Federation of European Accountants
Fédération des Experts comptables Européens

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Dear Mr Battiau,

Re: OECD International VAT/GST Guidelines – Draft Consolidated Version

FEE (the Federation of European Accountants)[1] is pleased to provide you below with its general comments on the draft consolidated version of the OECD international VAT/GST Guidelines as well as more detailed, technical comments on the Preface, Chapter 1 and Chapter 3 paragraphs 3.17 to 3.30 and 3.51 to 3.107 set out in the annex of this letter.

As mentioned in the background note of the draft Guidelines, the OECD international VAT/GST Guidelines do not impose legally binding VAT rules or prescribe legislative approaches but intend to serve as a basis for countries to frame their own laws and administrative practice, reduce impediments to international trade and improve the neutrality of VAT regimes worldwide while reducing opportunities for tax avoidance and creating more certainty for business and tax authorities.

In order to fulfil the above objectives, the development process of the Guidelines should be carefully designed and ensure that *all* stakeholders are timely consulted prior to the publication of any draft proposals. Although a Technical Advisory Group has been set up by the OECD (including representatives of governments, business and academic experts), we consider that the prompt involvement of other stakeholders, such as the professionals who use such Guidelines, is vital to ensure the applicability and effectiveness of such work.

[1] FEE is the Fédération des Experts comptables Européens (Federation of European Accountants). It represents 45 professional institutes of accountants and auditors from 33 European countries, including all of the 27 EU Member States. In representing the European accountancy profession, FEE recognises the public interest. It has a combined membership of more than 700.000 professional accountants, working in different capacities in public practice, small and big firms, government and education, who all contribute to a more efficient, transparent and sustainable European economy.

In addition to the Guidelines, the OECD could also consider to identify and propose potential ways on how VAT issues arising from international transactions could be resolved.

For further information on this letter, please contact Mrs Anastasia Chalkidou, FEE Project Manager by e-mail: anastasia.chalkidou@fee.be or at +32 2 285 40 82.

Yours sincerely,

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FEE President

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Annex: Comments on the Preface, Chapter 1 and Chapter 3 paragraphs 3.17 to 3.30 and 3.51 to 3.107

Our detailed comments included in this annex have been referenced with the relevant chapters and paragraphs of the draft OECD VAT/GST Guidelines. The wording used in the draft Guidelines in many instances was misleading or vague thus hampering the interpretation of the proposals. Therefore, we hereby provide indicative input on where improvements could be made based on our understanding from an EU viewpoint.

Preface

FEE appreciates that the context, the purpose, the scope and the development process of the Guidelines are included within the document itself, rather than in side-letters. Equally, the Table of Contents is welcomed – although it is at an interim stage - as it provides an overview of the overall structure of the Guidelines and their development. At a later stage of the document, the numbering of paragraphs and sections could be improved in order to avoid complicated referencing (e.g. Chapter 1 contains a section 1.3 and a paragraph 1.3).

Chapter 1: Core Features of VAT covered by the Guidelines

Overarching purpose of a VAT, paragraph 1.3

As paragraph 1.3 is the first instance in the document that the term "services" is used and in order to avoid the impression that the supply of intangibles would not be covered by a Value Added Tax with the core features described in Chapter 1, we recommend clarifying in paragraph 1.3 – rather than in paragraph 1.5 – that "services" include intangibles as well.

The central design feature of a VAT, paragraph 1.5

In this paragraph, the supply of intangibles is mentioned separately from supplies of services. However, in some jurisdictions (such as the European Union) the supply of intangibles is considered to be a supply of services. As this might be confusing without prior explanation, a footnote added to the word "services" in the last sentence of paragraph 1.3 would help.

VAT and international trade, paragraph 1.13

With one exception[2], the concept of services and intangibles crossing borders is not a concept to be found in EU VAT legislation. The location where the supply of services (including intangibles) takes place is determined once, and cannot be changed. The words "exportation" and "importation" are not suitable for services and intangibles, as their literal meaning implies something tangible which can be carried (i.e. portable).

[2] The exception is the supply of meals on board a means of transport, which – according to the European Court of Justice's judgment of 2 May 1996 Case number C-231/94 – under certain circumstances, can be qualified as a service for VAT purposes. Actually, catering is a supply of goods only considered as a supply of services for VAT purposes.

Therefore, we suggest to consider inserting a wording – perhaps a footnote might be more appropriate – clarifying that the terms "crossing borders", "exportation" and "importation" are meant to describe transactions in which the supplier and the customer (or their respective establishments) are located in different countries, and that the guidelines apply even if nothing tangible is carried from one location to another.

Chapter 3: Determining the place of taxation for cross-border supplies of services and intangibles

Guideline 3.5, paragraphs 3.17 and 3.18

The term "establishment" is not self-explanatory and should be reconsidered in this paragraph.

The Court of Justice of the European Union (CJEU) normally used the words "fixed place of business" as taken from the 6th VAT Directive, now replaced by the EU VAT Directive[3], which reads as a "place of business or fixed establishment" (Article 44).

More recent EU legislation uses the terms "fixed establishment" and "business establishment"[4], while in relation to tax treaty matters, the OECD uses the word "permanent" and provides a definition thereof. Therefore, it should be clarified whether the term "establishment of use" that is mentioned in the draft Guidelines (footnote 30) corresponds to any of the aforementioned terms.

In the third sentence of paragraph 18, it is mentioned that *"It is irrelevant whether this use is immediate or continuous or is intended to take place in the future".* In particular the reference to "immediate use" may be interpreted that any presence of a business can give right to taxation in the jurisdiction of such presence, regardless of the duration of its use.

For example, an architect working for four weeks on a construction site in another jurisdiction than the one where he has his fixed place of business uses a CAD software which has been supplied via the Internet when he was on site.

Conceptually, it is possible to consider the construction site as an "establishment" and to allocate taxing rights to the jurisdiction where the site is located. However, it would not be practical as the architect will use that software later in his home jurisdiction. Furthermore, it needs to be decided whether the jurisdiction of the construction site should get the full taxation rights or whether and how the taxing rights should be allocated between the jurisdiction where the architect runs his business normally and the jurisdiction where the construction site is located. It could be on pro rata basis using the actual use on site as a percentage of the expected total usability of the software, but that raises other questions e.g. about the "expected total usability" etc.

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[3] See http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2006:347:0001:0118:EN:PDF

[4] Articles 10 and 11 of Implementing Regulation (EU) No 282/2011, for supplies of services only, see http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2011:077:0001:0022:EN:PDF.

The OECD Model Tax Treaty and most actual treaties apply a De-Minimis Rule of a physical presence in a jurisdiction to qualify as a permanent establishment for taxation purposes. We suggest that such a limitation is included in the concept of "establishment" for indirect taxation purposes as well. Such clarification and distinction should be made in Chapter 3.

Recharge method, paragraphs 3.19, 3.21 and 3.68

Paragraph 3.19 is correct in stating that *"In line with normal business practice, these establishments of use will be charged for this service or intangible on the basis of internal recharge arrangements, in accordance with corporate tax, accounting or other regulatory requirements"*, and in adding in paragraph 3.21 that *"In situations where such recharge is not made, VAT will in principle be applied as if a recharge arrangement were effectively in place so as to ensure that taxing rights accrue to the jurisdiction of use"*.

However, there may be situations where the actual use of a service or intangible in a Multiple Location Entity (MLE)'s establishment is minimal, and the effort to measure the use accurately is not justified by the result. To account for such situations, we recommend extending the first sentence of footnote 31 using the following wording: *"The cases in which there would be use by one or more establishments other than the establishment that has entered into the business agreement without a recharge arrangement should remain limited for example, if the actual use of an establishment is minimal.*

Recharge arrangement, Box 3.2 and paragraph 3.28

In Box 3.2 it is stated that *"The recharge arrangement consists of elements that identify the parts of the MLE that make and receive an internal supply that is within the scope of VAT and the internal rights and obligations with respect to this supply".* This might be interpreted as applying only to recharge arrangements leading to an actual supply of services and intangibles.

According to a CJEU judgment[5], the supplies of services within the same legal entity are not subject to VAT, at least not within the European Union. This fact seems to be recognized in paragraph 3.28 where it is mentioned that "documents equivalent to invoices" may be considered as further evidence when clarifying the existence and content of the recharge arrangement.

Therefore, we suggest that the second sentence of Box 3.2 is partly amended as follows: *"…that make and receive an actual or deemed internal supply that is within the scope..."*

Application of recharge method, paragraphs 3.61-3.63 and paragraph 3.74

In article 168 of the EU VAT Directive[6] it is mentioned that: *"In so far as the goods and services are used for the purposes of the taxed transactions of a taxable person, the*

[5] CJEU judgment of 26 March 2006, Case C-210/04, FCE Bank.
[6] See http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2006:347:0001:0118:EN:PDF

taxable person shall be entitled, in the Member State in which he carries out these transactions, to deduct the following from the VAT which he is liable to pay".

The aforementioned CJEU's view that there are no supplies of services within the same legal entity means that a customer's establishment which acquires a service or intangible does not render a service in turn even if it recharges the cost to other establishments using the service or intangible. Lacking a taxed transaction, this interpretation may lead to a denial of the right to deduct input VAT to the customer's establishment if that establishment is not entitled to a full input VAT deduction, for example when it carries out financial services. A recently published Advocate General's opinion[7] might lead the CJEU to accept such treatment.

We understand that the OECD approach is different insofar as the recharge is treated as a "normal" supply to which no specific exemption applies. Although paragraph 3.63 states that *"This Guideline only deals with cross-border supplies of services and intangibles"*, the concept applicable to such cross-border supplies is based upon a deemed or actual supply within the scope of VAT (as expressed in paragraph 3.61, last sentence).

Therefore, if the recharge is made between two establishments of a MLE in the same jurisdiction, the recharging establishment technically[8] carries out a deemed or actual taxable transaction with the external supplier, while the other establishment's transactions define the VAT of the supply that will be deductible on a pro rata basis. The recharge to an establishment in another jurisdiction does not trigger VAT for the recharging establishment, but – under the Reverse Charge Rule – for the receiving establishment. As a consequence, the recharging establishment should be entitled to deduct the VAT paid to the external supplier on a pro rata basis to the extent of the recharges made, even if its normal transactions are exempt, without the right to deduct input VAT.

If this interpretation is correct, we suggest clarifying this in the last sentence of paragraph 3.61 by adding the following underlined text: *"Under the recharge method, this internal charge is treated as consideration for a supply within the scope of VAT and should give the right to deduct the VAT paid to the supplier on a pro rata basis, regardless of whether the customer's establishment otherwise carries out exempt transactions which do not give such right."*

As an alternative, such clarification could be made in paragraph 3.74 where the question of input VAT deduction is addressed.

Specific Rules, paragraphs 3.87-3.107

Except for a minor point addressed below, we believe that the OECD approach on whether to apply Specific Rules is reasonable and feasible.

[7] See Opinion of Advocate General Pedro Ruiz Villalón, published on 28 February 2013, in Case number C-388/11Crédit Lyonnais.
[8] This may not always be visible, if the establishments within the same jurisdiction are treated as a single taxpayer and file consolidated VAT returns.

Paragraph 3.107 highlights the need for a very close, clear and obvious link or association between the supply and the immovable property that has a sufficiently high potential to be manageable and enforceable in practice. In theory, that should be sufficient to avoid uncertainties about the applicability of the Specific Rule on Immovable Property. In practice, however, the reference to “intellectual services” – in particular with a broad meaning – might create uncertainties if such “intellectual services” are not somehow limited.

For example, when a Real Estate Agent provides information about Immovable Property in various jurisdictions to one client, such Agent is paid for the time spent, independently of whether the client eventually buys or leases the Immovable Property. Should that lead to an allocation of taxing rights to every jurisdiction covered by the survey?

The same question applies when, for example, a lawyer in the EU (supplier A) assists a US business customer to find a property somewhere in Europe. As the lawyer will use a network of colleagues (supplier B) in the various EU and non EU jurisdictions to find a suitable Immovable Property it is, of course, possible to allocate all these costs to the location eventually acquired or leased. However, we do not believe that it makes sense as by the time that the service is invoiced it is possible, but yet unknown whether the final (US) customer will select the specific property or not. From the point of view of the jurisdiction where supplier B is established, it can be argued that the service provided from supplier B to supplier A is closely linked to the property and thus justifies the application of the Specific Rule. However, it is questionable whether the same is true from the point of view of supplier A or from the US customer perspective and in particular when the US customer eventually decides either to select an Immovable Property outside the EU or refrains entirely from making such selection.

For the sake of legal certainty, a supply of services or intangibles must not change its place of supply with retroactive effect depending on conditions which are met or not some time after the supply (in the example here, whether the customer decides to select a given Immovable Property or not, and which one).

To remove such potential legal uncertainty, we recommend to include into the Guidelines a negative list of services which do not justify the application of a Specific Rule (perhaps as an annex), including legal consultation which is not linked to an identified Immovable Property right from the start. By such limitation, it is clarified that legal consultancy in a litigation about quality or quantity of a specific piece of land or building justifies the use of the Specific Rule while providing general advice on how to acquire Immovable Property should fall under the Main Rule.