their input VAT deduction on a pro-rata basis.

LORENZA CASARI
Italy – Turin
lorenza.casari@bdo.it

LATVIA

SMALL TRANSACTIONS THRESHOLD DECREASED

Currently, VAT registered persons must indicate in their VAT return each domestic transaction (the supply or acquisition of goods and services) separately, if the value of the transaction exceeds EUR 1,430 (excluding VAT). Detailed information about the transaction must also be provided, such as tax invoices; cash receipts; receipts or other payment documents related to non-cash payments; customs declarations; invoice number; date of the invoice; VAT ID number of the supplier or recipient; the supplier/recipient's name; type of transaction; and so on.

In contrast, VAT registered persons currently do not have to provide details on their VAT return about so-called "small transactions", which are domestic transactions valued under EUR 1,430. Small transactions can be summed and the amount simply reported as "other transactions". Moreover, when a VAT registrant has more than one transaction with the same supplier or recipient and the value of each transaction is less than EUR 1,430 (excluding VAT), the transactions can be summed and included under "other transactions", even if the total value of all transactions with that same supplier/recipient exceeds EUR 1,430.

Change in the small transaction threshold

Unfortunately, the government of Latvia recently decided to decrease the value of small transactions that must be reported separately. Effective 1 January 2017 the threshold will drop from EUR 1,430 to EUR 500.

Since tax returns must be submitted to the tax authority electronically, this change could place additional burdens on taxpayers that do not currently have the information technology in place to allow them to export the necessary information from their accounting system to the tax authority's data base.

INITA SKRODERE
GITA AVOTINA
Latvia – Riga
inita.skrodere@bdo.lv
gita.avotina@bdo.lv

LUXEMBOURG

VAT ON DIRECTORS' FEES – SOME CLARITY IN LUXEMBOURG?

On 30 September 2016, the Luxembourg VAT Authorities (Administration de l'Enregistrement et des Domaines) issued the long-awaited circular (N° 781) on the VAT treatment of directors' fees.

Until now, in Luxembourg the treatment of directors' fees could be described as being in a state of flux, as is the case in many other Member States of the European Union. There were lengthy debates on whether directors' fees were within the scope of VAT (that is, whether the directors were acting as VAT taxable persons), whether a VAT exemption was applicable (for example, article 44§1 (w) that would allow an exemption for the honorific activities of board members, or article 44§1 (d) that exempts the management of certain investment funds), or if they were simply taxable.

Taxation becomes the rule

With this circular, the Luxembourg VAT authorities express the view that when a person is sitting on the board of a company for consideration, a director carries out an economic activity (a supply of services) and so the director should be considered a taxable person for VAT purposes. This applies to Luxembourg resident directors and also to non-resident directors (in the latter case, the company is liable for the VAT due).

Some exceptions remain

The circular sets out the following exceptions to the principle set out above:

- Where a director is an employee of a company that itself acts as the director of another one (corporate directors). In this situation, the director remains dependent on its employer and so the director does not fulfil the criterion of a VAT taxable person. In such situations, the employer company becomes subject to VAT on the consideration received. This exception is in line with the current practice in Luxembourg.
- Where Luxembourg resident directors whose annual payments from directorship positions do not exceed EUR 25,000 (article 57 LVL) (potentially increased to EUR 30,000 in 2017). This exception still requires the director to register for VAT but it considerably simplifies the formalities imposed in terms of VAT compliance. Such taxable persons are not in a position to recover the input VAT.
- The Luxembourg VAT authorities also still accept that, in some circumstances, the directors' fees remain exempt from VAT when the activity is for honorific purposes (whatever it means) and the consideration received is intended mainly to cover the costs incurred by the director ("défraiement"). Given the lack of clarity of the terminology used, there is little doubt that interpretation of these two conditions will give rise to many debates. For example, when a doctor sits on the board of a public institute in Luxembourg, or a banker sits on the board of a Charitable Foundation, it will be a matter of interpretation whether the position is honorific and also of whether the amount paid can be considered to simply cover the costs of that person.

Despite the importance of the investment funds sector in Luxembourg, in a context where the VAT authorities are taking a position on the treatment of the directors' fees, it is surprising that the possibility of applying the VAT exemption of article 44§1 (d) LVL (the exemption covering the "management of investment funds") is not mentioned in this circular. In our view, because the position of a director on the board of a regulated investment fund primarily involves managing that fund, we believe that the related consideration will thus be exempt. The conclusion might be different, however, for a director's position in an Alternative Investment fund Manager (AIFM), a third party management company, or for a director's position in the management company of a "Fonds Commun de Placement" (FCP).

What BDO recommends

Private individuals acting as directors should now consider the necessity of registering for VAT and should start charging VAT on the consideration they receive for sitting on a board.

Being a VAT taxable person involves some other obligations, such as the correct invoicing of the services provided and the submission of VAT returns. The director should pay particular attention to the possibility that, by virtue of their director's fees, they may be subject to the special regime applicable to small entrepreneurs (the so-called "franchise", which applies to ventures whose earnings are below a threshold of EUR 25,000). And, if the director's total remuneration from all sources is less than EUR 500,000, the director might be entitled to apply rules that only require the Luxembourg VAT be chargeable only when the payment is actually received (article 25 LVL).

It should also be noted that where the VAT regime applies to directors' fees, the VAT applies on the gross remuneration of the director, in other words, including amounts withheld for income tax purposes.

Once registered for VAT, the directors should carefully analyse their input VAT recovery position. If they are entitled to claim input VAT, they should retain evidence of the input VAT they incurred on the costs that they report as deductible in their VAT return.

When paying directors who sit on their boards, Luxembourg companies should carefully consider their liability to declare and pay VAT on the remuneration paid, especially with respect to their non-resident directors (who can reside in or out of the European Union). The VAT registration of a director in their country of residence does not affect the obligations imposed on the paying entity, which remains liable for the Luxembourg VAT due. Regardless of the director's VAT obligations in their home county, a Luxembourg entity that pays directors must decide whether an exemption (such as article 44§1 (w) or article 44§1 (d) mentioned above) applies for Luxembourg VAT. In some instances, such as where a Luxembourg finance company has directors who are resident in other countries, payments to directors will even trigger a VAT registration liability in Luxembourg.

BDO can assist clients and guide them through the different scenarios that might be envisaged.

ERWAN LOQUET
Luxembourg
erwan.loquet@bdo.lu

MALTA

FANTASY SPORTS AND VAT

Beginning 1 August 2016, Malta no longer requires those offering Fantasy Sports (and similar skill games) to be licenced under the terms of the Lotteries and Gaming Act and the Remote Gaming Regulations. As a result, such endeavours can be conducted in, and from, Malta without the need for a licence. The removal of the licence requirement for gaming is (pardon the pun) a game changer, since the online gaming exemption from Maltese VAT is tied to licensed gambling activities. As a result, 18% VAT is due on fantasy sports offerings that are deemed to take place in Malta.

Of course, the removal of the licensing requirement provides an opportunity for skill game operators to relocate to Malta, as they are entitled to claim a credit for input VAT (when linked to taxable fantasy sports games), even though the place of supply of such offerings is in another jurisdiction, given that such games are generally considered to be electronically supplied services (and therefore deemed to take place where the non-taxable customer is established).

It should be noted that the position adopted by the Malta Gaming Authority is not necessarily in line with the VAT treatment afforded by the final customer's country of establishment, which could still exempt such supplies from VAT.

JOSEF MERCIECA
Malta
josef.mercieca@bdo.com.mt

THE NETHERLANDS

MIXING DEDUCTIBLE PROPORTION ON MIXED-USE INPUT GOODS AND SERVICES

The European Court of Justice (CJEU) recently handed down its decision in the Wolfgang and Dr. Wilfried Rey Grundstückgemeinschaft case (9 June 2016, C-332/14), which related to the amount of deduction on mixed-use input goods or services.

Based on the CJEU's decision in the BLC Baumarkt case, EU Member States have two options to determine what VAT is deductible and what VAT is not. In that case, the CJEU concluded that Member States can determine the amount of VAT deductible by applying a turnover-based method or on the basis of a different method, for example, floor area, if the alternative method results in a more precise determination of the deductible proportion.

In the Wolfgang and Dr. Wilfried Rey Grundstückgemeinschaft case, the CJEU concluded that a Member State cannot force a VAT entrepreneur to apply a combination of methods to get the most precise determination of the deductible proportion. Instead, the method applied must simply provide a more precise result than the result that would arise by applying the turnover-based method. The requirement of precision relates to the method of calculating the deductible proportion of the amount of VAT, not to assigning the goods and services used. In our view, with this decision, the CJEU leaves open the option for a VAT entrepreneur to mix both methods, if doing so leads to a more precise determination of the deductible amount.

The VAT deductible in this type of situation in the Netherlands is determined, in principle, by applying a turnover-based method. But, when the actual use of the (mixed-use) input goods or services (taken as a whole) differs from the assumed use by applying a turnover-based method, the deduction of VAT must be determined on the basis of actual usage.

According to Dutch case law, the burden of proof lies with the party claiming a deduction on the basis of actual usage instead of on a turnover basis. The taxpayer must provide evidence using objective and precise defined data. The actual usage can, for example, be proven on the basis of floor area, hours spent, amount of employees, amount of visitors, and so on.

In light of the Wolfgang and Dr. Wilfried Rey Grundstückgemeinschaft case, it seems there is a difference between the Dutch VAT law and the CJEU judgement regarding determination of the deduction of VAT on mixed-use input goods or services. According to the CJEU, to use something other than a turnover-based method, the alternative method should be more precise. In the Netherlands, the method based on the actual use of all input goods and services (taken as a whole) is supposed to be used if it better matches the real situation.

In addition to this difference, the Dutch Supreme Court (Hoge Raad, 10 January 2014, no. 09/01485) has determined that it is not possible to mix both methods. In the Dutch case, the taxpayer determined the input VAT on a building using the actual usage for rooms/areas that were used exclusively for taxable or exempt activities but the taxpayer applied a turnover-based method for the mixed-use common areas. The Dutch Supreme Court concluded that it was not correct to combine the two methods. Instead, the Dutch Supreme Court held that the amount of deduction should be determined using only one method. In practice, this means that a deduction on the basis of actual usage is not possible for mixed-use buildings, even if this would lead to a more precise determination of the deductible amount.

In our view, the judgement of the Dutch Supreme Court is now overruled by the Wolfgang and Dr. Wilfried Rey Grundstückgemeinschaft case. As a result, applying a combination of methods that provide a more precise determination of the deductible amount should be allowed in the Netherlands.

So, the Wolfgang and Dr. Wilfried Rey Grundstückgemeinschaft decision may give Dutch VAT entrepreneurs more room to determine the amount of deduction based on the EU VAT Directive than if they applied Dutch case law. Based on the Larentia & Minerva case, however, the Dutch Tax Authorities do not have this option because the tax authorities cannot rely on EU law directly if the EU law has not been correctly implemented in the Netherlands.

MARCO BEERENS
REMCO DONNERS
The Netherlands – Breda
marco.beerens@bdo.nl
remco.donners@bdo.nl

PHILIPPINES

VAT UNDER THE NEW ADMINISTRATION

The Philippines' VAT rate of 12% has been unchanged since 2007. However, the new administration is considering raising the rate to 15%.

The former Bureau of Inland Revenue (BIR) Commissioner has suggested that, in addition to adjusting the VAT rate, the VAT exempt transactions should also be reviewed. VAT is currently imposed on all consumer products except for food and products sold in their original state. Section 109 of the National Internal Revenue Code sets out the VAT exempt transactions.

Unless and until the new administration successfully convinces the House of the Representatives (Congress) of the need to increase the VAT rate and limit the VAT exempt transactions, the following applies:

- The VAT rate stands at 12%;
- Monthly VAT returns are due on the 20th day of the month after the close of the taxable period;
- The quarterly VAT return is due on the 25th day of the month after the close of the taxable quarter;
- The quarterly summary of sales and purchases is due on the 25th day of the month after the close of the taxable quarter for non-eFPS filers (electronic filers) and on the 30th day of the month after the close of the taxable quarter for eFPS filers.

EVANGELIE B. ABANTE
Philippines – Makati
ebabante@bdoalbaromeo.ph

ROMANIA

VAT TREATMENT OF CROSS-BORDER LEASING TRANSACTIONS

Cross-border leasing transactions are being used more and more in Romania. To understand the treatment of such transactions for VAT purposes in Romania, let's consider a hypothetical example.

Assume Company A is established and VAT-registered in Germany and enters into vehicle leasing agreements with Romanian companies. Let's also assume that Company A purchased the vehicles in another Member State (let's say Italy) and the vehicles are transported directly from the supplier to the Romanian lessee companies. So, if Company A performs intra-Community acquisitions in Romania, it is obliged to register for VAT purposes in Romania before it performs such operations.

If Company A is not considered established in Romania or is not established in Romania for the supply of leasing services, the lessee companies are liable to pay VAT for such services through a reverse charge mechanism, even if Company A is registered for VAT purposes in Romania.

Based on the Judgement of the European Court of Justice in case C-190/95 (ARO Lease BV), a leasing company cannot be regarded as having a fixed establishment in a State if it does not have in that Member State either:

- Its own staff;
- A structure that has a sufficient degree of permanence to provide a framework in which agreements may be drawn up; or
- Management decisions taken so that the services in question would be considered supplied on an independent basis.

If Company A does not have sufficient technical and human resources for negotiating, drawing up, signing, and administering the relevant leasing agreements in Romania, the company would not be considered established in Romania and would not have a fixed establishment in Romania. Therefore, in this situation, the leasing services would be subject to the reverse charge in Romania and would be invoiced to Romanian companies without VAT, using Company A's German VAT number.

VLAD MADARAS
DAN BARASCU
Romania – Bucharest
vlad.madaras@bdo.ro
dan.barascu@bdo.ro

SINGAPORE

"BELONGING" STATUS OF SUPPLIERS AND RECIPIENTS OF SERVICES FOR GST PURPOSES

Foreign companies supplying or receiving services in Singapore should pay attention to the new GST rules recently published by the Inland Revenue Authority of Singapore (IRAS). Unlike goods, where the taxability is dependent on the location of the goods at the time of supply, the "belonging" status – a term defined in the GST Act – affects the GST treatment of services supplied or received.

Determining the belonging status of suppliers and customers

In May 2016, the IRAS introduced a new guide that aims to provide greater clarity to businesses that make supplies of services to Singapore, or in Singapore, with regard to their GST obligations.

In Singapore, the place where the supplier "belongs" will affect whether a supply of services is within the scope of Singapore's GST, while the place where a customer belongs will affect whether a supply of services can be zero-rated for GST purposes. The place where a person belongs depends on where the person has their "business establishment" or "fixed establishment".

Meaning of "business establishment" or "fixed establishment"

Business establishment (BE) is the place from which the business is run. If the supplier carries on a business through a branch in Singapore, the supplier is treated as having a BE in Singapore.

A fixed establishment (FE) is an establishment, other than a BE, that has both the technical and human resources necessary to provide or receive services on a permanent basis.

The IRAS has mentioned several factors that businesses should consider in determining the belonging status when applying the place of supply and zero-rating rules.

With the newly published guidelines, overseas service providers need to determine if they must register for GST in Singapore. Making this determination requires considering which establishment is most directly concerned with the supply. Note that the concept of tax residency for income tax purposes is different from the concept of belonging for GST purposes. An overseas company that is a tax resident in Singapore may not necessarily belong in Singapore for GST purposes.

How BDO Singapore can help

BDO Singapore can help businesses:

- Review the business arrangement and belonging status to assess the GST treatment of transactions and determine whether compulsory registration applies; and
- Assist in submitting the requisite application for GST registration/exemption.

CHIN SIEN EU
AMY SIM
Singapore
chinsien@bdo.com.sg
amysim@bdo.com.sg

SLOVAKIA

CHANGES TO REVERSE-CHARGE AND COMPENSATION FOR UNPAID INPUT VAT DEDUCTION

Reverse-charge on the supplies of goods by foreign persons

A change in the reverse-charge mechanism for local supplies of goods by foreign persons to a Slovak-established entrepreneur was introduced as of January 2016. Under the new rules, foreign taxable persons do not charge Slovak VAT on invoices for local supplies of goods issued to Slovak-established entrepreneurs. Instead, the recipient is liable for application of a reverse charge. This does not apply to the distance sale of goods or supplies of goods to non-taxable persons, however.

The change can cause difficulties for some foreign entrepreneurs registered for VAT in Slovakia because they may not have any output supply to report in their Slovak VAT returns. In such cases, foreign entrepreneurs may not deduct input VAT in Slovakia on their Slovak VAT returns, though they would be registered for VAT in Slovakia.

In such situations, foreign entrepreneurs can claim the Slovak input VAT only through a VAT refund procedure. This change has negative cash-flow impact for foreign VAT payers, as the period within which VAT refunds are paid is significantly longer.

Compensation for unpaid input VAT deduction due to a VAT inspection

A proposed amendment to the Slovak VAT Act would introduce a right to compensation for input VAT deductions (plus interest on the input VAT deduction) that remain not refunded due to an on-going VAT inspection.

Under the amendment, the right to interest on an unpaid input VAT deduction will arise if the tax authority opens a VAT audit within the statutory deadline and the VAT audit takes more than six months. An annual interest rate of 1.5% is proposed. This change would be effective from 1 January 2017. The proposal for this amendment resulted from a case law development. This amendment is subject to on-going discussion at the governmental level and, if approved, must then be discussed by the Slovak parliament.

PETER POMPURA
MICHAELA KOMINAKOVA
Slovakia – Bratislava
pompura@bdoslovakia.com
kominakova@bdoslovakia.com

SOUTH AFRICA

THE SUGAR TAX SAGA CONTINUES

Obesity is a global epidemic. By 2012, the percentage of the South African population considered obese was 10.6% of men and 39.2% of women. Many factors impact obesity, such as consumption preferences, portion sizes, education, and physical activity. The World Health Organisation (WHO) recommends sugar intake of less than 10% of total energy intake per day and they have urged countries to use taxes and subsidies and other measures to change people's behaviour. The WHO specifically recommends measures designed to: incentivise healthier behaviours, improve affordability of healthier food options, encourage consumption of healthier options, and discourage consumption of less healthy options.

In February, to assist in curbing obesity, South Africa's Minister of Finance announced its intention to introduce a tax on sugar-sweetened beverages (SSBs) with effect from 1 April 2017. The main stakeholders have since opined on the merits and methods of implementation of such a tax. The National Treasury recently invited comments on its Policy Paper on the sugar tax. The media statement made reference to the Department of Health's Strategic Plan for the Prevention and Control of Non-Communicable Diseases 2013-2017 and to the National Strategy for the Prevention and Control of Obesity 2015-2020. These strategies aim to reduce obesity by 10% by 2020.

Treasury's Policy Paper (the Paper) lists the specific focus of the tax's coverage, its defined base, the tax rate, and how it will be administered as key considerations in designing and implementing a tax on SSBs. SSBs are defined as beverages that contain added caloric sweeteners such as sucrose, high-fructose corn syrup, and fruit-juice concentrates. The proposed tax will exclude beverages that contain natural sugars (or intrinsic sugars). The proposed rate will be 2.29 cents per gram of sugar. This will roughly equate to a 20% price increase on SSBs that have nutritional labels or information on the container, and almost 30% on unlabelled products (to incentivise labelling).

The proposed tax will be administered under the Customs and Excise Act through the application of the duty-at-source (DAS) principle. The Paper suggests that obesity is a major risk factor in the growth of non-communicable diseases (NCDs) and also refers to sugar's cause of tooth decay. The Paper suggests that the main fiscal interventions for NCD control include taxes on: SSBs, unhealthy nutrients (saturated or trans-fats, salt, and sugar) and unhealthy foods (defined by nutrient profiling), as well as with subsidies on fruits, vegetables, and other healthy foods.

International evidence of the impact of similar taxes on sugar suggests a variety of results. Many countries experienced a more than expected price increase, which may suggest that suppliers increased prices by more than the tax to increase profitability. Other countries experienced an increase in calorie intake, increased administrative burden, reduced competitiveness, and less than expected revenue yield. Some countries have experienced some degree of a substitution effect, job losses, a disproportionately higher impact on low-income earners, a lower than expected reduction in sugar intake, and a smaller than expected effect on obese individuals.

It has been estimated that a 20% sugar tax on SSBs could reduce obesity by 0.6% to 7.1% in men and 0.4% to 4.4% in women. It has been suggested that the imposition of a sugar tax could save the government in the order of ZAR 10 billion over the next 20 years in type 2 diabetes treatment. Estimates indicate that diabetes will cost South Africa as much as ZAR 2 billion in 2030. It has also been estimated that between ZAR 2 billion and ZAR 3 billion could be collected in sugar tax per annum.

Perhaps one of the most important effects to consider from the imposition of a sugar tax is the effect on the poor. Though there have not been many scientific studies in this regard, it is most likely that a sugar tax will be regressive, in that it will tax the poor relatively higher than the rich. Treasury argues, however, that arguments about tax regressivity only focus on tax payments and do not consider the benefits to the poor, such as reduced consumption of unhealthy food or SSBs. This argument is loaded with assumptions related to a number of things, such as the price elasticity of consumption of SSBs, especially by the poor. Research shows that the poor consume as much as 300% more beverages and SSBs than the rich, further underlining the regressive impact of the imposition of a sugar tax.

Globally, so-called sin taxes, such as a tax on sugar, have been used for many years and are based on the belief that behaviour can be altered by price manipulation. The introduction of a tax on sugar in South Africa may, in fact, be premature in light of the limited scientific and economic research that has been done in South Africa to date on the merits of a sugar tax and the impact of sugar on obesity, especially when compared to other unhealthy products. Such research and international experience are not conclusive on the likely success a sugar tax would have in substantially decreasing obesity. Factors such as the impact on the poor, the regressivity of the tax, the price elasticity of demand for SSBs, especially for lower income earners, the substitution effect (where consumption is shifted to more unhealthy options and unhealthy sugar-substitutes), the actual ratio of sugar intake through SSB consumption to total sugar intake, the impact on job losses, and the impact of other non-SSB unhealthy products on obesity, are all factors that require further research before the government makes a final decision on the tax. This debate is likely far from over.

FERDIE SCHNEIDER
South Africa – Johannesburg
fschneider@bdo.co.za

SPAIN

SPANISH REGIME FOR NON-ESTABLISHED TAXPAYER TO DEFER VAT ON IMPORT

As we reported in the April 2015 Indirect Tax News, an optional "deferral import regime" came into effect on 1 January 2015 under which taxpayers that fulfilled certain requirements can defer the payment of the VAT related to an import until such amount was included in their tax return.

The Spanish Tax Administration recently issued a binding ruling to clarify whether non-established taxpayers may benefit from this regime. In the ruling, the Tax Administration concluded that being non-established is not, in itself, an impediment to applying this regime.

But, it must be remembered that Spain's VAT regulations include a Special Regime that allows non-established companies that fulfil certain requirements to obtain a VAT refund without having to submit periodic VAT returns. (The Special Regime is meant to comply with the requirements of the VAT Directive so non-established EU companies can recover the VAT borne in another EU country.) Because companies that take advantage of the Special Regime do not submit periodic returns in Spain, companies that qualify under the Special Regime may not apply the "deferral import regime".

But, if a non-established company does not qualify under the Special Regime and therefore has the status of a Spanish taxpayer and is obliged to submit periodic VAT returns in Spain, they can enrol in the "deferral import regime", so long as they meet the other requirements.

ROSARIO ESTELLA
CARLOS BAUTISTA
Spain – Madrid
rosario.estella@bdo.es
carlos.bautista@bdo.es

ACQUISITION OF THE HEAD ENTITY OF A VAT CONSOLIDATED GROUP

On 5 May 2016, the Spanish Directorate General of Taxation (DGT) clarified what happens when a company that is part of a VAT consolidated group acquires a controlling share of the head entity of that group, in other words, the company that is domiciled in Spain and considered the head of the group.

The DGT concludes that, on acquisition of an interest of over 50% of the share capital of the head entity of a VAT consolidated group, the company acquiring the shares then becomes the group's new head.

The DGT's analysis of the timing of when the acquiring company actually becomes the head entity is as follows:

- Where the head entity of a VAT consolidated group is taken over by another company in the group, the status of the head entity passes to the acquiring company from the time the shares are acquired.
- Conversely, in the event of an exchange of shares where the head entity of the group is not dissolved, for example, in the event of a takeover, the acquiring company would not become the new head entity until 1 January of the calendar year following the year in which the exchange of shares takes place.
- When a change in the head entity takes place during the year, the acquiring company must inform the Spanish Tax Authorities of what companies comprise the "new" group. This must be done in December so that it will be applicable for the new calendar year.

DAVID SARDA
VERONICA TARGA
Spain – Barcelona
david.sarda@bdo.es
veronica.targa@bdo.es

VAT DEDUCTIBILITY ON A SHARE SALE TRANSACTION

On 27 April 2016 the Spanish Directorate General of Taxation (DGT) ruled on whether a company (ALFA) is entitled to a VAT input deduction. ALFA, which is engaged in managing moveable and immoveable assets, providing financial advisory services, and investment management, transferred a controlling share in the capital of a subsidiary company (GAMMA). The issue was whether the sale of a block of shares may be included in the scope of VAT.

The DGT began by reiterating that for financial transactions to qualify as a business activity, such transactions must be carried out in fulfilment of the business objectives or for commercial purposes. The DGT noted that "commercial purpose" requires a permanent and organised activity supported by people and infrastructure that is more substantial than the means that would be employed by a private investor. If a taxpayer has a commercial purpose, the sale of a block of shares may be included within the scope of VAT.

The DGT then analysed whether ALFA's sale of GAMMA's shares constituted a regular business activity of ALFA or whether it was, in fact, a marginal transaction that is ancillary to its business activities and therefore should not be included in ALFA's overall pro rata percentage.

Based on its analysis of the case law of the EU Court of Justice on the issue of whether an activity is ancillary, the DGT concluded that the sale of shares of a subsidiary is a VAT zero rated transaction that must be considered ancillary because it entails very limited use of assets and is not a transaction that recurs.

The DGT concluded that since the sale of GAMMA's share was ancillary to ALFA's business, the transaction will not be included when computing the deduction applicable pro rata.

DAVID SARDA
VERONICA TARGA
Spain – Barcelona
david.sarda@bdo.es
veronica.targa@bdo.es

UNITED KINGDOM

BREXIT – THE INDIRECT TAX IMPLICATIONS

On 23 June 2016 the UK voted to leave the European Union, sending shockwaves around the global economy.

This article summarises what we consider to be the key changes from a VAT and customs duty perspective to help those that do business in or with the UK plan for Brexit and maintain their competitive edge.

Introduction

Over the past 40 years the UK's tax laws have become entwined with the regulations within the EU, which look to ensure a level playing field for companies across the union and support the four pillars of freedom for members.

As the UK Government works through the economic impacts of Brexit and how it might be able to cushion the downside and support the upside through fiscal incentives, it will also need to unwind the complex connections between domestic and EU laws.

Customs duty

The UK is currently part of the EU Customs Union, consisting of all EU Member States plus the following territories:

- Channel Islands and Isle of Man;
- Andorra;
- Monaco;
- San Marino;
- Turkey.

The EU Customs Union gives the Member States the following Customs landscape:

- There are no customs duties payable on goods moved between jurisdictions within the Customs Union;
- There is a common external customs duty tariff imposed on goods entering the customs union, regardless of which jurisdiction they first enter through;
- There are a number of special procedures available to companies, offering duty savings and cash flow advantages.

On a formal exit from the EU, following the completion of the Article 50 process, the UK will no longer be part of EU's Customs Union. As a result, the external EU customs duty tariff could be imposed on goods imported from the UK. As customs duties on imported goods and materials are an absolute cost, this is likely to make it less attractive for EU companies and consumers to source goods from suppliers in the UK.

Similarly, the UK Government may extend the current UK customs duty tariff to imports from countries within the EU Customs Union, adding costs for UK companies reliant on raw material and finished goods from EU suppliers.

UK businesses should also be aware a Brexit will mean that the UK no longer has access to the EU's 34 external trade agreements with countries and trading blocks around the world.

This could also lead to increased customs duties on goods imported into these and 53 other jurisdictions with which the EU has some kind of preferential trading relationship – making UK goods potentially less competitive in those markets. It could also increase the cost of goods and materials imported from these countries, as well as the EU Customs Union members, for UK businesses and consumers.

Practical barriers would also arise as all goods would need to be customs cleared, adding time, complexity and cost to value chains.

Currently there are various customs reliefs available for companies importing goods into the UK, such as customs warehousing and Inward Processing Relief. As and when the UK Government considers independent UK legislation post Brexit, these may well be recreated in order to provide UK companies with the relief they need to remain competitive.

What should UK businesses be doing to prepare for these changes?

The potential for increases in costs for UK businesses importing and exporting goods and materials means that UK businesses should start to consider the following as part of their Brexit readiness planning:

- Are sales within the EU large enough to justify moving manufacturing and operations to an EU site to avoid a customs duty hit on margins?
- For imports, how would total costs (including duties) compare from EU suppliers versus potential non-EU suppliers?
- For current EU imports, can suppliers be changed easily? If not, do prices of goods need to be increased?
- For importing materials or unfinished goods in from outside the EU, is there a need for parallel inbound warehouses (one EU based and one UK based)?
- Is it economic to operate parallel sites in the EU and UK?
- Can prices be increased to absorb the additional duty cost and if so, by how much?

Finally, customs duties work both ways; it is likely that the UK will impose duties on EU imports if a comprehensive free trade arrangement with the EU cannot be maintained. Therefore, European businesses may be looking to acquire UK businesses to protect or expand their UK trade.
(continued on page 17)

VAT

The current EU Value Added Tax (VAT) system is part of the fiscal union which operates across the 28 Member States. Although each Member State has its own national VAT legislation, the basic principles and operation of the VAT system has its roots in the EU Directives and the European Court of Justice is the ultimate legal arbiter in disputes.

VAT is a transaction based tax that cascades through the supply chain and is intended to be ultimately borne by the end consumer. VAT is generally chargeable by a supplier of goods/services at the local rate in his Member State on all domestic supplies and supplies to private consumers (persons not registered for VAT) in other Member States. The system, however, taxes supplies of goods between businesses in different Member States under the 'destination' principle which aims to tax the supply at its place of consumption in the EU. Such supplies are generally (with a few exceptions) subjected to the VAT charge in the customer's own country under the Reverse Charge mechanism and a complex compliance framework exists to monitor such transactions and ensure they are correctly accounted for in the Member States – the EC Sales List and Intrastat Returns.

All EU, and most non-EU, businesses incurring costs in the EU are generally able to reclaim VAT across all Member States using the EU VAT Refund mechanism, providing they make supplies which are subject to VAT in the EU or make supplies elsewhere which would be subject to VAT if made in the EU.

The current system is therefore designed to make VAT accounting across borders within the EU as easy as possible for businesses.

Most goods and services "exported" to businesses/consumers located outside the EU will be VAT free but these may be taxed under the local sales/consumption tax.

Likely effect of Brexit on VAT

Various forms of VAT have been introduced in a wide range of jurisdictions across the world and these generate considerable revenues for governments, as does VAT for the UK exchequer. We would therefore not expect to see material changes to the domestic VAT rules immediately after Brexit, but the international picture could change dramatically in terms of both VAT treatments of international trade and the associated compliance rules. If the UK leaves the single market, this would bring the end of the EC Sales list and the Intrastat Return for UK companies, as statistics of imports and exports would be captured through customs documentation.

UK businesses may no longer be able to use the current EU acquisition and dispatch system for sales of goods to and from the UK, whereby input and output VAT is simply accounted for on their domestic VAT returns. Instead, they would become imports and exports that would need to clear customs (as discussed in our section on changes to Customs Duties) and for imports to incur import VAT charges. This will mean a cash flow disadvantage for UK importers caused by the delay between paying customs VAT charges and the entitlement to recover the input VAT on a subsequent VAT return. Companies currently mitigate this disadvantage for goods imported from outside the EU by using deferment and customs warehousing arrangements. The UK Government would need to consider if the retention of such arrangements for all imports following Brexit is appropriate for the UK economy and for supporting UK business.

UK exporters will be required to keep evidence of export in order to zero rate supplies to the EU, as they do for non-EU exports at present.

UK businesses that are required to register for VAT in some EU Member States – for example, because they hold stock there or make supplies to consumers in excess of the registration limits – may have to appoint a fiscal representative locally to deal with their returns.

We would expect that businesses supplying electronic services to individuals in EU Member States will need to register for VAT in an EU Member State under the Non-Union Mini One Stop Shop (MOSS) scheme (in addition to their UK VAT registration).

Businesses supplying travel services in the EU will no longer have automatic access to the Tour Operators Margin Scheme (TOMS) post Brexit and therefore will either need a VAT registration somewhere in the EU in order to access TOMS or to register and account for VAT in each country where travel services are supplied.

It is expected that it should still be possible to make claims for refunds of VAT incurred in EU Member States following Brexit. As non-EU members, these claims may need to be submitted under the 13th Directive, which is a paper based claim, accompanied by all of the original invoices, rather than via the electronic EU VAT refund scheme, so the resolution of these claims may take longer.

What should UK businesses be doing to prepare for these changes?

Businesses should ask themselves:

- How much more working capital will be needed to finance the VAT cash flow costs of imports and exports?
- How will multiple VAT registrations and their administration (as well as associated additional costs) be managed across the EU?
- If goods are currently distributed across the EU from a UK base, can you identify a suitable new location for post-Brexit EU sales?
- If you are involved in a VAT dispute based on EU legislation, can this be progressed ahead of an eventual Brexit?

Conclusion

Brexit will be a long and complex process, with its final form currently unclear. At this point in time, companies can do little more than start to consider the possible implications for the their business model. This will include discussing and taking a view on whether to progress certain matters before Brexit negotiations are concluded, such as attempting to resolve a VAT dispute based on EU legislation.

ANDY BUTTERWORTH
TOM KIVLEHAN
United Kingdom – London
andy.butterworth@bdo.co.uk
tom.kivlehan@bdo.co.uk

UNITED STATES OF AMERICA

SALES & USE TAX: DIRECT INVESTMENT IN THE UNITED STATES

A foreign vendor contemplating expanding its presence in the United States through direct investment may consider acquiring the stock or assets of another business, undergoing a merger with another business, forming a new entity, or some combination of these methods. These transactions can unintentionally create a tax obligation because sales and use tax typically applies to a transfer of ownership of tangible personal property, unless an exclusion or exemption applies, and it is rare that such transactions do not include a transfer of tangible personal property. And, a buyer that acquires the assets of a business may inherit the seller's unreported sales/use tax liability for all the states where the seller was engaged in business (sometimes referred to as successor liability).[1] So, a foreign vendor considering direct investment in the United States should understand the following:

- The transactions that may be subject to sales/use tax;
- The applicable exclusions or exemptions that may eliminate or minimise the amount of Tax due on the transaction; and
- How to avoid successor liability if it applies.

Particular attention should be paid to the legal form of the transaction because sales/use tax in the United States typically follows the legal form. But, a state may adopt some federal income tax concepts, which do not always follow the legal form, and so knowledge of federal income tax law may prove useful. In addition, direct investment-type transactions may implicate other types of taxes not discussed here (for example, income, gross receipts, realty transfer, and payroll taxes). An analysis that does not at least consider these other types of taxes may result in unwanted surprises.

Direct investment transaction types

Typically, direct investment transactions involve one or more of the following:

- Statutory merger;
- Asset acquisition;
- Stock acquisition;
- Capital contribution to a new or pre-existing business; or
- Liquidation.

If more than one step or transaction type is used to achieve the desired investment outcome, a separate sales/use tax analysis typically must be conducted for each one.

From the principle that sales/use tax typically applies to a transfer of ownership of tangible personal property, unless an exclusion or exemption applies, one may assume the following:

- A stock acquisition should not be subject to sales/use tax if no tangible personal property is used as consideration in the transaction. because stock is generally thought of as an intangible asset in the United States and no transfer or ownership of tangible personal property otherwise occurs; and
- To the extent tangible personal property is transferred pursuant to one of these other direct investment transaction types, the transaction is taxable, as a general rule, unless there is a specific exclusion or exemption under state law.

Therefore, it is possible that a stock transaction may be subject to sales/use tax. But, the transaction types of primary concern for sales/use tax purposes tend to be statutory mergers, asset acquisitions, capital contributions, and liquidations.

[1] In the United States, a buyer that acquires the stock (or other evidence of ownership) typically inherits all of the seller's liabilities because that stock represents an ownership interest in the assets as well as the liabilities of the entity. Most states provide a statutory exemption for a merger or exclude a merger from the definition of sale as a transfer that occurs by operation of law. However, a state may limit the exemption to a merger using only stock as consideration.

Sales and use tax exclusions and exemptions

Common exemptions relied on in connection with a direct investment-type transaction include the following:

- The isolated sale exemption (sometimes referred to as an occasional or casual sale exemption);
- The sale for resale exemption; and
- The manufacturing exemption and the research and development exemption, either individually or in combination.

A state may specifically provide an exclusion or an exemption for one or more of these direct investment-type transactions when certain requirements are met. The exclusion or exemption may even be found under the isolated sale exemption provisions.

For example, California specifically excludes from tax a transfer pursuant to a statutory merger[2], a contribution for an initial issue of an ownership interest, and a liquidating distribution where the liquidating entity does not receive any consideration other than cancellation of the ownership interests.[3] Georgia exempts a transfer of "tangible personal property made as a result of a business reorganisation when the owners, partners, or stockholders of the business being reorganised maintain the same proportionate interest or share in the newly formed business reorganisation."[4]

These exclusion and exemption provisions illustrate some of the limitations a state may apply to their use and the need to carefully read the related law to determine their applicability. For example, in California, the contribution exclusion does not apply where the contribution is made in exchange for anything other than an initial issue of an ownership interest (in other words, there is a timing limitation). In addition, the California liquidation exclusion does not apply where the distributing business entity receives consideration other than cancellation of the ownership interests (in other words, there is a consideration limitation).[5]

The Georgia exemption may not apply where the stockholders do not maintain the same proportionate interest following a business reorganisation (in other words, there is a proportional limitation).

Where a state does not specifically exclude or exempt the direct investment-type transaction at issue or where a limitation precludes application, a general isolated sale exemption may apply. For example, Kansas, similar to many other states, provides an exemption for "the nonrecurring sale of tangible personal property … by a person not engaged at the time of such sale in the business of selling such property," except certain motor vehicles.[6] So, even though the transaction itself may not be exempt or excluded from tax under this provision, a transfer of property the seller is not regularly engaged in the business of selling may be exempt or excluded (for example, a grocery store's sale of office equipment used in the administration of the business). Some states, like California, may limit the exemption to sales of tangible personal property held or used in a business that does not require a seller's permit.[7]

Where a transfer of tangible personal property may not be exempt under an isolated sale exemption or otherwise excluded or exempted, a sale for resale exemption may exempt tangible personal property the buyer is purchasing for resale, such as inventory. In addition, a manufacturing or research and development exemption may apply to a transfer of equipment the buyer anticipates using in its manufacturing or research and development operations. In a state like Kansas, which provides an isolated sale exemption, the combined application of that exemption and the sale for resale exemption could result in no sales/use tax due on the transaction, provided no motor vehicles are transferred.

Successor liability and bulk sale notification

A buyer may opt to engage in an asset acquisition to avoid the successor liability that, as a general rule, applies to a merger, stock acquisition, or capital contribution. However, where the buyer acquires the assets of a business in bulk, most states statutorily impose successor liability with respect to the seller's historic sales/use tax, as well as other state tax liabilities in some states. For example, Pennsylvania imposes successor liability on a buyer that acquires 51% or more of the assets of a business where the seller does not provide the state with 10 days' notice of the bulk sale, and the buyer fails to require the seller to provide a certificate showing all taxes have been reported and paid.[8] Some states, like Nevada, even require the buyer to withhold from the purchase price an amount representing any taxes due until the buyer receives the certificate from the seller.[9]

So, successor liability may apply to an asset acquisition. However, a buyer may avoid successor liability with respect to sales/use tax if the buyer makes sure that the seller provides bulk sale notification to the state and follows the applicable certificate and withholding requirements.

Conclusion

As discussed, a foreign vendor contemplating expanding its presence in the US through direct investment has several sales/use tax issues to consider, including the manner in which to implement the investment (for example, stock acquisition, capital contribution, and so on). Where the transaction involves the transfer of ownership of tangible personal property, the buyer should determine whether the transaction might be excluded from sales/use tax or if an isolated, sale for resale, manufacturing, or research and development exemption may apply. Also, bulk sale notification requirements and other procedures that may result in the avoidance of successor liability for state taxes should also be considered. Of course, implementation of the investment is just the beginning. Once US operations are underway, the buyer will need to concern itself with the sales/use tax treatment of its day-to-day transactions in states where it has a taxable connection.

STEVE OLDROYD
TODD FACIANA
United States – San Francisco
soldroyd@bdo.com
tfaciana@bdo.com

[2] Most states provide a statutory exemption for a merger or exclude a merger from the definition of sale as a transfer that occurs by operation of law. However, a state may limit the exemption to a merger using only stock as consideration.

[3] Cal. Code Regs. tit. 18, §1595(b).

[4] Ga. Code §48-8-3(21).

[5] A buyer should be careful to not too narrowly define consideration. For example, a state may consider the assumption of liabilities by a buyer as the economic equivalent of a receipt of cash and, therefore, treat the assumption of liabilities as consideration.

[6] Kan. Stat. §§79-3602(q) and 79-3606(l).

[7] Cal. Code Regs. tit. 18, §1595(b)(1).

[8] 72 Pa. Stat. §1403(a).

[9] Neb. Rev. Stat. §360.525(1).

CURRENCY COMPARISON TABLE

The table below shows comparative exchange rates against the euro and the US dollar for the currencies mentioned in this issue, as at 7 October 2016.

Currency unit	Value in euros (EUR)	Value in US dollars (USD)
Egyptian Pound (EGP)	0.10057	0.11250
Euro (EUR)	1.00000	1.11848
Hungarian Forint (HUF)	0.00328	0.00367
South African Rand (ZAR)	0.06477	0.07245

CONTACT PERSONS

The BDO VAT Centre of Excellence consists of the following persons:

Ivor Feerick (Chair)	Ireland	Dublin	ifeerick@bdo.ie
Andrea Haslinger	Austria	Vienna	andrea.haslinger@bdo.at
Erwin Boumans	Belgium	Brussels	erwin.boumans@bdo.be
Annette Pogodda-Grünwald	Germany	Berlin	VAT@bdo.de
Deirdre Padian	Ireland	Dublin	dpadian@bdo.ie
Erwan Loquet	Luxembourg	Luxembourg	erwan.loquet@bdo.lu
Rob Geurtse	Netherlands	Rotterdam	rob.geurtse@bdo.nl
Claudio Giger	Switzerland	Zurich	claudio.giger@bdo.ch
Sarah Halsted	United Kingdom	London	sarah.halsted@bdo.co.uk
Tom Kivlehan	United Kingdom	London	tom.kivlehan@bdo.co.uk
Steve Oldroyd	United States	San Francisco	soldroyd@bdo.com

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