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The Second VAT Simplification Directive - simplification but also a step backwards

Preface

On March 20th 1995, the Commission adopted the Second Simplification Directive. As a result of this, the Sixth Directive (78/583/EEC) and the various national laws changed. Some of the simplifications brought promised improvements. However, the Second Simplification Directive also contained some disadvantages. Taxable persons are now obliged to register more often for value added tax purposes in another member state of the European Union (EU). UNICE therefore suggests further amendments to the rules.

The old Article 28a

According to the old version of article 28a(5)(b), fourth indent, the dispatch or transport of any tangible property by or on behalf of a taxable person for the purpose of “the supply to the taxable person, under the conditions set out in (a), of contract work carried out in the member state of arrival of the dispatch or transport of the goods in question,” was not effected as a supply of a good for consideration.

In 1993, the effect of this article, together with article 9(2)(c) of the Sixth Directive, meant that taxable persons were often confronted with foreign VAT or obliged to register for value added tax purposes in another member state of the EU. If, for example, three taxable persons (a supplier, a contractor and a recipient) were involved with the delivery under contract of tangible property, the recipient was confronted with foreign VAT or obliged to register for value added tax purposes in another member state of the EU.

Therefore, the European Commission and the member states of the EU decided that the rules had to be simplified and in September 1993, the simplification measures were published. As a result of this, the recipient in the above mentioned example was neither confronted with foreign VAT nor the obligation to register in another country.

The Second Simplification Directive and the new article 28a

The new legislation deems the delivery of tangible property, made or assembled by a contractor from materials entrusted to him by his customer, to be a supply of a service from the contractor to the customer.

The place of supply of such a service is the place where those services are physically carried out (article 9(2)(c) of the Sixth Directive). By way of derogation from article 9(2)(c), a new article (article 28b, paragraph F) was introduced for the supply of cross-border services. This new article deems the place of supply of such a service to be within the territory of the member state which issued the customer with his VAT registration number. (This article is only applicable if the customer is identified for value added tax purposes in a member state other than that in which the service is physically carried out and if the goods are transported out of the member state in which the supply of the service takes place). As a result of the new law, administrative obligations were reduced.

The Second Simplification Directive also replaced the simplification measures of September 1993.

As a result of these changes introduced by the Second Simplification Directive, taxable persons are in a similar situation to that pertaining before the simplification measures of 1993. The following examples illustrate the point :

Example I

A (a taxable person in member state A) sells various materials to B (a taxable person in member state B). B contracts with X (also a taxable person in member state A) to manufacture new goods out of various materials. The materials are firstly transported (within the same member state) from A to X. Finally the new goods are sent to B in member state B.

According to the new legislation, the supply of the materials by A to B is a domestic supply in member state A and is subject to VAT in member state A. B is confronted with foreign VAT. The transport of the goods from member state A to member state B is deemed to be an intra-community transaction by B who is obliged to register for VAT purposes in member state A.

Example II

A (a taxable person in member state A) contracts to sell goods to B (a taxable person in member state B). A does not have a stock of the goods and employs C (a taxable person in member state C) to produce the goods from materials which are owned by A and which are transported to C. After production the goods are transported to B.

According to article 28a, the transport of materials from member state A to member state C is deemed to be an intra-community transaction because the goods are finally transported to another member state, namely B. This means that A has to register for value added tax purposes in member state C.

Conclusion

As a result of the Second Simplification Directive, taxable persons are in certain circumstances (three taxable persons situated in two or three different member states) confronted with foreign VAT or an obligation to register for VAT purposes in a country other than that in which they are established. In example I, B is confronted with foreign VAT and furthermore has to register in another member state. In example II, A is obliged to register in another member state.

Registration for VAT purposes, including filing VAT returns, is a time and money consuming activity. In some member states a taxable person is even obliged to appoint a fiscal representative

and this increases the cost to the trader. If however the measure abolished in autumn 1993 is adjusted and re-implemented in such a way that the supply of goods by A to B can be considered to be an intra-community transaction between A in member state A and B in member state B, then a major simplification can really be achieved.

UNICE calls on the Commission to draft a proposal to reflect this improvement for European business.

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