

VAT Newsletter

Important VAT, GST and
sales tax news from around
the world

Issue No. 9, December 2015

Introduction

Welcome to the ninth issue of Ernst & Young LLP's 2015 *VAT Newsletter* for the US and Canada. These newsletters cover a variety of topics, as value-added tax (VAT) can impact businesses in many ways. Approximately 160 countries now have a VAT, goods and services tax (GST), consumption tax, service tax or similar VAT, and the laws and regulations are constantly changing. We use this newsletter to inform you of significant changes taking place.

At the end of this newsletter, you will find contact details for the senior members of our teams in the US and Canada who can help answer any questions you may have about the articles in this newsletter or any other VAT questions.

We are interested in your feedback on the items covered and what topics you would like to see covered in the future. Please provide any feedback to Howard Lambert at howard.lambert@ey.com.

If you would like to subscribe to EY's other Indirect Tax updates, please click [here](#).



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Global

EY's *2015 Worldwide VAT, GST and Sales Tax Guide*

You can access the latest guide [here](#).

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Managing indirect tax controversy: dealing with audits and disputes

Managing indirect tax controversy is our new Global Indirect Tax thought leadership report, providing insights into how companies can anticipate and deal effectively with tax audits and resolve disagreements with tax administrations. You can access the report [here](#).



Americas

São Paulo, Brazil – Changes to the tax basis calculation of ICMS for software sales

On 29 September 2015, the São Paulo state government issued Decree 61,522, providing a substantial change to the tax basis calculation of the state VAT (ICMS) for transactions involving the sale of software to Brazilian clients.

Starting 1 January 2016, the sale of software will be subject to ICMS on the total sales price, which includes the software value, plus the electronic media and any other amounts charged to clients. Under prior rules in the state of São Paulo, the ICMS on the sale of software was calculated on the amount equal to twice the value of the carrier media only (e.g., compact discs, flash drives).

The change in the rules will bring a new chapter to the judicial discussion of whether it is legal to impose ICMS on the sale of software. As background, several software houses have been taking the position that ICMS should not be triggered on the sale of software to local clients because the software should not be classified as goods. In certain cases, tax authorities have accepted the position that ICMS is only triggered on the amount of the carrier media, which qualify as goods under São Paulo law.

In the past, the Brazilian supreme court (STF) had taken the position that the sale of software should be considered an acquisition of an intangible asset and, therefore, the sale of software is not subject to ICMS. According to the STF interpretation, only the sale of off-the-shelf software supported by physical

media and without any customization is subject to ICMS. On this basis, ICMS is presumably not triggered on the sale of software via download because there is no “circulation of goods.”

In a recent case, the STF issued a preliminary decision introducing a new interpretation of how ICMS is triggered for sales of software via download. Under this decision, ICMS is triggered on the sale of software via download because the sale should be considered a “circulation of goods.” The final judgment is still pending.

It is unclear whether ICMS applies to cross-border transactions involving software acquisition via download. When one is importing goods, the ICMS is paid on customs clearance, but that customs law does not include digital transactions. While it is still unclear whether ICMS will affect cross-border transactions, it is expected that state tax authorities will create a rule making software downloads subject to the tax.

Additionally, software license agreements are considered a service under the service tax law (ISS). As a result, sales of software via download could be subject to ISS and ICMS. The Brazilian Supreme Court is considering whether it is constitutional for municipalities to charge ISS.

Suriname – plans to introduce VAT system postponed

Plans to replace the current turnover tax with a VAT system in Suriname on 1 January 2016, have been postponed until further notice.



Asia-Pacific

China – Zero-rate VAT extended to more services to foreign entities

China's Ministry of Finance and State Administration of Taxation on 30 October 2015 issued Caishui [2015] No. 118 (Circular 118), which extends the zero-rate VAT regime to more services provided to foreign entities.

The following services provided to overseas clients by domestic entities or individuals shall be eligible for zero VAT rate:

- ▶ The production and distribution of radio, film and television programs.
- ▶ Technology transfer services, software services, circuit design and testing services, information system services, business process services and contract energy management services for subjects located overseas.
- ▶ Offshore service outsourcing business, including information technology outsourcing, business process outsourcing and knowledge process outsourcing, as prescribed in Attachment I of Caishui [2013] No. 106 (Circular 106), (i.e., notice regarding the launch of VAT pilot arrangements applicable to the railway transportation and postal service industries) (please refer to CTIE2013047 for details of Circular 106).

Tax calculation policies for export of services that zero VAT rate applies

- ▶ Domestic entities or individuals that calculate VAT payable based on a simplified

method shall apply VAT exemption policy (no input VAT allowed).

- ▶ Domestic entities or individuals that calculate VAT payable based on a general method shall apply the following tax calculation methods:
 - ▶ Manufacturing enterprises shall apply the VAT "exemption, credit and refund" (ECR) policy.
 - ▶ Foreign trade enterprises shall apply the VAT ECR policy for export of services purchased from third parties.

Foreign trade enterprises shall apply the VAT ECR policy for direct provision of services to overseas clients.

Applicable VAT refund rates

Applicable VAT refund rates of the abovementioned export services shall be the applicable VAT rates for the same services as prescribed in items 1 to 3 of Article 12 of Circular 106. Taxpayers should provide valid foreign exchange collection documents and export documents for the application of export tax refunds.

Effective date of Circular 118

Circular 118 shall become effective on 1 December 2015, and at the same time will revoke certain contents of Circular 106 that conflicted with Circular 118:

- ▶ Item 6 of Article 1 of Attachment III, the Transitional Policies for VAT Pilot arrangements, i.e., "the VAT exemption policy for off-shore service outsourcing business provided by pilot taxpayers from 1 January 2014 to 31 December 2018.

- ▶ Partial contents in Item 6 of Article 7 of Attachment IV, the Regulations on Services subject to VAT at Zero Rate or eligible for VAT Exemption Policies, i.e., “the VAT exemption policy for radio, television and film program distribution services in overseas.”
- ▶ Partial contents in Item 9 of Article 7 of Attachment IV, the Regulations on Services subject to VAT at Zero Rate or eligible for VAT Exemption Policies, i.e., “the VAT exemption policy for technology transfer services, energy performance contracting services, software services, circuit design and testing services, information system services, business process services, radio, television and film program production services as well as the exclusion of energy performance contracting services provided to subjects located in domestic areas.”

Our observations

The services eligible for either the zero VAT rate or VAT exemption are effectively exempt from output VAT. However, under the zero VAT policy, export services are exempt from output VAT, but the input VAT attributable to export services can be credited or refunded. Before the effectiveness of Circular 118, only research and development

services and design services provided to overseas clients are categorized as being eligible for the zero VAT policy. The issuance of Circular 118 further clarifies that the three types of abovementioned services shall be eligible for the zero VAT rate, which shall enhance the competitive strengths of the relevant Chinese service providers as their tax burden of qualifying export services shall be reduced. This would definitely increase the ability of Chinese service providers to compete with foreign companies in the global market.

Philippines – Court finds Canadian company entitled to underutilized VAT certificates

The Philippine Court of Tax Appeals, in *Manulife vs. Commissioner of Internal Revenue*, CTA No. 8701, held that a Canadian insurance company and financial services provider is entitled to PHP6.2 million (about US\$132,000) in underutilized VAT credit certificates on zero-rated receipts of PHP420 million (about US\$8.95 million) for the 2011 tax year.





Europe

European Union – VAT Expert Group: Paper on VAT grouping and *Skandia*

The VAT Expert Group (VEG), which assists and advises the European Commission (Commission) on VAT matters, has made available a paper (Taxation Paper No. 47) on VAT grouping and the potential implications of *Skandia* ([C-7/13](#)).

The paper comments on the VAT grouping across the member states and the VEG's view on the impact of *Skandia*. The paper is not the Commission's policy but may form the basis for further discussion both within the VEG and with the Commission. The paper highlights the VEG's view that VAT grouping is important for the European Union (EU) economy, and there is a strong need for consistency in the application of the *Skandia* ruling. The paper also sets out the VEG's view that the application of *Skandia* should be kept to a minimum and promotes the broad application of the approach taken following the *FCE Bank* case.

The paper and supporting annex can be accessed by clicking [here](#) and [here](#), respectively.

European Union – Consultation on modernizing VAT for cross-border e-commerce

On 25 September 2015, the Commission issued a [press release](#) announcing the launch of a [public consultation](#) to help identify ways to simplify VAT payment

procedures for cross-border e-commerce transactions in the EU.

In May 2015, the Commission published details of its strategy to create a [Digital Single Market](#).

From a VAT perspective, the Commission undertook to make legislative proposals in 2016 to reduce the administrative burden on businesses arising from the different VAT regimes applicable to cross-border sales, including:

- ▶ Extending the current “mini one-stop shop” regime to cover cross-border online sales of physical goods (i.e., distance sales)
- ▶ Introducing a common EU-wide VAT threshold to help online start-ups and small businesses
- ▶ Allowing cross-border businesses to be audited only by their home country for VAT purposes
- ▶ Removing the VAT exemption for the importation of small consignments from suppliers in third countries (i.e., low-value consignment relief)

Against this background, the consultation seeks the views of businesses and other interested parties on:

- ▶ The current VAT rules for business-to-consumer (B2C) cross-border supplies of goods and services
- ▶ The implementation of the 2015 changes to the EU VAT place-of-supply rules for B2C supplies of digital services and the Mini One Stop Shop

European Union – VAT rates applied in the EU member states as at 1 September 2015

The Commission has published an updated document reflecting the various **VAT rates** applied in the EU Member States as at 1 September 2015.

Ireland – Updated guidance on the different rates of VAT currently applicable

The Irish Revenue has issued **updated guidance** on the different rates of VAT currently applicable in Ireland and the circumstances in which they apply.

Slovakia – Amendment to the Slovak VAT Act approved by parliament

On 1 October 2015, an amendment to the VAT Act No. 222/2004 Coll., as amended, was approved by the Slovak parliament. Its final version awaits the approval of the president. The amendment introduces several changes that will come into force in two stages.

Changes effective from 1 January 2016

Cash accounting scheme

As we previously informed you in the tax alert issued in April 2015, a VAT “cash-accounting” scheme is being incorporated into the Slovak VAT Act for VAT payers with limited turnovers.

Taxpayers whose annual turnover does not exceed €100,000 (originally proposed as €75,000) may opt for the scheme, under which they declare output VAT only after receipt of customer payments. The same applies to input VAT deduction, which can be claimed only after the taxpayer has paid for a supply.

The change will also significantly impact a larger group of taxpayers if they enter into business transactions as customers of taxpayers opting into the scheme.

Extension of the scope of goods subject to reduced 10% VAT rate

The range of goods subject to the reduced 10% VAT rate was extended.

This applies for particular food products such as meat, fish, milk and bread. This change was incorporated into Annex No. 7 of the Slovak VAT Act.

It includes the codes of foods to which the reduced rate applies.

Introduction of reverse-charge mechanism for construction services

The reverse-charge mechanism should also apply to supplies of construction under a contract of work (or similar type of contract) and to the supply of goods with installation or assembly if the assembly or installation as a whole represents a construction service.

The main aim of this change is to limit the financial problems of companies operating in the construction industry, resulting from the insolvency or poor payment discipline of their customers, and to eliminate VAT fraud in the construction sector.

The reverse-charge mechanism also applies to cases where the recipient of the construction services mainly performs transactions not subject to VAT, but is already registered for VAT purposes for some particular reasons (e.g., legal entities incorporated for non-business purposes and public authorities). These recipients will pay VAT on construction services purchased, regardless of whether they are used for taxable activities.

Extended reverse charge for supplies of goods by foreign persons

The scope of reverse-charge mechanism for goods is being extended to all goods supplied by non-established taxpayers in Slovakia. As we have already informed you, locally established taxable customers should start to apply a reverse charge on goods from non-established suppliers in Slovakia. Distance selling will be the only exception.

Changes effective from 1 April 2016

Taxpayers will be obliged to separately report simplified invoices if the total amount of deductible VAT from simplified invoices for the tax period is €3,000 or more.

These invoices are reported in the VAT ledger in section B3 in aggregate amounts. This (simplified) regulation, as opposed to the previously accepted reporting of the aggregate value of simplified invoices (instead of each single invoice), is a reaction to occurrences of tax evasion revealed by the tax authorities.

Currently, it is not clear where a simplified invoice exceeding the threshold will be reported (in section B2 or in section B3 after its adjustments which will enable reporting of the invoices item by item). Taxpayers should prepare for changes in information systems.



Middle East, India and Africa

Namibia – Proposed introduction of VAT now in doubt

On 22 September 2015, the Namibian minister of finance tabled the Value-Added Tax (VAT) Amendment Bill and the Income Tax Amendment Bill to the National Assembly.

The proposed amendments have wide-reaching implications for many residents and nonresidents.

VAT proposals

The amendments to the Namibian VAT Act take effect on the first calendar day of the month following the month in which the VAT Amendment Act is published in the *Government Gazette*.

VAT registrations and cancellation of registrations

- ▶ The compulsory VAT registration threshold will be increased from NAD200,000 to NAD500,000 (approximately US\$14,398 to US\$35,995).
- ▶ Voluntary VAT registration will only be considered where:
 - ▶ There is a reasonable expectation that taxable supplies will be made for consideration after a period of time.
 - ▶ There is a reasonable expectation that future taxable supplies will exceed NAD200,000 in a 12-month period.

- ▶ The commissioner of inland revenue may cancel a voluntary VAT registration in certain circumstances
- ▶ A voluntary VAT registration will be allocated a six-month VAT period unless, upon written application, the commissioner of inland revenue has allowed a different VAT period

Import VAT accounts

- ▶ Provision has been made such that the Commissioner of Inland Revenue may require security or impose additional conditions before allowing the import of goods on an import VAT account
- ▶ The Commissioner of Inland Revenue may cancel the registration of an import VAT account in certain circumstances



EY newsletters and alerts

If you would like a copy of a green paper, newsletter or alerts covering some of the topics mentioned below, please click on the link or contact Howard Lambert at howard.lambert@ey.com.

Czech Republic: *EY Tax News* – September 2015: Ernst & Young s.r.o. has issued the September 2015 edition of its regular client newsletter, *EY Tax News*. From an indirect tax perspective, the following items may be of interest:

- ▶ Forward: commentary on the VAT gap in the EU
- ▶ Czech VAT Act amendments in the works
- ▶ Supreme Administrative Court (SAC) judgment: carousel fraud and emission allowances
- ▶ SAC judgment: application of VAT on technical improvements made by a future tenant

Latvia: *EY Tax Newsletter* – September 2015: SIA Ernst & Young Baltic has issued the September 2015 edition of its regular client tax newsletter. This edition features an item on amendments to the VAT law to provide for the taxation of the management of residential buildings and specify the procedure for exempting cultural services from tax.

Netherlands: *Tax Update Weekly* – Edition 38, 2015: to Ernst & Young Belastingadviseurs LLP's *Tax Update Weekly*, Edition 38 (17 September 2015), includes an item on the proposed budget changes, including restriction of reduced rate of VAT on medicines, energy and waste tax changes and tax procedural changes; Weekly Edition 39, 2015; Weekly Edition 40, 2015; and Weekly Edition 41, 2015.

Slovakia: *EY Tax & Legal News* – 7–8 July 2015: Ernst & Young k.s.' July/August 2015 edition of its regular newsletter, *EY Tax & Legal News*, includes the following VAT items:

- ▶ Court of Justice of the European Union judgment: importation of goods and VAT deduction by a freight carrier
- ▶ Judgment of the District Court of Trnava: excessive length of a tax audit

UK: *EY VAT News* – 14 September 2015; 21 September 2015; 28 September 2015; and 5 October 2015.

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