KPMG

VAT Newsletter

Hot topics and issues in indirect taxation

July 2019

NEWS FROM THE CJEU

Activity as a member of the supervisory board of a foundation

CJEU, ruling of 13 June 2019 – case C-420/18 – IO

The Court of Justice of the European Union (CJEU) has answered in the negative the question of whether an activity as a member of the supervisory board of a Dutch foundation is subject to VAT.

The case
IO is a member of the supervisory board of a Dutch foundation. According to this foundation's statutes, the supervisory board members are appointed for a term of four years. A person who has concluded a contract of employment with the foundation cannot belong to the supervisory board. The members of the supervisory board can only be suspended or dismissed due to negligence in exercising their duties, or other serious issues.

A supervisory board member cannot exercise the powers conferred upon the supervisory board alone, with the result that they do not act in their own name, for their own account or on their own responsibility but rather on the account and responsibility of the supervisory board. For his activity as a member of the supervisory board, IO receives a gross payment in the amount of EUR 14,912 per year. This payment is not dependent on either IO's participation in meetings or the hours he actually works. Whether IO's activity as a supervisory board member is subject to VAT is disputed.

Ruling
IO is not a taxable person in accordance with Art. 9, 10 of the VAT Directive as, while his activity must be classified as an economic activity, it is not exercised independently.

In the case at hand, IO's activity must be classified as an economic one as it is long-lasting and carried out for a consideration. Thus, IO receives an annual gross payment of EUR 14,912. Furthermore, the members of the supervisory board are appointed for a term of four years, which gives the payment received a sustainable character. It is therefore not relevant if IO only exercises one single mandate.

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IO does not exercise his supervisory board member activity independently as, in exercising this activity, he is in a subordinated relationship. It is true that in relation to the carrying out of the activity as a supervisory board member no hierarchical subordinated relationship to the chair of this foundation or the supervisory board exists. However, in exercising his tasks as a member of the foundation's supervisory board, IO acts neither in his own name nor for his own account or own responsibility. Thus, IO bears neither the responsibility that arises from activities carried out as a legal representative of the foundation, nor is he liable for damages which he may cause to third-parties in performance of his duties.

In addition, his situation distinguishes itself from that of a trader due to no economic risk at all accompanying the tasks carried out. That is to say, he receives a fixed remuneration that is not dependent on his participation in meetings or the hours he actually works. Therefore, in comparison to a trader, he exerts no appreciable influence on his revenue or expenditure. Moreover, any negligence committed in the course of his exercising his duties does not appear to have any direct impact on his remuneration; according to the foundation's statutes, this can only lead to his dismissal if a special process has previously been carried out.

Please note:
According to the tax authorities, an activity as a supervisory board member is in principle a business activity (see section 2.2. (2) sent. 7 VAT Application Decree with reference to the German Federal Tax Court (BFH) rulings of 27 July 1972, V R 136/71 and 20 August 2009, V R 32/08).

The CJEU ruling at hand should in principle have no significance for German supervisory board members of stock corporations, as the civil law position is different. This means that supervisory board members have, for example, the right to receive reports from the executive board. If the executive board refuses to report that which an individual supervisory board member has requested, the supervisory board member can take legal action in their own name to have the reports handed over. Furthermore, members of the supervisory board who violate their duties are liable to compensate the company, in accordance with § 116 sent. 1 Stock Corporation Act (AktG) in connection with § 93 (2) sent. 1 AktG, for any damages which occur as a result.

However, it could be different in the case of supervisory board members who are employees of a parent company, seconded to the supervisory board of a subsidiary. In this respect, appeal proceedings before the BFH are pending (V R 62/17; see VAT Newsletter April 2018). It remains to be seen how the BFH shall apply the differentiation between independent and dependent activities, established by the CJEU in the IO case, to the case under appeal.

Action against Germany on account of input tax refund procedures

CJEU, claim of 10 May 2019 – case C-371/19 – European Commission v. Germany

The European Commission has referred Germany to the CJEU on account of its EU input tax refund procedure practices.

The European Commission is asking the court to establish that Germany has breached its obligations arising from Articles 170 and 171 of the VAT Directive and from Article 5 of Directive 2008/9/EC, that it is systematically refusing to ask for missing data on VAT applications for reimbursement and is instead directly rejecting applications for reimbursement in these cases if such data could only be submitted after the deadline of 30 September.

Grounds for the claim
The Commission is asserting an infringement of the principle of VAT neutrality. This principle, it argues, requires every claim for reimbursement to be allowed if its material requirements have been met. If there are doubts about the fulfillment of material conditions for reimbursement, applications for reimbursement could only be rejected under Article 5 in conjunction with Article 21 paragraph 1 sentence 1 of Directive 2008/9/EC if information requests of the reimbursing member state were unsuccessful under Article 20 of this directive.

Furthermore, the Commission argues that Germany's interpretation of Article 20 (1) of Directive 2008/9/EC prevents taxpayers who are not resident in the reimbursing member state from effectively exercising VAT applications for reimbursement.

Germany's systematic refusal under Article 20 (1) of Directive 2008/9/EC to ask for additional information and documentation ultimately infringes against the principle of legitimate expectations, according to the Commission: upon receipt of the acknowledgement of receipt of the application for reimbursement, every taxpayers should be able to expect their application to be processed according to the provisions of this directive. If this does not happen, their trust in legitimate processing is violated, the Commission argues.

Please note:
Pursuant to Art. 15 (1) of Directive 2008/9/EC, applications for reimbursement must be submitted to the member state in which the respective taxpayer resides by 30 September of the calendar year following the reimbursement period. The application for reimbursement is only deemed to have been submitted if the applicant has provided all information required in Articles 8, 9 and 11. The member state in which the applicant resides must immediately transmit an electronic acknowledgement of receipt to the applicant.

Specifically, under Art. 8 (2) letter h of Directive 2008/9/EC, the application for reimbursement for every invoice must contain details of the goods and services acquired, itemized according to the codes pursuant to Art. 9 of Directive 2008/9/EC. If code 10 "other" is used, the nature of the goods supplied and services provided must be given. If the applicant expands code 10 with "ProfFees" or "Goods", then in the view of the Lower Tax Court of Cologne (ruling of 20 January 2016, ref. no. 2 K 1514/13; subsequently the BFH, ruling of 10 January 2019, V R 66/16) a formally complete application has been submitted to this extent. This is justified by the fact that the entries exceed the threshold of complete lack of content and have explanatory (added) value, albeit minimal, in respect of the required information (see also the CJEU submission of the BFH of 13 February 2019, XI R 13/17 on the input tax refund procedure; VAT Newsletter May 2019).

NEWS FROM THE BMF

Key features of VAT group taxation

BMF, Position paper, status 14 March 2019

The German Ministry of Finance (BMF) has presented the key features of group taxation in line with Art. 11 of the VAT Directive, which could replace the regulations on VAT groupings in Germany.

According to Art. 11 of the VAT Directive, following consultation with the VAT committee, each Member State can treat persons resident in its area, who may be legally independent but who are closely affiliated due to mutual financial, economic and organizational relationships, as one taxable person. Furthermore, a Member State which makes use of this possibility can take the necessary steps to prevent tax evasion or avoidance through use of this provision.

The following points shall apply in particular:

- Members of a VAT group should all be capable of being legal entities regardless of the legal form, insofar and as long as they are commercially active and have their office, seat of residence or subsidiary in Germany.
- The financial link to the group should arise through the group member taking on external responsibility for the VAT on revenue created by the group. The economic link should mean that the group members cooperate among each other on a commercial basis. The organizational link shall be the result of the approval of each group member for the group representative.
- Every VAT group shall specify a group representative (as a rule one of the members) that will be responsible for fulfilling all tax obligations for the entire group towards the tax authorities.
- The VAT group shall be created and terminated prospectively upon (electronic) application.
- All group members shall be jointly and severally liable to the treasury for the group's VAT.
- The VAT group, as one taxable person, shall only receive one VAT identification number.
- All previously existing VAT groupings shall be terminated at a date in the future. Before this date, there shall at all times be a possibility to submit an application for the creation of a VAT group. At the same time, an appropriate transition period shall apply.

The position paper was discussed with the federal/state working group "VAT Groupings" on 10 April 2019. Industry representatives made it clear that a lot of new knowledge was gathered which their members would first need to reflect upon.

Subsequently, in summer 2019, a position paper shall be addressed to the BMF. On this basis discussions should continue. The financial authorities expect support from industry with respect to politicians and the EU Commission; the model for group taxation should if necessary be submitted to the VAT committee for consultation in 2019. After that, the legislative process could be initiated in 2020. Ideally, the new law would come into effect on 1 January 2021, with a transition phase (in which both old and new laws would be applicable in parallel) until 31 December 2021.

NEWS FROM THE LOWER TAX COURTS

Input VAT deduction in connection with hospitality expenses

Lower Tax Court Berlin-Brandenburg, ruling of 9 April 2019, 5 K 5119/18

The Lower Tax Court Berlin-Brandenburg has issued its opinion on input VAT deductions in connection with hospitability expenses in accordance with § 15 (1a) sent. 2 German VAT Law (UStG). Contrary to the financial authorities, the Lower Tax Court takes the view that denying an input VAT deduction solely due to not promptly complying with the formal requirements of § 4 (5) sent. 1 no. 2 Income Tax Act (EStG) violates the principle of neutrality. Permission was granted for an appeal against the ruling.

The case
The VAT returns of a business consultant contained amounts for input VAT which arose on hospitality expenses incurred by him. In this case, it concerned business dinners with business partners.

The local tax office accepted the VAT returns. In the course of a tax audit, the auditors reached the conclusion that the input VAT claimed in connection with the hospitality expenses should not be granted, as the necessary entries in relation to the occasion and the participants were not given on the expenses receipt. The local tax office followed the auditor's evaluation and amended the VAT assessment.

In the objection filed by the consultant, he rectified – 4 years later – the still missing entries on the expenses receipts and continued to claim the input VAT deduction. Following an unsuccessful objection, the business consultant filed a lawsuit. He is of the opinion that from a VAT law point of view it is irrelevant when the entries are made on the expenses receipts. The input VAT deduction may not be denied solely as a result of a failure to comply with any possible formal requirements that exist.

The local tax office hold the view that an input VAT deduction in connection with hospitality expenses only comes into question if the entries regarding the occasion and participants, required for income tax purposes, are provided in a timely fashion. However, this did not happen in the case under dispute.

Ruling
The lawsuit was successful. The local tax office was wrong in denying the input VAT deduction.

From an income tax point of view, in accordance with § 4 (5) no. 2 sent. 1 EStG, expenses for providing hospitality to people for business reasons may not reduce profits as long as they exceed 70 per cent of the expenditure, which according to the generally prevailing understanding should be considered to be appropriate, and the extent of and business reasons for which are documented. To prove the amount of and the business reason for the expenditure, the taxable person must, in accordance with § 4 (5) sent. 1 no. 2 sent. 2 and 3 EStG, furnish the following particulars in writing: place, day, participants and reason for the hospitability as well as the amount of the expenditure. If it took place in a restaurant, it is sufficient to provide details on the occasion and those partaking of the meal; the bill for the meal must be submitted as well. An additional requirement for the income tax-related deductibility of hospitality expenses as operating expenses in accordance with § 4 (5) sent. 1 no. 2 EStG is the prompt creation of an internal receipt (see BFH, ruling of 26 February 2004, IV R 50/01, Federal Tax Gazette II 2004, 502).

From a VAT point of view, a full input VAT deduction, instead of the 70 per cent, is possible if the hospitability expenses are, from an income tax point of view and the generally prevailing understanding, to be viewed as appropriate and the amount of and business reasons for which are documented (see § 15 (1a) sent. 2 UStG). As an exception to the principle of the right to deduct input VAT, which guarantees VAT neutrality, a strict interpretation is advisable. The refusal of an input VAT deduction solely on the basis of non-compliance with the formal requirements – regardless of whether the taxable person can

prove the material requirements of the input VAT deduction – presents, according to the Lower Tax Court, a burden for the taxable person which is not compatible with the principle of VAT neutrality.

The Lower Tax Court refers in particular to the fact that it is possible to correct an invoice with retroactive effect even after a longer period of time has passed since the first issuance of the invoice (cf. CJEU, ruling of 15 September 2016 – C-518/14 – Senatex). So then, the subsequent and belated proof that hospitality expenses were incurred for business reasons, cannot lead to a refusal of the input VAT deduction.

Please note:
Companies must already keep proper hospitality receipts for income tax purposes. If, in an individual case, an operating expenses deduction and the associated input VAT deduction is denied, the entries missing but necessary for VAT purposes should be made up for and, with reference to the Lower Tax Court of Berlin-Brandenburg's ruling in this case and the expected appeals process, an objection should be lodged and an application made for the proceedings to be suspended in accordance with § 363 (2) German Tax Code.

IN BRIEF

Zero rating of transactions for the maritime industry I

BMF guidance of 18 June 2019 – III C 3 – S7155/19/10001: 001

Under § 4 (2) UStG, transactions referred to in § 8 (1) sent. 1 to 5 UStG are zero rated for the maritime industry. Zero rating (VAT exemption with entitlement of input VAT deduction) is based on Art. 148 letters a–d of the VAT Directive.

According to the tax authorities, qualifying ships must be existing vessels that, based on their construction type, are intended for acquisition by the maritime industry or for the rescue of shipwrecked persons; tariff classification is the determinant.

A vessel is regarded as "existing" at the earliest from the date of its (traditional) launch or lifting into dry dock. This formulation was added by the BMF guidance of 5 September 2018 – III C 3 – S 7155/16/10002. However, it did not clarify all doubtful issues that arise from practice.

The formulation has therefore been amended by the BMF guidance of 18 June 2019 as follows: "A vessel is regarded as 'existing' from the date of acceptance by the ordering party".

The principles of this guidance are to be applied to all pending cases. However, for sales carried out prior to 1 July 2019 (§ 4 (2), § 8 (1) sent. 1 UStG), there is no objection to following the previously applicable administrative opinion; furthermore, no invoice adjustments for 2018 and the first half of 2019 are required on the basis of the BMF guidance of 5 September 2018.

Zero rating of transactions for the maritime industry II

CJEU, ruling of 20 June 2019 – case C-291/18 – Grup Servicii Petroliere

The case in dispute concerns the Romania-based company Grup Servicii Petroliere. In May 2008, this company sold three offshore jackup drilling rigs used in the Black Sea to Maltese companies for a total of approx. EUR 82 million. The issue in dispute is whether Grup Servicii Petroliere was allowed to issue invoices without showing VAT for the supply of these rigs under Art. 148 letter c of the VAT Directive and applicable national law.

The CJEU has rejected zero rating under Union law in response to a submission from the Romanian court. Art. 148 letters a and c of the VAT Directive should be interpreted to the effect that the expression "ships used on the high seas" necessarily implies that the floating constructions in question are used for navigation. A ship can only be regarded as used for navigation if it is at least mainly or primarily used for transport in maritime space. Zero rating is thus not applicable to the supply of floating constructions such as the offshore jackup drilling rigs referred to in the main proceedings, which are primarily stationary for the offshore extraction of hydrocarbons.

Please note:
Under German law, too, the supply of such offshore drilling rigs is unlikely to be zero rated under § 8 (1) sent. 1 UStG. The qualifying vessels are therefore removed from certain positions/subpositions of the customs tariff. There is no reference to position 8905 of the customs tariff. This non-qualifying position encompasses "lightships, fire floats, dredgers, floating cranes and other vessels where navigation is of subordinate importance compared to their principal application; floating decks, floating or submersible drilling or production platforms".

KPMG LAW

Tax corrections during tax audit – Important changes to administrative directives

Background
In case the management of a company realizes that tax returns of the company which have been filed are incorrect, each member of the management is obliged by German law to immediately inform the competent tax authorities correspondingly and to correct the incorrect tax returns by informing the competent tax authorities about the correct facts and figures, unless they are statute-barred.

This obligation applies regardless of whether the tax period in question has already been subject to a notification of a tax audit, or such an audit is already ongoing. The information of the tax authorities is only unnecessary in the case, if the discrepancy has already been recognized during the tax audit.

In the context of preventative consulting, it is general practice to draft the obligatory information and correction letter in a way that it also fulfils the requirements for a penaltyfree or fine-free voluntary selfdisclosure as a precautionary measure (a so-called "self-disclosureproof" correction).

However, a penalty-free selfdisclosure is not effective for tax periods and tax types being subject to the tax audit. However, a fine-free self-disclosure is still possible in these cases.

Existing tax administrative directives
In line with the existing administrative directives, self-disclosure cases (if not explicitly named, then at least recognisable as such) were and are to be transferred as a matter of course to the criminal department for inspection. Additionally, any tax returns showing signs of possible intentional or gross negligent tax evasion must be transferred to the criminal department. There is no obligation to transfer tax corrections if they are without doubt based on subsequent findings of the taxpayer.

In effect, this allowed quite a broad margin of judgement for the tax official dealing with tax correction letters.

Changes to existing directives as of 1 January 2019
With effect on 1st January 2019 major restrictions on the margin of judgement for the tax authorities when dealing with tax corrections came into force. In concrete terms, tax authorities are now obligated to transfer all tax corrections submitted during an active tax audit (regardless of its explicit designation or content) to the criminal department for inspection.

We anticipate that this directive may be interpreted comprehensively by tax officials. As such, tax corrections for time periods not (yet) included in the scope of the tax audit may also be transferred to the criminal department during an active tax audit.

Please note:
The stricter auditing processes as presented above could have serious consequences regarding tax corrections. In future, the criminal department will receive significantly more tax corrections for inspection than previously.

This especially concerns cases in which a penalty-free self-disclosure is no longer an option due to the block imposed by a tax audit. It almost goes without saying that this means an increased risk of criminal procecution.

As the tax authorities' criminal specialists, start inspecting amendment notices earlier than ever, it makes sense from a business perspective to involve specialist lawyers and tax advisors from an equally early stage, especially when considering legal representation in the event of a prosecution.

KPMG Law Rechtsanwaltsgesellschaft mbH and the tax expert colleagues at associated KPMG AG Wirtschaftsprüfungsgesellschaft are ready to assist you.

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OTHER

VAT Reporting in the United Kingdom – Making Tax Digital for VAT

HMRC VAT Notice 700/22

The British tax authorities – Her Majesty's Revenue and Customs (HMRC) have implemented a new technological means by which companies have to keep their VAT records and report their VAT returns in the UK – called Making Tax Digital or MTD for VAT.

The new system is in place since 1st April 2019 and obligatory for all companies exceeding a threshold of GBP 85.000 in taxable turnover during a rolling 12 month period in UK unless they are already exempt from filing VAT returns in UK. Furthermore, a deferral group has been implemented, which allows a certain group of companies to only mandatorily use the MTD interface as of 1st October 2019. Companies, which are included in the deferral group have been notified by HMRC.

The first return to be handed in via the MTD interface is the first one due after the above mentioned deadline.

MTD for VAT requires that businesses maintain digital records in functional compatible software that:

- Enables the digital link of data from an Accounting System (ERP).
- Can create a VAT return from the digital records.
- Can connect to HMRC systems via an Application Programming Interface (API). The VAT returns have to be submitted via digital link to HMRC's portal through accredited software.

HMRC accepts a spreadsheet as a digital record however API enabled software will be needed to extract and submit the data. The software must be able to both send and receive data.

The intention behind MTD is to minimize VAT errors resulting from manual intervention.

A number of companies provide software solutions for the reporting of MTD VAT returns. HMRC has issued a list of accredited software programs, which is available at the homepage of HMRC (see below). KPMG VAT-Web is one of these solutions, which enables a compliant VAT return filing for MTD.

For more information, please refer to:

https://www.gov.uk/guidance/sign-up-for-making-tax-digital-for-vat

https://home.kpmg/de/en/home/insights/2019/01/vat-web-elektronische-umsatzsteuererklaerung.html

https://directservices.kpmg.de/html/en/vat-web.php

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* Trade & Customs

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