

In the continuing battle between the digital economy and the international tax system, the European tax system is about to claw back a point on the VAT front. From 1 January 2015, the VAT treatment of digital services supplied to consumers is changing and businesses making those supplies will need to be ready.

Currently, when digital services are supplied to consumers, the supplier accounts for VAT based on its own location. However, from the start of next year, this position will be reversed and the place of supply for VAT purposes will be the location of the consumer. If a supplier supplies digital services to consumers in several Member States, the supplier will be obliged to charge, and account for, VAT in each of those Member States – a potential administrative nightmare.

## Which Services Does this Affect?

“Digital services” broadly consist of broadcasting, telecommunications and e-services. HM Revenue & Customs (HMRC) have issued guidance on what each of these digital services encapsulates in high-level terms:

- **broadcasting** includes “the supply of television or radio programs to a schedule by the person that has editorial control of those programmes”;
- **telecommunications** includes “the service of sending or receiving signals by wire, radio, optical or other systems”; and
- **e-services** includes items such as apps, music downloads, gaming and e-books.

HMRC acknowledge that the provision of digital services “is a rapidly evolving sector” and that the services affected will undoubtedly be broader than those contained in the guidance (i.e. those listed above). However, HMRC have made clear that the rules applying to digital services will not extend to the supply of goods where the only use of an electronic system is to place the order for the good.

## Determining the Place of Supply

Currently, a supplier only needs to be concerned with its own location when accounting for VAT on digital services. The reversal of the place of supply brought about by the new rules will result in an increased burden on the supplier, who will be obliged to establish the correct place of supply and get the VAT treatment right. Suppliers will need to identify the place where their consumer is established, has their permanent address or usually resides. “Usual residence” is defined in EU VAT regulations as the place where a person has personal and occupation ties. As a result, if a consumer is a UK citizen but works and spends most of their time in another EU country, the place of supply to them of a digital service, and therefore where the VAT will be due, will be the other EU country - not the UK.

In certain circumstances, suppliers will be able to *presume* the location of a consumer. For example, if the service is supplied through a mobile phone, the location will be based on the country code of the SIM card. It will, however, be possible for the supplier to rebut the presumption - to do this, the supplier will need to collect and maintain three pieces of non-contradictory commercial evidence such as the billing address of the customer, the IP address of the device used by the customer or the customer’s bank’s address. In situations where there is not an automatic presumption, the supplier will be expected to obtain and keep records of two pieces of non-contradictory evidence showing the location of the consumer. In both situations, collecting this evidence will add a potentially costly and time-consuming administrative process to the majority of suppliers’ procedures, particularly if they will need to introduce new systems and controls in order to determine a consumer’s location.

## VAT Mini One Stop Shop (“MOSS”)

For suppliers who supply digital services to consumers based all around the EU, the additional layer of complexity introduced by the rules, and the new obligation to account for VAT in every country where consumers are based, may look a daunting prospect. However, thanks to the introduction of the European Union’s VAT MOSS online service, suppliers will only need to register in one EU Member State and submit one return and payment in each quarter in respect of all EU digital supplies.

There are two MOSS schemes: one for suppliers based in the EU; and one for suppliers based outside of the EU. The schemes are voluntary but, where suppliers are supplying to consumers across the EU, it is recommended they register as the scheme eradicates the need to register and account for VAT in every Member State where that supplier has a consumer. Registration in all Member States is open from October 2014 in all Member States and the scheme can be used from 1 January 2015.

## Where Should Suppliers Register?

HMRC have produced a handy flowchart (available [on the HMRC website](#)), which details where a supplier can register. Basically, a supplier can register for MOSS in the Member State where the supplier has its business establishment or head office. Returns will then be submitted detailing the supplier’s supplies of digital services and paying any VAT due. MOSS returns are an additional requirement to usual national VAT returns, which will still need to be submitted.

If a supplier uses the MOSS system *and* that supplier is registered for VAT in another Member State (i.e. as well as the one where it is registered under the MOSS scheme, which is possible where, for example, the supplier has a fixed establishment in more than one Member State), it will not need to account for VAT under MOSS in that other Member State.

Instead, the supplies made to consumers in that other Member State should be declared on the supplier's usual VAT return in its home jurisdiction. Suppliers based outside the EU can register in any Member State, although a supplier can only have one MOSS registration across the whole of the EU.

However, there is a big but with MOSS. In order to use MOSS, the supplier must already be registered for VAT – something that has attracted some criticism. For example, a small start-up e-services company in the UK that has not yet reached the UK VAT supplies registration threshold of £81,000 may still need to register and account for VAT in the Member States where its customers are located because many Member States do not have a VAT registration threshold (or have one that is set at a lower financial threshold than the UK). This leaves a small company in the unenviable situation of having to either register for VAT in every Member State it supplies to, or registering for VAT in the UK so that it can then register for (and take advantage of) MOSS. However, once the supplier is VAT registered in the UK, it will also need to charge and account for VAT on UK sales. This is presumably an unintended consequence of the registration requirements but is clearly something that is potentially very prejudicial to those small businesses that are affected.

Representative members of VAT groups can register their group for MOSS, allowing group members to account for VAT on the supply of digital services to consumers through MOSS. However, care is needed when dealing with VAT groups, not least because different Member States have different rules for VAT groups.

## What Happens Once Suppliers are Registered?

### Returns

MOSS returns need to be submitted within 20 days of the end of the calendar quarter return period, which may be a different date to the standard national VAT return. MOSS returns cannot be submitted before the end of the quarter so, each quarter, suppliers have 20 days to submit their returns. Nil returns must be submitted if no supplies are made and there are no *de minimis* rules for low value sales.

Returns can be amended by correcting the original return within three years. However, where national legislation allows a longer period for correcting returns, this national legislation will apply. For example, the UK allows for amendments to a VAT return for four years from the end of the tax period, so this duration will trump the MOSS' three years.

### Payments

One single payment, due at the same time as the return, is to be made to the Member State in which the supplier is registered for MOSS. Payments will be accepted electronically but there will be no direct debit facility. The Member State which receives the payment will then distribute the relevant amount of VAT to the other Member States in which the supplier has made supplies.

If a consumer has been invoiced in a currency other than the one used by the Member State where the supplier is registered for MOSS, the MOSS return will need to show the billed amount converted into the currency that the Member State uses, again increasing the administrative burden for suppliers who supply to various countries across the EU.

### Recovering input tax

The MOSS scheme only provides a way for suppliers to account for output tax. Input tax will still need to be recovered through the domestic VAT return.

### Invoicing

The supplier needs to adhere to the VAT invoicing rules in the consumer's location despite being registered for MOSS in one Member State. Although the majority of Member States do not require VAT invoices for supplies to consumers, suppliers will still need to be aware of the invoicing requirements in each and every Member State that they supply digital services.

### So...

As can be seen, the new rules are resulting in an array of changes for suppliers of digital services to consumers across the EU. Along with registration for MOSS, consideration needs to be given to consumer location and any specific invoicing rules where they are based. Small UK companies that provide digital services but which are not registered for VAT in the UK need to note that the changes have even wider implications for them given the differing VAT registration rules in the different Member States.

Christmas may not be such a peaceful season for suppliers that are caught by these changes. It is undoubtedly worth those suppliers spending some time checking the impact (if any) of these new rules on their business as soon as possible.

Should you have any questions on any of the above, or require any assistance ascertaining the effect of these changes for you, please contact any member of our Tax Strategy & Benefits team.

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