

March 3, 2014

Practice Group(s):
Tax

Update: EU VAT on E-Commerce

By *Valentina Farle, LL.M. and Rainer Schmitt*

Changes to EU VAT on E-Services as of 1 January 2015

What are E-Services?

There are a great variety of electronically provided services (“e-services”) and the respective market is rapidly growing. The general definition is that e-services are services which are delivered over the Internet or an electronic network and which, due to the specific nature and features of the supply, are highly dependent on information technology (“IT”); the supply of e-services is essentially automated, involves only minimal human involvement and is impossible to be rendered without IT.

Examples for e-services include inter alia website hosting; automated, online and distance maintenance of programs; online data warehousing; access to data bases; access or download of software, updates, images, digitized content of books and electronic publications; music; online market services functioning in accordance with automated procedures; workbooks completed online and marked automatically and other comparable network-based automated distance teaching; access to automated online games with network connected players; etc.

2008 Changes Effective 2015

As of 1 January 2015, European Union (“EU”) value added tax (“VAT”) rules regarding e-services will change for supplies made by EU suppliers to EU consumers (“B2C”). The respective changes to the EU VAT law were already enacted in 2008, but will only take effect as from 1 January 2015 onwards.

Current Regime for EU Suppliers

Under currently applicable EU VAT law, the place of such B2C supplies of e-services by EU suppliers is at the VAT-relevant location of the respective EU supplier. In effect, each EU supplier has to file only one VAT return with one single applicable VAT rate in the supplier’s EU member state for all his B2C e-services rendered into the EU. Taking advantage of the considerable differences in VAT rates throughout the EU, B2C e-service providers are now headquartered in EU member states with (relatively) low VAT rates, typically in Luxembourg.

Current Regime for non-EU Suppliers

In contrast, non-EU suppliers rendering B2C e-services to EU customers so far have to subject their respective supplies to VAT applicable in the respective customer’s EU member state. As a consequence, these non-EU suppliers of e-services B2C are currently confronted with up to 28 member states with differing VAT rates and differing VAT laws. The so-called VAT “mini one-stop shop” (“MOSS”) procedure provides for a limited relief from the respective administrative burden. The MOSS procedure was

Update: EU VAT on E-Commerce

established for non-EU suppliers of B2C e-services to EU customers, allowing them to file a single VAT declaration and make respective VAT payments in only one EU member state—which EU member state then forwards the respective declarations and VAT payments to the other relevant EU member states concerned. The MOSS procedure therefore provides a single portal for the filing of the VAT declarations and the making of VAT payments, but it does not relieve the burden for the supplier of the accounting for VAT, who has to take into account up to 28 EU member states' VAT rates and VAT laws. Due to these disadvantages, many non-EU suppliers of e-services established themselves within a suitable EU member state in order to benefit from the regime governing EU suppliers.

New Single Regime from 2015 onwards

As of 1 January 2015, the rules currently governing B2C e-services by non-EU suppliers to EU customers will practically extend to EU suppliers. The changes coming into effect on 1 January 2015 will result in the place of supply of all e-services always being the VAT-relevant location of the respective customer—irrespective of the VAT classification and location of the supplier and the customer; this already applies to e-services rendered to “VATable” customers, namely businesses, (“B2B”). If the customer is VATable (B2B) and located in the EU, the reverse charge procedure will apply and the customer will have to account for the VAT, not the supplier. If the customer is not VATable (B2C), the supplier has to account for the VAT in the customer's VAT-relevant EU member state, but may potentially benefit from the MOSS procedure.

Further EU Change Preparation Measures

The EU is currently preparing the new regime applicable as of 1 January 2015 with several implementing and accompanying measures. The EU Council enacted Council Implementing Regulation (EU) No 1042/2013 on 7 October 2013, which is directly applicable in the EU member states and is intended to deal with some of the most-pressing practical issues regarding the EU VAT treatment of e-services. The European Commission also published (nonbinding) comments on the MOSS procedure (Guide to the VAT Mini One Stop Shop, dated 23 October 2013), explaining some of the procedural aspects of the changes as of 1 January 2015. For March/April 2014, further explanatory notes on the determination of the place of supply for e-services are expected to be issued by the European Commission. Suppliers should carefully monitor and prepare for the new regime in view of such preparation measures of the EU, as well as taking into account further measures expected to be taken by EU member states.

Challenges for E-Services Suppliers

One of the main challenges for e-services suppliers from 2015 onwards is that in order to properly account for their EU VAT charges and comply with the EU VAT obligations relating to their e-services, they actually have to determine the relevant VAT features of each of their customers. This means that they have to determine (1) whether the recipient is a VATable customer (B2B) or not (B2C), and (2) where the customer as supply recipient is located for EU VAT purposes in order to determine the place of the supply, and therefore, the place where the supply is VATable. It will be necessary for the supplier to document the respective findings as to the recipient's VAT status and VAT-relevant location in order to reproduce them in subsequent VAT audits.

Update: EU VAT on E-Commerce

Furthermore, they have to determine the VAT rules and obligations potentially applicable to their e-services in the respective EU member state of that supply, being the customer's VAT-relevant location, including, for example, provisions on proper invoicing. The MOSS procedure may cover the filing of VAT declarations and the making of VAT payments in the single EU member state of the supplier's MOSS identification, if the supplier elects the application of the MOSS procedure and is eligible to do so. In the case of different potential MOSS identification EU member states, the supplier should evaluate these options in view of procedural details, language and other relevant features. With respect to aspects not covered by the MOSS procedure, there is no single gateway for all EU member states involved.

In order to gain and retain respective information and documentation on the VAT features of the supply and to collect and organize the information necessary for compliance with VAT obligations as well as implementing the VAT requirements regarding the supply itself, the ordering and billing procedures have to be amended and the respective IT environment needs to be adjusted.

In preparing for the 2015 changes, suppliers have to address inter alia consumer and data protection requirements and restrictions. Suppliers should check and potentially reshape and restructure supply chains and respective contractual arrangements as well as billing, payment and other aspects of the provision of such supplies.

Further consequences of the changes effective 1 January 2015 may, amongst others, also include the rethinking of the broader business set-up, which was established in view of certain applicable VAT rules. Business operations established in low-VAT-rate countries may be considered to be relocated to lower-cost countries. It could be advantageous for suppliers to seek the services of third-parties acting as intermediaries for e-services in order to avoid the additional burden arising from B2C supplies as of 1 January 2015. Moreover, in view of the upcoming changes, it should be checked whether these may affect e-services agreed on, paid for or rendered before the end of 2014, if these also relate to the period beginning 2015 onwards.

Details of Determination of Recipient's VAT Status

For the classification and documentation of the supply recipient's VAT status, it will be essential to request the customer to declare whether the order of e-services is made acting as a VATable person (B2B) or not (B2C).

As long as the customer of the supply has not provided to the e-services supplier such customer's individual VAT identification number with respect to the order, the supplier should assume that the supply is B2C, resulting in the supplier being liable for any respective EU VAT. It appears that if the customer subsequently provides the VAT identification number to the supplier or withdraws a communicated VAT identification number, the supplier has to change the respective VAT declarations resulting in a correction of the VAT charges, but details of such adjustment remain unclear at this stage. Furthermore, suppliers should check any communicated VAT identification number as valid and applicable as well as document their measures taken in order to identify and verify the VAT status of the customer with respect to the supply.

Update: EU VAT on E-Commerce

Details of Determination of Recipient's VAT Location

Regarding the customer's VAT-relevant location that is decisive for the place of the supply, further determinations are necessary and respective information must be gathered and stored:

Council Implementing Regulation (EU) No 1042/2013 of 7 October 2013 contains inter alia several presumptions for the VAT-relevant place of supply which shall assist the supplier of e-services in making the respective determinations for the VAT treatment of the supply. In the case of B2C supplies, the general rule is that the supply is VATable where the customer is established, has his permanent address or usually resides.

According to Council Implementing Regulation (EU) No 1042/2013 of 7 October 2013, in the case of e-services supplied at a certain location, such as a wi-fi hot spot, telephone box or kiosk, an Internet café, a restaurant or hotel lobby where the physical presence of the recipient of the supply at that location is needed for the service to be provided, it shall be presumed that the customer is established, has his permanent address or usually resides at the place of that location and that the service is effectively used and enjoyed there. Furthermore, regarding B2C supplies,

if received through a fixed line, these shall be presumed to be rendered at the place of installation of such fixed line, if received through a mobile network, the VAT place of supply shall be presumed to be the country identified by the mobile country code of the respective SIM card, and if received through a decoder or similar device at the location thereof. The presumptions are under certain conditions rebuttable, both by the supplier as well as by the tax authorities. For rebutting the presumptions and determining the place of supply if no presumption is applicable, rules are provided regarding the collection of a certain number of so-called non-contradictory items of evidence, such as the billing address of the consumer, the IP address of the device used, the bank details of the bank account used for payment, the consumer's mobile country code of the respective SIM card used, the location of the consumer's fixed land line or other commercially relevant information.

Details of Determination of Supplier

Council Implementing Regulation (EU) No 1042/2013 of 7 October 2013 also contains provisions as to the determination of the relevant supplier of e-services in certain circumstances, namely where e-services are supplied through a telecommunications network, interface or portal such as a marketplace for applications, which should be carefully analyzed by respective suppliers in each individual case. In certain cases, it will be decisive whether there is a clear indication of the relevant supplier, which is furthermore appropriately reflected in the respective contractual arrangements between all parties involved and in all respective invoices. Existing arrangements including respective order, billing and payment features should be reviewed in order to assess whether these and the respective VAT treatment applied so far are in line with the new provisions and determine whether changes are required.

Update: EU VAT on E-Commerce

Details of Applicability of New Rules

In some cases, it may be difficult to determine whether the old or the new rules are applicable to a certain e-service. This may particularly be the case if the e-service is rendered for a period of time starting before 1 January 2015 and ending thereafter, if the customer makes prepayments, if billing in stages or in periods is agreed on, if the e-services are contracted before 2015, but rendered only in 2015 or thereafter. The respective rules of the Council Implementing Regulation (EU) No 1042/2013 of 7 October 2013 need to be carefully analyzed in order to determine the applicability of the old or the new rules to a particular e-service. Further clarification may be provided by the announced further explanatory notes by the European Commission expected for March/April 2014, even though these are not binding on the EU member states.

Reduced VAT Rates for E-Books in the EU?

The provision of e-books is classified for VAT purposes within the EU as an e-service. Under EU VAT law, e-services shall be subject to the unreduced, standard VAT rates of the EU member states. Under their national VAT laws, some EU member states apply reduced VAT rates to e-books. Under currently applicable EU VAT law, the place of supply for e-books by an EU supplier to a consumer (B2C) is the EU member state where the supplier is based for VAT purposes. In combination, the reduced VAT rates on e-books in some EU member states and the rule for the place of supply of e-books by EU suppliers have both led to a concentration of e-book suppliers within the EU in such EU member states. The European Commission initiated respective infringement procedures against France and Luxembourg for their reduced VAT rates on e-books.

While the European Commission is currently taking France and Luxembourg to the European Court of Justice over their reduced VAT rates for e-books, the German coalition government has put the introduction of reduced VAT rates for e-books in the EU on the agenda: in a press release dated 27 January 2014, Ms. Monika Grütters, German state minister for Culture and Media, argues that the reduced VAT rates applicable to printed books should also become applicable to e-books and informs that the German coalition government has agreed to advocate the mandatory introduction of reduced VAT rates for e-books on the EU level. With this position, the German government is by no means isolated; thus, it can be expected that this issue will be taken up in the further course of this year.

Further Development of the Taxation Rules for the Digital Economy

The European Commission intends to further amend the rules governing the taxation of the digital economy. For this purpose, in 2013, it established an expert group on taxation of the digital economy which had its second meeting in January 2014. Respective information can be found under

http://ec.europa.eu/taxation_customs/taxation/gen_info/good_governance_matters/digital_economy/index_en.htm, which also includes information on respective VAT issues on the agenda. In accordance with a respective working paper on VAT issues, an extension of the new rules for e-services to the supply of goods ordered online is considered. Suppliers should carefully monitor respective upcoming changes and further developments.

Update: EU VAT on E-Commerce

Authors:

Valentina Farle, LL.M. (Sheffield)

valentina.farle@klgates.com

T +49.69.945.196.295

Rainer Schmitt

rainer.schmitt@klgates.com

T +49.69.945.196.290

For information about data protection, please turn to

Dr. Tobias Bosch, J.S.M. (Stanford)

tobias.bosch@klgates.com

T +49.30.220.029.410

K&L GATES

Anchorage Austin Beijing Berlin Boston Brisbane Brussels Charleston Charlotte Chicago Dallas Doha Dubai Fort Worth Frankfurt
Harrisburg Hong Kong Houston London Los Angeles Melbourne Miami Milan Moscow Newark New York Orange County Palo Alto
Paris Perth Pittsburgh Portland Raleigh Research Triangle Park San Diego San Francisco São Paulo Seattle Seoul Shanghai
Singapore Spokane Sydney Taipei Tokyo Warsaw Washington, D.C. Wilmington

K&L Gates practices out of 48 fully integrated offices located in the United States, Asia, Australia, Europe, the Middle East and South America and represents leading global corporations, growth and middle-market companies, capital markets participants and entrepreneurs in every major industry group as well as public sector entities, educational institutions, philanthropic organizations and individuals. For more information about K&L Gates or its locations, practices and registrations, visit www.klgates.com.

This publication is for informational purposes and does not contain or convey legal advice. The information herein should not be used or relied upon in regard to any particular facts or circumstances without first consulting a lawyer.

© 2014 K&L Gates LLP. All Rights Reserved.