

Preface

This book serves as an introduction to the current EU VAT system. It provides an overview of the functioning of the EU VAT system, as well as the concepts and rationale behind it. All explanations and examples are based on the legislative basis of the EU VAT system, i.e. the EU VAT Directive (2006/112/EC) and the EU VAT Implementing Regulation (282/2011).

The goal of this book is to enable the reader obtaining a basic understanding of the EU VAT system, or to refresh one's VAT knowledge *within a day's work*. Hence, this book is titled: 'VAT in a Day'. The concept of this book motivated the authors to make didactically sound choices as regards the depth at which the various subjects in this book are discussed. That implies that this book provides an account of the key provisions in the VAT Directive and the key case law of the Court of Justice of the European Union in the field of VAT. This book preludes 'Fundamentals of EU VAT Law'¹, which provides the reader with a thorough understanding of EU VAT law.

A special word of thanks goes to Kali Hague and Joyce Beckers for their valuable assistance in creating the first edition (2013) of this book.

The authors hope that this book generates enthusiasm with the reader for EU VAT law, so that the reader is stimulated to continue spending many more days studying the interesting, yet challenging topic of Value Added Taxes.

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1 Ad van Doesum, Herman van Kesteren and Gert-Jan van Norden, 2016, Fundamentals of EU VAT Law, Alphen aan den Rijn: Kluwer Law International.

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1. Introduction

VAT is an important revenue-generating tax in all EU Member States. In the European Union as a whole, VAT is responsible for generating approximately € 1,000 billion per year in tax revenues. These revenues play a huge role in the budgetary policymaking of the European Union and of the individual Member States in particular. The European Commission expects that in many Member States the importance of VAT will only continue to grow in the years to come, as opposed to the personal income and corporation taxes.

VAT is a so-called 'general consumption tax'¹, as it aims to tax all private consumption by individuals. Article 1(2) of the EU VAT Directive² reads:

"The principle of the common system of VAT entails the application of goods and services of a general tax on consumption exactly proportional to the price of the goods and services, however many transactions take place in the production and distribution process before the stage at which the tax is charged."

Over the years, VAT has proven to be a stable tax which, from the government's perspective, is levied in a relatively straight-forward way. Additionally, VAT is not subject to some of the disadvantages inherent to personal income and corporate taxation. For example, assessing and collecting tax on income and corporate revenues is an administratively burdensome and costly process. Moreover, levying taxes on income and labor has a negative impact on economic market conditions. Direct taxes on labor and corporate revenues share a nearly direct relationship with the market economy. When economic circumstances deteriorate, direct tax revenues also decline. Additionally, taxes on labor are sensitive to the ageing workforce; as the average age of the workforce increases, the number of wage earners decreases – resulting in a decline of tax revenues. Moreover, taxes on labor, income and profits have an distortive effect when goods or services are ultimately exported. The fact that VAT does not have these disadvantages – or at least to a lesser extent – may explain the ongoing worldwide shift from direct taxation (income tax and corporation tax) to indirect taxation (VAT).

1 By contrast, excise duties are taxes on the consumption or the use of certain products. They are mainly specific taxes.

2 Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax, OJ L 347, 11 December 2006.

Taxing private consumption is a complicated affair. It is virtually impossible to designate every private person a taxable person and then levy VAT from this person for the consumption he or she enjoys. Imagine that at the end of each month you have to declare to the tax authorities how much you consumed in that particular month; this would impose a heavy (administrative) burden on consumers, as well as on the tax authorities. Additionally, determining a private person's consumption (or the volume of his consumption) would be a very difficult and arbitrary process. This is because the term 'consumption' is ambiguous. For example, does consumption take place when a consumer buys a carton of milk but then spills the milk because the carton leaks? Attempting to determine factual consumption volumes at the level of the private consumer is not feasible. It is much easier to *approximate* consumption by establishing what the consumer spends in order to obtain the goods or services that he intends to consume. With regard to this, consumption taxes are generally levied in an indirect, instead of a direct manner. This implies that not the final consumer himself, but the person who enables the consumer to purchase a good or service is made responsible for collecting and remitting VAT to the tax authorities. Following the EU VAT Directive Article 2(1) EU VAT Directive), the supply of goods and services for consideration by a taxable person are transactions subject to VAT. This makes VAT a 'transaction tax'. In order to effectuate taxation, VAT does not measure and tax consumption volumes of private individuals directly, but rather links taxation indirectly to transactions carried out by entrepreneurs (taxable persons) which enable private individuals to consume.³ Since the person who is held liable to remit the collected VAT to the treasury is a different person than the person who is intended to bear the burden of VAT, the VAT is often classified as an 'indirect tax.'

With a view to taxing private consumption in an indirect manner, one could argue that it is unnecessary to tax supplies of goods and services between taxable persons and that it is sufficient to only tax supplies of goods and services by taxable persons to private persons: only the latter supplies lead to final consumption. The taxable person (the person who enables a private consumer to consume by supplying a good or service to him) could simply include the tax in the total price that the consumer pays for the supply. Under the assumption that this 'on-charge' of tax is perfect, the burden of the tax is thus borne by the consumer – even though the taxable person is liable to remit the consumption tax to the tax authorities.

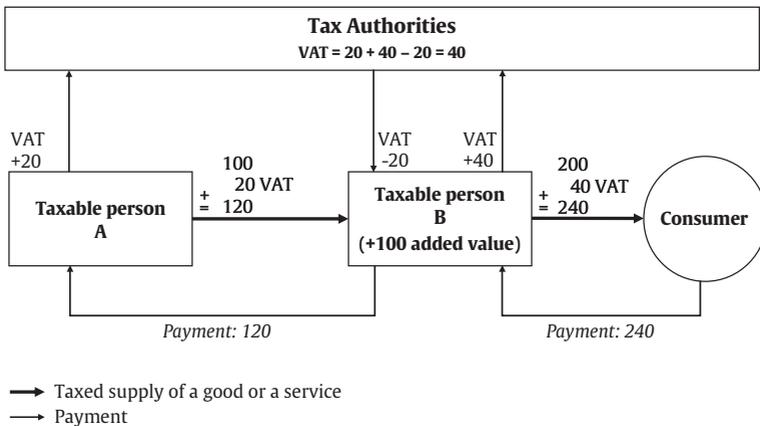
There are indeed consumption tax systems which only levy tax at the last stage in the chain of production and distribution. The sales tax which is levied in the United

³ See: European Commission, Green Paper on the future of VAT, Towards a simpler, more robust and efficient VAT system, 1 December 2010, COM(2010) 695 final. The European Commission states that: "Moreover, the key role of businesses collecting VAT must be properly recognized, since VAT is a consumption tax and not a tax on businesses".

States of America is an example of such a system. As opposed to the U.S. however, the legislative institutions of the EU have decided to introduce a turnover tax (the EU VAT) which subjects *all* transactions (so: in every stage of the production and distribution process) to taxation. The EU VAT thus is a consumption tax in the form of an all-stage turnover tax, and it is levied and collected through a system of 'fractional payments'. In each stage of the supply chain, the tax authorities collect a small amount of the total VAT due on the final product. An advantage of this system of fractional payments is that the risk of incorrect VAT filings (or even tax fraud) is spread over the entire supply chain.

In order to ensure that taxable persons do not carry the burden of VAT and that ultimately only *private* consumption is taxed, taxable persons are allowed to deduct VAT that has been charged to them by other taxable persons, insofar they use the input transactions for their own taxed output transactions. In that way, the right of deduction safeguards the 'neutrality' of VAT.⁴ The result is that every taxable person pays VAT over the value he or she adds to the good or service. Cascading of VAT generally does not occur because VAT is not levied on VAT. The next example illustrates the basic functioning of the VAT system.

Example 1: the basic functioning of the EU VAT system



Taxable person A supplies goods or services with a value of € 100 to taxable person B. A charges 20% VAT on the supply to B. Next, B pays an amount of € 100 + € 20 VAT = € 120 euro to A. Now, A declares € 20 of VAT on his VAT return and pays the € 20 in VAT to the tax

⁴ Cf. OECD International VAT/GST Guidelines (available at: <http://www.oecd.org/tax/consumption/international-vat-gst-guidelines-9789264271401-en.htm>, accessed October 9, 2017).

authorities. B supplies this good or service he purchased to the end consumer for a total amount (excluding VAT) of € 200 euro. B charges 20% VAT over the amount of this supply to the end-consumer. The consumer pays a total of € 200 + € 40 VAT = €240 euro to B. Subsequently, B declares the € 40 euro of VAT on his VAT return. However B can also deduct on his VAT return the VAT charged to him by A, which was € 20. The result is that B effectively pays an amount of € 40 – € 20 = € 20 to the tax authorities. The tax authorities received the total VAT payment of € 40 VAT in two different payments at two different moments in the production and distribution chain. (€ 20 of VAT via A and € 20 of VAT via B). However, the consumer bears the entire burden of the VAT because the consumer pays € 40 of VAT on the purchase and cannot deduct this VAT.

2. European VAT and National VAT Systems

All Member States of the European Union apply the same VAT system. VAT is harmonized amongst other through the EU VAT Directive (2006/112/EC).⁵ This VAT Directive serves as a blueprint for implementing VAT systems throughout the EU.⁶ Each State is required to implement the VAT Directive (transpose the VAT Directive into national law).⁷ However, Member States are free to choose the way that best serves their economies and national legal orders. It is the ultimate result of their implementation that matters.

The result is that ideally, all Member State levy VAT in the same manner, even though the legal systems of the Member States are not identical. This requires that the national provisions implementing the VAT Directive are interpreted in conformity with the wording and aim of the VAT Directive.⁸ When doubts regarding the interpretation of a provision in the VAT Directive arise, the national courts can – or in some cases: must – submit a “preliminary question” to the Court of Justice of the

5 This ‘VAT Directive’ is a recast of the ‘Sixth VAT Directive’ that was amended numerous times over the years. See: Council Directive 77/388/EEC of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment (OJ L 145, 13.6.1977, p. 1). In addition to the VAT Directive, there are other directives in the field of VAT that aim at harmonizing the VAT system (see, for example Directive 2008/9/EC and the ‘Thirteenth VAT Directive’). Council Directive 2008/9/EC of 12 February 2008 laying down detailed rules for the refund of value added tax, provided for in Directive 2006/112/EC (the VAT Directive) to taxable persons not established in the Member State of refund but established in another member State (OJ L 44, 20.2.2008, p. 23) and the Thirteenth Council Directive 86/560/EEC of 17 November 1986 on the harmonization of the laws of the Member States relating to turnover taxes – Arrangements for the refund of value added tax to taxable persons not established in Community territory (OJ L 326, 21.11.1986, p. 40).

6 In addition, binding implementing measures have been implemented to ensure uniform application of the VAT Directive. This has been done through the so-called ‘VAT Implementing Regulation’. See: Council Implementing Regulation (EU) No 282/2011 of 15 March 2011 laying down implementing measures for Directive 2006/112/EC on the common system of value added tax (recast), OJ L 77, 23.3.2011, p.1. The provisions of the VAT Implementing Regulation are directly applicable without transposition into national law.

7 CJEU 19 January 1982, Case 8/81, *Ursula Becker v Finanzamt Münster-Innenstadt*, [1982] ECR 00053.

8 CJEU 13 November 1990, Case C-106/89, *Marleasing SA v La Comercial Internacional de Alimentacion SA*, [1990] ECR I-04135.

European Union (CJEU). The CJEU then provides the national court with an explanation of the provision. In the field of VAT, the total count of CJEU rulings comes close to a 1,000.

When a national provision cannot be interpreted in line with the VAT Directive, the question is whether the corresponding provision of the VAT Directive takes precedence. The VAT Directive is addressed to the Member States and not to private persons. For this reason, private persons in principle are not able to appeal directly to the provisions contained therein. However, the CJEU ruled that in specific circumstances, a provision of national law that is not in line with a more favorable VAT Directive provision does not apply and the corresponding Directive provision applies instead.⁹ This allows a provision of the Directive to have a 'direct effect': whenever the provision of the VAT Directive is, so far as its subject-matter is concerned, unconditional and sufficiently precise, it may be relied on before the national courts by individuals against the State where the State has failed to correctly transpose the VAT Directive into national law.¹⁰ One further aspect of this settled CJEU case law is that the tax authorities are not allowed to rely on the VAT Directive against private individuals in lieu of incorrectly implemented national provisions.¹¹ Accordingly, if a provision of national law is more favorable for a taxable person than the one contained in the VAT Directive, the national provision takes precedence.

9 CJEU 1 February 1977, Case 51-76, *Verbond van Nederlandse Ondernemingen v Inspecteur der Invoerrechten en Accijnzen*, [1977] ECR 00113.

10 Cf. CJEU 26 February 1986, Case 152/84, *M. H. Marshall v Southampton and South-West Hampshire Area Health Authority (Teaching)*, [1986] ECR 00723.

11 Cf. CJEU 8 October 1987, Case 80/86, *Criminal proceedings against Kolpinghuis Nijmegen BV*, [1987] ECR 03969.

3. The Determination Scheme of VAT

The structure of the VAT Directive provides for a method that enables solving complex VAT cases. By applying the so-called 'VAT determination scheme', which can be derived from the structure of the VAT Directive, each VAT case can be solved in a clear and systematic manner. The steps (in order) in the determination scheme are as follows (the relevant provisions in the VAT Directive relating to each step are included in this overview):

1. **Who** (Taxable person)
Article 9-13 VAT Directive
2. **What** (Taxable transactions)
Article 14-30 VAT Directive
3. **Where** (Place of supply)
Article 31-61 VAT Directive
4. **How much** (Taxable amount/VAT rates)
Article 72-92 VAT Directive
Article 93-129 VAT Directive
5. **Exemptions**
Article 131-166 VAT Directive
6. **Liability** (Person liable for payment of VAT)
Article 192a-212 VAT directive
7. **Deductions**
Article 167-192 VAT Directive
8. **When and how** (Chargeable event and the chargeability of VAT)
Article 62-71 VAT Directive
9. **Administrative obligations**
Article 213-280 VAT Directive
10. **Special schemes**
Article 281-369 VAT Directive

In the following chapters, we discuss the above stages of the determination scheme in more detail.

4. Taxable Person

4.1. Introduction

VAT is remitted (paid) to the tax authorities by taxable persons. A taxable person is any person who independently carries out in any place any economic activity, whatever the purpose or results of that activity (Article 9 VAT Directive). In principle, there is no relation with the concept of a 'taxable person' in personal income and corporate tax.

The VAT Directive upholds a world-wide approach to the concept of "taxable person". A taxable person for VAT does not have to be established or residing in Member State or be a national of a Member State. In order for VAT taxation to occur in a Member State, the taxable person's *activities* (taxable transactions) must take place in that Member State. The place of supply rules determine where the taxable transaction takes place and (thus) which country has the right to levy VAT (see Chapter 6).

4.2. The Function of the Taxable Person Status

Under conventional personal income and corporate tax regimes, the taxable person is often the intended subject of taxation (i.e. that person is *intended* to be burdened by the tax). However, in VAT, the taxable person in VAT only plays an intermediary role. The taxable person collects and remits the VAT to the tax authorities, yet the (economic) burden of that VAT is ultimately carried by the private person who purchased the good or service. In other words, the taxable person functions as an unpaid tax collector on behalf of the tax authorities.

The aim of VAT, which is to tax private consumption to the fullest extent possible, can only be achieved by interpreting the concept of 'taxable person' broadly. Such a broad application ensures that as many supplies of goods and services as possible are subject to taxation, and that – ultimately – as much private consumption as possible is taxed. Another reason for interpreting the term 'taxable person' broadly is that only taxable persons are allowed to deduct the input VAT charged to them. The broad interpretation helps to ensure that taxable persons do not bear the burden of VAT and that the production and distribution chain is indeed relieved from this burden.

4.3. The Consequences of the Taxable Person Status

A most noteworthy consequence of being a taxable person is that one must charge VAT on the taxable transactions one carries out (i.e. supply of goods and services). However, on the input side of a business, the taxable person is in principle entitled to deduct all the VAT charged to him on the supplies of goods and services made to him, as well as all VAT on his imports and intra-Community acquisitions (see Chapter 5). In addition, the place where a service is supplied generally depends on the status (taxable person or not) of the person to whom this service is supplied (see Chapter 6). Other consequences are that a taxable person is obliged to maintain an adequate administration that is in accordance with the respective legal conditions, and issue invoices in compliance with the invoice requirements. A taxable person also has to remit VAT to the tax authorities for each VAT return filing period (see Chapters 11 and 12).

4.4. The Elements of the Definition of the Term 'Taxable Person'

Article 9 VAT Directive provides the definition of the concept of taxable person. The elements 'any person,' 'independent' and 'economic activity' from Article 9 VAT Directive are the central elements of this provision. In the following subsections, we will discuss each element separately.

4.4.1. Any Person

The legal form of a company is irrelevant for VAT. The term 'any person' does not only include private persons and legal persons, but also various kinds of entities which are not necessarily legal persons in all Member States, such as foundations, unincorporated associations and partnerships. Such entities can qualify as taxable persons if they independently carry out economic activities. The legal arrangement of the entity based on (national) civil law (e.g. is the entity incorporated? Does it have legal personality?) is thus irrelevant for VAT purposes. What matters is that the entity presents itself as an independent party to the outside world.

If an entity is a taxable person (e.g. a partnership, even though it may not have legal personality under the national law of a Member State), the partners, the directors or employees are not taxable persons for the economic activity that the entity carries out. This does not prevent these individuals from being taxable persons themselves if they carry out economic activities independently from the entity.

Example 2: the concept of 'any person'

John and Maggy carry out a restaurant business through a partnership that does not have legal personality under the law of the Member State in question. Further, on his own account, John is engaged in trading scrap metal.

Here, the partnership is the taxable person for the restaurant activities, not John and Maggy. John is the (only) relevant taxable person for the scrap metal business. Thus, there are two separate taxable persons carrying out two separate economic activities in this example.

The principle that the participants of a (cooperative) entity have to be viewed separately from the entity even implies that a participant (e.g. a partner in a partnership) can make supplies of goods or services to that entity. For example, in *Heerma*, the CJEU rules that a person is a separate taxable person as regards the leasing of a stable to the partnership of which that person and his spouse are the partners.¹²

The VAT Directive acknowledges that a person can act in various capacities. Article 2 VAT Directive only subjects to tax supplies of goods, services and intra-Community acquisitions by a taxable person *acting as such*.

The broad scope of the concept 'any person' suggests that a business group, consisting of multiple incorporated entities which all present themselves under the same business name (e.g. Microsoft), are to be considered as one taxable person. However, the CJEU did not adopt this view.¹³ Legally separate entities of a group of companies are only considered as one taxable person if they form part of the same VAT group (refer to Article 11 VAT Directive, see section 4.8).

4.4.2. **Independent**

A person will only qualify as a taxable person if that person *independently* carries out an economic activity. This condition prevents employees from qualifying as separate taxable persons (and thus be subjected to taxation) when they perform (economic) activities in the scope of their employment. In order to determine whether a person (employee) carries out his activities independently, one must establish to what extent he is subordinated to the employer or principal on the basis of the employment conditions and the responsibilities of the employer or principal.

In this context, the position of the director-shareholder is somewhat ambiguous. A director with a majority shareholding is, on the one hand, a director employed by the company and thus not independent with a view on the employment conditions and responsibilities of the company. However, on the other hand, he is a director and

12 CJEU 27 January 2000, Case C-23/98, *Staatssecretaris van Financiën v J. Heerma*, [2000] ECR I-00419.

13 CJEU 20 June 1991, Case C-60/90, *Polysar Investments Netherlands BV v Inspecteur der Invoerrechten en Accijnzen*, [1991] ECR I-03111.