VAT in a Day

A Concise Overview of the EU VAT System

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Dr. Frank Nellen

Rob Kappert
uitgeefbemiddeling

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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.

It would not have been possible to make this book available free of charge without the support of the Indirect Tax Fund. The Indirect Tax Fund is a unique collaboration of four universities (Tilburg University, Maastricht University, VU University Amsterdam and Leiden University) with the business community (Baker McKenzie, Deloitte, EY, KPMG Meijburg & Co, Loyens & Loeff and PwC) and the Tax Administration (Belastingdienst) in the Netherlands. The Indirect Tax Fund stimulates education and research in the field of indirect taxation.

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.

Nijmegen / Leiden, May 2021

1 Ad van Doesum, Herman van Kesteren Simon Cornielje and Frank Nellen, 2020, 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 over € 1,000 billion per year in tax revenues. These revenues play a huge role in the budgetary policy-making of the European Union and of the individual Member States in particular.

VAT is a so-called 'general consumption tax'[2], as it aims to tax all private consumption by individuals. Article 1(2) of the EU VAT Directive[3] 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 rapidly 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 a 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).

Taxing private consumption is a complicated affair. Even with modern technology, 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

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

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

how much you consumed in that particular month; this would impose a heavy (administrative) burden on consumers, as well as on the tax authorities. Also, it would have an impact on taxpayers' privacy. 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 to obtain the goods or services that he intends to consume. In this respect, 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.[4] 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 States of America is an example of such a system. As opposed to the U.S. however,

4 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".

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.

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.[5] 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 diagram illustrates the basic functioning of the VAT system.

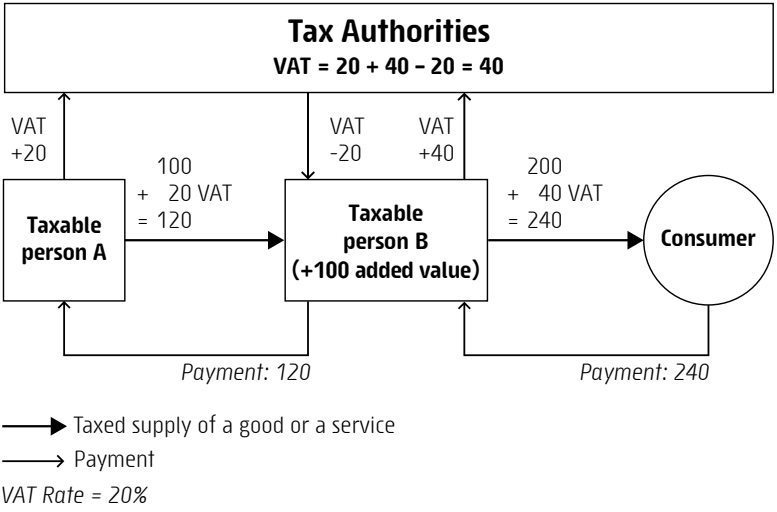

Figure 1: The basic functioning of the EU VAT system

5 Cf. OECD International VAT/GST Guidelines (available at: http://www.oecd.org/tax/consumption/international-vat-gst-guidelines-9789264271401-en.htm, accessed October 16, 2020).

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 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 final 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).[6] This VAT Directive serves as a blueprint for implementing VAT systems throughout the EU.[7] Each State is required to implement the VAT Directive (transpose the VAT Directive into national law).[8] 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.[9] 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 European Union (CJEU). The CJEU then provides the national court with an explanation of the provision. In the field of VAT, over 1,000 cases have been ruled by the CJEU.

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6 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).

7 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.

8 CJEU 19 January 1982, Case 8/81, Ursula Becker v Finanzamt Münster-Innenstadt, ECLI:EU:C:1982:7.

9 CJEU 13 November 1990, Case C-106/89, Marleasing SA v La Comercial Internacional de Alimentacion SA, ECLI:EU:C:1990:395.

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 in principle not able to appeal directly to the provisions contained therein. However, the CJEU ruled that in specific circumstances, a provision of national law which is not in line with a more favorable VAT Directive provision does not apply and the corresponding Directive provision applies instead.[10] 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.[11] 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.[12] 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.

10 CJEU 1 February 1977, Case 51-76, Verbond van Nederlandse Ondernemingen v Inspecteur der Invoerrechten en Accijnzen, ECLI:EU:C:1977:12.

11 Cf. CJEU 26 February 1986, Case 152/84, M. H. Marshall v Southampton and South-West Hampshire Area Health Authority (Teaching), ECLI:EU:C:1986:84.

12 Cf. CJEU 8 October 1987, Case 80/86, Criminal proceedings against Kolpinghuis Nijmegen BV, ECLI:EU:C:1987:431.

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 14-30b 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 281-369zc VAT Directive

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

4. Taxable Person

In this chapter we discuss the taxable person concept in EU VAT.

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. 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 can 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 must 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 1: 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.[13]

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.[14] 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).

13 CJEU 27 January 2000, Case C-23/98, Staatssecretaris van Financiën v J. Heerma, ECLI:EU:C:2000:46.

14 CJEU 20 June 1991, Case C-60/90, Polysar Investments Netherlands BV v Inspecteur der Invoerrechten en Accijnzen, ECLI:EU:C:1991:268.

4.4.2 Independent

Under Article 9 VAT Directive, a person will only have taxable person status if that person independently carries out an economic activity. Article 10 VAT Directive, which is merely accessory to Article 9 VAT Directive, excludes persons acting in an employer-employee type relationship from the taxable person concept for not acting independently. Consequently, to determine whether a person acts independently, two successive steps need to be taken:

1. Does an employer - employee relationship exist?

2. Does the person bear an economic risk?

Thus, first a test against Article 10 VAT Directive is performed. Subsequently, a test against the broader concept of independence of Article 9 VAT Directive is to be carried out.[15]

Employer – employee relationship

Article 10 VAT Directive 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. 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 majority shareholder who in practice has all the decision-making powers. In Van der Steen, the CJEU decided that a director with a majority shareholding who acts in name and on account of the company under his employment contract is not a taxable person for VAT.[16] The CJEU noted that the director-shareholder does not assume any economic business risk, which remains with the company. Further to the CJEU's decision, a director with a majority shareholding is not a separate taxable person for VAT when he carries out activities or taxable transactions within scope of his employment contract and on behalf of the company. It would seem that to establish whether director-shareholder is subor-

15 CJEU 13 June 2019, Case C-420/18 IO v Inspecteur van de rijksbelastingdienst, ECLI:EU:C:2019:490.

16 CJEU 18 October 2007, Case C-355/06, J. A. van der Steen v Inspecteur van de Belastingdienst Utrecht-Gooi/kantoor Utrecht, ECLI:EU:C:2007:615.

dinated to his company, it is relevant who bears the economic risk, which is in fact also the relevant criterion to determine in a broader context whether there is an independence in the pursuance of an economic activity (see below).

Bearing economic risk
To establish whether someone acts independently, the CJEU (also) takes into account the fact that the person in question bears the 'economic risk' entailed in their activities.[17] For example, a member of a Supervisory Board of a foundation was not bound to that foundation by any employer-employee relationship. Yet, he did not act independently, because he did not act in his own name, on his own behalf or under his own responsibility, but on behalf of and under the responsibility of that Supervisory Board. Moreover, he did not bear the economic risk arising from his activities, since he received a fixed remuneration which was not dependent on his participation in meetings or hours actually worked.[18]

Finally, the independency criterion is also relevant for determining whether a branch (not being a subsidiary) of a company is to be considered as a separate (taxable) person from the head office.[19]

4.4.3 Economic Activity

Article 9 paragraph 1 VAT Directive states that a person must carry out an economic activity to qualify as a taxable person. The VAT Directive defines the term 'economic activity' as any activity of producers, traders or persons supplying services, including mining and agricultural activities and activities of professions. Further, the VAT Directive provides that the term 'economic activity' also includes the exploitation of tangible or intangible property for the purposes of obtaining income on a continuing basis. Examples of such exploitation are the provision of a license to use certain intellectual property (intangible), or simply the letting of an immovable property (tangible). It is important to interpret the term 'economic activity' in a broad manner. Should one interpret the concept too restrictively, the possibility exists that certain transactions, ultimately leading to consump-

17 CJEU 25 July 1991, Case C-202/90 Ayuntamiento de Sevilla v Recaudadores de Tributos de las Zonas primera y segunda, ECLI:EU:C:1991:332 and CJEU 29 September 2015, Case C-276/14 Gmina Wroclaw v Minister Finansów, ECLI: EU:C:2015:635.

18 CJEU 13 June 2019, Case C-420/18 IO v Inspecteur van de rijksbelastingdienst, ECLI:EU:C:2019:490.

19 CJEU 23 March 2006, Case C-210/04, Ministero dell'Economia e delle Finanze and Agenzia delle Entrate v FCE Bank plc., ECLI:EU:C:2006:196.

tion, would escape taxation. Such an effect is not in line with the aim of VAT (as a general tax) to tax all supplies of goods and services.

Nonetheless, for an activity to be an 'economic' activity, the activity must correspond to one of the chargeable events defined in Article 2 VAT Directive.[20] This implies that the activity must consist of making supplies of goods and/or services for consideration. According to settled CJEU case-law, a supply of goods or services is made 'for consideration', if there is a legal relationship between the provider of the service and the recipient pursuant to which there is reciprocal performance, the remuneration received by the provider of the service constituting the value actually given in return for the service supplied to the recipient (see further Chapter 5, section 5.2.3).

It is not a requirement that economic activities are pursued with the intent of obtaining profits. It is sufficient that the purpose of the activity is to obtain income on a continuing basis, irrespective of whether the respective activity results in a financial profit or loss. For this reason, an organization that only supplies goods or services for free (i.e., there is no stipulated consideration in return) is no taxable person for VAT.[21]

As regards the start of economic activities, in Rompelman, the CJEU ruled that the initial investments of an entrepreneur are already to be considered as economic activities.[22] A person that has the intention to carry out economic activities is therefore considered as a taxable person, even though he did not carry out any output transaction yet. The rationale is that if initial investments do not give the investor the taxable person status, the VAT on the investments cannot be deducted. Ultimately, such non-deductible VAT will be included ('hidden') in the price of the taxable transactions once the business is started up, and subsequently the hidden VAT will be a part of the prices of other taxable persons further down the supply chain as well. In the end, the result is that private consumption is taxed more than once. This - from a system's perspective undesirable - effect is usually referred to as the 'cascading of VAT'.

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20 CJEU 12 May 2016, Case C-520/14, Gemeente Borsele v Staatssecretaris van Financiën and Staatssecretaris van Financiën v Gemeente Borsele, ECLI:EU:C:2016:334.

21 CJEU 1 April 1982, Case 89/81, Staatssecretaris van Financiën v Hong-Kong Trade Development Council, ECLI:EU:C:1982:121.

22 CJEU 14 February 1985, Case 268/83, D.A. Rompelman and E.A. Rompelman-Van Deelen v Minister van Financiën, ECLI:EU:C:1985:74.

It is difficult to determine whether a person has the intention to obtain income on a continuing basis by supplying goods or services. This is a process that requires an objective evaluation. If a person carries out activities regularly and structurally, one may conclude that he acts to obtain income from these activities on a continuing basis. A person who supplies goods or services on an incidental basis – even if for consideration – is in principle not a taxable person. Think of yourself selling one pair of old shoes on eBay; the singular nature of this act prevents you from becoming a taxable person and having to charge VAT. This simplifies the functioning of the VAT system, as it limits the number of taxable persons for VAT and thus reduces the administrative burden for all parties involved.

But what happens if you start selling products on eBay on a regular basis? At some point, an objective evaluation of the circumstances will lead to the conclusion that you indeed have started carrying out economic activities, or at least have the intention to start up such activities. Based on CJEU case law, factors such as taking 'active steps to market property' are to be considered when determining whether an activity is indeed an economic activity.[23]

And what to think of a person who uses solar panels on the roof of his house to produce electricity and who sells that electricity to the electricity company? In Thomas Fuchs, the CJEU considered that the exploitation of solar panels on a residential dwelling which are designed in such a manner that in any given month the electricity produced is (i) always less than the electricity privately consumed by its operator and (ii) supplied to the network in exchange for income on a continuing basis, falls within the concept of 'economic activities'.[24] Indeed, the concept of economic activity may be even broader than it seems to be at first sight.

A special case concerns the exploitation of tangible or intangible property for the purposes of obtaining income therefrom on a continuing basis, which, on the basis of Article 9 VAT Directive, is regarded as economic activity as well. For example, leasing an apartment normally takes place through one act (concluding a rental contract), but the income (installments) of the lease is received on a regular basis. In some Member States the granting of one interest bearing loan is considered as an economic activity, because it generates turnover on a continuous basis.

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23 CJEU 15 September 2011, Joined Cases C-180/10 and C-181/10, Jarosław Słaby v Minister Finansów (C-180/10) and Emilian Kuć and Halina Jeziorska-Kuć v Dyrektor Izby Skarbowej w Warszawie (C-181/10), ECLI:EU:C:2011:589.

24 CJEU 20 June 2013, Case C-219/12, Finanzamt Freistadt Rohrbach Urfahr v Unabhängiger Finanzsenat Außenstelle Linz, ECLI:EU:C:2013:413.

4.5 The Place of Establishment and the Concept of Fixed Establishment

The place of establishment or residence of a person (an entity) is irrelevant for determining whether he is a taxable person. Since VAT is only concerned with taxing transactions (supplies of goods and services), the location where the transaction takes place is more important.[25] The place of establishment or residence of (taxable) persons can however be decisive for the place where a transaction is considered to take place for VAT purposes. For example, as a main rule, cross-border supplies of services between taxable persons (B2B supply of services) take place where the recipient of the service is established, according to Article 44 VAT Directive (see Chapter 6).

A taxable person may be established in multiple places simultaneously. A company may have several stores (branches) in the same town or in different cities, but all of these stores are part of the same company. If such a company owns a branch located in a country different than the one in which the head office is located, and that branch is characterized by a sufficient degree of permanence and a suitable structure in terms of human and technical resources, that corporation is considered as also being established for VAT in that other country.[26] Such a secondary – as opposed to primary – establishment is called a 'fixed establishment'. The primary place of establishment (often referred to as 'head office') is essentially the place where the management is located and where the functions of the business's central administration are carried out.[27] Because the head office and the fixed establishment are, for VAT purposes, together regarded as one (trans-border) entity, any transactions between both fall outside the scope of VAT (they do not exist for purposes of VAT).[28]

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25 Nonetheless, the place of establishment may also play a role in other respects. See for example paragraph 4.8 on VAT Grouping.

26 See, among others: CJEU 4 July 1985, Case 168/84, Gunter Berkholz v Finanzamt Hamburg-Mitte-Altstadt, [1985] ECR 02251, CJEU 2 May 1996, Case C-231/94, Faaborg-Gelting Linien A/S v Finanzamt Flensburg, [1996] ECR I-02395, CJEU 20 February 1997, Case C-260/95, Commissioners of Customs and Excise v DFDS A/S, [1997] ECR I-01005, CJEU 17 July 1997, Case C-190/95, ARO Lease BV v Inspecteur van de Belastingdienst Grote Ondernemingen te Amsterdam, [1997] ECR I-04383, and CJEU 7 May 1998, Case C-390/96, Lease Plan Luxembourg SA v Belgian State, [1998] ECR I-02553.

27 See, Article 10 VAT Implementing Regulation 282/2011.

28 CJEU 23 March 2006, Case C-210/04, Ministero dell'Economia e delle Finanze and Agenzia delle Entrate v FCE Bank plc., [2006] ECR I-02803. If the fixed establishment is part of a VAT Group (see section 4.8), transactions between the head office and the VAT Group of which the fixed establishment is a member, are within the scope of VAT: CJEU, 17 September 2014, Case C-7/13, Skandia America Corp. (USA), filial Sverige v Skatteverket, ECLI:EU:C:2014:2225 and CJEU 11 March 2021, Case C-812/19, Danske Bank A/S v Skatteverket, ECLI:EU:C:2021:196

Example 2: Head Office and Branch
A Belgian branch (fixed establishment) of a Dutch company, called 'Squirrel BV' (the head office) maintains the software systems of the entire Squirrel company. The Dutch head office and other Squirrel branches in the Netherlands and in Germany pay a fee to the Belgian branch in remuneration for these activities.

The Belgian fixed establishment does not supply taxed services to Squirrel BV, even though the Belgian fixed establishment receives consideration for its services from the head office and other branches.

Until the CJEU's ruling in Dong Yang, it was generally accepted that subsidiaries (i.e. legal persons on their own right) could not be considered as a fixed establishment of their parent company.[29] However, in Dong Yang, the CJEU considered that it cannot be ruled out that a subsidiary held for the purposes of conducting economic activity by a parent company established in South Korea may constitute a fixed establishment of that parent company in a Member State of the EU, within the meaning of Article 44 VAT Directive.[30] The scope of this ruling remains rather unclear. Is it limited to situations in which a parent company is legally required to set-up a subsidiary in a Member State to do business in that country? Is it limited to the determination of the place of supply under Article 44 VAT Directive (B2B main rule for cross border services)? We expect that in the years to come, the CJEU will be asked to further clarify its ruling.[31]

4.6 Bodies Governed by Public Law

Previously, we noted that the legal form of a company is irrelevant for determining whether an entity is a taxable person. We also stressed that the term 'economic activity' is interpreted broadly. However, bodies governed by public law (hereafter: public bodies) are a distinct category of persons in the context of EU VAT.

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29 See, opinion of Advocate-General Kokott of 14 November 2019, Case C-547/18, Dong Yang Electronics Sp. z o.o. v Dyrektor Izby Administracji Skarbowej we Wrocławiu, ECLI:EU:C:2019:976.

30 CJEU 7 May 2020, Case C-547/18 Dong Yang Electronics Sp. z o.o. v Dyrektor Izby Administracji Skarbowej we Wrocławiu, ECLI:EU:C:2020:350.

31 See, for example, the pending CJEU Case C-333/20, Berlin Chemie A. Menarini SRL.

4.6.1 Acting as a Public Body or as a Taxable Person?

It is possible that a public body (such as state, regional and local government authorities and other bodies governed by public law) carries out activities which ultimately lead to consumption by private individuals. For example, a municipality may supply passports for consideration. Should VAT be levied on this transaction? On one hand it seems illogical that a public body (the state) by means of VAT would tax another public body (the municipality), but on the other hand the aim of VAT is to subject all consumption by private individuals to taxation. Additionally, a public body can engage in activities which are also carried out by private sector (market) parties.

For example, a ferry may be operated by a municipality as well as by a private entrepreneur. In case the municipality does not charge VAT on its ferry service, the municipality distorts competition because it can offer services at a lower price than the entrepreneur.

Following Article 13 VAT Directive, a body such as a municipality can act either in its capacity of public body, or in its capacity of taxable person. If the municipality acts as a public body, it is not a taxable person with respect to the activity it carries out. The supply it makes in that capacity is not subject to VAT and thus, in connection with that activity, the municipality does not have a right of deduction (see section 4.6.2). If a municipality acts as a taxable person, the activities are economic activities, and the transactions are taxable transactions which are subject to VAT – and thus taxed or exempt. The municipality may have a right of deduction when acting in its capacity as a taxable person, depending on the nature of the output transactions it carries out (see section 4.6.2).

Based on the VAT Directive and CJEU case law[32], four conditions must be fulfilled to conclude that a (legal) person acts in its capacity of public body and not as a taxable person:

1. The activity in itself must be an economic activity[33],
2. The activity must be carried out by a public body,
3. The activity must be carried out under a special legal regime applicable to the public body, and
4. There must be no significant distortion of competition.

To respect the principle that VAT is a general tax which applies to all supplies of goods and services, national judges are required to apply and interpret the above conditions in a restrictive manner and keep exceptions to a minimum.

If the criteria mentioned above are applied to the sale of passports by a municipality, there is, in principle, an economic activity (carried out on a continuing basis and for consideration) performed by a public body (the municipality). However, the activities are carried out under a special legal regime (i.e., public law, which determines the way municipalities should arrange the identification of citizens). There is no significant distortion of competition because only the municipality is (on grounds of public law) allowed to sell passports. This means that a municipality does not act as a taxable person if it issues passports. Conversely, the municipality acts in its capacity of taxable person if it operates a ferry – since not all four conditions are met.

4.6.2 Public Bodies and Input VAT

Only taxable persons can deduct the VAT charged to them by other taxable persons (see chapter 10).[34] A body which carries out activities both in its capacity of public body and taxable person, only enjoys a partial right of deduction. For

32 See, among others:CJEU 17 October 1989, Joined cases 231/87 and 129/88, Ufficio distrettuale delle imposte dirette di Fiorenzuola d'Arda and others v Comune di Carpaneto Piacentino and others, [1989] ECR 03233; CJEU 25 July 1991, Case C-202/90, Ayuntamiento de Sevilla v Recaudadores de Tributos de las Zonas primera y segunda, [1991] ECR I-04247, and CJEU 26 June 2007, Case C-284/04, T-Mobile Austria GmbH and Others v Republik Österreich, [2007] ECR I-05189.

33 If the activity is not an economic activity, it is for that reason alone that the person concerned does not act in its taxable person capacity.

34 Insofar as they use the goods and/or services for activities which allow for a right of deduction, see chapter 10.

this reason, public bodies normally have two distinct sectors (or subdivisions): one public sector and a private one. It is not always easy to distinguish between both sectors. In some Member States a municipality is considered to act as a public body if it develops urban development plans, but as a taxable person when executing that plan. Under those circumstances, are the costs of external advisors, planners, etc. linked to the activities in the public sector or those of the private sector? Note that a right of deduction only exists in respect of activities carried out as a taxable person (i.e., in the private sector). The fact that a public body acting in the public sector is not able to deduct VAT which is charged to it, creates an incentive for the body to internalize as many activities as possible. The reason is that outsourced activities are burdened with non-deductible VAT. However, 'insourcing' may from an economic point of view not always be efficient. To prevent VAT from affecting a public body's decision to outsource or insource an activity, some Member States implemented targeted compensation mechanisms, outside the VAT system (so-called 'VAT compensation funds'), to alleviate the cost of VAT on their acquisitions.[35]

4.7 Holding Companies

There is a vast body of CJEU case law on the taxable person status and capacity of holding companies. At first glance this may seem somewhat surprising, because dealings in shares (such as the issue and the sale of shares) are either outside the scope (not subject to VAT), or inside the scope of VAT, but exempt from VAT. However, on closer inspection, it shows that the taxable person status and capacity of a holding company is decisive for the deductibility of VAT on costs relating to the issue, acquisition, holding and sale of shares (see chapter 10).

In section 4.4.3 we indicted that the exploitation of property for the purpose of obtaining income on a continuing basis shall be regarded as an economic activity (see Article 9(2) VAT Directive). This means that the granting of an interest-bearing loan with a maturity of five years is an economic activity.[36] Following this reasoning, the holding of shares, from which the holder of the shares receives dividend, could also be economic activity as the shareholder should in principle receive income (dividend) on a continuous basis from the shares he holds. Yet, the CJEU decided in *Polysar* that the mere holding of shares is not an economic

35 For example: United Kingdom, Denmark, Sweden, Finland and the Netherlands. See: M.C. Wassenaar and R.H.J.M. Gradus, Contracting out: the importance of a level playing field, Research Centre for Economic Policy (OCFEB), 2001, (available via: http://repub.eur.nl/res/pub/818/rm0108.pdf, accessed March 3, 2021).

36 Cf. CJEU 26 September 1996, Case C-230/94, Renate Enkler v Finanzamt Homburg, [1996] ECR I-04517.

activity.[37] According to the CJEU, the mere acquisition and holding of shares in a company are not to be regarded as economic activities, conferring on the holder the status of taxable person.[38] A holding company confining itself to managing an investment portfolio in the same way as a private investor is not a taxable person.[39] It is consistent CJEU case law that the mere acquisition and holding of financial holdings in other undertakings does not amount to the exploitation of property for the purpose of obtaining income therefrom on a continuing basis because any dividend yielded by that holding is merely the result of ownership of the property. This conclusion may in part be explained by the fact that the shareholder does not really put property at the disposal of the company he invests in; the purchase and holding of shares simply implies that he participates in the capital base or equity of the company (i.e., he obtains ownership of something via capital investments). This is an essential difference between – for example – the letting of immovable property and the holding of shares. Additionally, the letting of immovable property, the granting of an interest-bearing loan or any other form of exploitation of (in)tangible property to derive income therefrom, usually requires relatively more effort than simply buying shares and merely holding them. The revenues (dividends) directly attributable to the shares arise from the mere ownership of the shares instead of the activities associated with the investment of capital. These considerations may explain the CJEU's ruling in *Polysar*.

If a holding company is not a taxable person for the purchase and holding of shares (a 'mere' holding company), the holding company is in principle[40] also not a taxable person when it sells those shares. Consequently, if a holding company is a mere holding company and then sells the shares it merely holds, the sale is in principle not subject to VAT (not taxable, so neither taxed nor exempt).

This does not mean that a holding company can never be a taxable person with respect to the holding of shares. The CJEU noted in *Polysar* that a holding company can be a taxable person if the holding company is actively involved in the management of the subsidiary. In *Floridienne-Berginvest*, the CJEU added that an involved holding company is only a taxable person with respect to the

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

38 See, for example: CJEU (Order of the Court), 12 January 2017, Case C-28/16, Magyar Villamos Művek Zrt. (MVM) v Nemzeti Adó- és Vámhivatal Fellebbviteli Igazgatóság, ECLI:EU:C:2017:7.

39 Opinion of Advocate General Kokott of 14 May 2020, Case C-42/19 Sonaecom SGPS SA v Autoridade Tributária e Aduaneira, ECLI:EU:C:2020:378, para. 46.

40 See: Ad van Doesum, Herman van Kesteren Simon Cornielje and Frank Nellen, 2020, Fundamentals of EU VAT Law, Alphen aan den Rijn: Kluwer Law International, pp. 489-490.

holding of shares if the involvement is accompanied with taxed or exempt activities provided for consideration to the subsidiary (for example advisory services or financing services).[41] However, dividends cannot be regarded as a consideration for (services accompanying the) involvement in the management of an entity.[42] Thus, the involvement must be expressed through taxable transactions which the holding company supplies to the subsidiary.

The difference between a private shareholder/investor (not a taxable person) and a 'controlling active parent company'[43] which is involved in the management of a subsidiary and in connection with that involvement supplies services to that subsidiary for consideration is that the private shareholder simply holds shares to realize a monetary return in the form of dividends. A controlling active holding company holds shares in a subsidiary to manage it through its power of control over the entity and to enhance the profitability of the group as a whole. These activities are considered as economic activities.

The holding of shares, as well the buying and selling of these shares, is also to be regarded as economic activity if it concerns commercial share dealing by brokers acting in the course of their business activities.[44] Moreover, the holding of shares or bonds can be an economic activity if it serves another economic activity. In the latter case, the holding of the shares must be a "direct, permanent and necessary extension" of the taxable activities of the taxable person.[45]

A holding company that is a taxable person with respect to the buying and holding of shares in principle also acts as a taxable person when selling these shares. In this regard it appears to be relevant whether the holding company selling the shares allocates the proceeds of the sale to its economic activity or to

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41 CJEU 14 November 2000, Case C-142/99, Floridienne SA and Berginvest SA v Belgian State, [2000] ECR I-09567. For completeness sake, we note that the CJEU ruled that where a holding company merely reinvests dividends received from its subsidiaries and outside the scope of VAT in loans to those subsidiaries, that in no way constitutes a taxable activity. The interest on such loans must, on the contrary, be considered merely as the result of ownership of the asset and is therefore outside the system of deductions.

42 CJEU 22 June 1993, Case C-333/91, Sofitam SA (formerly Satam SA) v Ministre chargé du Budget, [1993] ECR I-03513.

43 See: Ad van Doesum, Herman van Kesteren and Gert-Jan van Norden, share Disposals and the Right to Deduction of Input VAT, EC Tax Review 2010/2.

44 See, for example: CJEU 20 June 1996, Case C-155/94, Wellcome Trust Ltd v Commissioners of Customs and Excise, [1996] ECR I-03013, CJEU 6 February 1997, Case C-80/95, Harnas & Helm CV v Staatssecretaris van Financiën, [1997] ECR I-00745, CJEU 29 April 2004, Case C-77/01, Empresa de Desenvolvimento Mineiro SGPS SA (EDM) v Fazenda Pública, [2004] ECR I-04295 and CJEU 21 October 2004, Case C-8/03, Banque Bruxelles Lambert SA (BBL) v Belgian State, [2004] ECR I-10157.

45 CJEU 11 July 1996, Case C-306/94, Régie dauphinoise - Cabinet A. Forest SARL v Ministre du Budget, [1996] ECR I-03695.

the economic activity carried out by the group of which it is the parent company.[46] The sale of shares is considered as a supply of services under Article 14 VAT Directive. That service is subject to VAT, but it is exempt because of Article 135(1)(f) VAT Directive (transactions in shares).[47]

In summary, a holding company does in principle not become a taxable person with respect to the holding of shares in case it merely acquires, holds, or sells shares. This is different if the holding company is either actively involved in the management of a subsidiary and this involvement is accompanied by services for consideration, if the holding company is engaged in commercial share dealing, or if it holds shares as a (direct, permanent, and necessary) extension of its other economic activities.

In addition to the mere holding of shares, a holding company may also engage in other economic activities, like selling goods or providing services to third parties. In this situation, the holding company's activities can be subdivided into separate sectors, in a similar way that the activities of a public body can be split up into distinct sectors, namely in economic and non-economic activities.

4.8 VAT grouping

Article 11 of the VAT Directive includes an option for Member States to apply a so-called 'VAT grouping scheme'.[48] Under such a scheme, persons established in the territory of a Member State who are legally independent, but financially, economically, and organizationally linked to one another, are treated as a single taxable person for VAT purposes. A noteworthy consequence of a VAT group is that the group itself, not the separate persons forming that group, is the taxable person for VAT. Consequently, supplies between the members of the VAT group are considered as non-existent for VAT purposes and are therefore not taxable.[49] The rationale behind the VAT grouping facility is to allow for administrative simplification and the combatting of abuse (e.g., the splitting up of one undertaking among several taxable persons so that each may benefit from a special scheme).[50] A VAT

46 CJEU 8 November 2018, Case C-502/17 C&D Foods Acquisition ApS v Skatteministeriet, ECLI:EU:C:2018:888, para. 38.

47 CJEU 29 October 2009, Case C-29/08, Skatteverket v AB SKF, [2009] ECR I- 10413.

48 A correct implementation of this option requires the Member State that wants to avail itself of this option to consult the advisory committee on value added tax (the 'VAT Committee').

49 CJEU 22 May 2008, Case C-162/07, Ampliscientifica Srl and Amplifin SpA v Ministero dell'Economia e delle Finanze and Agenzia delle Entrate, [2008] ECR I-04019.

50 Explanatory Memorandum to the proposal for a Sixth Directive of 20 June 1973, COM (73)950.

group can produce tax advantages. For example, VAT savings may be achieved by the formation of a VAT group in case a company which cannot deduct input VAT is included in a VAT group with other companies that do have right to deduct input VAT. The VAT group as a whole then obtains a (partial) right of deduction of input VAT. As a result, VAT on overhead costs which were initially incurred by the company which had no right of deduction can now be (partly) deducted by the VAT group. It should be noted that the VAT group has no relation to the "group regime" in corporate income tax and, accordingly, different conditions apply.

The formation of a VAT group requires that the potential members:

1. are established in the same Member State,
2. are closely bound to one another through financial links,
3. are closely bound to one another by economic links, and
4. are closely bound to one another by organizational links.

The CJEU has ruled that Article 11 VAT Directive does not require that the members of a VAT Group each have taxable person status themselves.[51] It is required though that all entities that want to become part of the same VAT group must be established in the same Member State. Depending on the national legislation of the respective Member State, financial links are generally determined on the basis of equity percentages and the voting rights attached to those shares (how many percent of the shares / voting rights does one have? Is that sufficient to be financially linked?). Economic links generally relate to the fact that the various persons constituting the VAT group must have a similar or equal economic goal. Organizational links concern relations of power and management; it is required that the various persons operate within a setting in which they are bound to one another by management ties. Whether one person can exercise decisive influence over another in the group is also an important factor. Since the concept of VAT grouping is based on a facultative provision in the VAT Directive, which leaves the choice to implement it in national legislation to the Member States themselves,

51 CJEU 9 April 2013, Case C-85/11, European Commission v Ireland, not yet published and CJEU 25 April 2013, Case C-65/11, European Commission v Kingdom of the Netherlands, not yet published. The CJEU ruled that 1) it is not apparent from the wording of Article 11 of the VAT Directive that non-taxable persons cannot be included in a VAT group, 2) the context of Article 11 of the VAT Directive cannot be interpreted as meaning that non-taxable persons cannot be included in a VAT group, and 3) that the objectives of Article 11 of the VAT Directive do not militate in favor of an interpretation according to which non-taxable persons cannot be included in a tax group.

the precise conditions for VAT grouping may differ per state and some indeed did not even implement the concept.[52]

52 In its Communication on the VAT Group option of 2 July 2009, the European Commission proposes uniform guidelines for a correct interpretation of the condition about "financial, economic and organizational links. See: Communication from the Commission to the Council and the European Parliament on the VAT group option provided for in Article 11 of Council Directive 2006/112/EC on the Common System of Value Added Tax, COM(2009) 325 final. Also see the VAT Committee Working Paper of 16 February 2017, No. 918 concerning the meaning of "financial, economic and organizational links" among VAT group members, taxud.c.1(2017)982178 – EN.

5. Taxable Transactions

In this chapter, we discuss the taxable transactions in EU VAT.

5.1 Introduction

The principle of the common VAT system entails the application of VAT to goods and services (Article 1(2) VAT Directive). Based on Article 2(1) VAT Directive, there are four taxable events for VAT:

1. the supply of goods,
2. the supply of services,
3. the intra-Community acquisition of goods, and
4. the importation of goods.

Even though Article 2(1) VAT Directive denotes all four taxable events as "transactions", strictly speaking only supplies of goods and supplies of services can be regarded as "transactions". Of the aforementioned four taxable events, the supplies of goods and the supplies of services are the most important taxable events in VAT. Importing goods (transporting goods from outside the EU into the EU) and intra-Community acquisitions of goods (acquiring goods from other Member States) are also taxable transactions (Articles 30 and 20 VAT Directive respectively). However, these taxable transactions have a somewhat more technical character. In any case, the most essential taxable transactions in VAT are the supply of goods and the supply of services. In this chapter we focus on these two types of transactions. Nevertheless, in section 5.3 and section 5.4 we will discuss the intra-Community acquisition of goods and the importation of goods, respectively.

5.2 Supplies of Goods and Services

The supply of goods and the supply of services for consideration within the territory of a Member State by a taxable person acting as such are taxable transactions (Article 2(1)(a) and (c) VAT Directive. Accordingly, four conditions must be fulfilled for the transaction to be a taxable transaction. There must be:

1. a supply of a good or a service,
2. for consideration,
3. within the territory of a Member State,
4. by a taxable person acting as such.

This section focuses on conditions 1 and 2. Conditions 3 and 4 are addressed in chapters 6 (Place of supply) and 4 (Taxable person) respectively.

5.2.1 The Purpose of the Differentiation Between Supplies of Goods and Supplies of Services

A distinction must be made between the supply of goods and the supply of services. The reason is that the rules which apply for determining (among other aspects) the place of supply, the applicable VAT rate and the application of exemptions are not identical for supplies of goods and supplies of services.

Following Article 14 VAT Directive, goods are tangible property. Although somewhat less tangible, electricity and gas, etc. are also deemed as goods (Article 15 VAT Directive). A supply of goods is defined as a 'transfer of the right to dispose of tangible property as owner.' From the CJEU judgment in Safe, one can deduce that the concept "supply of goods" does not refer to the transfer of ownership in accordance with the procedures prescribed by the applicable national law. Thus, the supply of goods is an independent concept of Union law.

It covers any transfer of tangible property by one party (the supplier) which empowers the other party (the purchaser) actually to dispose of it as if he were the owner of the property.[53] In this regard, it must be determined whether the purchaser at any time obtains the right to decide in what way the goods must

53 CJEU 8 February 1990, Case C-320/88, Staatssecretaris van Financiën v Shipping and Forwarding Enterprise Safe BV, [1990] ECR I-00285.

be used or to what end.[54] Only if the purchaser obtains sufficient rights to use the goods as he sees fit and is actually in the position to use the goods at his sole discretion, does a supply of goods take place.

Based on Article 24 VAT Directive, the supply of service is defined as any transaction which does not constitute the supply of goods. By means of these two definitions of supplies of goods and supplies of services, the EU VAT system thus constitutes a closed system which in principle aims to encompass all forms of transactions.[55]

5.2.2 Composite Supplies

When engaging in a transaction a taxable person may provide a combination of taxable transactions or elements. In case these elements or transactions do not enjoy the same VAT treatment (e.g., different VAT rates are applicable), one must determine whether the elements or transactions constitute one single supply for VAT purposes (which is taxed at only one rate!) or multiple distinct supplies (each having its own VAT treatment). Following Card Protection Plan, the main rule is that every supply of a service must normally be regarded as distinct and independent and, second, that a supply which comprises a single service from an economic point of view should not be artificially split.[56] So as not to distort the functioning of the VAT system, the essential features of the transaction must be ascertained in order to determine whether the taxable person is supplying the customer, being a typical consumer, with several distinct principal services or with a single service. In particular, there is a single supply in cases where one or more elements are to be regarded as constituting the principal service, whilst one or more elements are to be regarded, by contrast, as ancillary services which share the tax treatment of the principal service. A service must be regarded as ancillary to a principal service if it does not constitute for customers an aim in itself, but a means of better enjoying the principal service supplied.

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54 CJEU,6 February 2003, Case C-185/01, Auto Lease Holland BV v Bundesamt für Finanzen, [2003] ECR I-01317, para. 34.

55 In some cases, the VAT Directive expands the scope of taxable supplies of goods and services. For example, the application or use of goods for private use is considered as a supply of goods or services if certain conditions are met. Moreover certain so-called 'internal supplies' can be considered as taxable supplies. However, it is not the place to discuss those particularities here.

56 CJEU 25 February 1999, Case C-349/96, Card Protection Plan Ltd (CPP) v Commissioners of Customs & Excise, [1999] ECR I-00973.

Example 3: Composite supplies
Stefano and Humberto sell sealed lunchboxes to children. Each box contains delicious sandwiches and a little surprise (a toy). The food is normally taxed at a reduced rate (for example 6%). The toy, if it is considered a separate supply of a good, is taxed at the standard rate (20%). The question is whether Stefano and Humberto carry out one single supply at the reduced rate of 6% or two separate supplies (one supply of sandwiches at the reduced rate and one supply of a good (the toy) at the standard VAT rate of 20%).

The supply of the food may be viewed as the main element of the supply because Stefano and Humberto are in the business of supplying lunch boxes. Arguably, in this case there is only one supply which is taxed at the reduced rate. Here the toy is an ancillary to the supply of the sandwiches.

5.2.3 For Consideration
A supply of goods or services is only taxable if the supply is made for consideration. Case law explains that to have a supply for consideration, the following conditions must be fulfilled:[57]

- There is a legal relationship between the supplier of the good/service and the recipient pursuant to which there is reciprocal performance;
- There is a subjective consideration for the good/service, which can be expressed in monetary terms, and
- The consideration received by the supplier of the good/service must constitute the value actually given in return for the good/service supplied to the recipient, i.e., there must be a direct link between the good/service provided and the consideration received in return.

57 CJEU 5 February 1981, Case 154/80, Staatssecretaris van Financiën v Association coopérative "Coöperatieve Aardappelenbewaarplaats GA", [1981] ECR 00445, CJEU 8 March 1988, Case 102/86, Apple and Pear Development Council v Commissioners of Customs and Excise, [1988] ECR 01443, CJEU 23 November 1988, Case 230/87, Naturally Yours Cosmetics Limited v Commissioners of Customs and Excise, [1988] ECR 06365 and CJEU 3 March 1994, Case C-16/93, R. J. Tolsma v Inspecteur der Omzetbelasting Leeuwarden, [1994] ECR I-00743.

For a legal relationship to be existent, it is sufficient that the parties involved have concluded a written or oral agreement.[58] Normally, a consideration for a good or service will be a monetary amount, but the consideration may also exist in the form of goods or services (barter exchange). Two conditions must be fulfilled for a direct link to exist between the supply and the remuneration: 1) the consideration will not be paid if the supply does not place, and 2) the supply will not take place if no consideration is paid.

For example, an organ grinder who is a street performer sometimes receives money from people passing by. The organ grinder does not supply services for consideration, as the service he provides is not directly linked with the consideration received.[59] The organ grinder will play music on the street regardless of whether he receives money from each of the people that walk by.

In Apple & Pear, the CJEU held that to determine whether there is a direct relationship between the activities of the 'Apple and Pear Council' (a legal person having members) and its members, it was relevant to determine whether the Council had acted in the common interest of its members.[60] In this situation there was legal duty for all members to pay the fee to the Council. The fee was paid regardless of whether the member obtained an advantage from the Council's promotion of apples and pears. For this reason, the CJEU determined that there was no supply of a service for consideration. A golf club, on the other hand, that made facilities available to its members (a golf course, dressing rooms, etc.) for a yearly fee performed services against consideration even if the member did not effectively use the facilities. The golf club provided a service by making the facilities available, and this service was performed in exchange for a fixed fee (consideration).[61]

5.3 The Importation of Goods

Supplies of goods in the EU are generally taxed with VAT.[62] Countries outside of the EU do not always levy VAT. Without further arrangements, it would be cheaper for final consumers and businesses that cannot fully recover input VAT to

58 CJEU 17 September 2002, Case C-498/99, Town & County Factors Ltd v Commissioners of Customs & Excise, [2002] ECR I-07173.

59 CJEU 3 March 1994, Case C-16/93, R. J. Tolsma v Inspecteur der Omzetbelasting Leeuwarden, [1994] ECR I-00743.

60 CJEU 8 March 1988, Case 102/86, Apple and Pear Development Council v Commissioners of Customs and Excise, [1988] ECR 01443.

61 CJEU 21 March 2002, Case C-174/00, Kennemer Golf & Country Club v Staatssecretaris van Financiën, [2002] ECR I-03293.

62 See however Chapter 8 on exemptions.

purchase goods from suppliers outside the EU than from within the Member State they reside in. To prevent a distortion of competition, the entry of goods within the EU is regarded as a taxable 'transaction' (refer to Article 30 VAT Directive). This ensures 'external neutrality'.[63] In order for the importation of goods to be a taxable event for VAT purposes, it is not necessary that the importer of the goods is a taxable person. Unlike the taxable transactions 'supplies of goods and services' and 'intra-Community acquisitions of goods', the importation of goods is a taxable 'transaction' regardless of the taxable person status of the importer. The levy of VAT on importation of goods is closely connected to the levy of customs duties: the VAT Directive contains direct references to Customs law.

The VAT Directive contains some exemptions for importations of goods.[64] For example, there is an exemption for the importation of personal luggage, which allows tourists to avoid having to pay VAT on their personal luggage (clothes, etc.) when they (re-)enter the EU. Naturally, there are limits and conditions to the exemption.

The 'importation' of services is not a taxable transaction in itself. The so-called 'place of supply rules' in combination with the rules on the person liable to pay the VAT serve to guarantee the external neutrality of VAT in case of services. The place of taxation of services depends on the location at which they are deemed to take place for VAT purposes (see Chapter 6).

5.4 The Intra-Community Acquisition of Goods

The European Union intended to create an internal market by removing fiscal borders between the Member States in 1993. Since the physical controls disappeared, it became impossible to levy VAT at the intra-EU borders upon physical importation. Because of this change, the concepts of "intra-Community supply" and "intra-Community acquisition" were introduced for transactions (supplies of goods) between taxable persons.

The intra-Community supply of goods and their intra-Community acquisition are in fact two sides of the same coin. Together they form one and the same (commercial) transaction. However, the intra-Community supply creates rights and obligations for the supplier and the tax authorities in the Member State of the supply (see

63 Ad van Doesum, Herman van Kesteren Simon Cornielje and Frank Nellen, 2020, Fundamentals of EU VAT Law, Alphen aan den Rijn: Kluwer Law International, p. 42.

64 Ad van Doesum, Herman van Kesteren Simon Cornielje and Frank Nellen, 2020, Fundamentals of EU VAT Law, Alphen aan den Rijn: Kluwer Law International, p. 640 and further.

Chapter 6 on the place of supply of goods), whereas the intra-Community acquisition creates rights and obligations for the purchaser and the tax authorities in the Member State of acquisition (see Chapter 6 on the place of the intra-Community acquisition).[65]

A basic intra-Community transaction consists of an intra-Community supply for consideration by a taxable person acting as such in one Member State and an intra-Community acquisition of those goods by a taxable person (or non-taxable legal person) in another Member State. It is essential that the goods are physically transported or dispatched in the course of the supply from the one Member State to the other. In essence, the system of intra-Community supplies and intra-Community acquisitions functions as follows.

Example 4: A basic Intra-Community supply

Company A in Germany supplies goods to Company B in the Netherlands. The place of the supply is Germany (see Chapter 6). Since the goods are transported in the course of the supply and the goods actually leave Germany, this supply is an intra-Community supply ('ICS') of goods. This intra-Community supply is VAT exempt with a right to deduct input VAT (some Member States apply a zero-rate, which is essentially the same thing, see Chapter 8). Consequently, the goods leave Germany (the Member State of dispatch) VAT-free. Company B, the buyer of the goods (who must also be taxable person) effects an intra-Community acquisition ('ICA') of the goods in the Netherlands (the Member State of arrival of the goods). The intra-Community acquisition of goods is a taxable event in itself. Company B must report the intra-Community acquisition in its VAT return and (in principle) pay the VAT that is due on the acquisition. If Company B has a right to recover input VAT in full, he can deduct the VAT on the acquisition in the same VAT return. Consequently, he will not be required to actually pay the VAT to the tax authorities. The diagram below summarizes the VAT treatment of such a straightforward intra-Community supply and intra-Community acquisition:

65 CJEU 27 September 2007, Case C-409/04, The Queen, on the application of Teleos plc and Others v Commissioners of Customs & Excise, [2007] ECR I-07797.

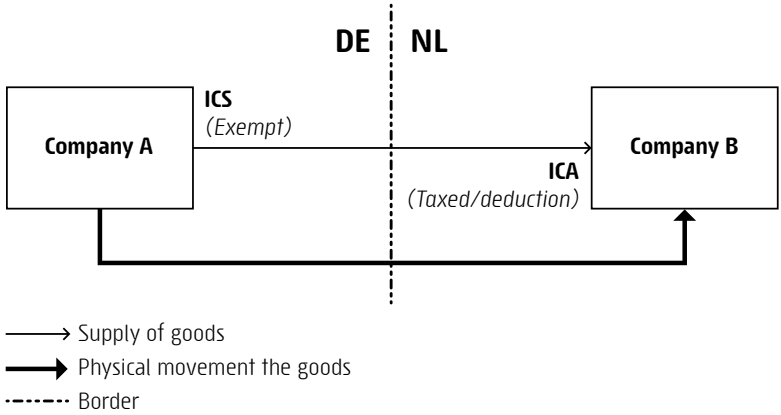

Figure 2: A basic Intra-Community Supply

It follows from the above that the intra-Community acquisition is subject to VAT in the Member State where the transport ends, against the VAT rate applicable there. If the acquirer of the goods (the Dutch company B in the example) subsequently supplies the goods to a private individual in the Netherlands, that (local) supply will be subject to Dutch VAT at the Dutch (standard or reduced) VAT rate. The system of intra-Community supplies and intra-Community acquisitions thus realizes that the VAT ultimately taxes consumption at the place most likely for consumption. A different method of taxation applies for services (see Chapter 6).

5.5 Not a Taxable Transaction: Transfer of a Totality of Assets or Part Thereof

If a taxable person transfers his business (his assets and liabilities), this in principle means that this taxable person carries out supplies of goods/services for every asset that he transfers. However, it may be rather burdensome to determine a price (taxable amount for VAT) for each and every separate supply of goods/services that such a transfer entails. Moreover, a taxable person transferring his assets would have to charge VAT on each and every supply which the customer subsequently has to pay to him. If there is a time difference between the moment that the supplier must remit the VAT on the supplies to the tax authorities and the moment that the customer pays the purchase price (and the VAT on that price), the supplier has to pre-finance the VAT on the whole transfer. Similarly, the transferee may have a cash-flow disadvantage if he must pay the VAT to the transferor at a moment earlier than the moment on which he receives the VAT back from the tax authorities (assuming that the transferee has a full right of deduction).

To avoid these complications of a transfer of a going concern, Article 19 VAT Directive allows Member States to consider the transfer of a totality of assets or part thereof not as a supply of goods. This rule is commonly called the "no supply rule" or the 'transfer of a going concern' ('TOGC') scheme. Article 29 VAT Directive provides that Article 19 VAT Directive applies in the same manner to services. Member States which avail themselves of this option may adopt any measures needed to prevent tax evasion and avoidance.

These provisions enable the Member States to facilitate transfers of undertakings or parts of undertakings by simplifying them and preventing cash flow disadvantages for the transferee and transferor. If a Member State has made use of that option, the transfer of a totality of assets or part thereof is not regarded as a supply of goods or services for VAT purposes. Instead, the person to whom the goods are transferred is to be treated as the successor to the transferor. Most Member States made use of this option in the VAT Directive, albeit that they apply different conditions to treat a transfer of a totality of assets or part thereof as a supply outside the scope of VAT.

The VAT Directive does not contain a definition of the concept of 'a transfer, whether for consideration or not or as a contribution to a company, of a totality of assets or part thereof'. It is however an independent concept of Union Law. In Zita Modes, the CJEU ruled that it covers the transfer of a business or an independent part of an undertaking including tangible elements and, as the case may be, intangible elements which, together, constitute an undertaking or a part of an undertaking capable of carrying on an independent economic activity.[66] Conversely, it does not cover the simple transfer of assets, such as the sale of a stock of products. Moreover, the transferee must not immediately liquidate the activity transferred and sell the stock, if any. There must be an intention to operate the business, or the part of the undertaking transferred. However, it is not necessary that the transferee pursues the same type of economic activity as the transferor did prior to the transfer.

66 CJEU, 27 November 2003 Case C-497/01, Zita Modes Sàrl v Administration de l'enregistrement et des domaines, [2003] ECR I-14393.

6. The Place of Supply

The VAT Directive contains rules which, following implementation into national VAT law, allocate VAT taxing competences for every supply, be it goods or services. These rules are commonly referred to as the 'place of supply' rules. A different set of rules applies to the supply of goods than to the supply of services.

6.1 The Place of Supply of Goods

It is important to recognize that since July 1, 2021, special rules apply to cross-border supplies of goods to private consumers, where the goods are dispatched or transported by or on behalf of the supplier (so-called 'distance sales'). We refer to section 6.1.2. In section 6.1.1, we will first outline the general place of supply rules for the supplies of goods.

6.1.1 The Main Rules on the Place of Supply of Goods

The decisive factor in determining the place of supply of goods is whether the goods are dispatched or transported in the course of the supply. In case transport takes place in the course of the supply, the place of supply is where the transport of the goods begins (see Article 32 VAT Directive).[67] If the goods are not dispatched or transported, the place of supply is the place where the goods are located at the time when the supply takes place (see Article 31 VAT Directive). In that situation, a Member State can only levy its own national VAT rate if goods are located within its borders at the time when the supply takes place.

Example 5: A local supply of goods

Susan buys a radio alarm clock at a store in Latvia.

The store is a taxable person and supplies a radio alarm clock (a good) for consideration to Susan. The place of supply is where the good is at the time of the supply because the radio alarm clock is not transported in the course of the supply. Here, the place of supply is Latvia. The VAT Directive does not provide an exemption for this kind of supply, so the store must charge the standard Latvian VAT rate on the supply of the radio alarm clock to Susan. However, if the radio alarm clock is transported in relation to the supply (for example, the store mails it to Susan's house in Riga, Latvia),

67 Special place of supply rules apply to supplies by the importer and subsequent supplies, supplies of goods with installation and assembly, supplies of goods on board ships, aircraft or trains and supplies of goods through distribution systems (gas, electricity).

then the place of supply is where the transport begins.[68] In this case the place of supply does not change because the transport beings at the radio alarm clock store which is located in Latvia. Susan will still be charged Latvian VAT at the standard VAT rate.

Example 6: A cross-border supply of goods
An Italian bakery stores its inventory of frozen pizzas in a refrigerated warehouse in Rotterdam, the Netherlands. The Italian bakery sells the pizzas from this warehouse to a restaurant in Bruges, Belgium. The pizzas are delivered to Bruges with a special truck.

The Italian bakery is a taxable person (Article 9 VAT Directive) and supplies the pizzas (goods) to a restaurant in Bruges (Belgium) in its capacity as a taxable person for consideration. The pizzas (goods) are transported from the Netherlands to Belgium, so the place of supply is the place where the transport begins, the Netherlands.[69]

Because this supply involves the physical transport of goods from one Member State to the other (intra-Community supply), and the customer is a taxable person acting as such, an exemption with the right of deduction is applicable (Article 138(1), VAT Directive). The Italian bakery is required to file a tax return for VAT in the Netherlands to report the intra-Community supply. The Italian bakery is still required to file the return even though it does not charge VAT. The Belgian restaurant carries out an intra-Community acquisition of goods and must self-assess Belgian VAT on its Belgian VAT return.

6.1.2 Distance Sales

Since 1 July 2021, the VAT Directive contains a specific regime (the distance sales scheme) which applies to cross-border business to consumer (B2C) supplies of goods whereby the goods are dispatched or transported by or on behalf of the supplier. A distinction is made between EU distance sales[70] and non-EU distance sales[71].

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68 Please note that this is not a so-called distance sale, because the goods are not transported cross-border in the course of the supply.

69 Again, this is not a distance sale, because it is a B2B supply of goods.

70 'Intra-Community distance sales of goods'.

71 'Distance sales of goods imported from third territories or third countries'.

EU Distance Sales

If the main rules on the place of supplies of goods were to apply to cross-border B2C supplies whereby the supplier transports the goods from one Member State to the Member State of the consumer, the VAT of the Member State of departure of the goods would apply. Since the VAT rates in the EU have not been harmonized, strict adherence to this manner of taxation would lead to VAT rate shopping by private consumers. This is the main reason for the EU distance sales regime.

An EU distance sale is a cross-border, intra-EU supply of goods to a consumer.[72] It requires that the goods are dispatched or transported by or on behalf of the supplier[73] from a Member State other than that in which dispatch or transport of the goods to the customer ends (Article 14(4), para. 1 VAT Directive).

The place of supply of intra-Community distance sales of goods shall be deemed to be the place where the goods are located at the time when dispatch or transport of the goods to the customer ends, which is typically the place where the customer resides (Articles 33(a) and 59c VAT Directive).[74] This means that the supplier must charge the local VAT of the customer's Member State on its supply. To facilitate the filing of VAT return(s) and the payment of VAT to the tax authorities in the customer's Member States, the supplier may[75] apply the so-called 'One Stop Shop' ('OSS'). This special scheme entails that the supplier may register for VAT in one Member State and then file, through the tax authority's online portal of that Member State submit its OSS filing and pay the VAT due in the (various) customer's Member States.

Non-EU Distance Sales

A non-EU distance sale is also a B2C cross-border supply of goods to a consumer. The essential difference with EU distance sales is that a non-EU distance sale covers the supply of goods, transported or dispatched of from a third territory or third country, to a customer in a Member State. A distinction is made to non-EU distance sales in a 'two countries situation' and those in a 'three countries situation'.

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72 The term consumer in this respect covers non-taxable persons as well as taxable persons and non-taxable legal persons, whose intra- Community acquisitions of goods are not subject to VAT.

73 This includes the situations in which the supplier intervenes indirectly in the transport or dispatch of the goods.

74 An annual EUR 10,000 turnover applies, up to which the place of supply remains in the Member State where the transport of the goods begins.

75 Once the OSS is applied, it must be applied for all EU distance sales.

A two countries situation exists if the transport of the goods to the customer ends in the same Member State as in which they enter the EU. In that situation, the place of supply is in that Member State, provided that the non-EU distance sale is reported through the so-called 'Import OSS scheme' (also referred to as the 'Import Scheme'). It is important to realize that this scheme does not relate to the reporting or the payment of VAT upon importation of the goods in the EU (which is a taxable event separate from the supply of the goods), but to the reporting and the payment of VAT on the supply (the distance sale) of the goods. If the Import OSS scheme (iOSS) is applied, under Article 143(1)(ca) VAT Directive an exemption applies to the importation. Only goods that have a value an intrinsic value not exceeding EUR 150 can be reported through the iOSS.

A three countries situation exists if the goods are imported in a Member State different from the Member State in which the transport or dispatch of the goods to the customer ends. In that situation, the place of supply is in the latter Member State, regardless of whether the supplier applies the iOSS (Article 33(c) VAT Directive). The importation of the goods into the EU is exempt from VAT, if the iOSS is applied (which is only possible if the goods have a value an intrinsic value not exceeding EUR 150).

6.2 The Place of Supply of Services

With regard to the place of supply of services, there are two main rules. The first applies to services rendered to taxable persons or customers regarded as such for the purpose of applying the place of supply of services rules (B2B supplies), the second to services rendered to non-taxable persons (B2Csupplies). Each of these main rules has its own set of exceptions.

The scope of the place of supply rules is not limited to EU service suppliers and recipients. Therefore, these rules not only apply to services by or to (legal) persons established / residing in the EU, but also to services supplied by / to a (legal) person established / residing outside the EU.

6.2.1 Services Supplied to Taxable Persons (B2B-Services)

The main rule for B2B services is that if a taxable person supplies a service to another taxable person, the place of supply is where the recipient's business is established or where the recipient has its fixed address or usually resides (Article

44 VAT Directive).[76] This main rule ensures that the right to levy VAT is allocated to the country where consumption of the service is likely to take place. If the main rule is applied, Article 196 VAT Directive stipulates that the reverse charge mechanism applies (see Chapter 9). The application of this mechanism prevents the supplier from having to register for VAT in in the Member State where the customer is located, charge local VAT and remit that VAT on a local VAT return. The reverse charge mechanism shifts the liability (not the place of the supply) to pay VAT (i.e., VAT liability) from the person who supplies the service to the person who receives the service. The recipient of a service (customer) then becomes liable to pay and remit VAT to the tax authorities in the country where the supply takes place. (See also below). The customer must self-assess the VAT on the supplied service and report it in his VAT return. If the purchaser has a right to deduct (see Chapter 10), he can deduct the VAT on the same VAT return. Consequently, even though he must report the (purchase of the) services in his VAT return, he will not be required to actually pay the VAT to the tax authorities. Please note that if the B2B main rule for the place of supply of services applies, the supplier is still required to report the supply in a periodic 'recapitulative statement' (see Chapter 12)

Example 7: A cross-border B2B service
A Japanese law firm advises a Fabryka Group Poland, a Polish company on the possibilities to incorporate a Japanese subsidiary (Fabryka Group Ltd.). Both the law firm and Fabryka Group Poland are taxable persons for VAT.

The place of supply of the service (legal advice) is determined on the basis of the B2B main rule (cf. Article 44 VAT Directive) and is Poland – since Fabryka Group Poland is established there. The VAT liability as regards the service is shifted from the supplier (law firm) to Fabryka Group Poland as customer (see Article 196 VAT Directive). Fabryka Group Poland will report the service in its Polish VAT return, self-assess VAT, and subsequently deduct the VAT on the same VAT return. Consequently, even though he must report the (purchase of the) services in his VAT return, he will not be required to actually pay the VAT to the tax authorities. This would be different in case Fabryka Group Poland would not have a (full) right of deduction of input VAT. In any case, the law firm does not have to register for VAT purposes in Poland to report the service, as Fabryka Group Poland does this.

There are various exceptions to the main rule of Article 44 VAT Directive. The overview below provides an overview of the B2B main rule and the exceptions thereto:

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76 According to Article 44 VAT Directive, if services are provided to a 'fixed establishment' of a taxable person located in a place other than the place where the taxable person has established his business, the place of supply of those services shall be the place where that fixed establishment is located. However, it is not the place to discuss such particularities here.

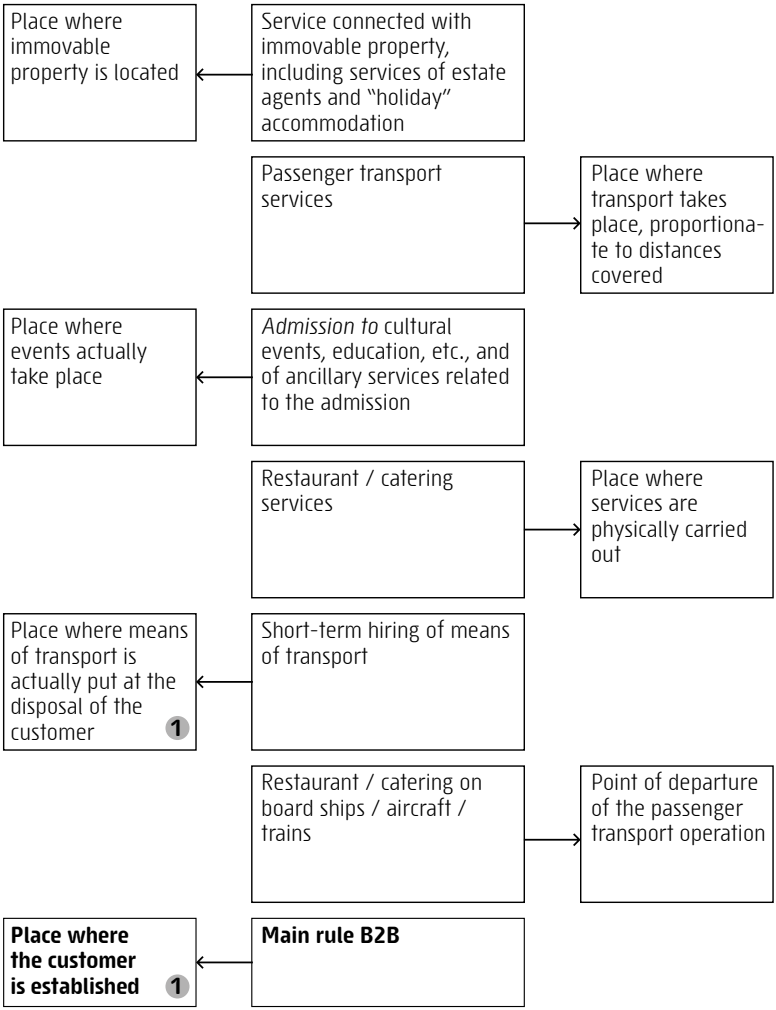


Figure 3: Overview place of supply rules B2B services.[77]

77 See: Ad van Doesum, Herman van Kesteren Simon Cornielje and Frank Nellen, 2020, Fundamentals of EU VAT Law, Alphen aan den Rijn: Kluwer Law International, p. 199.

Key to figure 3:

1. *If a Member State implements the effective use and enjoyment rules (Article 59a VAT Directive), the place of supply is where the effective use and enjoyment of the service takes place.*

6.2.2 Services Supplied to Non-taxable Persons (B2C Services)

The main rule for services to non-taxable persons (B2C) is that the place of supply of the service is where the supplier has established his business (Article 45 VAT Directive).[78] For practical reasons, the legislator chose to tax (cross-border) services at the place where the supplier is established or resides rather than where the consumption is likely to take place. To partly mitigate the implications of this choice – which is contrary to the legal nature of VAT as a tax on consumption – there are various situations in which exceptions to this main rule apply. Examples are: services connected with immovable property, advisory services (and other intellectual services) supplied to non-EU recipients, admission to cultural and artistic events, etc.

Example 8: A cross-border B2C service

Daphne, who just moved from Bonn to Hamburg (Germany), is looking for a nice picture to put up against the wall of her living room. A Russian photographer (established in Moscow) sells a license to use a picture he has once made to Daphne. The Russian photographer is a taxable person for German VAT purposes, but Daphne is not.

The B2C main rule of Article 45 VAT Directive applies here, the place of supply is located outside Germany, so the photographer does not charge (German) VAT. No reverse charge mechanism applies.

As is the case with the main rule for B2B supplies of services, there are also various exceptions to the main rule for B2C supplies of services. The overview below outlines the B2C main rule and the exceptions thereto:

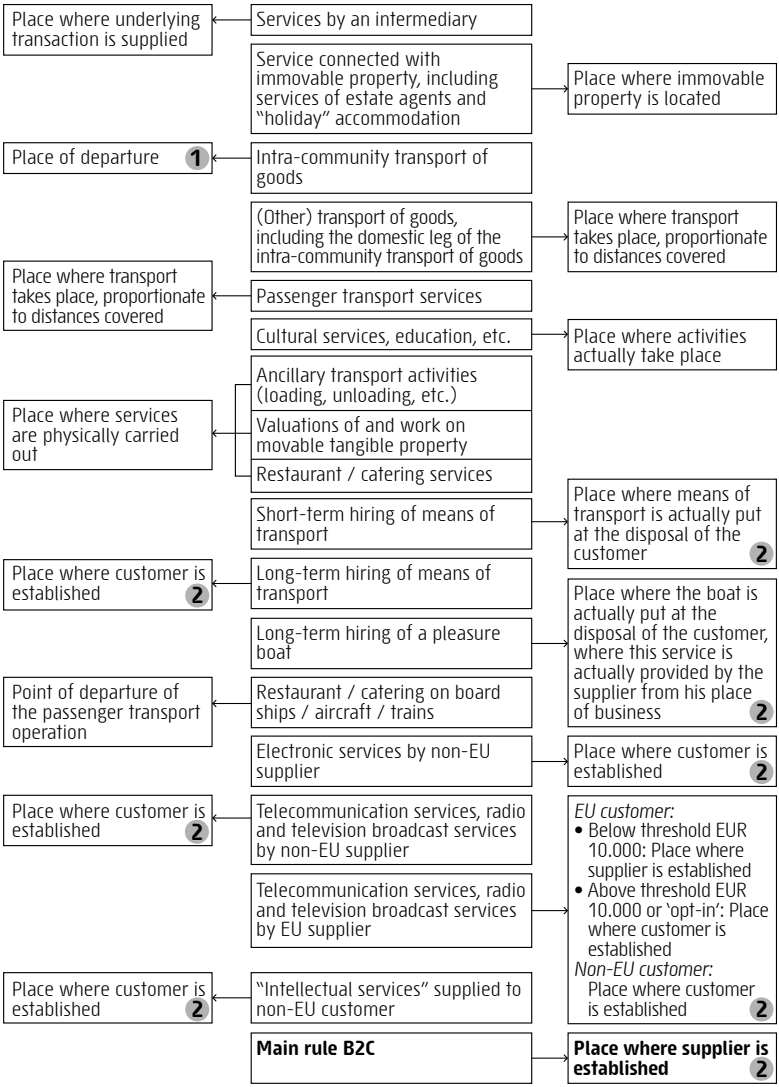
Key to figure 4:

1. *Member States need not apply the tax to that part of the intra-community transport of goods to non-taxable persons corresponding to journeys made over water, which do not form part of the territory of the Community (Union).*

2. *If a Member State implements the effective use and enjoyment rules, the place of supply is where the effective use and enjoyment of the service takes place.*

78 Again, the place of supply may be different if the recipient has a fixed establishment in another Member State. Discussing such particularities goes beyond the scope and purpose of this book.

Figure 4: Overview place of supply rules B2C services.



If a non-EU supplier supplies a B2C service which, based on the place of supply rules outlined above, is to be situated in an EU Member State, the supplier can make use of a one stop mechanism. The one stop shop scheme (in this context referred to as the 'non-Union scheme') allows non-EU taxable persons to account for the VAT on those services via a web-portal in the Member State in which they are identified for VAT. This prevents them from having to register for VAT in each and every Member State where their customers are located. If a supplier opts to use the non-Union scheme, he must use the scheme to declare and pay VAT for *all* these services in the EU. A similar OSS mechanism applies if an EU supplier provides B2C services which are, based on the place of supply rules, situated in a Member State other than in which the supplier is established (this OSS mechanism is commonly referred to as the 'Union scheme'.

6.3 Electronic services

The taxation of B2C electronic services in VAT/GST poses particular difficulties: how can the place of consumption be determined and how can VAT/GST effectively be levied on such services, without causing too heavy administrative burdens for businesses? The EU VAT Directive contains a balanced mechanism to tax electronic services.

The place of supply of electronically supplied services (as well as telecommunication and radio and television broadcasting services) is located in the customer's country (taxation on the basis of the destination principle). To simplify the levying of VAT, both EU and non-EU suppliers of such services to non-taxable persons resident in the EU can apply the so-called one-stop shop scheme.

Annex II to the VAT Directive contains a list of the services which are considered as being electronically supplied services. This list is non-exhaustive. Service providers will have to assess whether their services qualify as electronically supplied services. In that regard, they can refer to Article 7 VAT Regulation, which defines 'electronically supplied services' as services which are delivered over the internet or an electronic network and the nature of which renders their supply essentially automated and involving minimal human intervention, and impossible to ensure in the absence of information technology. Moreover, this provision includes a more detailed list of services that are, and are not, to be regarded as electronically supplied services. Article 7(2)(f) VAT Regulation refers to Annex I of the VAT regulation, which contains further examples of electronically supplies services.

The VAT Regulation also contains several presumptions and evidence rules on the basis of which it may be determined whether the customer is a taxable person and in which Member State he is located. Article 9a VAT Regulation sets out specific rules with respect to the supply of electronic services via a 'platform', such as a marketplace for applications. In essence, these rules mean that by law fiction the platform is not seen as a broker, but as a party that buys and sells.

6.4 The Place of Importation

With respect to all four taxable transactions, it is necessary to determine which country can levy VAT. This is no different for importation (one of the four taxable transactions - or better: taxable events). As a main rule, Article 60 VAT Directive determines that the place of importation is where the goods are located when they (physically) enter the Community.

6.5 The Place of an Intra-Community Acquisition

In Chapter 5 we indicated that an intra-Community acquisition is always coupled with an intra-Community supply. The place of the intra-Community supply is where the transport of the goods begins (see Article 32 VAT Directive, discussed in Chapter 5). Since an exemption with the right of deduction applies – see Article 138(1) VAT Directive – the intra-Community supply is effectively not taxed in the Member State where the transport begins.

However, in the Member State where the intra-Community acquisition takes place, VAT indeed becomes chargeable because the taxable person acquiring the goods carries out a taxable event in its own right: the intra-Community acquisition of goods. The place of an intra-Community acquisition is where the transport of the goods to the person acquiring them ends (Article 40 VAT Directive). If the acquirer has a full right of deduction, he can deduct the VAT on the intra-Community acquisition in the same VAT return as the one he reports the acquisition in. Consequently, even though he must report the intra-Community acquisition in his VAT return, he will not be required to actually pay the VAT to the tax authorities.

In a way, the rules with respect to the intra-Community acquisition of goods are similar to those concerning the reverse charge mechanism. However, there is a fundamental (technical) difference. The intra-Community acquisition is a taxable transaction (event) in its own right, carried out by the acquirer of the goods. The reverse charge mechanism only shifts the liability to the pay VAT on a supply carried out by the supplier from the supplier to the customer. It does not create a taxable event at the level of the customer.

In late 2017, the European Commission has proposed new VAT legislation which aims to gradually overhaul the current system of intra-Community supplies and acquisitions. The central premise of the 'new intra-Community system' is to apply the destination principle to intra-EU supplies of goods, meaning that the supplier of the goods will have to charge VAT in the Member State of destination of the goods against the VAT rate applicable there. A proposal containing the full details of these plans was presented in 2018. Political agreement on the acceptability of the revised system has not been reached since and it appears that the legislative procedure is on hold.

7. Taxable Amount and VAT Rates

If a taxable person carries out a taxed supply of goods or service, he must determine how much VAT is to be mentioned on the invoice (unless the reverse charge mechanism applies) and to be reported in the VAT return. To be able to do this, the taxable person is required to determine 1) the amount on which VAT is due (taxable amount) and 2) the VAT rate. We will discuss the taxable amount in section 7.1 and the VAT rates in section 7.2.

7.1 Taxable Amount

Since VAT ultimately aims to tax consumption by private individuals, the taxable amount of a supply must be as close as possible to the value of the consumption. Arguably, the value of consumption is best approximated by the spending power that the consumer sacrifices to obtain the good or service to be consumed. However, because VAT taxes transactions, it was decided to use the consideration for the supply as the taxable amount. Therefore, Article 73 VAT Directive stipulates that the taxable amount for supplies of goods and services is everything which constitutes consideration obtained or to be obtained by the supplier, in return for the supply, including subsidies directly linked to the price of the supply.

This principle uses a subjective approach to the valuation of a transaction, not an objective one. The initial price paid is the starting point for determining the taxable amount. If the price of the good or service supplied is later adjusted (through discounts, a promotion, etc.), the taxable amount can also be adjusted under certain conditions. All this implies that if parties agree on a consideration (price) which is lower than usual (i.e., lower than an objective market value), this consideration is still the taxable amount for VAT. Nonetheless, we note that the VAT Directive allows Member States, in certain situations and under certain conditions, to change the taxable amount to the 'open market value' – e.g., if affiliated parties engage in tax evasion or avoidance (see Article 80 VAT Directive).

7.2 VAT Rates

Member States are required to apply a standard VAT rate which should be at least 15% of the taxable amount (Article 96 and 97 VAT Directive). Further, Member States may apply one or two reduced rates to certain specified goods or services (98 to 101 VAT Directive, also see Annex III). Member States often apply reduced rates to goods or services which they regard as life necessities (foodstuffs or medical supplies) or services that require a high degree of manual labor (hair-

dressing, reparations of clothes, window and house cleaning). The VAT rates apply to supplies of goods and services as well as to the importation and the intra-Community acquisition of goods.

The applicable VAT rate is often not of practical importance for B2B transactions, as most taxable persons can deduct VAT which is charged to them. However, the application of the correct VAT rate is indeed important in the last stage of the production and distribution chain (i.e., at the retail level) and in situations in which the respective taxable person does not have a full right to deduct (e.g., in case he carries out exempt transactions).

It is important to note that the exportation of goods and the intra-Community supply of goods are also taxable transactions but are effectively zero-rated (an exemption with the right to deduct applies). See Articles 138 and 146(1)(a) VAT Directive in combination with Article 169(b) VAT Directive.

8. Exemptions

The EU VAT is a general tax which aims to tax the consumption of all goods and services. Exemptions should in principle not be part of such a consumption tax. Nevertheless, the VAT Directive contains various exemptions which imply that no VAT becomes chargeable whenever a transaction is carried out which falls inside the scope of one of the exemptions.

A notable consequence of many exemptions in the VAT Directive is that the taxable person carrying out the exempt supply has no right of deduction on input VAT on costs which are (directly) related to that supply. However, there are essentially two types of exemptions: exemptions for which the taxable person carrying out the exempt supply does not have a right of deduction and exemptions for which he does have a right of deduction. We will discuss both basic types below.

8.1 Exemptions Without a Right of Deduction

Chapter 2 and Chapter 3 of the VAT Directive contain the exemptions for which in principle no right of deduction exists. Article 132 VAT Directive lists the exemptions for certain activities in the public interest. Examples are exemptions for supplies by the public postal services, hospital and medical care, supplies of services closely linked to welfare and social security work, education, and childcare. Article 135 VAT Directive contains a variety of 'other exemptions', such as exemptions for insurance transactions, the granting and negotiation of credit, management of special investment funds, transactions in shares, interests in companies or associations, debentures and other securities. The supply of a building or parts thereof and land which has not been built on (not being building land), is also exempt.

In general terms, the exemptions in VAT were conceived partially to prevent that VAT would increase the cost base of certain transactions (e.g., healthcare), and also because it would be practically difficult to impose taxation on other transactions (e.g., financial services). The exemption for the supply and renting out of immovable property, as well as the exceptions to this exemption, are based on the notion that immovable property is an asset with a long life span which can be used both for productive and consumptive purposes. Nevertheless, the exemptions, despite their existence, do not fit well with the legal nature of VAT as a general tax on consumption. This is one of the reasons that the CJEU has ruled that the exemptions should be interpreted strictly.[79]

If one of the exemptions mentioned in Article 132 or 135 VAT Directive applies, the taxable person carrying out the supply should not charge VAT to its customer. A consequence of the application of the exemption is that the taxable person has in principle no right to deduct the VAT he paid (input VAT) on the goods and services purchased in relation to his own exempt output transaction.[80] Article 168 VAT Directive clearly states that a right of deduction only exists in so far as the purchased services and goods are used for the purposes of taxed transactions. In case a taxable person uses purchased goods and services for his own exempt transactions, the input VAT paid on the purchases thus represents a cost for this supplier. It can be considered paradoxical that a taxable person making taxed supplies is completely relieved of the burden of VAT (through the right of deduction of input VAT), whereas the taxable person making exempt supplies in fact bears a burden of VAT (since he cannot deduct the input VAT).

A VAT exemption only works properly if the taxable person carrying out the exempt supplies incurs little or no input VAT. In the current market economy, this is not very common anymore. In fact, in case an exemption is applied within a supply chain consisting of taxable persons carrying out taxed transactions, a more likely result is that VAT will accumulate, meaning that VAT is charged on a taxable amount which already includes a certain amount of hidden VAT. This happens if a taxable person A carries out an exempt supply to another taxable person, B. Since A has no right of deduction of input VAT, he includes ('hides') the non-deduct-

79 See for example: CJEU 15 June 1989, Case 348/87, Staatssecretaris van Financiën v Stichting Uitvoering Financiële Acties, CJEU 5 June 1997, Case C-2/95, Sparekassernes Datacenter (SDC) v Skatteministeriet, [1997] ECR I-03017 and CJEU 6 November 2003, Case C-45/01, Christoph-Dornier-Stiftung für Klinische Psychologie v Finanzamt Gießen, [2003] ECR I-12911.

80 Article 169 VAT Directive contains exceptions to this principle. For example, subject to conditions the VAT paid on goods and services used for exempt banking, financial and insurance transactions to non-EU customers is deductible (Article 169(c) VAT Directive.

ible VAT on his own purchases in the price he charges to B. Subsequently, if B carries out a taxed supply to a final consumer, and uses the supply by A for his own supply, VAT is charged by B on a price which already includes the hidden VAT. Such cascading of VAT (VAT on VAT) is undesirable, and contrary to the principle of neutrality – but is a given outcome of the current VAT system in which exemptions without a right of deduction are a given.

8.2 Exemptions With a Right of Deduction

The VAT Directive not only contains exemptions without a right of deduction, but also exemptions for which a right of deduction indeed exists. Examples are the exemption for intra-Community supplies of goods (Article 138 VAT Directive) and the export supplies of goods (Article 146(1)(a) VAT Directive). Article 169(b) allows deduction of input VAT in relation to such 'exempt' supplies. An exemption with the right of deduction (implemented as a 'zero rate' by some Member States) allows the supplier carrying out a ´cross-border´ supply to a) not charge VAT on his supply, and b) deduct any input VAT on costs related to the supply. The goods thus arrive in the country of destination VAT-free, i.e., without any VAT burden (hidden or real) imposed by the country of origin. In fact, this is how a 'true' VAT exemption functions. The reason for the existence of such exemptions is that they enable taxable persons carrying out economic activities to compete on the global market without being hampered by a VAT burden on their national exports. An exemption with a right of deduction is more in line with the legal nature of VAT than an exemption without a right to reduction because it ensures that cascading of VAT does not occur.

9. The Person Liable for Payment of VAT

In this chapter, we explain the rules on the appointment of the person who is liable to pay the VAT on a supply to the tax authorities.

9.1 Main Rule

Normally, the person who carries out the taxable transaction (the supply of goods or services, the intra-Community acquisition or the importation) is also the person who is liable to pay VAT to the tax authorities and to report it on a VAT return. As regards the supply of goods and services, Article 193 VAT Directive stipulates that VAT shall be payable by any taxable person carrying out a taxable supply of goods or services. We refer to Articles 200 and 201 VAT Directive for intra-Community acquisitions and importations, respectively.

9.2 The Reverse Charge Mechanism

In Chapter 6, we already mentioned that there are situations in which a different person than the taxable person carrying out the supply is liable to remit VAT to the tax authorities. Generally, this other person is the customer or recipient, i.e., the (taxable) person acquiring or purchasing the goods or services. This shifting of the VAT liability is commonly referred to as the 'reverse charge mechanism'.

For example, Article 196 VAT Directive states that VAT shall be payable by the person to whom services referred to in Article 44 VAT Directive (i.e., so-called B2B main rule services) are supplied.[81] Article 194 VAT Directive allows Member States to also apply the reverse charge mechanism in other situations where the taxable supply of goods or services is carried out by a taxable person who is not established in the Member State in which the VAT is due. That way it can be prevented that foreign companies must register for VAT in the Member State where their supply is considered to take place (see Chapter 6, on the place of supply rules). Moreover, from a tax authorities' perspective it is often easier to audit (and/or assess) a company established in their own country than to audit (and/or assess) a company established in another country.

If a person other than the supplier is liable for VAT, the supplier should not charge VAT on the price of the goods or services supplied. Instead, the customer self-assesses the VAT due on the supply and reports it in his own VAT return. In the same

81 Under the condition that the supplier is not established in the Member State in which the recipient is established.

VAT return, he can deduct this self-assessed VAT as input VAT, insofar he uses the goods or services for carrying out purposes for which a right of deduction exists. The overall outcome of a VAT return solely containing such reverse charged supplies, is that effectively, no VAT is payable. Such a return is completed purely for administrative reasons if no other transactions are to be reported.

10. The Right of Deduction of Input VAT

This chapter deals with the 'cornerstone' of the VAT system, the right of deduction.

10.1 Introduction

The right to deduct input VAT ensures that the burden of the VAT is not carried by taxable persons. It may in principle not be limited.[82] The right is an essential element of VAT: the CJEU has on occasion referred to it as the cornerstone of the VAT system.

Article 168 of the VAT Directive allows taxable persons to deduct input VAT in so far as the goods and services they purchased are used for the purposes of their own taxed transactions. For a right of deduction to exist, the input transactions must have a direct and immediate link with the output transactions giving rise to a right of deduction.

The word 'taxed' in Article 168 VAT Directive implies that no right of deduction exists for input VAT on purchased goods and services which are used for exempt transactions. In this case the input VAT is a business expense. In Chapter 9 we already explained that this is the paradoxical character of VAT: A taxable person who makes a taxed supply is not affected by VAT (because of his right to deduct input VAT), whilst a taxable person who makes an exempt supply carries the burden of VAT (because he cannot deduct input VAT).

10.2 Proportional Deduction

If a taxable person buys goods or acquires services which he uses both for taxed and exempt supplies, he can deduct only a portion of the input VAT. For practical reasons, the deductible portion of input VAT (the so-called pro rata percentage) is in principle based on turnover proportions. The deductible input VAT is calculated following the formula detailed in Article 174 VAT Directive: turnover for which a right of deduction exists (numerator), divided by total turnover (denominator). Member States may use slightly different approaches. For example (but not limited to), Member States may authorize or require a calculation of the propor-

82 CJEU 26 May 2005, Case C-465/03, Kretztechnik AG v Finanzamt Linz, [2005] ECR I-04357, CJEU 13 March 2008, Case C-437/06, Securenta Göttinger Immobilienanlagen und Vermögensmanagement AG v Finanzamt Göttingen, [2008] ECR I-1597, CJEU 4 June 2009, Case C-102/08, Finanzamt Düsseldorf-Süd v SALIX Grundstücks-Vermietungsgesellschaft mbH & Co. Objekt Offenbach KG, [2009] ECR I-04629 and CJEU 29 October 2009, Case C-29/08, Skatteverket v AB SKF, [2009] ECR I- 10413.

tional deduction for each sector of a taxable person's business (Article 173(2)(a and b) VAT Directive or on the basis of the use made of all or part of the goods and services (Article 173(2)(c) VAT Directive). The example below explains the calculation and application of the 'standard' pro rata method of Article 174 VAT Directive.

Example 9: Pro rata deduction
A Dutch bank grants interest bearing loans to private persons in the Netherlands. The granting of interest-bearing loans is exempt from VAT (Article 135 paragraph 1 sub b VAT Directive). For this kind of activity no right of deduction exists. The bank also provides financial advice to its clients, but there is no VAT exemption applicable to the supply of such services. Therefore, for these services a right of deduction does exist. The turnover of the loans (interest) that the bank receives is 2,000,000 euro. The turnover generated with the advisory services is 6,000,000 euro. The bank buys a computer which it will use for the granting of interest-bearing loans and for supplying financial advice. The bank paid 1,000 euro + 200 euro VAT = 1,200 euro for the computer.

Because the computer is used for both VAT exempt and non-exempt activities, the input VAT on the computer must be deducted on a pro rate base (proportional deduction). The pro rata deduction is equal to the turnover for which a right of deduction exists, divided by total turnover: 6,000,000 / (6,000,000 + 2,000,000) = 0,75 (75%). The bank may deduct 150 euro (i.e., 75% of the 200 euro paid in VAT on the purchase of the computer).

10.3 Adjustment of Deductions

As regards capital goods, Article 184 VAT Directive lays down a special system of adjustment of the input VAT that a taxable person initially deducted. Based on this provision, the initial deduction shall be adjusted where it is higher or lower than that to which the taxable person was entitled. It is left to the Member States to lay down the detailed rules for applying the so-called adjustment-rules.

The adjustment rules allow for adjustments to the initial deduction of input VAT if, at a later stage, but within a certain period (the so-called 'adjustment period)', the use of the goods changes from usage for supplies for which a right of deduction exists to supplies for which no right of deduction exists and vice versa. This special adjustment regime for capital goods is explained and justified by the durability of those goods and the attendant writing-off of their acquisition costs.[83] The goal and purpose of these rules is to ensure the accuracy of deductions and hence the

83 CJEU 15 December 2005, Case C-63/04, Centralan Property Ltd v Commissioners of Customs & Excise, [2005] ECR I-11087.

neutrality of VAT. The adjustment rules make it possible to avoid inaccuracies in the calculation of deductions and unjustified advantages or disadvantages for a taxable person where, in particular, changes occur in the factors initially taken into consideration in order to determine the amount of deductions after the initial deduction has been made. The likelihood of such changes is particularly significant in the case of capital goods, which are often used over a number of years, during which the purposes for which they are used may alter.[84]

The annual adjustment of input VAT must be made in respect of one-fifth of the VAT charged on the capital goods, or if the adjustment period has been extended, in respect of the corresponding fraction thereof. In the case of immovable property, Member States may extend the adjustment period up to 20 years.

10.4 Deduction and Private Use

On the basis of Article 176 VAT Directive, Member States may retain exclusions of deduction which were in effect on January 1, 1979, or, in case the respective state acceded to the Community at a later date, from that date onwards. The Netherlands, for example, have traditionally excluded consumptive expenses (food and drinks) in restaurants, bars and hotels from deduction. The reasoning is that VAT on such consumptive expenses should not be deductible, even if the lunch or dinner is held during a business meeting, because the personal benefit of such expenses outweighs that of the business (at least, according to the Dutch legislator).

To correct for private application or usage of other goods and services, Article 16 VAT Directive VAT Directive contains an alternative approach. If the VAT on goods or the component parts thereof was wholly or partly deductible, the application by a taxable person of such goods forming part of his business assets for private use or purposes other than those of his business is treated as a supply of goods for consideration (see Article 26 VAT Directive for services). The taxable person privately consuming the good or service is not able to deduct the VAT on this taxed 'deemed service', and in this way, consumption does not go untaxed after all.

Full input VAT deduction is not possible if a taxable person purchases immovable property, which he uses partly for his business purposes and partly for his private purposes, even though he labeled the immovable property as a business asset

84 CJEU 30 March 2006, Case C-184/04, Uudenkaupungin kaupunki, [2006] ECR I-03039.

for VAT purposes.[85] Article 169(a) provides that in the case of immovable property forming part of the business assets of a taxable person and used both for purposes of the taxable person's business and for his private use or that of his staff, or, more generally, for purposes other than those of his business, VAT on expenditure related to this property shall be deductible only up to the proportion of the property's use for purposes of the taxable person's business. During the so-called 'adjustment period' (five to twenty years, see section 10.3), the initial deduction will be adjusted where it is higher or lower than that to which the taxable person was entitled. Each year one-fifth (or up to one-twentieth, depending on the duration of the adjustment period) of the VAT charged on the immovable property, is adjusted. Member States may apply the same mechanism to other goods forming part of the business assets (Article 169(a)(2) VAT Directive).

Example 10: Deemed Supply
A baker takes a loaf of bread from his bakery to eat at home.

The baker is a taxable person, and he is considered (internally) supplying a good to himself in his private capacity as a non-taxable person. Based on Article 16 VAT Directive, VAT must be charged on this 'internal supply', reported on his VAT return, and paid to the tax authorities. This prevents the 'free' loaf of bread from being consumed untaxed.

In case a Member State has not made use of the option provided for in Article 168(a)(2) VAT Directive, taxable persons who buy movable goods which they use both for private and business purposes can fully label the goods as business assets. Then, they can fully deduct the VAT on the purchase of the good (assuming they meet the regular conditions for the deduction of input VAT). Articles 16 and 26 VAT Directive again function to ensure that private consumption does not remain untaxed. To the extent that the taxable person uses the goods for his private purposes, a deemed supply takes place.

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85 If an item is used for both business and private purposes the taxable person may choose to allocate this item in full, or in part, to either his business and/or his private assets. See, for example: CJEU 11 July 1991, Case C-97/90, Hansgeorg Lennartz v Finanzamt München III, [1991] ECR I-03795, CJEU 8 March 2001, Case C-415/98, Laszlo Bakcsi v Finanzamt Fürstenfeldbruck, 2001 ECR I-01831, and CJEU 8 May 2003, Case C-269/00, Wolfgang Seeling v Finanzamt Starnberg, [2003] ECR I-04101.

10.5 Non-Taxable Activities

Because the VAT Directive provides for a right of deduction only for transactions which are used for the purposes of taxed transactions, the wording of Article 168 VAT Directive seems to suggest that a taxable person carrying out non-taxable activities (i.e., transactions outside the scope of VAT, such as a supply not for consideration, the issuing of shares, or the transfer of a going concern - see Chapter 5) does not have a right to deduct input VAT. However, based on CJEU case law there may still be a right of deduction, insofar as the purchases have a direct and immediate link with the whole economic activity of the taxable person.[86]

86 See, for example: CJEU 26 May 2005, Case C-465/03, Kretztechnik AG v Finanzamt Linz, [2005] ECR I-04357.

11. The Process of Levying VAT

If a taxable person is required to charge VAT on a supply, he must also determine when that VAT becomes payable to the tax authorities. The chargeable event occurs and VAT becomes chargeable when the goods or the services are supplied (Article 63 VAT Directive). In case a payment is made before the goods or services are supplied, VAT however becomes chargeable upon receipt of that payment. Article 66 VAT Directive allows Member States to derogate from the main rule in Article 63 VAT Directive, as it states that they can determine that VAT becomes chargeable at one of the following times:

- No later than the time the invoice is issued;
- No later than the time the payment is received.

Where an invoice is not issued, or is issued late, within a specified period from the date of the chargeable event.

According to Article 206 VAT Directive, any taxable person liable for payment of VAT must pay the net amount of the VAT when submitting the VAT return. Article 250 VAT Directive states that every taxable person is required to submit a VAT return setting out all the information needed to calculate the tax that has become chargeable and the deductions to be made. In general, this implies that taxable persons report (among others) their taxed transactions as well as the deductible input VAT. The net of the payable and deductible VAT is paid to the tax authorities, or, if resulting in a negative amount, received back from the tax authorities. The tax authorities are generally authorized to check the filed VAT returns and impose additional VAT assessments (possibly including fines and interest) on taxable persons in case it becomes clear that the VAT return was filed incorrectly.

The examples below show the basics of how VAT is reported in a VAT return.

Example 11
*Paul and Francesco own a company that sells bottles of beers and snacks to private individuals. The company is a taxable person for VAT (the legal form is not relevant in VAT, see Chapter 4). All supplies take place in a Member State where the standard VAT rate is 21% and the reduced VAT rate is 6%. The company sold 1,600 bottles of beers for 2.16 euro each (price inclusive of VAT). Therefore, the total turnover inclusive of VAT from the sales of beer is 3,456 euro. In this Member State, beer is taxed against the standard VAT rate (21%). The total VAT included in the supplies of beer is 21/121 * 3,456*

*euro= 600 euro. The company also supplied 200 snacks for 4.24 euro each (inclusive of VAT). The total turnover, inclusive of VAT from the snack is therefore 848 euro. The snacks were subject to a reduced VAT rate of 6%. The total VAT charged on the snacks is equal to 848 * 6/106=48 euro. Paul and Francesco paid 300 euro of input VAT on the beers they purchased from the brewer and 15 euro of input VAT on the snacks they purchased from a supermarket.*

Description	***Turnover***	***VAT***
Supplies/services taxed at 21%	*3,456*	*600*
Supplies/services taxed at 6%	*848*	*48*
Total VAT payable		*648*
Input VAT (deductible VAT)		*-/-315*
Total amount due or to be refunded		*333*

Example 12

As under Example 12, but now Paul and Francesco also invested in a new bar which they purchased for 10,000 euro + 2,100 euro VAT. Paul and Francesco may deduct input VAT on their purchase. The total input VAT on their VAT return now exceeds their total output VAT. The tax authorities owe Paul and Francesco a repayment of VAT.

Description	***Turnover***	***VAT***
Supplies/services taxed at 21%	*3,456*	*600*
Supplies/services taxed at 6%	*848*	*48*
Total VAT payable		*648*
Input VAT (deductible VAT)		*-/-2,415*
Total amount due or to be refunded		*-/-1,767*

Example 13

As under Example 13, yet Paul and Francesco also buy a jukebox for their bar from an American supplier. The place of supply is America (the place where the goods where located at the time the transport begins). The supply of the goods is therefore not subject to VAT. The price of the jukebox is converted from dollars to euro, and the total price exclusive of VAT is 7,001 euro. The jukebox is imported in the Member State where the company is established, where the supplies take place and where the VAT rates are 6% and 21%. The importation of the jukebox is a taxable transaction for VAT (refer to Article 2(1)(d) VAT Directive, see Chapter 5). With respect to the importation of these goods, use is made of the option of Article 211 VAT Directive which has been implemented in this Member State. Consequently, the VAT due by reason of the importation need not be paid at the time of importation but must be entered as such in the VAT return. In the same VAT return, this import VAT can be deducted as input VAT. Thus, effectively, the importation itself does not lead to a VAT payment. Paul and Francesco file the following VAT return:

Description	***Turnover***	***VAT***
Supplies/services taxed at 21%	*3,456*	*600*
Supplies/services taxed at 6%	*848*	*48*
Importation of goods	*7,001*	*1,215*
Total VAT payable		*1,863*
Input VAT (deductible VAT)		*-/-3,630*
Total amount due or to be refunded		*-/-1,767*

12. Administrative Obligations

The tax authorities rely on taxable persons to levy VAT. Taxable persons act as 'unpaid tax collectors' for the tax authorities because they collect VAT from their customers in all stages of the production and distribution chain and then pay that collected VAT to the tax authorities. To enable the tax authorities to monitor VAT collection, the VAT Directive provides for various administrative obligations for taxable persons. The most important obligations are as follows:

- Every taxable person shall state when his activity as a taxable person commences, changes or ceases (VAT registration, Article 213(1) VAT Directive).

- Taxable persons are required to issue invoices (that comply with the VAT Directive) for every supply of goods or services (Article 220 VAT Directive).

- Taxable persons must periodically file VAT returns and pay the VAT due resulting thereof (Article 250 VAT Directive).

- Taxable persons must periodically file a recapitulative statement of their intra-Community supplies of goods and services made to taxable persons in other Member States (Article 262 VAT Directive).

- Taxable persons must keep financial accounts (Article 242 VAT Directive).

13. Special Schemes

There are special VAT schemes for certain types of transactions and for certain types of taxable persons. These schemes apply to for example: small enterprises, farmers and travel agents. Special schemes are in principle beyond the scope of this book. Nonetheless, the One Stop Shop schemes (the iOSS, Non-Union Scheme and the Union Scheme) have been discussed in Chapter 6 on the place of supply. We refer to that chapter for further reading.

14. Conclusion

This book provided a concise overview of the most noteworthy aspects of the VAT system. VAT is a quickly and continuously evolving field of taxation. VAT is a budgetary instrument that increasingly provides both the national governments and EU institutions with much needed resources to carry out their public tasks. As opposed to direct taxes, the budgetary importance of consumption taxes – including VAT – is only increasing. Further, the EU VAT is typically a European tax, which, again in contrast to direct taxes, is harmonized to a great extent. As such, it is exemplary for the continuing integration of the various Member States and their fiscal systems.

The complex relationship between the various legislative instruments that apply at both an EU level (e.g., the VAT Directive, the refund directives, the VAT Implementing Regulation) and at a national level (e.g., the national VAT acts and guidelines) characterizes the study of VAT as one of the most challenging fields of taxation. In addition to that, anyone studying or working in the field of VAT is confronted with a large volume of CJEU case law (over 1,000 cases on VAT) and the case law of the national courts of the Member States.

This book gave the reader the opportunity to get an impression of the fundamentals of the VAT system, within a day. Surely, understanding the ins and outs of the VAT system will take more than a day's work. However, since VAT is such an interesting form of taxation, that seems to be a blessing rather than a curse.