Ireland

By Brian Butler

Place of Supply of Services: New VAT Rules Applying in the European Union

Introduction

This column concerns certain aspects of the so called "EU VAT Package" which made a number of changes, mainly with effect from January 1, 2010, to the VAT system operating within the EU. The column focuses on the changes to the rules concerning the place of supply of services and related reporting requirements. The changes have application to all Member States, but particular reference is made to Ireland. The column also focuses on cases where services are provided from one business to another business ("B2B" scenarios).

The term "supply of services" has very broad application for VAT purposes. As well as the performance of acts, it includes the assignment of intangible property and the toleration of a situation. Therefore, for example, the grant of a licence is a supply of services for VAT purposes as is a restrictive covenant.

The rules for determining the place of supply of services are a fundamental aspect of the EU VAT system as in order to come within the charge to VAT in a Member State a service needs to be supplied in that Member State. A common set of rules is needed to ensure that a service does not inadvertently fall outside the VAT net or become subject to VAT in two or more Member States. The former could arise if a service supplier in Ireland supplied a service to a customer established in France and the Irish VAT rules deemed the service to be supplied in the Member State of the customer and the French VAT rules deemed the service to be supplied in the Member State of the supplier. The latter (a double VAT charge) would arise if, keeping with the

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same example, the Irish VAT rules deemed the service to be supplied in the Member State of the supplier and the French VAT rules deemed the service to be supplied in the Member State of the customer.

The Change

Under the rules applying up until January 1, 2010, the general rule applying to B2B services was that they were deemed to be supplied in the county of establishment of the service supplier ("supplier location" rule).This meant, for example, where a service supplier established in Ireland supplied services to a business customer established in Germany, the service was deemed to be supplied in Ireland. If the service was a vatable service, Irish VAT was applicable. However, there were a number of exceptions to the general supplier location rule that deemed services to be supplied other than where the supplier was established. The main exception was the one that deemed certain types of services to be supplied in the country where the service recipient was established ("customer location" rule). This exception applied to a wide range of services including: services of consultants, legal services, advertising services, provision of staff, transfers and assignments of copyrights, patents, licences, trade marks and similar rights. Indeed most B2B services which would be supplied cross-border fell within this exception.

Effective January 1, 2010, the general rule applying to B2B services is that they are now deemed to be supplied in the country of establishment of the customer ("customer location" rule). This means, for example, where a service supplier established in, say, the United States supplies a service to a business customer in Ireland, the service is deemed to be supplied in Ireland. If the service is a vatable service, Irish VAT applies. This does not mean the U.S. service supplier is obliged to register for VAT in Ireland and has to apply VAT to its fees. The matter of who is responsible for accounting for the VAT is a separate matter. In the general application of VAT, the supplier of a service is responsible for accounting for the VAT. However, in a cross border B2B scenario, the service recipient is generally the accountable person. This avoids the need for a service supplier to register for VAT in the Member States of its customers; instead the customer accounts for the VAT under the so called "reverse charge" accounting basis. The result is that the customer ends up in the same position regarding VAT as that which would apply if he were to receive the same service from an Irish service supplier.

Exceptions to the General Rule

Under the new system, the new general customer location rule does not apply to all services. The principal exceptions are as follows:

- Services connected with immovable property (land and buildings) are deemed to be supplied where the property is located.
- Cultural, artistic, sporting, scientific, educational, entertainment and similar services are deemed to be supplied where those activities actually take place.
- Restaurant and catering services are deemed to be supplied where they are physically carried out.
- Short-term hire of means of transport (30 days or less, and 90 days or less for vessels) is deemed to be supplied where the means of transport is actually put at the disposal of the customer.
- Passenger transport services are deemed to be supplied where the transport takes place, proportionate to the distance covered.

Also, Member States may, in certain circumstances, employ a "use and enjoyment" rule where they consider it appropriate to eliminate or impose a VAT charge. In Ireland, this rule is applied in relation to hiring out goods used and enjoyed in Ireland where the customer is based outside the EU and, under the general customer location rule, the place of supply would be outside the EU. It also applies in Ireland to hiring out means of transport used and enjoyed outside the European Union where the customer is based in Ireland and, under the general customer location rule, the place of supply would be Ireland.

New Reporting Requirement

Since January 1, 1993, there has been a requirement for businesses to report details of intra-Community supplies of goods. This mainly involves the sale of goods, but it also extends to scenarios where there is a movement of goods without a sale such as a company moving goods to a branch located in another Member State. The report, called a "VIES" (VAT Information Exchange System) return in Ireland, provides

details of the VAT number of the consignee(s).The VAT authorities in the Member State of the consignee can use the report to police the VAT treatment of the goods involved.

Since January 1, 2010, there is a need for businesses to also report details of intra-Community supplies of B2B services where the services are subject to VAT in the customer's Member State. There was already a need to include customer VAT numbers on invoices issued in relation to such intra-Community supplies of services. However the new reporting requirement has focussed the need for service suppliers to obtain customer VAT numbers. The absence of a number does not mean the VAT place of supply rule changes and, in principle, it is still possible to treat the place of supply as the customer's Member State. However, it could result in unwarranted attention from the VAT authorities and the imposition of penalties. With this in mind, the best practice is to obtain customer VAT numbers in all cases.

A Welcome Development

In general, the change is considered to be a welcome development and has brought greater clarity to the VAT treatment of cross border B2B services. Of course, new reporting requirements are never welcome and are a drain on costs and resources. However, apart perhaps from the initial investment, in this case, the cost and effort involved with compliance is relatively low.

The main benefit is the elimination of VAT incurred by a business customer, which could have been a deterrent in relation to effecting a transaction or activity. This could involve VAT incurred by a business where the VAT is not recoverable or, where the VAT is recoverable, in practice it might take considerable time and therefore involve a funding cost. The following are examples of problems with the pre–January 1, 2010, rules:

- **Aircraft leasing:** Let's consider a company based in one Member State leasing aircraft to a domestic airline based in another Member State. Subject to very limited exception, in accordance with the general supplier location rule, the lessor would have been obliged to charge VAT on the lease rentals. The airline would have been entitled to recover the VAT under the "foreign trader" VAT repayment provisions; however this could take a number of months and possibly longer in some cases. (Under the new general customer location rule, the lessor does not charge VAT and this eliminates the need for the "foreign trader" reclaim.)
- **Administration services:** Take the case of a company based in the EU providing administration services to a company based outside the EU engaged in the provision of exempt vocational training. Under the general supplier location rule, the EU based service supplier would have been obliged to charge VAT on its fees. The company based outside the EU would not have been entitled to recover the VAT. (Under the new rules, VAT does not arise.)
- **Management services (typically involving services supplied by a parent company to a subsidiary):** There were many different approaches taken to the VAT treatment of management services. These include treatment as a single service subject to the general supplier location rule, treatment as a single service (akin to consultancy) subject to the customer location rule and treatment as multiple services subject to different rules. This area warrants its own article, but for the moment, I will just flag the matter as problematic in the past. (Under the new rules, the position is clear: the general customer location rule applies.)

Additional VAT Costs

The change is not welcome by all businesses as in some cases it has resulted in new VAT costs in respect of services received by businesses established in the EU. Here are some examples:

- **Management services:** As mentioned above, prior to January 1, 2010, many different approaches were taken to the VAT treatment of management services. In a scenario where management services were supplied from a parent based outside the EU to an EU-based subsidiary, in many cases, reverse charge VAT treatment was not applied on the basis that the services fell under the general supplier location rule. Where the subsidiary was engaged in VAT exempt activities, such as the provision of most financial services, this involved avoiding an absolute cost. From January 1, 2010, the general customer location rule applies and there is now an additional cost in respect of the VAT.

- **Leasing cars:** Many Member States do not allow VAT recovery in respect of car leasing even where the lessee is fully engaged in vatable activities. Prior to January 1, 2010, it was possible to avoid a VAT cost by effecting cross-border leasing arrangements. For instance, a German leasing company could lease cars to an Irish lessee engaged in vatable activities. The lease rentals were subject to German VAT, but the Irish lessee could reclaim the German VAT through the "foreign trader" VAT reclaim procedure. With limited exception, VAT recovery in respect of car leasing is not available in Ireland, but this arrangement avoided an Irish VAT charge arising. From January 1, 2010, the general customer location rule applies, which means Irish VAT arises and it not recoverable.
- **Rating services:** These were generally regarded as falling within the customer location rule. However, some advisors and businesses considered them to be subject to the general supplier location rule. The latter approach involved funds and other recipients of rating services not accounting for VAT on the receipt of the services from service suppliers based in other jurisdictions. In general, the service recipients would not have been entitled to recover VAT so this treatment involved avoiding an absolute cost. From January 1, 2010, it is clear that the general customer location rule applies, and there is now an additional cost in respect of the VAT.

Some Anomalies

Since the change, a few scenarios have been encountered that produce peculiar VAT outcomes in relation to services involving Irish businesses. The general customer location rule, invoicing requirements and the VIES returns are intended to produce an outcome whereby intra-Community supplies of vatable services are reported and can be policed.

However, in some situations involving Irish suppliers of intra-Community vatable services, there is no VAT invoicing requirement, and VIES returns are not applicable. This arises where an Irish business is not obliged to register for VAT as it is not the accountable person in respect of any vatable activity or transaction. This scenario would be unusual and is most likely to arise where a company is established to effect specific transactions. For instance, it might involve a company established in Ireland to lease equipment to a customer established in France. Because the Irish leasing company is not accountable for Irish VAT (the customer accounts for French VAT), it is not obliged or entitled to register for VAT in Ireland and VAT invoicing and VIES returns do not apply.

In practice, the Irish company might need to register in order to recover French VAT incurred on the purchase of the leased goods (assuming it purchased the goods in France). The claim would be made under the "foreign trader" reclaim procedure and this would require having an Irish VAT registration. The Irish company would need to carry out some transaction to justify an Irish VAT registration. This might involve buying and selling some low value goods.

Another peculiar outcome results from a scenario involving a head-lease and sub-lease structure concerning means of transport used and enjoyed outside the EU. Where there is a non-Irish head-lessor and an Irish sub-lessor, there can be a mismatch in relation to the VAT treatment of the place of supply of the head-lease. The head-lessor will, under the general customer location rule, regard Ireland as the place of supply, whereas the Irish entity, under the "use and enjoyment" rule, will consider the service to take place outside the EU. The Irish entity will not be obliged or entitled to register for VAT and this presents a problem for the head-lessor as it cannot quote a VAT number for its customer nor report the transaction on its VIES (equivalent) returns.

In both scenarios above, it is presumed that the confused VAT outcome is unintentional. It would be appropriate to change the VAT registration rules to accommodate an optional VAT registration in the circumstances; indeed this matter has recently been raised with the Irish VAT authorities and they have indicated that they are favorably disposed.

Final Comments

There are still many issues to clarify regarding the VAT position of cross-border services including these:

- What is the scope of services "connected with" immovable property?

- How does a supplier decide to which of his customer's several establishments his services are supplied?
- What does "used and enjoyed" mean?
- Exactly what is a "means of transport"?

However, these changes are welcome as they bring greater clarity, reduce the need for "foreign trader" VAT reclaims and the extent of VAT chargeable on services supplied to businesses based outside the EU. In some scenarios, it does result in new VAT costs arising, but it is difficult to find fault with this aspect as, almost invariably, they involve services used and enjoyed in the EU.