



8 May 2012

Taxand

OECD

Piet Battiau, [piet.battiau@oecd.org](mailto:piet.battiau@oecd.org)

Head of Consumption Taxes Unit

Centre for Tax Policy and Administration

OECD, 2, rue André Pascal

75775 Paris Cedex 16

France

Dear Piet,

**Re: Taxand Responds to OECD International VAT / GST Guidelines**

Further to the publication of the “OECD International VAT / GST Guidelines”, Taxand is pleased to provide combined feedback on the guidelines from around the world.

Taxand is pleased to be involved in this initiative. Our summary comments and observations are as follows:

**Taxand’s Take**

- ❖ Taxand welcomes these draft guidelines and agrees on the importance of more international co-ordination in addressing a growing risk of double-taxation and unintended non-taxation in an increasingly globalised economy.
- ❖ Taxand agrees with the overarching purpose of a VAT being a broad-based tax on final consumption.
- ❖ The burden of value added taxes is not only based on the amount of tax due on a transaction. The administrative burden resulting from the collection and remittance of VAT by businesses should not be neglected. The latter burden lies fully on businesses.
- ❖ The OECD should aim to have reciprocity requirements abolished in consumption tax situations.
- ❖ The allocation of taxing rights services and intangibles purchased by a “multiple location entity” (MLE) should not be made based on business agreement alone.

We trust these comments will help the OECD to finalise the VAT / GST Guidelines and commentary. We would be happy to have a further discussion to follow up on our comments and recommendations.

Yours sincerely,

**Taxand**





## Taxand's OECD International VAT / GST Guidelines Response

### Preface

**Public comments are invited on the draft Preface of the Guidelines below, setting out the context of the Guidelines, their purpose and scope and their development process.**

Taxand welcomes these draft guidelines and agrees on the importance of more international co-ordination in addressing a growing risk of double-taxation and unintended non-taxation in an increasingly globalised economy.

Taxand, is the world's largest independent tax organisation across nearly 50 countries, hopes that its comments will assist in the development of guidelines that represent a broad range of views and experience from around the world.

### Chapter 1

**Public comments are invited on the draft Chapter 1 of the Guidelines below, setting out the core features of VAT-systems to which the Guidelines are intended to apply**

#### CORE FEATURES OF VALUE ADDED TAXES COVERED BY THE GUIDELINES

##### 1.2 Overarching purpose of a VAT: a broad-based tax on final consumption

Taxand agrees with the overarching purpose of a VAT being a broad-based tax on final consumption. Notwithstanding our agreement on the overarching purpose, we note the potential for a VAT to have a significant impact on low-income households particularly where there are limited or no exceptions made for supplies of basic necessities.

We also note that a VAT is often imposed in parallel with further taxes, duties, and levies which display at least some of the characteristics of a VAT. The burden for businesses in complying with multiple layers of tax that work in different ways needs to be considered carefully.

Lastly we note that this paragraph mentions that "final consumers may include not only private individuals, but also various entities that are involved in non-business activities." This comment ignores that in many jurisdictions VAT/GST exempt business (Banking, Insurance, Healthcare) that are fully involved in business activities are rejected the right to recover in punt VAT. These sectors are deemed to be consumers which ultimately lead to the fact that the cost price of these activities contains a significant amount of (unrecoverable) hidden VAT.



### **1.3 The central design feature of a VAT: staged collection process**

Taxand agrees that a staged collection process is a crucial feature that distinguishes a VAT from other indirect taxes and allows for the generally higher standard rates to be applied than those seen in sales tax systems.

We note a recent tendency in the European Union for member states to introduce a reverse charge mechanism on domestic transactions where governments see certain transactions being prone to fraud. For example, Missing Trader Intra-Community (MTIC) fraud in its various guises – whereby criminals conspire to obtain intra-community goods VAT-free and ‘go missing’ with the VAT charged on the onward supply of goods without remitting that VAT to the tax authorities – is of significant and increasing concern among EU member states.

While the increasing application of a mechanism which makes the customer liable to account for VAT on domestic transactions may be effective in combatting particular instances of VAT fraud, we note that this tendency has the effect of drawing a VAT away from the central feature of staged collection and that such measures should be used with caution.

### **1.4 VAT and international trade: the destination principle**

Notwithstanding our agreement with the overarching purpose of a VAT to be a tax on final consumption determined by the destination principle, we note the potential for a considerable compliance burden to fall on businesses in the supply chain, particularly multi-national businesses, that are required to collect VAT from customers in multiple jurisdictions.

Please also see our response to Guideline 3.3.

### **1.5 VAT and international trade: implementing the destination principle**

In supporting jurisdictions implementing the destination principle, there is a role for the OECD to provide some guidelines on an international control method to verify where the customer resides. This can be for example by an online platform for verifying businesses but as this seems difficult under privacy laws, at least a standard set of documentation that can be regarded as sufficient proof that the destination of the supply of services and intangibles has been verified.

### **1.6 Application of generally accepted principles of tax policy to VATs: the Ottawa Taxation Framework Conditions**

The principles mentioned in this paragraph are largely the same as the criteria mentioned in Guideline 3.6. If these principles are identified as the generally accepted tax policy “principles that governments apply to conventional commerce”, it would be our suggestion to use the same wordings whenever these principle are mention.



## CHAPTER 2

### NEUTRALITY OF VALUE ADDED TAXES IN THE CONTEXT OF CROSS-BORDER TRADE

#### Guideline 2.1

#### **The burden of value added taxes themselves should not lie on taxable businesses except where explicitly provided for in legislation**

Taxand fully agrees with Guideline 1. The VAT recovery and exemption with credit mechanisms should ensure that in any event the value added tax / goods & services tax is not a cost for businesses unless there is a consumption element.

Taxand notes that in modern life this guideline is sometimes difficult to maintain when businesses structure their activities in a way that results in VAT becoming a cost. Below we list examples of situations that can create conflicts with guideline 1:

- ❖ **Centralised finance activities:** because of VAT rules on central invoicing, this can result in irrecoverable VAT. The central finance function could encounter partial exemption issues where, had the activities been kept in house; all VAT could have been recovered.
- ❖ **Burden on foreign VAT:** the process of recovering foreign VAT can be burdensome. Although cross border VAT issues are dealt with by other guidelines, the additional effort to recover foreign VAT increases the VAT burden on taxable businesses.
- ❖ **Cash flow:** by virtue of businesses dealing with VAT they are acting as unpaid civil servants. The collection of VAT has an on-going impact on the cash flow of taxable businesses.
- ❖ **Advertising and promotional activities:** where goods / samples are provided for free may from time to time lead to irrecoverable VAT. Often VAT legislation fails to recognise that taxable businesses in the course of their business will not act out of charitable motives. In fact all advertorial and promotional activities are aimed at generating increases in taxable sales. Taxand's view is that VAT deduction blocks and corrections should be kept to a minimum in order to allow businesses to grow their business in a VAT neutral way.
- ❖ **Vouchers:** similar to the point on advertising and promotions, the VAT treatment of vouchers and the lack of common approach internationally leads to an important financial and administrative burden for businesses. In line with the current alignment in the EU, the OECD may be able to set guidelines in this respect as well.

Taxand would like to point out that the burden of value added taxes is not only based on the amount of tax due on a transaction. The administrative burden resulting from the collection and remittance of VAT by businesses should not be neglected. The latter burden lies fully on businesses.

Fraud is a big issue, especially in the EU where the cross border taxation involves zero rating. Businesses acting in good faith run the risk of dealing with fraudulent companies. Where governments miss out on VAT, the natural reaction is to turn around to the party acting in good faith to collect any VAT left unpaid by the fraudster.



On top of that, the legislator will impose even more administrative burden on all traders including the good guys. Due to the acts of fraudsters, bonafide traders run the risk of being burdened with VAT and extra administrative burden. With indirect tax fraud getting increasingly sophisticated, it is clear that raising the administrative burden will hardly result in catching fraudulent traders. Fraudulent parties will make sure that they tick all the boxes necessary.

## **Guideline 2.2**

### **Businesses in similar situations carrying out similar transactions should be subject to similar levels of taxation**

An important aspect of neutrality is indeed that businesses in similar situations that carry out similar transactions should be subject to similar levels of taxation. The OECD commentary correctly stipulates that similar transactions of similar business should be treated equally.

Another area to be considered is where the VAT treatment of the activities is connected to the quality of the business supplying goods or services and not the content of the transaction. The VAT treatment of certain medical services is attached to the question of whether (national) medical insurance policies will pay the cost (see for example the currently pending Zimmermann ECJ case C-174/11).

In Europe we have seen several examples of cases where member states were forced by the ECJ to adjust their rules for VAT treatment, focusing on the provider rather than the transaction. For example:

- ❖ Do you need to be an insurance company to perform exempt insurance services CPP (ECJ case C-349/96 Card Protection Plan)
- ❖ Quality of medical [professional to be allowed to performed an exempt medical service (ECJ case C-45/01, Christoph-Dornier-Stiftung für Klinische Psychologie)

Taxand considers that to fulfil the principle set out in Guideline 2, the quality of the service provider as a determining factor to the VAT treatment of a transaction should be kept to a minimum.

## **Guideline 2.3**

### **VAT rules should be framed in such a way that they are not the primary influence on business decisions**

Guideline 3 focuses on the impact of VAT on cross border investment and other business decisions. Taxand appreciates the guideline sets out the ideal picture. However with differing VAT systems in different countries around the world, there will be different aspects connected to the decision on whether or not to operate in a certain jurisdiction.



The two most important reasons that business decisions are influenced by are 1) the applicable VAT rate and 2) the willingness of a jurisdiction to adapt to changes in the market.

#### **VAT rates**

If among a relatively small number of neighbouring countries the VAT rates fluctuate significantly, the different VAT rates may influence business decisions. In this respect we refer for example to businesses offering electronic services that have moved to Luxembourg or Madeira to benefit from relatively low VAT rates.

With the upcoming changes in the EU to provide electronic reporting services to non-business customers, the EU will comply with Guideline 3 to a much larger extent.

#### **Adaption of legislation to newly developed products and services**

Electronic and telecommunications services have been a source of influence on business decisions for many years in Europe. Current rules from a VAT compliance perspective make it almost impossible for non EU parties to enter the market of internet communications (VOIP) as they are required to be VAT registered in 27 member states. Another example is the supply of books in a form other than paper (CD, eBooks). Where the content is still the same, the VAT treatment is different solely based on the medium. Countries' adapting the VAT rules to these changes is likely to attract more business because of the VAT treatment.

A similar situation occurs currently in India. Rules around VAT and business tax are still in the process of adapting to the purchase of eBooks, software and similar products. Taxand recommends the OECD provides further guidance and a uniform explanation of cross border supply of electronic services, software licensing and telecommunication and similar services to apply Guideline 3 in an efficient manner.

#### **Guideline 2.4**

**With respect to the level of taxation, foreign businesses should not be disadvantaged nor advantaged compared to domestic businesses in the jurisdiction where the tax may be due or paid**

Taxand fully supports this guideline. However, where disadvantages for foreign businesses occur, this is rarely the result of the actual amount of VAT due, but most often it is due to the fact that VAT recovery is blocked or difficult, no export credit exists or due to reciprocity rules no refund is possible.

On another note we point out that often local businesses have competitive disadvantage compared to foreign business, as goods and services foreign business are in many VAT / GST systems subject to a reverse charge. As a result buying goods or services from a foreign company improves the cash flow position of the company.



Only with respect to goods supplies this advantage can be mitigated due to increased freight costs. Due to place of supply rules, services from foreign business may even be not taxable at all. An example of the latter is electronic services in India (online information and database access or retrieval services) supplied to Indian customers. If supplied by a foreign party, these are not subject to service tax.

#### **Guideline 2.5**

**To ensure foreign businesses do not incur irrecoverable VAT, governments may choose from a number of approaches**

See below for combined comments.

#### **Guideline 2.6:**

**Where specific administrative requirements for foreign businesses are deemed necessary, they should not create a disproportionate or inappropriate compliance burden for the businesses**

As guidelines 2.5 and 2.6 are closely linked, we combine our comments on these guidelines.

Taxand agrees that indeed there are various ways to avoid foreign VAT / GST being incurred while irrecoverable. However, in our view it would be more beneficial for business if these approaches involved the foreign company not being required to register or submit refund requests. The reason is that these procedures require expertise on local requirements, which should not be deemed to exist with a foreign business. A system with zero rates and reverse charge mechanism is therefore preferred as an approach.

One issue that needs to be addressed is how businesses can prove that they deal with foreign businesses. Taxand is of the opinion that the OECD can play a key role in adopting a uniform certificate of taxable status that foreign businesses can then use to make themselves known as foreign taxpayers.

#### **2.4 Applying the VAT neutrality principles in the context of cross-border trade: Commentary on the Guidelines**

Taxand agrees that dealing with VAT/GST neutrality will lead to certain challenges. Although we agree that a consistent use of a limited number of specific place of taxation rules, will help, but current practice shows that this is not enough. Behind the application of straightforward place of supply rules, there is also the definition of the specific services that need harmonisation.

Examples of types of services that can give rise to confusion are service of architects (real estate related or not), supplies of software (electronic service or not depending on medium used for supply),



recharged services (can they keep the original character, i.e. can a marketing services be recharged by a company that is not an advertising company), warranties and supplies of goods together with installation of the equipment.

#### **2.4.1 Principles of good tax administration**

##### **Box 2.1**

- 1. Guidance - Relations with Taxpayers - Revenue authorities are encouraged to:**
  - 1.1 apply tax laws in a fair, reliable and transparent manner**
  - 1.2 outline and communicate to taxpayers their rights and obligations as well as the available complaint procedures and redress mechanisms**
  - 1.3 consistently deliver quality information and treat inquiries, requests and appeals from taxpayers in an accurate and timely fashion**
  - 1.4 provide an accessible and dependable information service on taxpayers rights and obligations with respect to the law**
  - 1.5 ensure that compliance costs are kept at the minimum level necessary to achieve compliance with the tax laws**
  - 1.6 where appropriate, give taxpayers opportunities to comment on changes to administrative policies and procedures;**
  - 1.7 use taxpayer information only to the extent permitted by law**
  - 1.8 develop and maintain good working relationships with client groups and the wider community.**

Taxand agrees with the Principles of good tax administration. With respect to point 1.4 we note that the OECD should encourage countries to make information on the tax position of taxpayers available in a number of foreign languages to be defined by the OECD.

#### **2.4.2 Reciprocity**

Taxand takes the view that the OECD misses out on an opportunity to refrain from letting the Guidelines take no position on the desirability of jurisdictions adopting reciprocity requirements. The reciprocity rules make sense in the area of direct taxes (which almost all countries have) but are completely misplaced in an environment with VAT/GST which still a large number of countries do not levy. Taxand takes the view that the OECD should aim to have reciprocity requirements abolished in consumption tax situations.



### 2.4.3 Groups of countries

Taxand fully agrees with the commentary on groups of countries bound by a common legal framework for their VAT system (most noteworthy being the EU in this respect).

## CHAPTER 3

### DETERMINING THE PLACE OF TAXATION FOR CROSS-BORDER SUPPLIES OF SERVICES AND INTANGIBLES

In this Chapter, public comments are invited on:

- ❖ the draft Guidelines on place of taxation for cross-border supplies of services and intangibles to businesses that have establishments in more than one jurisdiction, as set out in paragraphs 3.17 to 3.30 and in paragraphs 3.51 to 3.86
- ❖ the draft Guidelines on the implementation of specific rules for determining the place of taxation for cross border business-to-business supplies of services and intangibles, as set out in paragraphs 3.87 to 3.107.

Underpinning this work is the assumption that parties involved act in good faith and that all supplies are legitimate and with economic substance. Issues connected with tax evasion and avoidance will be addressed as part of future work

#### Guideline 3.1

For consumption tax purposes internationally traded services and intangibles should be taxed according to the rules of the jurisdiction of consumption.

Please see our response to Guideline 3.2

#### Guideline 3.2

**For the application of Guideline 3.1, the OECD has adopted the following Guideline:**

For business-to-business supplies, the jurisdiction in which the customer is located has the taxing rights over internationally traded services or intangibles.

In order to tax consumption, although this is not a perfect method, especially in the field of services and intangible it makes sense to tax at the jurisdiction in which the customer is located. However, services are hard to trace and accepting this Guideline will automatically lead to imperfections in the application of the underlying principle. Some examples where it is difficult to get the jurisdiction in which the customer is located and the actual consumption in the same place is in a Globally import sector like mobile telecommunication. Taxand agrees that for now the jurisdiction in which the customer is located is the preferred solution.

#### Guideline 3.3

**For the application of Guideline 3.2, the OECD has adopted the following Guideline:**



The identity of the customer is normally determined by reference to the business agreement.

We agree that the business agreement is an important factor in determining the identity of the customer and therefore where services are consumed in circumstances where the supplier and customers are located in different jurisdictions.

We note that it is typically the taxing authorities of the jurisdiction where the supplier of services or intangibles is located who will need to be satisfied that those services or intangibles have been consumed in a jurisdiction other than where they have authority.

It may be useful to consider a minimum threshold of evidence that should be available for the purposes of determining the identity of the customer particularly to the satisfaction of the authorities in the supplier's jurisdiction.

#### **Box 3.1**

##### **Business Agreement**

Business agreements consist of the elements that identify the parties to a supply and the rights and obligations with respect to that supply. They are generally based on mutual understanding.

An area of concern is that Business Agreements are drafted by the parties and for the benefit of the partners and not necessarily for the purpose of providing guidelines for taxing the underlying services. The OECD takes clearly a risk by looking at the subjective documents lie a Business Agreement for deterring the place of taxation. If anything the VAT jurisprudence by the European Court of Justice shows in recent years that “substance over form gets more and more traction” when it comes to determining the VAT consequences of Business Agreements.

#### **Guideline 3.4**

For the application of Guideline 3.2, the OECD has adopted the following Guideline:

When the customer has establishments in more than one jurisdiction, the taxing rights accrue to the jurisdiction(s) where the establishment(s) using the service or intangible is (are) located.

Although the approach set out in Guideline 3.4 is in line with the destination principle, in practice it will be difficult to determine where the establishment(s) using the service or intangible is (are) located. In general a customer with establishments in more than one jurisdiction will operate a central procurement company/entity and it may not always be clear at the moment of purchase of the service or intangible where the use will occur. An important issue that the country of use will encounter is the lack of visibility of the transfer and use of the service or intangible. We also refer to our comment on Guideline 3.5.



### **Guideline 3.5**

For the application of Guideline 3.4, the OECD has adopted the following Guideline:

In those cases where the services are used by one or more establishments other than the establishment that entered into the business agreement, the taxing rights are allocated in two steps. In the first step, taxing rights are allocated to the jurisdiction where the customer establishment that enters into the business agreement is located. In the second step, taxing rights are allocated to the jurisdiction where the customer establishment that uses the service or intangible under a recharge arrangement is located.

The measures set out in Guideline 3.5 and Box 3.2 looking after the recharge of the service or intangible may not always solve the issue as often a head office will be compensate of the a lump sum amount under a management agreement and not for each individual service or intangible purchased.

### **Box 3.2**

#### **Recharge arrangement**

The recharge arrangement is the arrangement that undertakes the role of the business agreement for internal recharges that are treated as supplies within the scope of VAT under the recharge method. 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.

Besides the complication expressed in our comment on Guideline 3.5, the Recharge arrangement can in several jurisdictions (EU most noteworthy) run into the complication that services rendered between establishment that are part of the same legal entity these are outside the scope of VAT. The Recharge arrangement would result in significant adaption of the VAT legislation which is in breach of current ECJ jurisprudence.

### **Guideline 3.6**

The taxing rights over internationally traded services or intangibles supplied between businesses may be allocated by reference to a proxy other than customer location as laid down in Guideline 3.2, when both the following conditions are met:

a. The allocation of taxing rights by reference to customer location does not lead to an appropriate result when considered under the following criteria:

- ❖ Neutrality
- ❖ Efficiency of compliance and administration
- ❖ Certainty and simplicity
- ❖ Effectiveness



❖ Fairness.

b. A proxy other than customer location would lead to a significantly better result when considered under the same criteria.

It is Taxand's view that the majority of the Guidelines presented by the OECD are clear and stimulate members to adapt a neutral and effective VAT/GST system, Guideline 3.6 does exactly the opposite. The wording provided is very vague and will most certainly be perceived as an invitation to countries to adapt a wide range of proxy requirements in order to attract the local taxation a large variety of services. It is Taxand's view that the OECD should avoid that taxing rights are allocated by reference to a proxy in all B2B situations. We can imagine that in B2C situation it is sometimes unavoidable but this is not the case in B2B situations.

### **Guideline 3.7**

For internationally traded business-to-business supplies of services and intangibles directly connected with immovable property, the taxing rights may be allocated to the jurisdiction where the immovable property is located.

We agree that taxing rights on supplies of services and intangible directly connected with moveable property should be allocated to the jurisdiction where the property is located. We note there are often instances where there is uncertainty as to whether a certain service or intangible is sufficiently related to the immovable property to be taxed where the immovable property is located. We welcome the use of common features of supplies of services and intangibles to assist in this determination.

### **3.4 Business to final consumers ("B2C") supplies**

Not relevant at this stage.

\*\*\*



## APPENDIX I

### CONTACT DETAILS

#### Taxand Global Indirect Tax Service Line Leader

**Richard Baxter**

T. +44 20 7663 0750

M. +44 7798 530023

E. [richard.baxter@alvarezandmarsal.com](mailto:richard.baxter@alvarezandmarsal.com)

#### Taxand Global Indirect Tax Service Line Deputy Leader:

Alain Recoules

T. +33 170388817

M. +33 626565028

E. [alain.recoules@arsene-taxand.com](mailto:alain.recoules@arsene-taxand.com)

#### Taxand Global Indirect Tax Coordinator:

Paul Bakker

T. +31 6 5254 64 59

M. ++31 20 757 09 07

E. [paul.bakker@vmwtaxand.nl](mailto:paul.bakker@vmwtaxand.nl)

#### Taxand Global Indirect Tax Knowledge Team:

Leigh Clark

T. +31 757 09 07

M. +31 6 5254 6459

E. [leigh.clark@alvarezandmarsal.com](mailto:leigh.clark@alvarezandmarsal.com)

### ABOUT TAXAND

Taxand provides high quality, integrated tax advice worldwide. Our tax professionals – more than 400 tax partners and over 2,000 tax advisors in nearly 50 countries - grasp both the fine points of tax and the broader strategic implications, helping you mitigate risk, manage your tax burden and drive the performance of your business.

We're passionate about tax. We collaborate and share knowledge, capitalising on our expertise to provide you with high quality, tailored advice that helps relieve the pressures associated with making complex tax decisions.

We're also independent — ensuring that you adhere both to best practice and to tax law and that we remain free from time-consuming audit-based conflict checks. This enables us to deliver practical advice, responsively.



Taxand has achieved worldwide market recognition. In the International Tax Review's (ITR) World Tax 2012, over 95% of Taxand locations are ranked top. 35 countries were voted top in the ITR Transaction Tax Survey 2012 and in the ITR Tax Planning Survey 2012.

Taxand has received over 40 national awards and 13 regional awards in the ITR European, Americas and Asia Tax Awards since 2009. These include European Private Equity Tax Firm of the Year, European Indirect Tax Firm of the Year, European Tax Policy Firm of the Year, Asia Transfer Pricing Firm of the Year, Asia Tax Policy Firm of the Year, and Latin America Tax Disputes Firm of the Year. Full details of awards and further information about Taxand can be viewed at

[www.taxand.com/media/factsheet](http://www.taxand.com/media/factsheet)

[www.taxand.com](http://www.taxand.com)