

## **Taxation: Commission proposes amendments to the VAT treatment of electronically delivered services**

*The European Commission has presented a proposal for a Directive to modify the rules for applying value added tax (VAT) to certain services supplied by electronic means as well as subscription-based and pay-per-view radio and television broadcasting. The objective of the proposal is to create a level playing field for the taxation of digital e-commerce in accordance with the principles agreed at the 1998 OECD Ministerial Conference and to make compliance as easy and straightforward as possible. The proposal mainly concerns the supply over electronic networks (i.e. digital delivery) of software and computer services generally, plus information and cultural, artistic, sporting, scientific, educational, entertainment or similar services. The proposal would ensure that when these services were supplied for consumption within the European Union, they were subject to EU VAT, and that when these services were supplied for consumption outside the EU, they were exempt from VAT. The changes modernise the existing VAT rules to accommodate the emerging electronic business environment and to provide a clear and certain regulatory environment for all suppliers, located within or outside the EU. The proposal also contains a number of facilitation and simplification measures aimed at easing the compliance burden of business.*

"These amendments would facilitate electronic commerce by giving business security and certainty as to its obligations under the EU VAT system", said Taxation Commissioner Frits Bolkestein. "By modernising the VAT system to address the electronic delivery of services, we will ensure that all stakeholders are able to participate on a fair and equitable basis in the development of the information society in accordance with the principles agreed at the 1998 OECD Ministerial Conference in Ottawa."

The proposal aims to amend the European Union's VAT system to take account of the emergence of the Internet as a medium for international commerce. A basic principle of the EU VAT system is that all supplies for consumption within the EU are subject to VAT, whilst supplies for other jurisdictions are not. In the case of physical goods purchased over electronic networks and then delivered by traditional means, the existing VAT system provides for taxation in accordance with this well-established principle. Accordingly, the growth of the Internet requires no changes in respect of transactions involving physical goods.

The current VAT rules do not, however, adequately address the supply of services delivered online by digital means, notably as regards such services traded between EU and non-EU countries. Such supplies were simply not envisaged at the time the current VAT legislation was established. As a result, application of the current VAT rules to electronically delivered services produces discriminatory results. At the moment, electronically delivered services originating within the EU are always subject to VAT irrespective of the place of consumption, whilst those from outside the EU are not subject to VAT even when delivered within the EU.

This situation has the potential to constitute a major distortion of competition and to place EU service providers at a disadvantage relative to non-EU service providers.

The proposed amendments to the VAT rules will correct this situation, providing a level playing field for EU and non-EU operators and reinforcing the fundamental principle that taxation should take place in the jurisdiction where consumption occurs. Stated simply, electronically delivered services for consumption within the EU will be subject to VAT, whilst those for consumption outside the EU will not be subject to VAT.

Under the proposal, the application of VAT would depend on the tax status and location of the recipient. Electronic services delivered from one Member State to businesses located in another Member State within the EU would be generally supplied without VAT, with the VAT paid by the business customer on a self-assessment basis with his regular VAT returns (the so-called 'reverse charge mechanism'). Where electronic services were delivered from one Member State to consumers in another Member State within the EU, the supplier would continue to charge VAT at the applicable rate in the Member State where the supplier was registered. For example, an Italian company selling software and delivering it over the Internet to a consumer in Spain would continue to charge VAT at the rate applicable in Italy, as at present.

### **Arrangements for non-EU operators**

For non-EU operators, the administrative obligations would be as simple and straightforward as possible. Non-EU operators would only have to register for VAT purposes where they undertook business to consumer transactions. They would not have to register if they undertook only business to business transactions because business customers pay the VAT themselves on a self-assessment basis under the so-called 'reverse charge mechanism'. Where their annual sales to consumers in the EU exceeded a minimum turnover threshold of €100,000, non-EU operators would be required to register for VAT purposes, but only in a single Member State (they could choose any Member State where they supplied services). They would then charge VAT at the rate applicable in the Member State they have chosen and only have to deal with a single tax administration within the EU.

Finally, the proposal would also clarify the rules concerning the application of VAT to radio and television broadcasting services supplied on subscription or pay-per-view basis. These services are increasingly significant commercial activities, and the current VAT legislation discriminates against European based suppliers. The proposed changes would ensure that EU and non-EU suppliers operate under the same rules concerning VAT and place of supply.

The proposal reflects the result of widespread consultations on the taxation issues raised by the growth of electronic commerce undertaken by the Commission with the Member States' tax administrations and with business representatives.

The proposal will now be forwarded to the EU's Council of Ministers for adoption, which can take place once the European Parliament and the EU's Economic and Social Committee have given their Opinions.

For further information concerning the proposal, see also MEMO/00/...

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