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The Definitive Guide to Solving VAT Problems



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Chelco VAT Ltd

PART I

Value Added Tax (VAT) within the EU has become such a complex topic that a systematic approach is required in order to solve VAT problems. This present article focuses on such an approach that could, when followed, become an invaluable aid for both businesses and VAT advisors.

LEGISLATION: DIRECTIVE AND REGULATIONS

The complexities arise from the way that the EU VAT system is set-up. At the top of the pyramid lies the VAT Directive¹, with Member State (MS) choosing how to transpose its provisions into their national legislation. The European Commission also issues binding regulations as a preferred legal instrument through which to aid the harmonization process.

An interesting point to note is that where a MS's national legislation is not in line with the VAT Directive, the VAT Authorities are bound and must follow what their national VAT legislation provides for. A taxable person however can refer to the provisions of the VAT Directive directly when discussing with the tax authorities of his/her MS. This is because the directives have a direct ef-

fect. However, European Court of Justice (ECJ) rulings have also confirmed that not all provisions of a Directive have a direct effect – only those that are sufficiently precise and unconditional.

LANGUAGE AND INTERPRETATION

The VAT Directive itself has been translated in all 24 official languages of the EU, but this is not always possible to do for all the underlying documents as well.

Every language version is as binding as each other. This means that in the case of a difference arising from translation, there is no language version that prevails. ECJ rulings have confirmed that a MS may not apply against an individual a regulation which at the time of its application has not been properly published in the Official Journal of the EU in the official language of that MS.

OPTIONS AND DEROGATIONS

The VAT Directive offers several instances where MS are allowed to exercise various 'options to derogate' from the provision of an article. This has created a very non-uniform VAT base across the EU, compounded by different interpretations from the national VAT authorities. The ECJ offers

1. Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax, as amended.

2. I would like to clarify that the VAT Directive does not refer to the term 'zero rated', nor does such a term exist in all MSs. The Directive refers to exemptions. Therefore 'zero rated' is where an exemption with right of deduction exists. An 'exempt transaction', as per the Cyprus VAT legislation, is thus a transaction for which no right of deduction exists.

guidance on interpretation of specific provisions, only when a relevant case is referred to it.

VAT queries are seldom straightforward given the vast and broad legislative background. So how should they be tackled? Here is how.

HOW TO TACKLE VAT PROBLEMS

In analyzing any VAT scenario, the five-question systematic approach below offers a logical thought-process to finding the solution to a VAT query.

1. The question of taxable person

Establishing whether a taxable person exists is the first step to understanding the transaction. Generally, if there is no taxable person, then there is no transaction to tax.

The VAT Directive defines a taxable person in Article 9 as any person who, independently, carries out in any place any economic activity whatever the purpose or results of that activity.

If however a taxable person does exist on the supplying end, then the transaction could be a business-to-consumer (B2C), which entails one set of rules; and if a taxable person also exists on the receiving end, then there is a business-to-business (B2B) relationship, governed by other rules.

Specifically, the VAT advisor needs to ascertain whether the transaction under review involves:

- (a) a taxable person with the right of deduction;
- (b) a taxable person without the right of deduction (eg a university);
- (c) a taxable person that follows a special scheme of small undertakings or the special scheme for farmers;
- (d) a non-taxable legal person (eg a government); or
- (e) a non-taxable person.

Every one of the above carries different implications of how VAT may be applied.

2. The question of taxable transaction

There are only four types of taxable transactions, identified in Article 2 of the VAT Directive, as follows:

- (a) supply of goods (this includes 'exports' which are zero rated²);
- (b) supply of services;
- (c) intra-community acquisition of goods; and
- (d) imports.

Identifying which of the four transactions is taking place, in conjunction with the type of taxable or non-taxable person, are paramount to understanding the VAT treatment of the

transaction. Once the above have been determined, the VAT adviser can proceed with question 3.

3. The question of place of the taxable transaction

The place of supply is arguably one of the most challenging questions, mainly because of the number of special rules and derogations that exist across the MSs. The VAT advisor must use the correct rule based in local national rules, in the country where the place of supply is deemed to take place.

Different rules determine the place of supply of goods and the place of supply of services.

PLACE OF SUPPLY OF GOODS

Indicatively, for the place of supply of goods, this could be:

- The place where the goods are (eg when the sale of goods are not transported, or in the case of distance sales that fall below the registration threshold in the other MS);
- The place where transport begins (eg when the goods are transported);
- The place where goods are installed or assembled;
- The place where transport ends (eg for intra-community acquisitions); or
- The place where the customer is established (eg for intra-community supplies).

In addition, special rules exist for intra-community acquisitions that result from triangulation or ABC transactions.

The rules governing chain transactions in general require particular attention, as several factors themselves may influence the decision of whether and where VAT is due. For example, if in a chain transaction the original supplier is outside of the EU (eg Switzerland or Norway), then the question of who undertakes the importation as well as who is responsible for the transportation is fundamental to the decision-making process.

There are separate rules governing the supply of goods on board ships, aircrafts or trains, which also need careful consideration. There are also special rules governing the sale of gas, electricity, heating and cooling energy sold through gas systems or energy networks, between taxable persons. The thing to note here is whether the customer will purchase the good (eg the gas) for own consumption (in which case VAT is payable in the country of consumption) or for re-sale (in which case VAT is payable where the customer is established).

In addition, the place of supply for imports is the country where the goods enter the community or the MS where such goods cease to be covered by customs arrangements. ■

Continued in Issue No.117, December 2014

Part II explains the place of supply of services, exemptions and Persons liable to pay tax. It also features a table summarizing the rules relating to the place of supply of services for B2B and B2C transactions.

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PART II

Continued from Issue No. 116, September 2014



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PLACE OF SUPPLY OF SERVICES

For place of supply of services, the 2010 amendment¹ to the VAT Directive introduced simplified general rules for B2B and B2C services. However, the MSs, in negotiating the rules, and in fear that businesses and consumers would choose the MS with the lowest rate of VAT, also imposed special place of supply rules, allowing for a total of 15 derogations, nine of which only apply to B2C transactions, one which applies only to B2B transactions, and five of which apply to both B2B and B2C transactions. The table below summarizes in simple terms the place-of-supply-of-services rules.

Rules relating to both B2B and B2C transactions	
Type of service	Place of supply
Connected with immovable property	Where immovable property is located
Passenger transport	Where transport takes place
Restaurant and catering services	Where services physically carried out
Restaurant and catering services on board ships, aircrafts or trains within the EU	Point of departure
Short-term hiring of means of transport	Where means of transport is put at disposal of customer
Rules relating to B2C transactions only	
Type of service	Place of supply
Intermediaries	Where underlying transaction takes place
Transport of goods, other than intra-community transport	Where transport takes place
Intra-community transport of goods	Place of departure
Services and ancillary services relating to cultural, artistic, sporting, scientific, educational, entertainment and similar activities	Where the activities take place
Valuations of, and work on, movable tangible	Where services physically carried out

1. Council Directive 2008/8/EC of 12 February 2008

property	
Ancillary transport activities (eg loading, handling)	Where services physically carried out
Long-term hiring of means of transport	Where customer is established
Electronically supplied services (from 1.1.2015)	Where customer is established
Various intangible services when customer is outside the EU	Where customer is established
In all other cases	Where the supplier has established his business
Rules relating to B2B transactions only	
Type of service	Place of supply
Admission to cultural, artistic, sporting, scientific, educational, entertainment and similar events, including ancillary services to the admission	Where the events take place
In all other cases	Where the customer has established his business

Once the place of supply of the transaction has been determined, the fourth question can be addressed.

4. The question of exemptions

Different exemptions exist in the legislation and due care should be given to determine whether the transaction under review is covered by one of the exemptions. If an exemption exists, there is no VAT.

The exemptions could arise as a result of:

- Exports;
- Intra-community supplies;
- International transport;
- Supplies to vessels or aircrafts;
- Supplies under diplomatic and consular arrangements; or
- Supplies under VAT warehousing arrangement.

If no exemption exists, then question 5 should finally be addressed.

5. The question of the person liable to pay the tax

Once the above have been established, the question of who is liable to pay the tax is not always straightforward. Certain provisions of the VAT Directive, such as Article 196, which discusses the reverse charge on services received from outside of the recipient's MS, are uniform across the 28 MSs. Others, such as Article 194, which allows for MS to decide whether the re-

ipient of a service, which is carried out by a supplier outside of that MS, should account for the VAT, are different across the MS. So it is imperative to have knowledge of the local legislation of the country where the supply takes place, and determine whether the person liable to pay the VAT is:

- (a) the supplier;
- (b) the customer;
- (c) the person to whom the services are supplied; or
- (d) a tax representative.

The VAT advisor, in answering the above should also be aware if the client has multiple VAT registrations in other MSs, and the reasons behind such registrations, as this may determine the answer to question 5. ■



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He sits on various committees charged with VAT and other tax matters and has authored a number of tax syllabuses. He lectures extensively on VAT and Cyprus taxation and has authored a number of related articles on matters pertaining to Cyprus and EU tax.

He also regularly advises reputable international professional bodies on advanced Cyprus VAT taxation.