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EXECUTIVE SUMMARY OF THE IMPACT ASSESSMENT

Accompanying the document

**Proposal for a
COUNCIL DIRECTIVE**

**amending Directive 2006/112/EC on the common system of value added tax, as regards
the treatment of vouchers**

{ COM(2012) 206 final }
{ SWD(2012) 127 final }

1. Problem definition

Transactions involving the purchase of goods or services increasingly involve vouchers. These can take many forms including but, not limited to, prepaid telephone credits, tear-off coupons which lead to a discount and electronic codes which generate an entitlement to goods or services or something as traditional as a gift voucher. What they have in common is that vouchers are not in themselves the primary purpose of a transaction but rather facilitate the purchase of other goods or services.

Vouchers can have an impact on the taxable nature of the underlying transaction. This can involve the timing of a transaction, the place where it occurs and the value to be assigned to the exchange between buyer and purchaser. All of these factors can in turn influence the VAT consequences of the transaction and, as a result, the tax revenues of Member States. Given the increasing complexity and sophistication of many commercial transactions (particularly those facilitated by technology), this is a growing phenomenon.

The VAT Directive¹, on which the common VAT system of the Member States is based, has no provisions which address vouchers. This is largely because of the age of the legislation. It was enacted in 1977 when vouchers were perceived as marginal and not giving rise to any particular VAT complications. The first pre-paid telecom cards did not appear until the early 1980s and mobile telecom services only became generally available during the 1990s.

Although vouchers are used widely in commercial transactions, prepaid telecom services are by far the single most important area in economic terms. In preparing this impact assessment, a survey² concluded that per annum revenue from prepaid telecoms subscription (now overwhelmingly electronic rather than card based) could be estimated at €36 billion. All other types of vouchers have an estimated total annual value of about half that.

The amount of tax involved is clearly substantial. The lack of common rules in the VAT Directive has meant that over time Member States have developed their own national practices for ensuring correct taxation of the underlying transaction. Unfortunately this has evolved in an uncoordinated fashion. One fundamental dichotomy is between those Member States who seek systematically to tax the value when a voucher is issued and those who tax on redemption. This gives rise to mismatches in taxation which in turn can cause either double or non-taxation. Double taxation is probably relatively rare (if not, it might be expected that there would be more complaints) but in reality it will more often than not simply kill the market, leaving no measurable statistical trace. There is however strong anecdotal evidence that this is a systemic problem for enterprises trying to develop pan-EU business models using vouchers. Non-taxation does not always readily declare itself and macro-level data is hard to come by. Nevertheless, preparatory work here uncovered sufficient evidence that non-taxation is systematically exploited by some operators in the telecom sector who see an opportunity for an unjustified price advantage or merely to increase profits. This information comes either from tax administrations that

¹ Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (OJ L 347, 11.12.2006, p.1)

² "Study of the VAT treatment and quantification of vouchers at an EU level for the provision of economic analysis in the area of taxation" Final Report from Deloitte of 14 July 2010 (as revised). This study is annexed to the Impact Assessment.

identify revenue losses which are not always easily stemmed as well as from businesses complaining about unfair competition. Meanwhile, other operators whose objectives include being tax compliant, will simply refrain from involvement in opportunities, particularly cross-border ones, where the tax consequences are not clear.

2. Subsidiarity

Within the limits of the available data, the Impact Assessment (particularly in its revised form) substantiates the need for action at EU level to resolve these problems. The distortions in the functioning of the internal market and the concerns of industry players about unfair competition are illustrated by reliable reports from established players.

Because the underlying problems can be attributed to shortcomings in EU legislation (in the VAT Directive) which can only be rectified by action at EU level, it is not possible for Member States, acting independently, to remedy the situation and to achieve the objective of uniform application of the tax.

3. Objectives

Other than rectifying the mismatches in taxation mentioned above, uncertainty about the proper tax treatment has given rise to a succession of ECJ cases involving vouchers where either national tax administrations or businesses have resorted to litigation in a search for order. This path has been occasioned by problems in the calculation of VAT on discounts, treatment of input tax, promotional gifts linked to vouchers, advance payments generally as well as the computation of the taxable amount for transactions involving vouchers. Particular problems arise in the distribution of vouchers through chains of distributors, a widely employed commercial practice which often extends to cross-border arrangements. Whilst helpful, none of the decisions of the Court have totally cleared the air and, in the absence of more fundamental and systematic clarification, further recourse to the ECJ on questions relating to the VAT treatment of vouchers is inevitable. The proposal aims to rectify this situation.

Increasing functionality in vouchers, notably prepaid mobile credits, has blurred the dividing line between vouchers and innovative payment systems. In order to ensure correct taxation, this line has to be clearly defined and neutrality assured.

4. Policy options/Assessment of impacts

Three possible policy options for dealing with these problems have been identified.

Taking no action would mean that the problems would persist and probably grow as they are not capable of resolution without action at EU level. The consultation of stakeholders was strongly against such an approach. Doing nothing at EU level would be fundamentally unsatisfactory as current difficulties would only grow, giving rise to increased uncertainty and litigation. Member States do not really have the tools to deal with mismatches in taxation unilaterally, particularly as the VAT Directive in its current state does not provide guidance on arriving at a consistent treatment.

The use of soft law options, such as guidance notes or similar instruments, are only of real value when the underlying legislative provisions are sound. This is not the case here since the problems identified can generally be attributed to the absence of clear rules in the VAT Directive. Seeking resolution through an approach which stops short of full legislative reform, perhaps through the use of soft law structures such as guidelines, has

some initial attraction but is finally considered as unsuited to a fundamental tax problem. Where taxation is concerned, soft law will always be a second-best to a legislative formulation and is generally only useful to compliment or explain what is already provided for in legislation. Here, the fundamental problem is a lacuna in the VAT Directive and this is not amenable to a soft law solution.

The problems identified reveal the need for modernisation in several articles in the VAT Directive. The objectives identified can only be met by amending them and introducing other appropriate consequential amendments in the Directive.

5. Assessments of impacts

Impacts vary according to the roles of different players and the nature of the problems which they now contend with.

For tax administrations, the main objective of the exercise is to close down the loopholes in the tax system which allow or facilitate schemes aimed at the avoidance of taxation. This will be manifested through a reduction in tax avoidance or unintended non-taxation. Secondary benefits, with positive effects on businesses, would be the elimination of double taxation and the negative economic consequences this entails as well as a reduction in uncertainty about tax compliance obligations. Those Member States who have indicated that they suffer revenue losses because of mismatches in taxation under the current rules will see an end to these losses. As indicated in the main text, reluctance on their part to supply specific data on tax losses makes it difficult to quantify the likely benefit.

Actual compliance costs savings are hard to quantify but this does not mean that they are insignificant. Although the impact on recurring standard VAT compliance costs are not expected to be a major factor, the effect on once-off or intermittent costs associated with inconsistency and complexity in tax rules is expected to yield savings.

Litigated solutions, which are a feature of the ongoing problems, are expensive and often unsatisfactory for stakeholders. Reducing the need to have recourse to the courts would represent a significant economic saving, albeit one which is difficult to quantify.

For businesses more generally, achieving order and consistency in these tax rules across the Internal Market will remove barriers to commercial innovation. It is difficult to measure the impact here but the economic benefits can be measured in more qualitative terms. Clear and consistent tax rules should provide, for the telecommunications industries in particular but also for retail distribution operators, an environment which enables them better to reap the economic benefits of the Internal Market.

The expected economic impact on main market players and on the market structure is set out in qualitative form, given the lack of quantification of the tax avoidance problem. The underlying analysis is however based on standard economic reasoning and on knowledge of the sector built up during the investigatory work.

The expected impact of a legislative proposal will to some extent be asymmetric. Business location will be more closely linked to economic and competitive factors rather than tax arbitrage. A reduction in the degree of fragmentation in the Internal Market is to be expected, bring with it benefits of greater market efficiency, choice for consumers and better economies of scale. Some small and marginal operators, whose business

model is entirely predicated on tax arbitraging, may need to adapt if they are to survive in this environment.

No marked social impacts are really expected. Those businesses which might be adversely affected are small, few in number and are not significant employers. Suppliers of pre-paid telecom vouchers whose primary focus is tax arbitraging are often virtual operations with a negligible physical presence. Conversely however, the improved market environment should yield price reductions, notably for international telecommunications benefiting consumers who use pre-paid services.

6. Comparison of options

This leads to the conclusion that a modernisation of the provisions of the VAT Directive is the only way to deliver a robust long term solution. This should include definitions of the different kinds of vouchers, clarification of the tax treatment of distribution chains, rules on computation of the taxable amount and the time of taxation as well as the consequences for the right of deduction.

The VAT problems associated with vouchers can at times appear to be extremely technical. For this reason, the preparatory work involved considerable consultation with Member States and with the businesses involved. In the latter instance, this went much wider than the formalities of the public consultation and in practice extended over the whole timescale of this project. Particular care was taken to cover the implications of innovative practices and to ensure at least some degree of future-proofing for the proposal. As a result, the approach recommended is based on a broad consensus among stakeholders as to what is needed. It is however probable that one consequence of any proposal will be to recognise that some services, notably those offered by telecom operators which had their origins in vouchers, have evolved into something which compete with more traditional payment service providers and neutrality now requires a level playing field for tax purposes.

7. Monitoring and evaluation

It is established practice for the Commission to monitor the implementation by Member States of legislation such as is envisaged here. No further measures are foreseen.