CHANGES TO THE VAT PLACE OF SUPPLY RULES

From 1 January 2015

SPEED READ: **From 1 January 2015, the VAT rules regarding place of supply will once again change. EU-based businesses involved in providing electronically supplied services (including telecommunications, broadcasting and other electronic services) to non-business consumers will need to be aware, and change their relevant procedures. Some businesses, typically those based principally outside the EU, but with an EU fixed establishment, may even contemplate moving their business location if their choice of EU establishment has until now been based on using a low VAT rate on supplies of services. Businesses affected by the changes will be required to charge and account for VAT on those supplies in the EU Member State where their customer is established.**

The changes are being introduced in conjunction with the extension of the "Mini-One Stop Shop" system ("OSS") to EU-established businesses, designed to reduce administrative burdens by allowing suppliers to declare and account for VAT in one Member State.

THE PLACE OF SUPPLY RULES AND THE 1 JANUARY 2015 CHANGES

The place of supply rules govern where a particular supply takes place, and therefore determine which Member State and which party is obliged to collect the tax due on the supply.

The 1 January 2015 changes will affect those businesses involved in the supply of telecommunication services, television and radio broadcasting services and businesses involved with other electronically supplied services where the customer is a private individual or organisation that is not in business, such as certain charities and public bodies, which are not registered for VAT and make no business supplies (a "B2C" supply).

Currently, where the supplier has an establishment in the EU, the place of supply of the affected services is the country where the supplier is established. This enables the supplier to charge VAT at a uniform rate, relevant to its location, to all non-business clients, wherever they are based. As a result there has been a distortion between EU-based businesses and non-EU based businesses. For non-EU based businesses, the place of supply has been where the non-business customer is based since 2010. Accordingly non-EU based businesses have had to account for VAT at the rate relevant to their customers' location and have therefore had to account for VAT at variable rates, and in numerous jurisdictions. As a result, a number of non-EU businesses have set up establishments in low-VAT jurisdictions, typically Luxembourg, and been able to charge VAT at a low uniform rate to customers throughout the EU, taking advantage of the rules for EU-established businesses.

Accordingly, under the new rules, the place of supply will be the customer's jurisdiction, wherever the supplier is based, be it an EU-based or non-EU based business. For business-to-business transactions, the customer will still be able to account for any tax due through the reverse charge, i.e. the business customer will account for the VAT in its jurisdiction (also known as the "tax shift"). However, in a B2C supply the reverse charge is not possible. As a result, liability to account for any VAT due in a Member State will rest entirely with the supplier.

The extended OSS will reduce the obvious administrative burden that this change could have led to, because the supplier will only be liable to register and account for VAT in one Member State. However, there are a number of issues that will need to be considered and planned for in advance.

POINTS FOR CONSIDERATION

Although the change is more than sixteen months away affected businesses should be making the changes they will need to make in preparation. Issues that will be important to consider include:

- **Pricing structures**

  Different Member States have different rates of VAT, and the supplier will be supplying services in different countries which attract different rates. Will your business want to charge the same flat (VAT-inclusive) rate for its services across the EU, which will affect the margin made on the services, or will it have a differential pricing structure per jurisdiction, depending on the VAT rate. Accounting systems will need to be developed to cope with multiple VAT rates.

- **Exactly where a customer is located**

  There are particular rules to be applied for determining where a customer is located and accordingly where the VAT must be accounted for. The draft EU Regulation (to be inserted as Articles 24a - 24g Regulation 282/2011) provides for particular scenarios which a supplier must adhere to in determining where a customer is located. Obviously consumers move around, and may be receiving the services far from home, for example on a mobile device, and there need to be rules to enable suppliers to know where to account for the VAT:

- When services are provided at a location such as a telephone box, internet café, wi-fi hotspot or similar, where the recipient must be physically present in order for the service to be rendered to him, the irrebuttable presumption is that the customer enjoys and effectively uses the services at that location (and so that is where the place of supply takes place). If the location is on board a ship, aircraft or train travelling within the EU, the country of departure is deemed the country where the supply takes place.

- In certain circumstances, a supplier is entitled to assume that a customer enjoys services in a particular location unless the supplier has evidence to the contrary (a "rebuttable presumption"). Those circumstances are:

  - Where services are supplied via a residential fixed land line, wherever the fixed land line is installed;

  - Where services are supplied through a mobile network against subsequent collection of payment, wherever is the mobile country code of the SIM card;

  - Where services are supplied needing a fixed viewing card, the place to which the viewing card is sent with a view to it being used there;

- Where none of the above scenarios apply, a supplier needs to obtain two separate pieces of evidence to identify where the customer is established, i.e. has his permanent address or usually resides (and therefore where is the place of supply). The non-exclusive list comprises:

  - Customer details such as billing address;

  - IP address of the device used by the customer or any method of geolocation;

  - Bank details such as the location of the bank account used or the customer's billing address;

  - The mobile country code of the customer's SIM card;

  - The location of the residential fixed land line through which the service is supplied; and

  - Other commercially relevant information that is obtained by the supplier.

Currently, HMRC accepts that a business making B2C supplies can rely on the customer's self-declaration combined with a reasonable level of verification. That verification can include the postal address for goods delivered, or verification of payment method. This will be clarified and updated in draft legislation due to be published in autumn 2013. Building verification processes into a supplier's IT systems will need to be considered.

- **Is the customer actually in business**

There will be some customers who will claim they are in business, or who offer false VAT registration numbers, to avoid VAT being charged by the supplier (a real business customer avoids VAT being charged to him by the supplier but is generally liable to account for VAT under the reverse charge). The supplier's obligation to verify this information requires him to validate the VAT number the business customer gives, and check that against the name and address supplied. This can be cross-referenced with data held by the country where the business customer is purportedly based (article 18(1)(a) Regulation 282/2011). If the customer informs the supplier he has applied for but not yet received a VAT number, the supplier should verify the information using normal identification checks (article 18(1)(b) Regulation 282/2011).

If a customer claims not to be in business or is otherwise a non-taxable person, a supplier can take that information as correct unless a VAT number has been sent to him (draft insert to article 18(2)). This is because the supplier will need to account for VAT under the OSS in any event. The obligations to check if a customer claims to be a non-EU business (so the supply is not in the EU) remain the same, namely that a certificate is required from that non-EU country's competent tax authority. Current HMRC guidance advises that alternative suitable evidence includes business letterheads or other commercial documents indicating the nature of the customer's activities.

- **Considering relocation**

If a non-EU business has relocated to Luxembourg or another low VAT jurisdiction to take advantage of the current place of supply rules for EU-based businesses, that business may now wish to contemplate relocating again, either out of the EU or to another jurisdiction that offers efficient direct tax regimes such as the UK or Ireland. Businesses will be aware of the increasing importance of ensuring realistic transfer pricing arrangements are in place, to ensure that the appropriate amount of corporate income taxes are paid in the jurisdictions where the business has operations. The key point is that a low VAT rate will no longer be a factor which influences non-EU businesses involved in these types of businesses to relocate to a particular jurisdiction.

- **Consider legal and contractual issues with agents and distributors located in Member States**

- **Consider storage and retention of data issues**

- **Consider effects on existing EU VAT registrations**

Existing EU VAT registrations in a place where the business has a fixed establishment may need to be cancelled, as supplies may no longer be taking place there.

- **IT systems capabilities**

There will be a significant and obvious knock-on effect on registration and compliance costs as IT systems will invariably need to be updated.

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