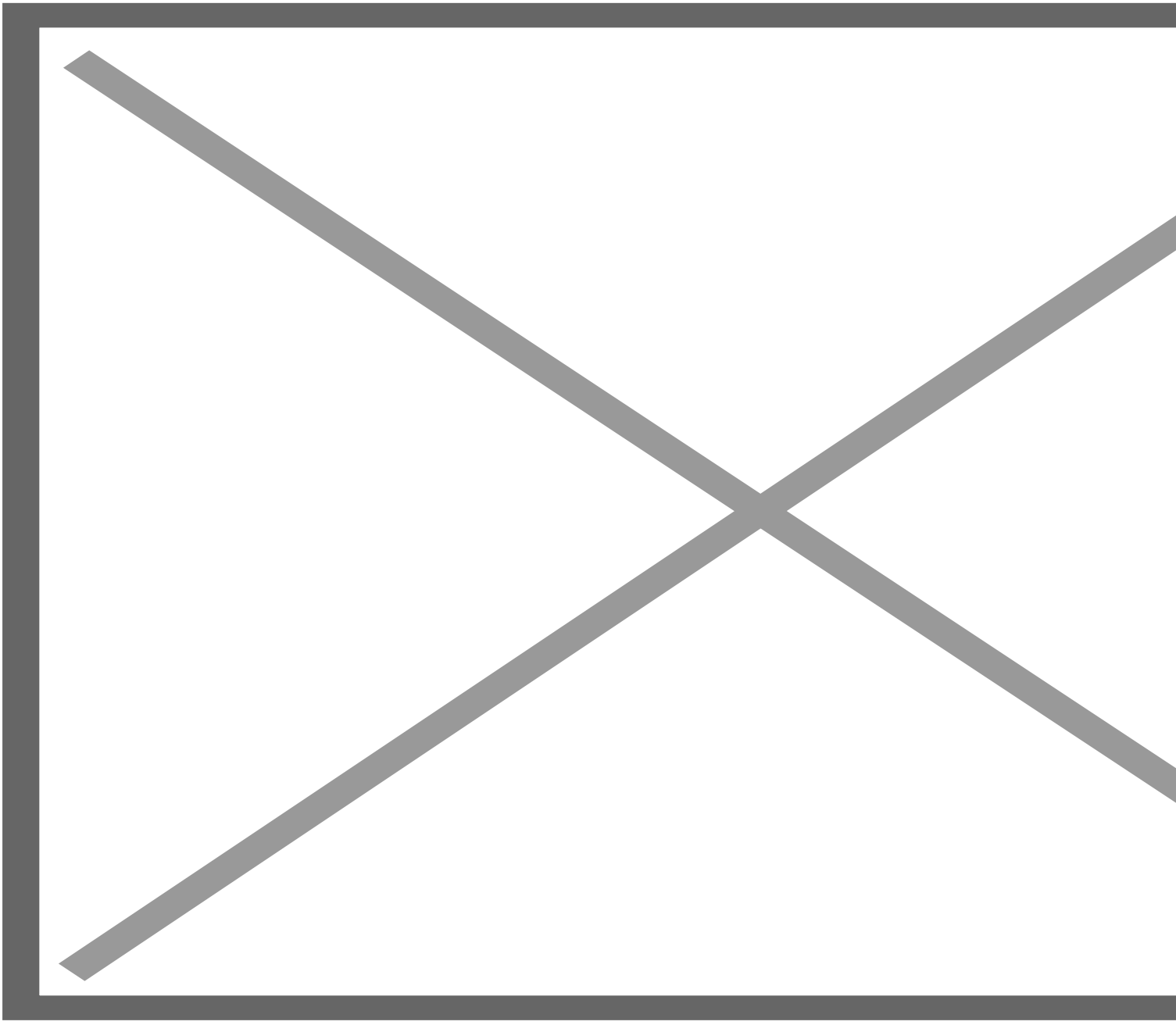
Concession shopping

Indirect Tax



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Now that the mini one-stop shop is live, Tarlochan Lall considers where we are now

Key Points

What is the issue?

The mini one-stop shop (MOSS) went live on 1 January 2015. The feature that has received most recent attention is its potential adverse impact on small and micro businesses

What does it mean for me?

Small businesses with UK supplies below the registration threshold formerly faced the risk of having to charge VAT on UK supplies. This could have made the whole business venture uneconomic

What can I take away?

The latest guidance in HMRC's Business Brief 46/2014, published on 11 December 2014, sought to solve that problem. It has introduced a concession for small businesses so that, even if they use VAT MOSS, they do not need to account for and pay VAT on sales to its UK customers

The mini one-stop shop (MOSS) went live on 1 January 2015, although it is still an optional means of accounting for VAT on digital services. For those who supply these services to consumers in EU member states the choice is between having one MOSS registration and multiple registrations in the other countries. VAT will, however, be due one way or the other.

What digital services are affected?

MOSS applies to digital business-to-consumer (B2C) supplies, and covers telecommunications, broadcasting and electronic services. The supply takes place where the customer is located, and can trigger multiple VAT registration requirements and the optional use of MOSS. The latest guidance on the meaning of digital supplies, how to establish where the customer is located and how to operate MOSS, is included in Business Brief 46/2014. Although this is a good reference point, HMRC and the European Commission have produced other detailed guidance.

Small and micro businesses

It is MOSS's potential adverse impact on small and micro businesses that has received recent attention. VAT registration thresholds in member states do not apply if a business is neither established nor has a fixed establishment in that country. That has always been the case. However, unlike distance sales of goods, for which thresholds of €100,000 or €35,000 apply in member states, there is none for supplies for digital supplies. The first euro of sales can trigger registration obligations.

Changes introduced by the FA 2014 for UK-based businesses wishing to use MOSS impose a requirement of UK VAT registration. Small businesses with UK supplies below the registration threshold, currently £81,000, faced the risk of having to charge VAT on UK supplies when otherwise they would not have had to do so, potentially making the whole business venture uneconomic. This prompted much campaigning and alarm that small businesses would be deterred from doing business with customers in other EU member states. BB 46/2014 seeks to solve that problem.

VAT accounting concession

The statutory requirement to register remains if a business wishes to have a UK MOSS registration. But for UK supplies, as long as they are below the registration threshold, BB 46/2014 confirms the small business:

- '...will not lose [its] UK VAT registration threshold'; and
- it will … 'not need to account for and pay VAT on sales to [its] UK customers'.

This appears to be an extra statutory concession introduced under HMRC's care and management powers. The conditions for this treatment are that the business:

- is 'a UK-based supplier of digital services';
- opts to use the VAT MOSS; and
- has UK taxable turnover below the UK VAT registration threshold.

There should be limited scope for disputes with HMRC about the second and third conditions. The first may lend itself to disputes over whether a non-UK business is 'UK based' and whether it is making 'digital supplies'. UK-based probably means either established in the UK or a business with a fixed establishment. The definition of a fixed establishment has become a hot topic since the European Court's decision in Welmory sp. z o.o. V Dyrektor Izby Skarbowej w Gda?sku, Case C-605/12. That case raises the issue of whether the use of computers, servers and software without human resources in a country is enough to create a fixed establishment. The ECJ concluded those are matters for the national court to determine.

Disputes may also arise over what are digital supplies. The lack of a statutory basis for the concession in BB 46/2014 potentially precludes the rights of appeal to the First-tier Tribunal. A small business's only choice may be to seek judicial review. That is not only prohibitive in terms of costs, but a specialist tax tribunal is the more appropriate forum to resolve such a dispute than the High Court. The CIOT has already made representations that the concession should be put on a statutory footing.

Whether the concession gives rise to any issues of EU law is a further potential issue. The European Commission issued a bland statement on the UK's approach in BB 46/2014. It said that it 'will evaluate the implementation of the new VAT rules in the context of a possible future extension of the one-stop shop and would be open to proposing adaptations based on the feedback it will receive in this context'.

It is understood that at least some in the Commission regard the issue addressed by BB 46/2014 a UK problem, for which the UK should seek its own solution. The VAT registration threshold in the UK is one of the highest. Some countries, such as Spain, have no threshold and many have low thresholds. That is apparently why member states could not agree a threshold for digital supplies, which is why it is nil.

The Commission's statement indicates that there may be prospects of a threshold being imposed on member states, such as the one for distance sales of goods under Art 34 of the Principal VAT Directive. That, however, may be some time away.

Economic activity

Registration obligations for businesses would be triggered if sales constitute economic activity within the meaning of Art 9 of the Directive. In principle, any economic operator, in particular a small or micro business, could argue that its activities are not economic activities. Given the concession in BB 46/2014, the issue is likely to arise in other member states. Art 9 would be critical, although any relevant local rules (including local case

law) may need consideration. The definition of economic activity in Art 9 is wide, and deceptively so. The concept is embodied in the definition of taxable person in that Article thus:

‘“Taxable person” shall mean any person who, independently, carries out in any place any economic activity, whatever the purpose or results of that activity.’

It is well established that the test of whether an activity is an economic one is objective and is determined regardless of the motives of the operator undertaking it.

Clues to limitations on that definition are in the Directive and case law. First, VAT is due on supplies for consideration made by a ‘taxable person acting as such’. Second, the second paragraph of Art 9(1) reads:

‘Any activity of producers, traders or persons supplying services, including ... activities of professions, shall be regarded as “ economic activity”. The exploitation of tangible and intangible property for the purpose of obtaining income there from on a continuing basis shall in particular be regarded as an economic activity.’ (My emphasis)

The person alleged to be a taxable person must be acting as – relying on the words ‘acting as such’ – a producer, trader, supplier of services or a professional. Arguably, activity must be carried out on some repeated basis. Essentially, the activity must be an ‘undertaking earnestly pursued’.

The ECJ in *S?aby v Minister Finansów*; *Kuc? and another v Dyrektor Izby Skarbowej w Warszawie* (Joined Cases C-180/10 and C-181/10) [2011] STC 2230 stated that the scale of sales is not itself decisive. Referring to *Wellcome Trust Ltd v Customs and Excise Comrs* (Case C-155/94) [1996] STC 945, the ECJ recognised that a large volume of sales may fall outside the scope of economic activity. The tipping point is likely to be found in the following test espoused by the ECJ, namely:

‘... where the party concerned takes active steps to market property by mobilising resources similar to those deployed by a producer, a trader or a person supplying services within the meaning of the second sub-paragraph of Art 9(1) of the VAT Directive’. (Para 39)

That case concerned agricultural land which had been re-designated for development. Issues concerning economic activity are likely to arise for start-ups, some hobby trades, but also businesses of substantial scale. In such cases, if charges are made (ie the first euro) for anything done, the question of economic activity will arise. It will be necessary to demonstrate objectively that, despite the charge, evidence shows that the operator is not acting as a trader, producer or person supplying services. Without convincing evidence, obligations to account for VAT will arise.

Resolution of the issues would involve questions of facts, which would fall to be determined by the local courts where the customers are located. That is the place where either a VAT registration would need to be affected or VAT accounted for through the MOSS registration. The issue for those with a MOSS registration would be whether VAT needs to be accounted for. Again, that would present difficulties for most, let alone small and medium-sized businesses. The electronic structure created for MOSS does not provide for these types of issues to be resolved.

Input tax

BB 46/2014 contains useful guidance on the recovery of input tax, even where the UK business does not charge VAT on UK supplies. It confirms that input tax incurred in the UK, but attributable to EU sales, can be

recovered through the UK VAT registration. BB 46/2014 states:

‘Unless you wish to reclaim VAT on business expenses or purchases in relation to your EU sales, you should enter “0” in every box on the return. If you do wish to reclaim VAT in relation to EU sales, you should complete boxes 4, 5 and 7.’

However, any VAT incurred in other member states and is attributable to those EU sales must be recovered through the VAT refund portal.

Conclusion

The time for making first MOSS returns is looming, so theoretical issues may become real issues. BB 46/2014 and other published guidance provide a useful starting point.

Some issues may require greater investments in terms of intellectual and economic capital. We should start to see whether business can cope with the issues or whether they are insurmountable.