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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

Delegations will find attached Commission document SWD(2012) 127 final.

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COMMISSION STAFF WORKING DOCUMENT

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**

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MODIFICATIONS FOLLOWING THE OPINION OF THE IMPACT ASSESSMENT BOARD

A first submission of this impact assessment was discussed by the Impact Assessment Board at its meeting of 12 January 2011. The opinion of the Board issued on 14 January indicated areas where improvements were needed. It was suggested that the evidence of the existence of problems at EU level needed further development and that this should be supported by the available evidence in order to sustain the case for EU action. It was also suggested that the report should consider whether there were different ways of modifying the VAT Directive and that the analysis of the economic impact on the different actors in the VAT chain should be strengthened.

In order to take into account the recommendations of the Board a number of changes have been made. In section 1.2 (starting page 5), evidence is adduced on the basis of documented instances of mismatches in taxation or competitive distortions to justify the need for action at EU level. Because of difficulties in sourcing data on tax mismatches, it is qualitative rather than quantitative. This notwithstanding, the quality of the anecdotal evidence is sufficiently strong and broad-based to establish the need for action. In section 4.3 (starting page 27) the approach to modifying the VAT Directive is developed and explained in the context of the need to work within its existing structure and which imposes constraints on choice. The suggestions raised in the IAB's opinion about possible choices in modifying the VAT Directive are addressed in the expanded text. The deliverable however is to bring the VAT treatment of vouchers within the established VAT methodology in a consistent manner rather than to develop specific new VAT provisions for vouchers. The difficulties encountered through scarcity of reliable economic data have had negative consequences in developing the quality of the analysis of the impact on the different actors in the VAT chain and this relies heavily on qualitative evidence. This is addressed in section 1.4. The background to the baseline scenario is addressed in section 2.10 and also under the *status quo* option in section 6, albeit that the shortcomings in the availability of data mean that this is assessed in qualitative terms. Finally two tables (starting page 32) seek to strengthen the analysis of the economic impacts by setting out in schematic form, the main impacts of the preferred choices on the different actors.

1. PROCEDURAL ISSUES AND CONSULTATIONS OF INTERESTED PARTIES

1.1. Dialogue with national tax administrations of Member States

Because of the technical nature of the taxation of vouchers¹ and concerns about increasing diversity in treatment, preparatory work had to involve national tax administrations. Vouchers were first discussed in DG TAXUD's VAT Working Party No 1 in 2004. The initial analysis concluded that, for VAT purposes, vouchers fell into defined categories. A distinction can be drawn on where goods or services supplied are sufficiently defined that the VAT consequences are clear from the moment the voucher is issued and where the VAT consequences can only be known at the time of redemption. The former can be referred to as a single purpose voucher (SPV) and the latter as a multi purpose voucher (MPV).

Since VAT is a tax on consumption, it is not the supply of a voucher but rather the underlying goods or services to which it carries an entitlement that should be taxed. The practicalities of achieving just such an outcome require a distinction between SPVs and MPVs. Furthermore,

¹ The question of what constitutes a voucher for VAT purposes is addressed in section 2.

the taxable amount for the supply of goods or services should be the sum paid by the final purchaser using the voucher. For certainty and simplicity, the face value of the voucher is in principle the presumptive taxable amount (after allowing for the VAT element) of the supply. The redeemer of the voucher, whether or not he has issued it, should be the person liable to pay VAT. It was also posited however that circumstances might arise where someone else than the redeemer can be held jointly and severally liable for payment of the VAT (the issuer or an intermediary for instance).

Member States agreed with this broad line of approach but asked the Commission to take account also of VAT treatment in distribution of vouchers.

Three further meetings with Member States followed during 2004 and 2005. These explored the chargeability of the tax, the treatment of distribution chains, the taxable amount for the supply of redeemed goods or services, cash-back and money-off vouchers, as well as general compliance issues. Within a distribution chain of MPVs the Commission suggested that the taxable amount of the distribution service will be the difference between the face value of the vouchers and the purchase price paid. Furthermore, it argued that transactions involving vouchers are not to be regarded as (exempt) financial services. Alternative solutions for the treatment of cash-back and money-off vouchers were considered, taking account of relevant ECJ judgments.

Additional discussions with Member States took place during 2006 and 2007, covering, *inter alia*, the preparation and outcome of a public consultation.

A final meeting discussed the general principles for taxing transactions involving vouchers and considered an early draft outline of legislative provisions. As such transactions can be relatively complex, involving changes in the value of a voucher as it progresses through a chain, different economic models of distribution, the margins or fees of intermediaries as well as resolving uncertainty regarding the taxable amount, they were held on the basis of a paper outlining examples of multilayered transactions involving vouchers.

1.1.1. *Fiscalis seminars*

In addition to these meetings, vouchers were discussed at two Fiscalis² seminars.

During a seminar held in 2002 on schemes for the artificial reduction of the taxable amount for VAT avoidance purposes, participants outlined concerns about the use of vouchers in the course of promotional schemes. The Commission was urged by Member States to investigate the risks to tax revenue and to consider whether action was needed.

A second seminar was held in 2006, specifically on the tax treatment of vouchers. It examined the detailed VAT treatment of vouchers, the use of vouchers in promotion schemes and innovative payment systems which raises issues about the limits of vouchers. Attention was given to the potential for cross-border mismatches as well as practical problems arising from differences in national interpretations attributable to shortcomings in the VAT Directive.

To develop an appreciation of evolving commercial practices, speakers and discussants from business were invited. This helped to identify and raise awareness of VAT problems with vouchers because of the increasing sophistication and functionality of these instruments but

² The Fiscalis programme is a Community programme aimed at improving the operation of tax systems in the internal market. Seminars on tax issues have been a regular feature.

also concerns about the technical difficulties in securing an equitable charging of VAT. The seminar also addressed issues relating to the practical implementation of the ECJ judgments.

The discussions emphasised the following points.

- The need for a dividing line between the issue and the distribution of MPVs and more complex innovative payment systems which fall under exempt financial service. A level playing field for tax is however required between suppliers of broadly similar services.
- Any future proposal should ensure clear, correct and consistent taxation through the distribution chain of an MPV.
- Some harmonisation of the technical qualification of vouchers is needed. The time of taxation should be aligned so that it would normally be predicated on the ultimate supply of the underlying goods or services rather than the sale or supply of the voucher itself. This can only be assured by updating the EU legislation.

1.2. Public consultation

In November 2006 the Taxation and Customs Union Directorate-General issued a consultation paper seeking views from the public and business. It described the inconsistencies in the VAT treatment of vouchers between Member States, explaining that these inconsistencies may offer opportunities for tax avoidance or may raise situations of double taxation or non-taxation (for cross-border transactions).

In describing several kinds of vouchers the consultation paper analysed possible options for their VAT treatment taking into account such fundamental elements as the place and the time of supply and the taxable amount. Also the dividing line between vouchers and more generalised means of payment was analysed in order to avoid unwelcome distortions.

Mention was made of existing ECJ case-law to clarify the understanding of the interpretation of the current legal framework.

The paper was addressed to stakeholders who issue or deal in vouchers of all kinds, and businesses operating or using payment systems as well as their advisors.

The purposes of consulting the public on this issue were to:

- check the accuracy of the analysis;
- gather relevant feedback; and
- assist the Commission's services in developing their thinking on the subject.

Over 30 responses were received.

Virtually all agreed with the analysis and tentative definitions put forward and no strong negative comments were expressed on the options proposed. Technical complexity of this sector and the diversity of the respondents' business models meant that the results did not however point to a clear course of action. Nevertheless, a number of priority areas were highlighted as needing attention in any legislative initiative. These included:

- The competitive balance between some more developed forms of vouchers (particularly offered by a number of telecommunications operators) and the classic means of payment such as credit and debit cards is considered particularly important. The neutrality of treatment between systems having the same functionalities is considered fundamental and any change in the legislation should not disregard this principle.
- Strong emphasis from business respondents on the need to clarify the VAT treatment of vouchers in a market which is constantly increasing and constantly evolving and indication of the misunderstandings and misapplications of the VAT rules with which they are faced.
- Divergence of national rules affects the development of the market.
- Change in the VAT treatment should take into account the time needed by business for adaptation of their systems. A transitional period should be considered.

The consultation document itself and a summary of the responses can be found at http://ec.europa.eu/taxation_customs/common/consultations/ and should be seen as annexes to this Impact Assessment.

In addition, the work leading to the preparation of the Impact Assessment has unearthed a significant body of well documented individual cases where the consequences of shortcoming in VAT legislation at an EU level and be substantiated and shown to be economically significant (see box below). In the absence of hard data, these documented examples describe disruptive or distortive scenarios which are of sufficient materiality to warrant action. Although the evidence presented, as is typical of information on tax avoidance activities, is largely anecdotal, it is both sufficiently diverse and representative to sustain the existence of a systemic problem

- **Problems currently being experienced by a pan-EU telecommunications operator.**

A recent (2011) contribution from a large multi-national telecommunications group gave the following details. The company has given this information on the basis that it will not be identified³.

The company systematically tries to avoid double taxation as this will either reduce its margins or make its prices unattractive. Moreover, even if the VAT Directive and its related jurisprudence do not countenance double taxation, it is often impractical to recover a part of the double charge, particularly where this is composed of myriad small sums even if the overall total is significant. Moreover, it would be difficult to reach agreement with the Member States concerned on who has the taxing rights with going to litigation. Where double taxation is inescapable, it is usually commercially impossible to pass the full cost on to customers (as some of the competitors do not face this problem,) so the company absorbs a large part of it. The company identifies recurrent double taxation in the following instances:

- *Customers of Member State A using vouchers issued in Member State B to top up their mobile accounts in Member State A. Double taxation occurs where Member State A*

³ In order to respect confidentiality, these examples of existing difficulties do not identify specific operators or individual Member States. Each case however is a description of documented cases of such problems received directly from authentic sources.

requires VAT to be accounted on usage while Member State B collects VAT at point of sale.

- *Where a Member State collects VAT on top ups at point of sale but the top up is subsequently used to purchase goods or services that are not subject to VAT (or are not subject to VAT at the standard rate) or to purchase goods or services from a 3rd party.*

The company estimates that within the EU, it overpays around €3,500,000 because of unavoidable double taxation. Their 2011 submission to the Commission gives a detailed breakdown (not for publication) of how this figure is made up from detailed figures for UK, Germany, Netherlands, Spain, Italy, Czech Republic, Greece, Hungary, Ireland, Malta, Portugal and Romania. The company has a significant presence in these markets.

This figure may seem relatively small if not given proper context. Even if extrapolated, based on the market share of this company, to the total market, quantifiable double taxation would probably not exceed €20,000,000. This however would be a gross understatement of the significance of the problem.

Businesses however will seldom tolerate high levels of double taxation on an ongoing basis. They may lobby to change the rules which cause this but for small and medium-sized firms the typical response would simply be to avoid such situations. A frequent result of double taxation is to kill the market and the relatively low reported figures for actual double taxation need to be seen in this context. Hence, the real economic cost is the opportunity cost of ventures not pursued due to the shortcomings in the current VAT rules. This will be particularly marked for sectors with a high share of smaller operators or for new entrants to the market who need attractive pricing offers to attract customers and can neither absorb nor pass on the consequences of double taxation.

- **Market access problems experienced by content provider.**

A further recent example given to TAXUD concerns the take up of 3rd party purchases in countries which tax mobile recharges at point of sale. A UK provider of ring-tones attempting to sell to the Italian market and collect payment from the customers' prepay balances will find the fact that Italian VAT has to be accounted for by the network operator (without any viable mechanism for avoiding or recovering UK VAT) a significant commercial obstacle. The source did not offer any figures for double taxation suffered but made the point that the commercial reaction would be simply to close down this line of business as unsustainable.

- **Tax losses being experienced by Member State.**

The following example of non-taxation was recently (2010) brought to the attention of TAXUD by a Member State which was suffering revenue losses because the provisions in the VAT Directive were open to more than one interpretation:

Member State A (the source of this information) applies a system of taxation upon redemption system which leaves it open to tax arbitraging in the cross-border sale of prepaid telecommunications vouchers resulting in non-taxation of the service. Prepaid vouchers are marketed on the domestic market by telecommunications operators established in Member State B which normally charges taxation upon the sale of vouchers. In practice, these vouchers are for a fungible service and can be widely used, including in other Member States. Where a voucher is sold in Member State B to an intermediary established there in Member

State A, the sale is not taxable in Member State B because under the general rule on the chargeability of VAT for B2B services, this service occurs in the Member State of the recipient. Under the current rules, VAT will not be collected in the Member State A (where taxation is on redemption) if the voucher is redeemed against a telecommunications service by a private individual in this Member State. Following the general rule on the chargeability of VAT on B2C services, this telecommunications service is deemed to take place in the Member State of the telecommunications operator but there is no mechanism for collecting VAT when the private individual using the service does so in another Member State.

The tax losses suffered have not been disclosed to the Commission but were sufficiently significant that Member State B (at the behest of Member State A) gave consideration to changing its VAT law to end the mismatch. In the event, the legislative change was very limited (seemingly, Member State B did not want to expose itself to another mismatch elsewhere) and this has not ended the tax losses for Member State A.

- **Telecommunications operator complains that inconsistency in VAT rules for prepaid mobile exposes it to unfair competition.**

The Commission has recently received a complaint from a big telecommunications company Q established in Member State X. The complaint related to non-taxation of prepaid cards sold by retailers in Member State X of prepaid phone cards issued by another telecommunications company R established in Member State Y. This is possible through exploitation of differences in the time of taxation between the two countries. Since the sale of prepaid phone cards by company Q in Member State X carry VAT, a serious distortion of competition between companies Q and R has developed.

The authorities in Member State X have also drawn the attention of the Commission to this specific problem which is leading to tax losses. The level of these losses was not disclosed but the Member State stressed the absolute need to establish a level playing field for vouchers since the current situation distorts competition within the Community and leads to tax losses.

- **National tax administration informs Commission of systemic tax losses which can only be closed off by modernising the provisions of the VAT Directive.**

Member State M reports significant ongoing problems with prepaid mobile credit vouchers originating in Member State K and which escape all VAT. Member States K taxes on redemption and Member State M taxes on issue. The mismatch is systematically exploited by an important number of small distributors who see an opportunity to either increase margins or offer lower prices. In many instances, they sell vouchers aimed at ethnic or emigrant communities with attractive rates for calls to particular countries. The authorities in Member State M have had some limited success in closing off tax losses by initiating prosecutions under the abuse of rights principle. This however is proving to be a cumbersome way of addressing the issue and falls well short of being a panacea. There are a large number of small operators distributing the vouchers which meet a demand for cheap calls. If one is prosecuted successfully, another will fill the space here. The problem can only be resolved definitively by reforming the EU VAT rules.

- **A company which markets games downloads, generally paid for by vouchers, finds that it has to contend with persistent double taxation in developing its presence across the EU single market.**

Company D is an established VAT registered entity in EU Member State E where it operates a games download business. Customers are young people who do not generally have credit cards. Payments for downloads can however be made using pre-paid cards (vouchers) which are distributed by retailers. The interpretation of the VAT rules applied in the Member State where the company is established mean that VAT will always be due there. As however different interpretations apply in other Member States, the distributors in several of these Member States also have to account for VAT, notwithstanding that VAT has already been paid in E. It is impractical to recover this double taxation and as the retail price of the voucher is constant, the cost is absorbed by the company. The economic impact varies according to the combination of Member States concerned but can involve up to 35% of gross revenue from vouchers going to fund the VAT liability. Although this has not finally prevented the business model from proceeding, the company continues to face barriers in understanding the different rules and reconciling the variable margins (which also impact distributors) caused by double taxation.

- **Position of EBF on distortion in the EU payment service sector.**

The European Banking Federation wrote: "that a consistent VAT-treatment is highly desirable to ensure a level playing field for payment service providers that active in the Single European Payments Area. (...) At present we observe that the VAT-regimes in Member States are different between Member States for similar payment services." The EBF concludes that this can only be rectified by modernising the VAT Directive.

- **Observations of the BBA on competitive imbalances.**

The British Bankers' Association "considers that it is imperative that a new definition (or definitions) of what constitutes a voucher is introduced at the earliest opportunity. This would avoid potential distortions in the way exemptions are currently applied.(...) Compared to the telecommunications operators the financial services companies suffer the additional costs of both irrecoverable VAT and regulation." The BBA sees the current lack of clarity and consistency as conducive to unfair competition.⁴

In the view of DG TAXUD, the problems described here are clearly of an EU nature, generally extending across more than one Member State and cannot adequately be resolved at Member State level. They are sufficiently documented and sufficiently serious to warrant action. The evidence here is also consistent with other, albeit less documented, examples of mismatches and competitive problems encountered by business, something which confirms the representative nature of the examples cited here.

1.3. Deloitte Study

The study commissioned from Deloitte⁵ addressed two questions – firstly what economic significance attaches to vouchers and secondly why there are VAT consequences.

As far as the quantitative part of the study is concerned, the objective was to provide an economic justification for making a legislative proposal remedying the problems identified.

⁴ Letter of 26 January 2007 from the BBA to the Commission.

⁵ "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 of 14 July 2010 (as revised). This study is annexed to this Impact Assessment.

The highest justification is in mismatches, whether actual or potential, between Member States which might have tax consequences. Therefore the study focuses on both actual and potential cross-border exposure. Even in cases where there is limited evidence of actual cross-border trade involving vouchers, the potential may be sufficient to justify legislative change in order to close off sources of mischief but also to give certainty to compliant businesses.

As is often the case in studies of this nature, particularly where tax policy is concerned, willingness to share data is not always optimal. Obtaining comprehensive and accurate detailed figures was not always possible. The pragmatic objective however was to establish an indicative overview of the relative importance, in monetary value of the main European voucher markets. The methodologies applied were evaluated against this perspective.

The study confirmed that pre-paid telecommunications services were by far the single most important category of vouchers with an annual value well in excess of other categories combined. For 2008 (the most recent year where reasonably complete figures are available), the total value of pre-paid mobile credits issued in the EU is approximately €37 billion⁶. This is also the field where concerns about tax problems have been most frequently identified.

The next most significant category are gift vouchers where the EU total is between €6 billion to €20 billion. Limited data precluded a more specific finding. The methodology used to arrive at this range is explained in the study. Gift vouchers have not generally seen as a source of VAT problems⁷. There are however some developing issues arising from inconsistency in national VAT treatments, particularly for retailers who operate in several Member States or who have pan-EU business models which may act as a barrier to wider market penetration.

Discount vouchers are estimated at a minimum of €2 billion.

The qualitative part of the study is limited to the most economically significant area. It provides an overview of the VAT rules throughout the EU 27 for prepaid telephone vouchers, identified as by far the most important category of vouchers in monetary terms.

1.4. Difficulties encountered

Accessing data has been a recurrent problem in this exercise. The limitations this imposed are set out in the introduction to the Deloitte study.

For the most part, there has been little centralised collection of data for these activities. In consequence, the consultant was often dependent on direct approaches where responses were often just adequate. This could be attributed to commercial confidentiality but also perhaps to misguided (but largely unvoiced) concerns about provoking more onerous taxation.

Given the significance of prepaid telecommunications, an approach was made to that industry's representative body to assist but this was not fruitful. Some individual companies were cooperative. The consultant drew extensively on existing Commission documents on the industry⁸, without which the value of the study would have been greatly diluted.

⁶ Deloitte study, page 12.

⁷ See however paragraph 2.9.1 below on unused vouchers.

⁸ Notably, COM (2009) 140 final: *14th Report on the implementation of the telecom regulatory package* which is credited at several points in the Deloitte study.

Because of these difficulties and, general budget constraints the quantitative parts of the study concentrate on a limited sub-set of Member States that were considered as representative.

The basic problem remains that there is no systematic collection of statistics on transactions involving vouchers. Any estimate of the market size would have to be made on the basis of approximate estimate based on surveys but the response rate from the sector was low. Measuring the extent of the problem was further hampered by the nature of the issue at hand – there is a natural tendency to conceal cases of non-taxation and this is typically only brought to light when another company starts to identify its consequences in terms of unfair competition. Double taxation will more often than not simply kill the market without leaving any statistical trace.

It is also difficult to forecast a growth rate for the voucher market for the following reasons. The most important driver of the size of the voucher market is the demand for pre-paid telecommunications vouchers. This variable is, in turn, determined by the rate of growth of the market for mobile telephony services multiplied by the share of pre-paid contracts on the total. The latter is strongly dependent on country and company-specific pricing policies, as shown by the high degree of dispersion in this statistic observed by country (in the Deloitte report). As pricing policies and consumer behaviour can change relatively quickly in the IT sector, it would be imprudent to make a forecast of the future development of the size of the voucher market. It seems reasonable to assume that it will remain roughly unchanged in its order of magnitude in the near future.

2. POLICY CONTEXT, PROBLEM DEFINITION AND SUBSIDIARITY

2.1. Why is there an issue in relation to the VAT treatment of vouchers which needs to be resolved?

In common parlance, the term "voucher" may have a multiplicity of meanings but the focus of this Impact Assessment is on commercial schemes where the voucher carries a right to goods or services or to reduction in their price and is used in transactions which are subject to VAT.

A voucher can be either in a tangible (*e.g.*, card⁹ or paper) or intangible (*e.g.*, electronic message) form. The rights entailed in a voucher are balanced by obligations assumed by the issuer or redeemer. Technical developments, deregulation of services (particularly telecommunications) and commercial innovation have allowed such schemes to grow in sophistication and to extend beyond the boundaries of individual Member States.

These developments have evolved since the current legislation was enacted in 1977¹⁰ and there is no specific guidance there on how vouchers should be treated. VAT issues arise nevertheless because a voucher can influence the time and place of taxation, the taxable amount and create uncertainty about compliance obligations.

⁹ The term "card" is employed fairly frequently throughout this paper, particularly where this reflects common commercial usage. It should however be understood as encompassing equivalent intangible instruments including in particular credits in electronic form which may be stored on a sim card or elsewhere.

¹⁰ Sixth Council Directive (77/388/EEC) of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment (OJ 1977 L 145, p. 1), replaced, with effect from 1 January 2007, by Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (OJ 2006 L 347, p. 1) – henceforth referred to as the "VAT Directive" or otherwise simply "the Directive".

It cannot however be said that these problems really go to the heart of the VAT system. There is no uncertainty about the taxability of the underlying transaction, the supply of goods or of services. Technical clarification is however required on how taxation should be applied at a detailed level. Inconsistency or uncertainty can otherwise cause tax losses or double taxation. There is also the risk that insecurity about the tax consequences of business transactions act as a damper on commercial innovations, particularly for cross-border transactions.

With no clear common VAT rules, independent approaches by Member States can lead to mismatches but also contribute to tax avoidance and form barriers to business. The rules in the VAT Directive do not take sufficient account of commercial developments, particularly in cross-border and chain transactions. Clarification is needed on the taxable amount and the time of taxation. The limited guidance given by the ECJ in a number of judgments on vouchers has been helpful but has not totally resolved the uncertainty facing taxable persons. The objective of the intended proposal is to deal with these issues by clarifying and harmonising the rules in Community legislation on the VAT treatment of vouchers.

The VAT treatment of vouchers might be relatively straightforward if the only impact were on the taxable amount or time of taxation in a direct sale between a retailer and a final customer. However, when the transactions involve a chain of intermediaries or have cross-border elements, a uniform application of the current VAT rules is hard to achieve.

Recurrent problems occur with telephone pre-payment cards, illustrating the problems created by uncertainty on the time of taxation. When a pre-paid credit is issued in one Member State where it is regarded as a payment on account for the service (and taxed upfront) and subsequently used in a Member State which taxes the telecommunications service received against the voucher when the service is supplied, both will levy VAT. The former however will tax when the voucher is issued and the latter when it is used (or redeemed). This is legitimate from both perspectives, but the result is double taxation. In the converse situation no Member State would levy VAT and the result is unintended non-taxation.

The consequences go beyond what might be expected from occasional purchases by consumers seeking to avail of lower prices. There is at least *prima facie* evidence of systemic commercial-scale schemes to exploit tax avoidance opportunities by issuing pre-paid telecommunications vouchers where they are not taxed on issue with the sole intention of marketing them to consumers where they are not taxed on use. The nature of the market for wholesale telecommunications services facilitates such *ad-hoc* arrangements.

Moreover, the evolution of some voucher-based systems brings them increasingly close in terms of functionality to established payment systems (*e.g.*, credit card, electronic purse) and the dividing line is not clear, raising competitive issues. Conversely, credit card companies are introducing pre-paid money cards which are ever closer in functionality to the prepaid services offered by telecommunications companies.

Discussions confirmed that differences in treatment are widespread. Individual Member States when faced with situations which are not specifically provided for in the VAT Directive have adopted *ad-hoc* solutions, which cause problems particularly for cross-border transactions.

2.2. Situation today - treatment of vouchers in Member States

The information available¹¹ confirms that for prepaid telephone credits the VAT treatment varies widely. This inconsistency leads to double or non-taxation and in practice operates as a barrier to full exploitation of single market opportunities.¹²

The experiences recounted in Section 1.2 (Public Consultation), notably the anecdotal accounts of difficulties being experienced by operators and by national tax administrations, confirm the existence and significance of problems.

The position in Member States can be summarised as follows:

Member State	Time of VAT liability	Other Comments
Austria	At sale	Normal VAT rules apply
Belgium	When the voucher is actually used.	The sale of prepaid telephone cards or sim card credits is not subject to VAT in Belgium and is seen as outside the scope of VAT as it concerns the exchange of money for money. Agents are considered to be acting as “transparent agents” and special administrative arrangements apply. The issuers of prepaid telephone cards are entitled to full input tax deduction.
Bulgaria	At sale	Special rules for intermediaries and non-EU telecommunications operators.
Cyprus	Time of sale	
Czech Republic	At sale	Special rules for intermediaries and non-EU telecommunications operators.
Denmark	At sale	Special rules for intermediaries and non-EU telecommunications operators.
Estonia	At sale	Normal VAT rules apply
Finland	At sale	Exempt if multi-functional.
France	At sale	Special rules for intermediaries and non-EU telecommunications operators.

¹¹ This is confirmed by the Deloitte report, see in particular Appendix 7.

¹² Such mismatches can of course open up opportunities for tax-arbitraging, even to the extent of complete tax avoidance. Eliminating these lacunae cannot be seen as a restriction on legitimate business opportunities. The reality is that uncertainty about the tax consequences or the likelihood of an unfavourable tax outcome creates barriers for compliant business, with a decrease in the number of possible market interveners

Germany	The time at which the liability to pay VAT arises depends on the type of voucher and may be the time of supply, activation or actual use.	The VAT treatment depends on whether: <ul style="list-style-type: none"> - the voucher is used for telecommunications services provided by a telecommunications company which is known at the time the card is purchased; or - the voucher is used for payment for telecommunications services provided by a telecommunications company, which is known only at the time the card is activated; or - the voucher is multi-purpose and can be used for payment for telecommunications services as well as goods or services provided by a third party supplier.
Greece	At sale	Special rules for intermediaries.
Hungary	At sale	Special rules for intermediaries and non-EU telecommunications operators.
Ireland	Depends on the place and time of the supply of the prepaid voucher.	Special provisions for prepaid vouchers which are subsequently used outside the EU. Special rules for intermediaries.
Italy	On redemption	
Latvia	At sale	Special rules for intermediaries.
Lithuania	At sale	
Luxembourg	Depends on nature and functionality of voucher.	For telecommunications services, taxation is generally on actual use.
Malta	Not clear	VAT treatment of vouchers is on an <i>ad-hoc</i> basis.
Netherlands	Generally taxed on redemption.	The sale of telecommunications vouchers is exempt from VAT, being considered as the supply of a security. Card-issuing companies and resellers of prepaid telephone cards should therefore not be entitled to deduct input VAT.
Poland	At sale	Where a telecommunications voucher (sim card credit) can be used to purchase other services or goods, payment of VAT is by imputation.
Portugal	At sale	

Romania	At sale	
Slovenia	At sale	VAT correction can subsequently be made if subsequent use justifies it.
Slovakia	At sale	
Spain	At sale	If functionality of voucher extends beyond mere telecommunications, taxation is at redemption.
Sweden	On redemption	
United Kingdom	Generally on redemption	In practice, where the voucher leads to the supply of a mixture of goods or services which attract different VAT rates (including zero rates), a composite rate may be applied.

As far as the effect on individual Member States is concerned, those who tax vouchers at the time of issue or first sale face the risk of tax arbitraging using vouchers issued in Member States where these are tax on redemption. This is particularly the case for prepaid mobile telecommunications credits. Mobile virtual network operators (MVNOs) and smaller operators base their business model on buying network capacity from the network operators and the fungibility of this capacity allows that vouchers issued in one Member State are easily used in another.

The mismatches outlined above cause adverse budget consequences for a group of Member States which would be rectified by aligning the time of taxation.

Conversely, this alignment will also see the end of double taxation. As explained elsewhere, both double and non-taxation are not easily measured. The probability however is that non-taxation is more significant. The consequences of dealing with the shortcomings identified should be a net increase in tax revenue, accruing to those Member States who currently suffer from tax arbitraging.

2.3. Situation today – decisions of the ECJ which relate to vouchers

Because Community legislation is silent on the correct VAT treatment of transactions involving vouchers, the ECJ is asked to provide clarification. Whatever common rules exist, are largely dependent on this case law. The question arises as to whether the Court has helped or has it raised issues which in turn need resolution in legislation. It would therefore be useful to look at the decisions of the Court in this area and to consider which aspects, if any, need to be considered in contemplating a legislative initiative.

In **Argos Distributors Limited**¹³ the Court held that Article 11(A)(1)(a) of the Sixth Directive (now Article 73 of the VAT Directive) must be interpreted as meaning that, when a supplier has sold a voucher to a buyer at a discount and then promised to accept that voucher at its face value in full or part payment of the price of goods purchased by a customer who was not the buyer of the voucher, and who does not normally know the actual price at which

¹³ Case C-288/94 *Argos Distributors Ltd v Commissioners of Customs and Excise* [1996] ECR I-5311.

the voucher was sold by the supplier, the consideration represented by the voucher is the sum actually received by the supplier upon the sale of the voucher.

The issue at dispute concerned the calculation of the VAT which the company must pay on the sale of goods paid for by vouchers. In the Court's view, the taxable amount is the amount of money received by the company when it accepts vouchers as payment for its goods which is the sum that is received from the sale of the voucher less any discount allowed. This decision is accepted as a clarification leading to a consistent application of the law. No further action is required here.

In **Elida Gibbs**¹⁴ the Court interpreted Article 11(A)(1)(a) and Article 11(C)(1) of the Sixth Directive (now Article 73 and Article 90(1) and (2) of the VAT Directive) as meaning that the taxable amount as far as a manufacturer is concerned is equal to the selling price charged by him, less the amount indicated on the voucher and refunded where

- (a) the manufacturer issues a money-off voucher¹⁵ in a promotion scheme, which is redeemable at the amount stated on the coupon by or at the expense of the manufacturer in favour of the retailer,
- (b) the cash-back voucher, which is distributed to a customer in a sales promotion campaign, may be accepted by the retailer in payment for a specified item of goods,
- (c) the manufacturer sells at the "original supplier's price" direct to the retailer and
- (d) the retailer takes the voucher from the customer on sale of the item, presents it to the manufacturer and is paid the stated amount.

The same would apply if the supply is made by the manufacturer to a wholesaler rather than directly to a retailer. The company sought a repayment of the output tax which had previously been accounted for on the basis that reimbursement amounted to a retroactive discount.

In the view of the Court the taxable amount must equate to the amount actually paid by the final consumer. The problem it faced in achieving this result is that the rebate received by the consumer does not follow the links in the contractual chain. In its search for neutrality, the Court had concluded that the taxable turnover of the manufacturer should be reduced with a consequent reduction in its VAT payments. It did not however see any need to adjust the position of any other parties in the chain such as a wholesaler or retailer.

This leaves uncertainty about the correct treatment when the ultimate consumer is a taxable person (the invoice received from the retailer will overstate the correct reclaimable VAT).

The Court seems to say that, in the circumstances outlined here, a free gift (the cash-back voucher given by the retailer to the customer) does not have direct VAT consequences. Questions remain on how to ensure neutrality for all participants in a distribution chain.

In **Kuwait Petroleum**¹⁶ the Court held that in interpreting Article 11(A)(3)(b) of the Sixth Directive (now Article 79(b) of the VAT Directive), the terms "rebates" and "price discounts" cannot be applied to reductions covering the whole cost of supplying redemption goods.

¹⁴ Case C-317/94 *Elida Gibbs Ltd v Commissioners of Customs and Excise* [1996] ECR I-5339.

¹⁵ The judgment speaks of "coupons". For ease of reading, the term "voucher" is used here.

¹⁶ Case C-48/97 *Kuwait Petroleum (GB) Ltd v Commissioners of Customs and Excise* [1999] ECR I-2323.

Article 5(6) of the Sixth Directive (now Article 16 of the of the VAT Directive) leads to the conclusion that the application by an oil company of goods which are given to a purchaser of fuel in exchange for vouchers obtained according to volume of fuel purchased at full retail price under a sales promotion scheme and where the goods are not of small value, must be treated as a supply for consideration within the meaning of that provision.

There is no link between the consideration and the goods given by *Kuwait Petroleum* since the price for the fuel was the same whether the customer took the vouchers or not.

Here the Court seems to say no retrospective adjustments is needed in respect of a money-off voucher. There is no need therefore for any legislative follow-up.

In **BUPA**¹⁷ the Court noted that VAT is a tax on supplies of goods or services, not on payments. Therefore, payments on account can only be linked to future supplies of goods or services if, at the time of payment, those supplies have clearly been identified. Consequently, advance payments do not fall within the scope of the VAT Directive, if they take the form of lump sums paid for goods referred to in general terms, which may be altered at any time by agreement between the customer and supplier, and from which the customer may possibly select articles on the basis of an agreement, from which he may unilaterally withdraw at any time, thereupon recovering the unused balance of the advance payments.

It can be posited that the observations of the ECJ here regarding the advance payments also apply to prepaid telephone credits. When a prepaid credit is acquired, it may not be certain what goods or services will be purchased. In such circumstances, the supply of prepaid telephone cards should not be the occasion for charging VAT.

In purchasing a prepaid telephone credit, it could even be considered that the buyer merely moves money from his bank account to a means of payment that can be used for the purchase of a variety of services, not only telecommunications services, but also information or ring tones, etc., or parking time at a car park. Purchasing a telephone card could be compared with making a withdrawal of cash. In that situation, the “buyer” merely exchanges the money from his bank account into cash money. That change in the form of money should be outside the scope of VAT because the exchange of money is not a taxable event for VAT purposes.

As far as vouchers are concerned, the line adopted by the Court here would seem to confirm that if at the time a voucher is issued, it is not possible to say what goods or services will be purchased with it, the consequence is that the voucher should not be subject to VAT.

In **Société thermale d'Eugénie-les-Bains**¹⁸ the Court held that Articles 2(1) and 6(1) of the Sixth Directive (now Articles 2(1)(c) and 24(1) of the VAT Directive) must be understood to mean that a sum paid as a deposit, in a contract for the supply of hotel services (subject to VAT) and where the client opts not to complete the transaction in circumstances where the deposit is retained by the hotel, there is no direct connection with the supply of any service for consideration and the payment is therefore not subject to VAT.

¹⁷ *Case C-419/02 BUPA Hospitals Ltd and Goldsborough Developments Ltd v Commissioners of Customs & Excise* [2006] ECR I-1685.

¹⁸ *Case C-277/05 Société thermale d'Eugénie-les-Bains v Ministère de l'Économie, des Finances et de l'Industrie* [2007] ECR I-6415.

Can the same reasoning be applied to vouchers where a payment has been made but the voucher is never redeemed with the result that there has been no supply of goods for consideration? If yes, unredeemed vouchers should be seen as giving rise to no tax liability.

In **Commission v Germany**¹⁹ the Court confirmed that the taxable amount in the hands of the retailer for a sale to a final consumer was the retail price, in effect the amount paid plus any further amount reimbursed to the retailer by the manufacturer.

The importance of this judgment is that here the Court reaffirmed the full force of *Elida Gibbs*, despite attempts by the German and UK governments to persuade it to reconsider its position in that case. Neutrality requires that VAT should not be charged on an amount greater than the true proceeds of the transaction of supply and this must take account of what the trader has to part with, even if this entails some loss of revenue for the tax authorities.

In **Astra Zeneca**²⁰, the ECJ has confirmed that a company giving face value retail vouchers (conferring a right to goods or services) to its employees as part of their remuneration was in receipt of a supply of services for consideration and that this was subject to VAT.

The vouchers in question confer a right to acquire goods or services whose nature is unspecified. They cannot therefore constitute a supply of goods for VAT purposes but rather must be a supply of services within the meaning of Article 24(1) whereby any transaction which does not constitute a supply of goods is to be regarded as a supply of a service.

This confirms the nature of the supply of a voucher as a supply of a service. Since however the desired outcome will always be to tax the underlying goods or services which are ultimately supplied against a voucher rather than the voucher *per se*, any legislative changes which define vouchers must also ensure that double taxation is avoided.

The flow of litigation attributable to difficulties in interpreting the provisions of the VAT Directive in relation to vouchers has not ceased. A more recent referral to the ECJ²¹ has highlighted the difficulties caused by the existing legislation. It concerns a company who issues prepaid telecommunications vouchers which are sold through distributors in other Member States. The question posed by the referring tribunal was whether the company can be considered as making two supplies for VAT purposes – one at the time of the initial sale to the distributor and another at the time of redemption (when the prepaid credit is actually used to make phone calls). In the event of that being the case, the Court is asked how VAT should be applied through the distribution chain.

The need for a referral to the Court is a clear indication of the difficulties that are being encountered with the legislation. Any resolution offered by the Court, however, will only extend to the specific questions posed and the specific circumstances which gave rise to them. Unless a definitive resolution is found, and this can only be by modernising the relevant EU legislation, there will be an ongoing need for such litigation in the search for clarity. This is not a desirable scenario²².

¹⁹ Case C-427/98 *Commission of the European Communities v Federal Republic of Germany* [2002] ECR I-8315.

²⁰ Case C-40/09 *Astra Zeneca UK Ltd v HMRC* [2010] ECR I-

²¹ Case C-520/10 *Lebara Ltd v The Commissioners for Her Majesty's Revenue & Customs*

²² The amount of tax at stake is not specified in the aforementioned Lebara case but other evidence indicates the impact of a double taxation charge for an individual calling card company in similar circumstances would fall within a range of €25 to €45 million.

2.4. Uncertainty and inconsistency in the definitions

There is no definition of a voucher in the VAT Directive, something which does not lend itself to a consistent outcome. It can be seen both from discussions with stakeholders, and in particular from the decisions of the ECJ, that vouchers have a range of characteristics which influence the tax consequences. The Court has not provided a general definition of a voucher but has rather dealt with the specific issues with which it has been presented.

Whilst the guidance of the Court has undoubtedly been of benefit in bridging the gaps created by outdated legislation, it has not produced a comprehensive set of rules. It is however clear that there is no single concept of a voucher and that any attempt to define vouchers has to be on the basis that there are several different kinds of vouchers.

The Deloitte study²³ identifies different types such as free vouchers, paid vouchers, single-purpose or multi-purpose vouchers and discount vouchers. These are not mutually exclusive categories and an individual voucher may fall under more than one of these characteristics.

The study concludes that one particular type of voucher – prepaid telecommunications – is by far the largest single category and can be both single and multi-purpose in functionality. Total pre-paid mobile revenue is estimated (for 2008) at €36 billion²⁴. Although most usage is domestic, the potential for cross-border use is relatively high.

The total minimum monetary value for gift vouchers has been estimated at €9 billion²⁵. Other significant areas are loyalty cards, estimated at €4 billion²⁶ and discount vouchers which are estimated at €2 billion²⁷. Cross-border usage is generally limited for each of these categories although specific technical problems can occur with discount vouchers. Any solution should deliver a clear and consistent understanding of what a voucher is, in all its different manifestations, ideally through clear definitions which are applied consistently.

The study estimates the minimum monetary value of the EU voucher market at €52 billion. Given that prepaid telecommunications accounts for almost 70% of that figure, it merits special attention. Here technological development and innovative business practices raise questions about the very nature of vouchers and whether such an apparently traditional concept covers what is actually occurring in the market place. Increased functionality may put into question the merits of any approach which is based on an outdated understanding.

The perspective taken so far has been that prepaid telephone credits should be regarded as vouchers and, where appropriate, as multi-purpose vouchers. This might have the consequence that the supply of certain vouchers or at least some elements of the supply should be seen as a supply of money and should be ignored for VAT purposes. In this perspective, the transfer of money from one point (say, the customer's mobile phone) to another point (the supplier of goods or services) might be exempt from VAT on the basis of Article 135(1)(d) of the VAT Directive.

The purchase of prepaid telephone credits could also be regarded as an advance payment for the goods or services, which will be supplied to the cardholder at a later moment. In this

²³ Deloitte study. Page 11, *et seq.*

²⁴ Deloitte study. Page 23.

²⁵ Deloitte study. Page 33.

²⁶ Deloitte study. Page 38.

²⁷ Deloitte study. Page 42.

respect, Article 63 of the VAT Directive provides that “*the chargeable event occurs and VAT becomes chargeable when the goods are delivered or the services are performed. However, where payments are made on account before the goods are delivered or the services are performed, VAT becomes chargeable at the time of receipt of the payment and upon the amount received*”.

On balance, the acquisition of prepaid telephone credits which offer no other functionality than telecommunications services in the country where they are issued could be regarded as constituting an advance payment, which is subject to VAT. However, due to the increasing multi-functional character of prepaid telephone credits, it is not always clear for what future supplies will arise. At the time of acquisition of the prepaid credit, the VAT regime applicable to the future supplies (subject to VAT at the standard or a reduced rate or exempt from VAT or indeed the Member State where the VAT might arise) cannot always be predicted.

2.5. Tension between protecting revenue and ensuring the absence of barriers to commercial innovation

2.5.1. Development of innovative payment systems

The issues at stake become more complex if prepaid telephone cards can also be used to purchase services other than telecommunications services. These are increasingly used to purchase services from other suppliers, acquiring a multifunctional character. They can also be used for traffic or weather information, financial information, medical advice, ring tones, parking fees, or for participating in online lotteries or games. The range of options is increasing rapidly. In some parts of the world, mobile phone services enable subscribers to send money in instant transactions at competitive costs²⁸. Here there is a combination of a telecommunications service a different type of supply, *i.e.* a “content” service supplied by a third party but paid for through the prepaid telephone card.

As regards those combinations of services, different views could be taken:

- a telecommunications service is supplied enabling the final recipient to acquire content from a third-party. The content supplier provides the content service to the final recipient; or
- a telecommunications service is provided enabling a third-party to deliver content service to the final recipient. The content supplier not only provides the content service to the final recipient but also the telecommunications service, *i.e.* ensures that the content service is delivered to him; or
- since the final recipient of the combined supply pays the telecommunications company through the prepaid telephone card, the telecommunications company supplies the total package to the final recipient after the content service has been supplied to it by the third-party supplier.

The main issue arising in those situations is the determination of the VAT liability of the parties concerned. Payment for the content services by means of the telephone card is not only convenient for the third-party suppliers, whose share in the total price is usually relatively

²⁸ See <http://news.bbc.co.uk/2/hi/africa/6510165.stm>. There is no evidence of such money transfer services being available within the EU but the technical possibility is clearly there to include on a sim card a money transfer menu that allows account funds to be managed.

low. It is also the only practical method because, since the services are delivered through a (mobile) telephone, the third-party suppliers do not even know the identity of their customers.

If the relationship between the telecommunications company and the third-party supplier is not clearly defined, there is a risk that the telecommunications company could also account for VAT on the total value of the service. This not only gives rise to the risk that the company accounts for VAT on supplies made by third parties but may also have the effect the right to deduct input tax if the supply involves an online lottery or purchase of financial or medical information. As previously pointed out, the transfer of money from one point (say, the customer's mobile phone) to another (the third-party content provider) might be considered as exempt from VAT with negative consequences for deductibility.

In practice, there is some confusion about the correct VAT treatment of content services paid for by prepaid telephone cards. In similar situations, the parties involved may assess the VAT consequences in a different way and a more consistent treatment is needed. It is difficult to see how this can be achieved other than by updating the legislation in the VAT Directive.

This could be based on the principle that content providers make their supplies directly to the final recipient as that respects the final recipient's perception of the transaction where the content provider alone make the supplies. It also provides a valid solution in those cases in which the telecommunications companies do not wish to take responsibility for the content, for example the correctness of medical advice, or do not wish to be associated with *e.g.*, adult content.

On this basis, the content provider must determine the VAT status of its supplies and, if they are subject to VAT, account for and pay the VAT due on the content services. Where those services are exempt from VAT, the exemption only affects the content provider's, not the telecommunications company's, right to deduct input tax. The telecommunications company merely collects the price from the final recipient on behalf of the content provider. That service can be treated as an exempt transaction in relation to payments, but also as debt collection, which is subject to VAT. However, since the core business of telecommunications companies is the supply of telecommunications services, the most obvious solution is to treat its service rendered to the content provider as a telecommunications service, enabling the content provider to deliver its services through the telecommunications network to the final recipients and, as an ancillary service, collect the price from the final recipient on behalf of the content provider. The telecommunications company would charge VAT to the content provider in respect of the supply of telecommunications services. The advantage here is that the telecommunications company does not run into input tax deduction issues.

There are however an increasing range of scenarios where the commercial reality of the operation would not justify such an approach. Where the reality is that a telecommunications service provider offers what is in effect a comprehensive payment service or money transfer service, they clearly enter into competition with the traditional or established providers of such services. It is difficult to see a justification for different tax treatments.

2.6. Problems concerning the taxable amount

Assuming that most prepaid telephone cards merely constitute a special type of money with VAT due on the purchase of goods or services, since these cards are often distributed through a network of agents, the question arises of what the taxable amount must be.

Where the face value of the prepaid telephone card is €10 and the card is distributed through an agent, who earns €2, the payment made by the holder of the card for goods or services supplied by the card issuer is higher than the amount received by the issuer of the card. For example, where the card is issued by a telecommunications company and is used at face value to purchase telecommunications services, the recipient of the services pays €10, whilst the telecommunications company only receives €8. Here it does not make much difference whether the agent acts as an intermediary, i.e. acting in the name and for the account of the card issuer and earning a commission of €2 for his intermediary services, or as a commission agent, i.e. acting in his own name but for the account of the card issuer and receiving the card for a price of €8 and, subsequently, supplying it for a price of €10.

Under *Argos*, the taxable amount is the payment actually received by the card issuer. On the basis of that judgment, the taxable amount for the services supplied by the telecommunications company in the above example, for which the supplier received payment by means of the prepaid telephone card, would be €8.

On the other hand, in *Bally*²⁹, the ECJ declared that, where a customer purchases goods or services, and pays by means of a credit card, the taxable amount for the supply is the total amount paid by the customer, not the lower amount actually received by the supplier from the credit card company. In that case, the ECJ declared that the payment received by the supplier of the goods and services was the balance of the payment made by the customer (€10) and the value of a service rendered by the credit card company to the supplier (€2). On the basis of that judgment, the taxable amount for the services supplied by the telecommunications company in the above example, for which the supplier received payment by means of the prepaid telephone card, would be €10.

The view that the supplier of goods and services must account for VAT on the full payment made by the customer was supported by the ECJ's decisions in *Freemans*³⁰ and *First Choice Holidays*³¹. In *Freemans*, the ECJ ruled that a reduction of the purchase price can only reduce the taxable amount if the reduction is actually used by the customer. Since the holder of a prepaid telephone card does not receive a reduction, the supplier of the goods and services should account for the VAT on the payment made by the customer (€10). In *First Choice Holidays*, the amount that the travel agent must pay to the tour operator in excess of that received from the traveller constituted consideration for the supply of services by the tour operator. There was a direct link between the additional amount that the agent (as a "third party") paid to the tour operator and the supply of the services to the traveller. On this basis, the additional amount paid by the agent must be included in "the total amount to be paid by the traveller" for the purpose of calculating the taxable amount.

On the basis of the above ECJ case law, it could be argued that, where prepaid telephone cards are distributed through agents, the issuer of the card who also supplies the goods or services to the holder of the card must account for VAT:

- on the full price paid by the recipient of the goods and services (i.e. €10) where the agent acts as an intermediary, i.e. in the name of the issuer of the card; and
- on the amount actually received (i.e. €8), where the agent acts as a commissionaire, i.e. in his own name.

²⁹ Case C-18/92 *Chaussures Bally SA v Belgian State, Minister for Finance* [1993] ECR I-2871.

³⁰ Case C-86/99 *Freemans plc v Commissioners of Customs & Excise* [2001] ECR I-4167.

³¹ Case C-149/01 *Commissioners of Customs & Excise v First Choice Holidays plc* [2003] ECR I-6289.

Where the agent acts as a commission agent, the prepaid telephone card is deemed to be supplied to him (for a price of €8) and, subsequently, by him (for a price of €10). By contrast, where the agent act as an intermediary, the total price received by the issuer of the card is deemed to be the total price (€10) paid by the holder of the card, and the difference between that payment and the net amount received by the card issuer (€10 – €8) must be attributed to a separate service rendered by the intermediary. However, in practice, the view that the agent acts as an commission agent is not very realistic because prepaid telephone cards nearly always state the name of the issuer (usually, the telecommunications company). Therefore, the cardholder knows that, where he uses the prepaid telephone card to obtain telecommunications services, those services are directly provided by the card issuer (and not by the commission agent).

2.7. Time of supply

Under Article 63 the tax becomes chargeable when the services are performed or goods are delivered. The Directive however also provides that in the case of a payment on account (an advance payment) which is made before the performance of the service or the delivery of the goods, the tax is chargeable on receipt of the payment and on that amount.

For this to happen, sufficient clarity about the goods or services in question is required so that VAT can be correctly charged. If a voucher can be used only with the Member State of issue for the supply of a defined product, the VAT rate applicable is clear from the outset. Where it can be used at the holder's discretion to acquire range of goods or services, then the applicable tax may not be known in advance.

Uncertainty would also apply where a voucher, issued say by a retail chain, can be redeemed against similar goods but at outlets in several Member States. The time of supply (time of taxation) cannot therefore always be fixed at the time a voucher is paid for. Any solution will have to take account of the reality that taxation can occur either at the time a voucher is first issued or at the time it is redeemed for goods or services.

2.8. Supply of prepaid telephone cards by intermediaries

Many prepaid cards are distributed through intermediaries, perhaps involving two or more Member States. Since the supply of such prepaid telephone cards should not be a taxable transaction for VAT purposes, questions arise on the treatment of the intermediary services.

The intermediary services could be regarded as services for the promotion of the supply of the underlying goods and services. Under that view, the intermediaries must charge VAT on their commission and, where the issuer of the prepaid telephone cards renders taxable telecommunications services to the cardholders, the VAT on the intermediary services would be deductible as input tax.

Alternatively, the intermediary service could be regarded as a transaction concerning payments, which is exempt from VAT under Article 135(1)(e), although, Member States may also allow financial service providers to opt for taxation.

Treating the intermediary services as taxable transactions produces an optimal result, in that the VAT on the intermediary's operating expenses would be deductible and, therefore, must not be absorbed as hidden tax in the commission charged to the card-issuing companies. It is certainly defensible that the activities of the intermediaries promote the distribution of taxable

goods or services and, in view of the fact that distribution of prepaid telephone cards should be ignored for VAT purposes, it would not make any sense if that distribution were to be burdened by non-deductible input tax.

2.9. Other problems identified

In the course of the preparatory work, a number of other areas of concern were raised. Some of these could only be considered peripheral or their resolution would require changes which are disproportionate to the scale of any problem identified.

2.9.1. Unused vouchers

If a voucher does not lead to any supply, then any payment made for the voucher is not subject to VAT under current legislation. The logic underlying the ECJ's decision in the *Eugénie-les-Bains* case seems to confirm this, albeit the facts of this case relate to a forfeited deposit rather than a payment for a voucher.

The possibility of a relatively high level of unredeemed vouchers was raised. For gift vouchers in particular, there is anecdotal evidence of significant non-redemption and some tax administrations expressed concern that this represented income outside the scope of VAT. For vouchers taxed on issue, it might seem logical that businesses would seek to recover this tax if the voucher remains unused but it is unclear to what extent this happens in practice.

The Deloitte report gives some indication of the rate of unused vouchers, particularly in the gift voucher segment where the share of unused vouchers is considered highest (see page 33 of the study). The percentage of unredeemed vouchers here was estimated at around 10%. Elsewhere the share of unredeemed vouchers was found, unsurprisingly, to vary strongly depending on the type and market segment (from 1% to around 20%). It has to be said however that there are many reasons why a company will understate the extent to which its vouchers are unredeemed.

Changing the tax treatment of unredeemed vouchers would require a modification to the supply of services provisions in the VAT Directive. Such change would presumably lead to additional tax revenue but there are at least two arguments against taking such a step.

In some cases unredeemed vouchers may be so scarce as to be hardly worth recording but in others companies may be secretive to protect an untaxed stream of revenue. Apart from the issue of quantification, a more practical issue would be determining what an unredeemed voucher is. Many vouchers will have an expiry date and there would be logic in making use of that. Realistically however if the expiry date determines that an amount becomes taxable, this will merely encourage businesses to extend the life of a voucher indefinitely.

Changing the rules on the taxation of unredeemed vouchers might therefore have little real effect.

2.9.2. Premium call services and charity donations

It is not clear that there is a relevant VAT problem linking vouchers and premium call services *per se*.

The income which charities receive in the form of donations is usually outside the scope of VAT. From time to time however charities or somebody acting on their behalf make use of

premium SMS or call services to facilitate donations. This involves the donors making use of a telecommunications service to give money to a cause. Normally this involves a payment for the service, which is collected by the telecommunications service provider and passed on to the charity, possibly after the operator has deducted its operational costs. The telecommunications service which is provided to the donor is however considered to be a single service for VAT purposes and the entire sum paid will attract tax. The amount available to be passed on to the charity will be what is left after deducting this VAT (and possibly the operator's costs).

Charities see this outcome as the collection of VAT on donations which would otherwise be exempt. It is not however practical, or perhaps even necessary, to address this issue here but rather it seems there might be scope for service providers and tax administration to cooperate on an administrative resolution of any problem.

2.9.3. *Business gifts*

In the course of the consultation, mention was made of unevenness in the tax treatment of so-called "business gifts". Article 16 of the VAT Directive sets down some rules for goods which are given away free of charge. Where these are used as samples or as "gifts of small value", they need not be treated as supplies for consideration and consequently ignored for VAT purposes. The corresponding provisions on services differ slightly. It had been suggested that clarification was needed here, mainly because of significant differences among Member States in their understanding of "small value". There were also concerns about some residual differences between goods and services.

Without denying that differences exist, it could only be concluded that the internal market or distortive impact was minimal, even non-existent. Accordingly, no action is envisaged here.

2.10. **Baseline scenario and its evolution.**

The baseline scenario for this Impact Assessment, in so far as pre-paid telecommunications credits are concerned, is one of mismatches in taxation which give rise to problems in tax collection and to difficulties in maximising Internal Market opportunities. Shortcomings in available data have meant that this baseline is sustained by a combination of strong and consistent anecdotal evidence (in Section 1.2) as well as an analysis of the actual tax treatment in Member States (in Section 2.2).

The situation for non-telecommunication vouchers is seen as experiencing a constant increase in the volume of vouchers as well as growing diversity in their form, content and application³². All of the stakeholders consulted have expressed concerns about the consequences of not addressing the VAT problems – the only exception being some operators whose vouchers are limited to the Member State within which they are sold, distributed and redeemed and where local solutions have been found to tax issues. For others meanwhile, cross-border trade involving vouchers always causes problems³³.

Furthermore, in the absence of corrective action, tax neutrality will be increasingly difficult to ensure between different payment systems which deliver the same result in paying for goods and services. Significant and growing problems are foreseen by business as long as the tax system cannot ensure that the choice of payment instrument should not be determining factor

³² Submission from Federation of Enterprises in Belgium.

³³ Submission from EuroCommerce.

and the same tax charge should apply to a supply whether a customer uses cash, a voucher or any other form of consideration³⁴.

The consequences for this baseline scenario, if no action is taken would see a continuation of existing problems for both business and tax administrations. The following consequences can be reasonable envisaged, based notably on experiences to date:

- There would be a continued need to seek recourse to the ECJ in the ongoing absence of clear common rules. This is not a path readily accessible to smaller businesses (because of the costs involved) and they will continue to suffer the consequences of uncertainty and inconsistency in tax rules.
- Decisions by national courts also playing a role in fixing national tax rules. The absence of rules at EU level increases the likelihood that these decisions will be uncoordinated and increase, by increasing fragmentation, add to the complexity and inconsistency faced by businesses.
- Revenue losses attributable to mismatches or aggressive tax planning will persist. Double taxation would probably be limited in its actual impact and its effect felt in limitations on market opportunities.
- The absence of a level playing field will continue to hamper the development of pan-European business models in areas of commerce which make use of vouchers. It is difficult to quantify this because of the shortcomings in data on the existing situation but also because many businesses will simply refrain from certain ventures because of tax uncertainty and this is not always detectable.

As a result of the adoption of Council Directive 2008/8/EC of 12 February 2008 amending Directive 2006/112/EC (the VAT Directive) as regards the place of supply of services, with effect from 1 January 2010, new tax rules on the place of supply of services have come into effect. Certain of these changes which concern services such as restaurant and catering services, the hiring of means of transport, cultural, sporting, scientific and educational services are likely over time to exacerbate the uncertainty caused by the lack of common rules for transactions using vouchers.

For telecommunications, broadcasting and electronic services, the introduction of the new rules on the place of business to consumer supplies will however be delayed until 1 January 2015. The purpose of these changes is to ensure that to the maximum extent possible, the tax on the consumption of services accrues to the Member State where they are consumed. This is a crucial reform where these are services which can be supplied remotely such as telecommunications. There are now real fears that, unless the VAT rules here are reformed, vouchers issued in one Member State and used by consumers in another can be employed to frustrate the intention of legislators by facilitating tax arbitrage. The existing pattern of mismatches in the time of taxation³⁵ lends itself to such a probability.

From the foregoing, it is difficult to envisage a positive evolution of the current baseline scenario in the absence of intervention. The conclusion has to be that this is not a problem which can be resolved through benign neglect.

³⁴ Submission from European Telecommunications Network Operators.

³⁵ See table in section 2.2.

2.11. Subsidiarity

Action by Member States alone could not achieve the objective of uniform application of VAT due to the possibility of different interpretations of rules. The current legislation is not clear and its heterogeneous application by Member States is the main reasons for the problems being encountered. Clarifying the VAT treatment of taxable goods and services supplied against vouchers requires an amendment of the Directive.

The relevant VAT rules are set out in the VAT Directive. These rules can only be amended via the Community's legislative process. The proposed changes of the VAT Directive are needed in order to re-establish neutrality and this falls under the exclusive competence of the Community.

The proposal aims at a harmonised interpretation and application of the VAT rules through a common definition of vouchers. This will require that Member States apply the same rule and so avoid distortion in taxation, eliminating double or non-taxation.

The reasons set out above are clear and the scope of the proposal is limited to what Member States cannot satisfactorily achieve themselves and can only be achieved with Community legislation.

3. OBJECTIVES

The Commission's starting point was set out in the consultation paper of March 2006. The general objective for any initiative here is to remove uncertainty from the tax system, protect public revenue and deliver neutrality in competition on the basis of a consistent application of the taxing rules. The consultation paper foresaw that possible measures should be assessed in the context of three deliverable and specific objectives:

- **Dealing with mismatches in place and/or time of taxation**

To rectify the problems caused by the absence of clear rule (as explained above), a clear and consistent tax treatment for the main types of vouchers needs to be set out in a manner which removes the risk of mismatches between Member States. It is likely that this objective can only be fully achieved if the VAT Directive is modernised.

- **Dealing with the consequences of certain ECJ decisions**

The specific objective here is to ensure that the decisions of the Court are consistently applied. If implementing these decisions creates uncertainty or technical difficulties (e.g., applying the *Elida Gibbs* principles to chain transaction), legislative clarification may be needed.

- **Setting clear lines between vouchers and innovative payment systems**

Technical and regulatory changes have led to a degree of convergence in the provision of payment services where innovative products now compete with more traditional systems. The tax rules should take account of the need for tax neutrality between different categories of service providers who deliver competing services.

4. POLICY OPTIONS

Three possible paths arise. One might be for the Commission to do nothing, leaving it to Member States to find *ad hoc* solutions or to seek guidance from the ECJ. A second option would be to achieve the objectives by revisiting the legislation. A third is to consider whether the same result could be achieved by other means, for instance issuing guidelines.

A further theoretical option might be to resolve the tax difficulties by simply banning the use of vouchers in any circumstances where tax might be at risk. This would indeed end concerns about non-taxation or double taxation and would remove uncertainty for business. It would however be totally disproportionate and cannot be given serious consideration.

Stakeholder views – how addressed.

Public sector stakeholders (tax administrations).	Private sector stakeholders (business and consumers).
Member States have repeatedly identified this as an issue where the Commission must take remedial action.	Discussions with stakeholders and their advisors have consistently pointed to the need for the Commission to deal with the VAT problems being encountered with transactions involving vouchers. <i>(Addressing) the (VAT) treatment of vouchers is long overdue and the current fragmented interpretation results in both nil and double taxation ... (and) hampers the development of business in the Single Market³⁶.</i> <i>Problems arise frequently with cross-border treatment of vouchers – we agree with the objectives set out in the (Commission's) consultation paper³⁷.</i> <i>We welcome the Commission's review and the prospect of harmonised VAT accounting on vouchers across the EU.³⁸</i>

4.1. Doing nothing.

The work undertaken indicates that difficulties in this area will continue unless corrective action is taken. These difficulties originate from gaps in the VAT Directive which lead Member States towards individual uncoordinated approaches. Doing nothing is not a realistic option, particularly as both national tax administrations and private sector stakeholders are unanimous in seeking an end to the current uncertainty.

³⁶ Submission from Business Europe.

³⁷ Submission from Chartered Institute of Taxation.

³⁸ Submission from Voucher Association (UK)

Left unresolved, current difficulties will only grow. For telecommunications vouchers, there is at least anecdotal evidence of increasing systematic attempts to exploit mismatches in taxation and even organised VAT fraud targeting the gaps in coverage which vouchers cause³⁹.

Stakeholder views – how addressed.

Public sector stakeholders (tax administrations).	Private sector stakeholders (business and consumers).
Doing nothing is not an option for Member States tax administrations.	The majority of the comments received raised the unsatisfactory nature of the current situation and emphasised the need for action in this area.
	Not a single respondent in the public consultation or elsewhere advocated doing nothing.
	<i>The lack of consistent VAT treatment, reporting rules and documentation requirement for transactions creates significant uncertainties and compliance challenges for business. Resolving these issues should be a priority for the Commission.</i> ⁴⁰
	<i>Le monde des entreprises se réjouit de l'attention prêtée par la Commission européenne à la problématique des bons</i> ⁴¹

4.2. Soft law approach

VAT is an important source of revenue for Member States who are therefore extremely cautious about any possible limitation of their powers in this respect.

The Council only adopts provisions for the harmonisation of legislation concerning VAT to the extent that such harmonisation is necessary to ensure the establishment and functioning of the internal market and to avoid distortion of competition. While the Treaty prescribes no particular legal instrument, VAT has mainly been regulated by means of directives. No powers have been delegated to the Commission⁴², so all substantive changes need to go

³⁹ See "The Italian Job -- Voice Over Internet Protocol MTIC Fraud in Italy" by Professor Richard T Ainsworth published in Taxanalysts 1 June 2010.

⁴⁰ Tax Executives Institute, Inc.

⁴¹ FEB-VBO Federation of Enterprises in Belgium.

⁴² Under Article 290 TFEU, a legislative act may delegate to the Commission the powers to adopt non-legislative acts of general application to supplement or amend certain elements of the legislative act. The exercise of these powers is dealt with in a Communication from the Commission to the European Parliament and the Council: Implementation of Article 290 of the Treaty on the Functioning of the European Union (COM(2009) 673).

through the established legislative procedure, involving unanimous adoption by the Council. Under Article 398 of the VAT Directive, the Council has explicitly reserved for itself the power to adopt implementing measures (Implementing Regulations).

The use of so-called soft law, which has no binding force, can be advantageous in some instance. However its effectiveness depends on the type of regulatory environment in which it functions. With few exceptions, VAT has not developed as a fertile ground for so-called soft law measures. Reflecting this, in the more than 40 years which have passed since the first steps were taken to the creation of a common VAT system, the Commission has only once issued a Communication to the Council and Parliament on a VAT issue⁴³.

Guidelines on the application of the VAT provisions adopted by the Council have also been issued by the VAT Committee, a consultative body made up of representatives of Member States with no legislative powers, from time to time (on the basis of consensus). Such guidelines however do not represent an official interpretation of the law. As they are not binding on Member States, the guidelines do not prevent differences in practice from persisting.

In a very limited number of instances, these guidelines have evolved into more formal instruments through being transposed into Council Regulations (at which stage of course they cease to be soft law). The agreement reached on guidelines may pave the way for a subsequent agreement in the Council but it does not, as such, solve the underlying inconsistencies in the VAT system which hamper the smooth functioning of the Internal Market.

Soft law instruments are of value where there is no question about the underlying soundness of the legislative provisions being addressed or interpreted, the purpose of such instruments being merely to achieve order or a more consistent understanding.

If however pragmatic or other reasons were to point to a solution based on soft law, the desired outcome could possibly be achieved through either a Communication or VAT Committee guideline. A Council Regulation could then be considered if the underlying primary legislation is sound but this is far from the case here.. Otherwise, a soft law approach could conceivably address some of the detailed remedial measures list in the next section but, for brevity, these are not repeated here.

Stakeholder views – how addressed.

Public sector stakeholders (tax administrations).

Guidelines (or soft law) in the views of Member States would only be feasible if primary law provides a clear base from which guidance could be drawn. This is not the case here.

Private sector stakeholders (business and consumers).

The need for legal certainty was a priority for many respondents.

A key element to avoid imposing onerous administrative obligations on business is to ensure (through EU law) the adoption of uniform definitions, consistent

⁴³ *Communication from the Commission to the Council and the European Parliament on the VAT Grouping option provided for in Article 11 of Council Directive 2006/212/EC on the common system of value added tax. COM 2009(325) of 2 July 2009.*

interpretations, consistent administrative practices and consistent compliance requirements by all Member States.⁴⁴

For some businesses such as telecommunications the present arrangements for vouchers will make the proposed Place of Supply of Services Directive⁴⁵ unworkable in practice. The VAT Directive needs to be updated accordingly⁴⁶.

4.3. Legislative measures

The VAT treatment of vouchers involves issues which touch on in several articles of the VAT Directive. The objectives listed above could be met by amending them and introducing additional provisions as appropriate.

It is a fundamental tenet of the VAT Directive (itself the outcome of a recast of Council Directive 77/388/EEC of 17 May 1977, the Sixth VAT Directive) that a greater degree of harmonisation would serve to enhance the neutrality of the tax in both domestic and intra-EU trade⁴⁷.

In interpreting EU VAT legislation, the ECJ has drawn heavily on the teleological method of interpretation whereby it relies on the design and purpose of the provisions of the Directive. Individual provisions of the VAT Directive form part of a complex system of taxation and their function is usually best understood when they are read together with other provisions⁴⁸.

These two long established factors, the need for a harmonised approach and that the provisions of the Directive need to be read together, mean that when it is necessary to modify the Directive any changes must be presented in a manner which conforms to the established ordained methodology of the Directive. The reality therefore is that once the desired outcome is clear, there will seldom if ever be significantly different ways of modifying the Directive and any proposal will have to respect a settled order.

The various elements listed here are not to be seen as sub-options but rather form part of a coherent overall approach to modifying the VAT Directive in a manner which is coherent with the overall structure and philosophy of the Directive.

4.3.1. Introducing clear definitions

There is no definition of a voucher in the VAT Directive. Article 65 provides that "where a payment is to be made on account before the goods or services are supplied, VAT shall

⁴⁴ Tax Executives Institute, Inc.

⁴⁵ The reference is to Council Directive 2008/8/EC of 12 February 2008, the relevant provisions of which come into effect on 1 January 2015 and effect the VAT treatment of a range of services including telecommunications.

⁴⁶ TelefonicaO2.

⁴⁷ See in particular the 4th, 5th and 7th recitals in the preamble.

⁴⁸ See judgement of 20th October 1993, *Balocchi v Ministero della Finanze dello Stato*, [1993] ECR I-5105.

become chargeable on receipt of the payment and on the amount received. On the other hand (in *BUPA*) the Court has said where the goods or services cannot be known in advance, the payment cannot be subject to VAT. This should be made clearer in the Directive if the legislative path is chosen.

In addition, at least the following would be required.

A **general definition of a voucher** for VAT purposes would cover vouchers which carry a right to receive certain goods or services, or to obtain a discount when acquiring those goods or services, or to receive a refund, at the time of redemption. That right can be a value expressed in terms of monetary value or of a percentage (of reduction) or of units or quantity.

The issuer of the voucher accepts a corresponding obligation but this obligation may also extend to other commercial operators who participate in the arrangements. Within the general category of voucher, some specific types of voucher will need to be explained.

A **single purpose voucher** (SPV) is one where the goods or services involved can be identified at the time of issue or supply of the voucher to a sufficient extent that the tax consequences of their supply are clear. A voucher ceases to be a SPV when the applicable VAT rates for the redeemable goods or services varies, or cannot be known in advance. SPVs would be taxed at the time when they are issued.

If a voucher can be used to acquire a specific identifiable good (for example a book token usually leads to the acquisition of a book) within a single Member State, the tax consequences (rate and destination) would be clear from the outset. If however if the voucher can be redeemed against books or DVDs (which generally attract a different tax rate) or it can be redeemed in branches in other Member States (where not only the tax rate might be different but the tax would also accrue to a different tax authority) then this certainty disappears and it would not be possible to compute the tax correctly at the time of issue. The voucher is then a **multi-purpose voucher** (MPV). This should be relatively straightforward to define if it were to cover any voucher that would not fall under any other category.

A **free voucher** is one that is issued without any charge, normally with the intention of promoting a product or a service. Examples of free vouchers are those that can be found in newspapers or simply given away by businesses to their customers. Following the views of the Court in *Kuwait Petroleum* the relevant test to determine whether the voucher discount has been supplied free of charge should be whether or not the customer has the right to pay less if he does not want to take the offered voucher.

A **discount voucher** can probably be seen as a subcategory of free vouchers. The discount can be expressed either as a percentage or as a fixed amount. It represents a right to a discount either directly from the issuer or from the redeemer of the voucher. It does not carry a money value in that it cannot generally be redeemed for money in the absence of any purchase. A line will need to be drawn between a discount voucher leading to a price reduction on a product or a service and vouchers that are sold at a discount and this merely reflects the way intermediaries earn their margin.

In concrete terms, this would require the insertion of a new article in the VAT Directive. The established logic of the Directive would indicate that it should be situated within Title IV (Taxable Transactions) Chapter 3 (Supply of Services). This should set out a legal definition of a voucher for VAT purposes, taking due account of the essential characteristics which

istinguish vouchers from other instruments, notably monetary payments in money or close equivalents, used to acquire goods or services.

The definitions in this new article should extend to the categories identified above. In addition, in order to delimit clearly the scope of vouchers, it should make that any instrument or transaction which can be considered as a payment service (notably payments, transfers, cheques and other negotiable instruments) under other provisions of the Directive is not a voucher for VAT purposes.

In addition, it would be necessary to include a further clarification in Chapter 3 to ensure that the operations linked to a voucher are not taxed twice. This risk arises since, in the case of an MPV, a right exists up to the point of redemption but this right is linked to the supply of goods or services. The assignment of that right, and the supply of goods or services at the time of redemption should be regarded as a single transaction.

Stakeholder view – how addressed.

Public sector stakeholders (tax administrations).

Private sector stakeholders (business and consumers).

A majority of the views received by the Commission from stakeholders were supportive of the need to clarify the legal nature of vouchers for tax purposes in the VAT Directive including defining the main categories of vouchers. Some respondents even suggested specific forms of wording for inclusion in the Directive as definitions⁴⁹.

We agree on the desirability of a broad definition of vouchers (in the VAT Directive)⁵⁰

Sony supports the introduction of harmonised legislation based on the MPV guidelines addressed in the consultation⁵¹.

4.3.2. *Distribution of vouchers through a chain and the distributor's margin*

It would be necessary to amend Article 25 so as to confirm that the activity of distributing a voucher in the name and on behalf of a third party against a fee for that distribution is to be treated as a service. This usually happens in a distribution chain involving agents.

Further provisions would be needed to deal with the consequences of a voucher's distribution reflecting the fact that in a distribution chain, the price usually paid to obtain a voucher increases at each stage by an amount which is the margin made by each distributor. If VAT is

⁴⁹ e.g., European Telecommunications Operators Association and European Banking Federation.

⁵⁰ Royal Dutch Telecom KPN.

⁵¹ Sony.

applied to the sale price, the margin made by distributor is taxed. However, if it is also being proposed that the sale of an MPV does not trigger VAT (because here the tax is chargeable only at the time of redemption) there is a risk that the margin of the distributors would not be taxed. To avoid this, it would be necessary to provide that any positive difference between the nominal value of the voucher and the amount paid by the seller/distributor to the preceding seller/distributor is payment for a service and taxed as such.

Taxing the margin made by distributors separately avoids interfering with the nominal value of the voucher which will be the taxable amount, at the time of redemption, for the goods or services to be supplied. Usually the price at which the issuer sells the voucher at the beginning of the chain differs from the price paid by the customer at the end of the chain because distributors add their margin to the price of the voucher. Separate taxation, as a distinct service, of these distributors' margins avoids any mismatch between the value of the voucher at the beginning and the end of a chain. The distribution of a voucher, made by a commission agent or by the owner of a voucher, would be regarded as a service supplied for consideration (as expressed in the margin achieved) rather than being treated as a sale of the voucher.

Member States have in some cases developed local practices which generally ensure that tax is collected without any undue disruption of business. For cross-border distribution this cannot be said with the same certainty. In making a legislative proposal, there might be a case for limiting any impact to such cross-border arrangements, leaving purely domestic arrangements to the discretion of Member States. The drawback here is that businesses wishing to exploit single market opportunities may well then be faced with two different sets of VAT obligations for their voucher distribution chains – one for domestic operations and another for intra-Community. This would not be a desirable outcome. Any legislative proposal from the Commission should therefore cover the VAT treatment of all voucher distribution chains.

In concrete terms, this would involve additional indents to Article 25 (which clarifies what can be considered as a supply of services for VAT purposes) would have the purpose of clarifying that when the price paid for a voucher increases at each stage in a distribution chain, the benefit this represents to distributor is to be considered as a supply of services for VAT purposes. This new provision would ensure the margin for distribution is separately taxed as an independent service.

Stakeholder views – how addressed.

Public sector stakeholders (tax administrations).

In the absence of any provisions in the VAT Directive, Member States have been left to their own devices and developed their own solutions. These give rise to frequent problems of compatibility when they interact.

Although they are probably reluctant to change what is already in place, there is a general acceptance common provisions in the Directive are needed to deal with intra-EU arrangements.

Private sector stakeholders (business and consumers).

Beyond drawing attention to the difficulties they encounter in this area (notably with intra-EU arrangements), few of the stakeholders have made specific suggestions on how this should be addressed in legislation. Among those who did go into detail, the changes being contemplated here are close to those suggested by the stakeholders.

Dealing with (problems) in relation to the

supply of vouchers through interlediararies (has) resulted in the introduction of complex anti-avoidance legislation in 2003 (in the UK). We suggest that where face-value vouchers are sold by the issuer to an intermediary at less than face value, the adjustment to the consideration on redemption should be disapplied by the new EU legislation so that VAT is chargeable on the full value at the time of redemption⁵².

4.3.3. Taxable amount for transactions involving vouchers

The rules for the computation of taxable amount in transactions for VAT purposes are set out in Articles 72 to 92 of the VAT Directive. They do not however adequately deal with some of the complexities which arise from vouchers, particularly where complex distribution chains are involved and part of the consideration may be generated from a party who is remote to the actual transaction. The taxable amount is not a subjective concept but rather one where certainty is paramount and any potential for misunderstanding should be eliminated.

The taxable amount, in the case of vouchers, needs to be defined as anything received or to be received (in money or in kind) against a voucher by the issuer of the voucher in order to ensure that the normal rules for the computation of the taxable amount can be applied.

This clarification is needed to take account of the value of the distribution service supplied by the distributor of a voucher in a chain involving commission agents. It should be defined with sufficient clarity to obviate the practice of netting off which makes it difficult to identify the value of the service supplied at each stage in a chain.

It should also resolve any residual uncertainties in the correct application of the guidance provided by the Court in the *Elida Gibbs* case.

The objective for any legislative change is merely to ensure that that standard rules for the taxable amount can be applied consistently in all cases.

A further amendments to Article 25 would also be envisaged to ensure that in the case of a free discount voucher, the correct taxable amount is applied when the voucher is redeemed in a Member State other than the one in which it has been issued.

In addition, the existing provisions in Title VII (Taxable Amount) Chapter 2 (Supply of Goods or Services) would need the insertion of specific provisions on the computation of the taxable amount for the underlying transaction or transactions as well as the taxable amount relating to distribution and redemption services. A modification will also be needed (in Article 79) regarding the correct treatment of discounts in operations involving vouchers.

Stakeholder views – how addressed.

Public sector stakeholders (tax

Private sector stakeholders (business and

⁵² Submission from Tax Faculty of the Institute of Chartered Accountants.

administrations).

The changes under consideration here are broadly in line with the views expressed by tax administrations.

consumers).

The specific technical issues here were not taken up by many stakeholders but, in the context of the general desire for order and legal certainty, the issue of removing any uncertainty about the taxable amount cannot be overlooked.

Where a taxable supply is made, the taxable amount should be based on the consideration paid by the final consumer where no intermediary is involved⁵³

We agree the definition of the taxable amount of goods or services supplied against a voucher in the Consultation Paper. We also agree the comment in the same paragraph that the sale of an MPV should be considered as outside the scope of VAT and that it is not necessary to identify the taxable amount of the voucher itself⁵⁴.

We agree with the principles applied to the taxable amount as set out in the Consultation Paper⁵⁵

4.3.4. Time of taxation

An SPV is to be seen as a voucher giving a right to receive only a specific good or service with the customer paying in advance for what will be received later.

The point in time when the tax becomes chargeable is currently regulated by Articles 62 to 67 of the VAT Directive. Article 65 provides that the tax becomes chargeable “on receipt of the payment and on the amount received” where a payment is to be made “on account before the goods or services are supplied”. The last phrase refers to goods and services to be received when the quantity is not already known. To apply this provision to the vouchers it is necessary that the voucher is linked to a “quantity” or a “quantity unit” of a good or a service already identified.

Therefore the application here of the above-mentioned rule should not cause any particular problem and VAT can be charged at the time of sale on the basis of the consideration paid. Such a treatment should be applicable to all SPVs.

The VAT rate applicable to prepaid vouchers should be the same rate applicable to the good or service to be supplied on redemption of the voucher.

⁵³ Submission from European Telecommunications Operators Association.

⁵⁴ Submission from Voucher Association.

⁵⁵ Submission from British Retail Consortium Brussels.

If a voucher can be used in more than one Member State, VAT would have to be accounted for in a manner which deals correctly with differences in VAT rates. This can only be achieved at the time of redemption. Time of taxation lies at the heart of any distinction between an SPV and an MPV. The distinction lies in whether there is sufficient certainty to charge tax at the time of issue or whether it is necessary to wait until the goods or services are supplied.

Since the time of taxation in a transaction involving a voucher can at the moment be either at the time the voucher is issued or at the time of redemption (when goods or services are supplied), there might appear to be a choice to be made in opting for one or the other as the norm. This might seem to be confirmed by the evidence on mismatches in taxation which are attributable to timing differences between Member States.

It is not however a question here of presenting arguments in favour of one or another of these choices (there are only two possible choices for the time of taxation here – issue or redemption). Rather it is the case that certain types of vouchers lend themselves to one of these choices whilst others are more appropriately (and practically) taxed at the other. The Directive however contains no guidance on this and as a result there is inconsistency between Member States with the consequences for tax revenue and market opportunities outlined above.

The path chosen here is to clarify in legislation which vouchers should be taxed on issue and which should be taxed on redemption in a manner that achieves consistency across all Member States and ensures that similar transactions are taxed in a similar manner.

It might be theoretically conceivable to contemplate alternative solutions whereby all vouchers are taxed on issues or all vouchers are taxed on redemption. Both however would lead to considerable practical difficulties. The former would be impossible to administer in practice as the tax consequences are not always clear at the time of issue. Taxing vouchers generally on redemption could be contemplated but it would be a highly disruptive step. The market for single purpose vouchers, taxed at the time of issue, is a considerable one and the tax obligations are relatively easily handled by both businesses and tax administrations. Introducing what would amount to a tax deferral obligation (by taxing on redemption rather than issue) would be extremely disruptive for established business models and would be seen as a highly disproportionate measure carrying little tangible benefit ("harmonisation for the sake of harmonisation") by all stakeholders. Furthermore, it would probably encourage the artificial introduction for purely tax deferral reasons in situations where a simple payment on account is made before goods or services are supplied. Under the current VAT system, such payments are taxed upfront but the use of a voucher would, if these were to be generally taxed on redemption, mean that VAT would be levied only when the transaction is completed. Hence, these options are not considered to be realistic.

The concrete measures needed in the VAT Directive to give effect to this would involve a modification to Article 65 making specific reference to SPVs and, conversely, a modification to Article 66 to ensure that its provisions exclude SPVs.

Stakeholder views – how addressed.

Public sector stakeholders (tax administrations).

Private sector stakeholders (business and consumers).

The changes under consideration here are broadly in line with the views expressed by tax administrations.

This was generally seen by stakeholders as a fundamental issue to be overcome by addressing the relevant provisions in the VAT Directive.

In our view, the time of supply for an MPV is determined by the normal (existing) rules but this needs to be clarified in the legislation. The sale of an MPV constitutes a supply of services for VAT purposes and the time of supply should be determined by the VAT Directive in Article 65. This however should not be confused with the time of supply of the underlying goods or services and payment for an MPV cannot be regarded as a payment on account for these goods or services⁵⁶.

4.3.5. Right of deduction questions

It would be necessary to make certain consequential adjustments to the rules on the right of deduction.

Where the issuer of an MPV redeems the voucher against taxed transactions, Article 168 provides that he can deduct the VAT due or paid in relation to the issue of that voucher. Where the MPV is redeemed, in the course of transactions which give rise to deduction, by someone other than the issuer, the latter should also have an equal right to deduct VAT.

An appropriate modification to Article 169 would be needed to achieve this result.

The issue did not arise in consultations with private sector stakeholders but is required for completeness.

4.3.6. Issuing of invoices and simplification issues

Certain minor consequential changes in the wording of Articles 220 and 226 would be needed to reflect changes made elsewhere in the VAT Directive.

Some other changes in the VAT Directive would be needed to avoid the creation of disproportionate administrative burdens for business as an incidental outcome of the wider rationalisation of the VAT treatment of vouchers, notably to limit the impact of Article 28 which was never intended nor is appropriate to operations involving MPVs.

In the course of discussions with stakeholders, many business respondents stressed the need for a suitable time lag in implementation to take account of the reality that IT system changes are costly and have to be planned, usually requiring at least 12 months' notice. One realistic way of responding to these concerns would be to schedule the proposed changes in the rules

⁵⁶ Submission from Voucher Association.

for vouchers to come into effect on 1 January 2015, coinciding with the recently adopted changes in the rules on the place of supply for certain telecommunication and other services.

Stakeholder views – how addressed.

Public sector stakeholders (tax administrations).

No specific views were advanced by tax administrations under this heading but they are likely to have a constructive approach to simplification and would have similar concerns about lead-in.

Private sector stakeholders (business and consumers).

Simplification and sufficient preparation time were a constant request from the businesses concerned.

Operators should be allowed sufficient time to change the accounting and other systems should the Commission deem that significant changes to the current rules be required ...a lead-in time of one year would be prudent⁵⁷.

The Commission's willingness to introduce simple rules for a complex world is much appreciated⁵⁸.

5. ANALYSIS OF IMPACT

5.1. Main impacts of proposal to reform the treatment of vouchers in the VAT system.

The following tables provide an overview of the expected economic impact on main market players and on the market structure. The descriptions are mainly in qualitative form, given the lack of quantification of the tax avoidance problem. The analysis is however based on standard economic reasoning and on knowledge of the sector built up during the investigatory work.

The expected business impact will be as highlighted in the table. Business location will be more closely linked to economic and competitive factors rather than tax arbitraging. 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. Conversely however, the improved market environment should yield price reductions, notably for international telecommunications benefiting consumers who use pre-paid services.

⁵⁷ Submission from European Telecommunications Operators Association.

⁵⁸ Submission from Hewlett Packard.

5.1.1. Table A - Impacts on the main market players (prepaid mobile telecommunications).

<i>Player type</i>	<i>Situation before reform</i>	<i>Situation after reform (impact).</i>	<i>Comments/Explanation</i>
<i>Pan-EU and other international major telecoms operator</i>	<p>Faces significant irrecoverable VAT costs in some countries because of double taxation → impact on margins on markets which it cannot abandon</p> <p>Cross-subsidisation of lines of business</p> <p>Faces tax risks, uncertainty</p> <p>Faces competition from operators enjoying more favourable VAT treatment</p> <p>Faces risk of competition from unscrupulous operators</p> <p>Some operators more touched than others (e.g. pure B2B wholesalers may be only marginally affected)</p>	<p>Resolution of double taxation problem</p> <p>Reduced compliance costs</p> <p>Reduced distortion of pricing structure</p> <p>Enjoys level playing field</p>	<p>See page 6 of working paper for examples of problems currently being encountered.</p>
<i>Mainly domestic telecoms operator</i>	<p>Discouraged from seeking international integration by tax uncertainty, complexity (but rationalisation of industry tends to encourage partnership arrangements).</p>	<p>Certainty of tax treatment will make them more likely to move into new markets or new market segments for pre-paid mobile services</p>	<p>Many traditional national operators are gradually disappearing through a process of rationalisation in the industry.</p>
<i>Mobile</i>	<p>Branded sellers in</p>	<p>Removal of tax</p>	<p>Often have limited infrastructure</p>

virtual network operators (MVNO)	<p>particular will wish to maximise market penetration across MS where brand is established – mismatches in taxation will act as a barrier here.</p> <p>Marketing or functionality often restricted to a single Member State to avoid unmanageable tax consequences.</p>	<p>obstacles will allow for better exploitation of single market opportunities.</p>	<p>and will not have own-licence frequency allocation but can nevertheless attain significant size, using platform of major operators.</p> <p>May often operate as branded sellers using established brands (e.g. a large supermarket chain) with existing customer base.</p>
New entrant.	<p>Effectively shut out of parts of single market possibilities due to VAT obstacles</p> <p>Ethnic markets which attract new entrants and/or small operators are typically cross border – as such they are particularly vulnerable to taxation mismatches. These markets are price-sensitive and the cost of supporting double taxation may be prohibitive for a new entrant.</p>	<p>More opportunities to expand across single market without encountering tax difficulties.</p> <p>Consistent transparent prices across all Member States</p>	<p>Can be set up with relatively little capital, purchasing capacity on what is effectively a spot market. This leads to more choice and better prices for consumers.</p>
Content providers	<p>Lack of clarity on tax consequences extend to content downloads as well as mere connectivity.</p> <p>Heavily dependent on vouchers as target market may often not have credit cards.</p> <p>Tax mismatches create additional cost and hinder</p>	<p>Restrictions on single market opportunities without encountering tax difficulties (or carrying double taxation) would be avoided.</p> <p>Consistent transparent prices across all Member States</p>	<p>(e.g. UK content provider – see page 7 of WP)</p>

	internal market possibilities.		
Tax arbitragers	Buys and sells contracts based mainly on VAT differences	Unintended tax based cost advantage is removed. Successful modernisation of the VAT Directive would see an end to this category.	Typically smaller or recent entrants who target mismatches in taxation on an opportunistic basis, buying capacity wherever they can.
Voucher distributors	Face considerable tax uncertainty, particularly on intra-EU operations.	Intra-EU distribution arrangements are made easier when tax obstacles are removed. Complex tax compliance obligations are simplified.	Branded re-sellers often have well developed intra-EU distribution networks associated with their primary business (e.g., supermarket retailers) which they would like to exploit fully.
National tax administrations	Must attempt to limit tax avoidance, arbitrage through un-coordinated action – this effects all operators and is not always successful. Transient operators who come and go, operating on an opportunistic basis, cause problems for tax administrations. Voucher sector produces revenue losses and is difficult to control in practice, particularly because of its fragmented nature at the lower level. The 18 MS taxing at issue or on sale exposed to losses on vouchers coming from MS	Saves regulatory and administrative costs as incentive for uncoordinated regulatory action removed. Ensures that tax revenue is collected and goes to the correct Member State.	

taxing upon use			
Consumer	<p>Owing to tax differences, location may impact on prices and choice of operator</p> <p>Efficiency of markets and quality of choice may be hampered by distortive presence of operators targeting primarily tax savings.</p> <p>Double taxation will often fall on the customer in the form of higher prices.</p> <p>Tax system fragments the market and leads to higher prices.</p>	<p>Will benefit from more competition, more choice and more attractive prices.</p>	<p>Unclear tax rules leading to double taxation which will often fall on the consumers as higher prices.</p>

5.1.2. Table B - Impacts on market / sector structure

<i>Variable</i>	<i>Situation before reform</i>	<i>Situation after reform (impact)</i>	<i>Comment / Explanation</i>
Number of operators	Highly varied across Internal Market, in some cases depending also on tax advantages	<p>Tax arbitragers (and possibly some other marginal operators) might go out of business following reduction of tax distortions, more level playing field.</p> <p>This will probably however be compensated by more attractive opportunities for new entrants who currently hesitate because of uncertainties in the tax system.</p>	<p>Trend today is towards rationalisation in the industry.</p> <p>Infrastructure is provided by large international players who may or may not sell direct to public.</p> <p>They in turn support a large and diverse group of smaller operators who provide mobile phone services but do not necessarily possess the entire infrastructure required to provide it.</p>

Type of operators	Differs widely depending, <i>inter alia</i> , also on tax advantages or tax compliance rules.	Possibly, greater homogeneity as loss of tax arbitrage possibilities creates some convergence towards a single, most efficient business model. Conversely, level playing field for tax may attract more intra-EU operators or encourage nationally based operators to expand.
Tax compliance costs	High and uneven	Lower and more even across Internal Market
Tax avoidance / tax evasion	Situation creates opportunities for tax avoidance	Tax avoidance opportunities reduced or even eliminated.
Sale prices	Depending on price elasticities, some of the tax differences might be passed over to consumers, resulting in price differentiation across internal Market. Fragmentation of Internal Market prevents companies fully to exploit economies of scale.	Removal of tax distortions expected to lead to greater price convergence across the internal market, particularly for price-sensitive market segments owing to higher elasticity. Better opportunities for international integration should allow lower average prices and better quality in the long run.
Degree of competition	Not strictly based on efficiency / biased	Will better allow more efficient operators to grow. Removal of distortive factors will tend to increase competition.
Geographical distribution of businesses	Business attracted to establishing in MS taxing upon use to exploit tax differences by targeting consumers in MS where tax is on sale of voucher	Business location orientated towards economic efficiency

The main objective of this initiative is to close down the currently existing loopholes in VAT legislation which allow or at least facilitate schemes aiming at avoiding taxation. From the perspective of tax administrations, the principal desired impact is therefore a reduction in tax avoidance or unintended non-taxation on this account. Secondary benefits involve the elimination of the risk of double taxation and the distortion this generates, as well as a reduction in economic agent's uncertainty about the legal obligations needed to ensure tax compliance.

This is not an initiative which is likely to have a major impact on the operation of the EU's common VAT system outside the sector specifically targeted. The intention is to deal with conditions which have arisen through developments in technology, and to a certain extent deregulation, and which were not envisaged at the time the provisions of the VAT Directive were first enacted.

Other than those already provided for in the Directive and implemented by Member States, no new obligations for taxpayers or tax administrations are envisaged.

The changes envisaged will close down certain openings for tax avoidance or evasion which are being exploited today. These however are not activities which readily declare themselves and accordingly it is not possible to quantify the impact of their elimination. Nevertheless, one can evaluate the potential benefits against a number of considerations. First, the telecommunications sector, where the study has identified the biggest market segment for vouchers at around €36 billion, is of great importance: it directly accounts for about 3% of EU GDP and, according to the latest data, almost € 50 billion in annual investment. Second, the sector is at the forefront of technological innovation and a key driver of innovation and growth in other sectors as well. Third, within the high technology sector, the European telecommunications industry has been performing relatively well in terms of the international competition and has therefore demonstrated an important potential to contribute to maintaining EU competitiveness. It is therefore crucial not to distort the functioning of the sector by allowing investment and trading choices to be dictated by the desire to exploit tax loopholes instead of maximising economic efficiency. This is all the more true as the dimension of the problem is bound to grow in the absence of any regulatory action as traders 'learn by doing' and reinvest their profits in new schemes. Furthermore, the economic possibilities inherent in the increasing common ground between mobile telecommunications and mobile payments risk been stifled if there is no clarity on the tax treatment applicable or if the tax system does not assure neutrality in competition between competitors.

Inaction at EU level would on the other hand bring with itself a clear risk that individual Member states introduce ad-hoc solutions in an uncoordinated manner, which would result in undermining the Internal Market in the sectors concerned. Conversely, removing uncertainty and inconsistency in the tax treatment of voucher-facilitated transactions, particularly in telecommunications, is expected to facilitate business development and give some reduction in overall compliance costs.

In the course of the public consultation and in ongoing dialogue, these points were repeatedly made by private sector stakeholders. They did not however quantify their expectations for enhanced business and no independent data is available but there is a

reasonable expectation of positive economic impacts even if these are difficult to quantify. The overall size of the market, for prepaid telecommunications in particular, is however both significant and continues to grow⁵⁹. This in itself would provide sufficient justification for removing any unnecessary tax-based barriers for business and the economic benefits can only be positive.

Actual compliance cost savings are hard to quantify but this does not mean that they can be dismissed. Little or no impact is expected on recurring standard VAT compliance costs (record keeping, periodic declarations, *etc*) as no changes are envisaged in the obligations which create them. Any savings are likely to be found elsewhere. Responding to uncertainty, inconsistency and complexity in VAT, particularly when this is attributed to differences between Member States in applying the tax, usually manifests itself in once-off or intermittent actions. Their cost will vary according to how business deals with them and the saving generated by their partial or total elimination would not be easy to verify. The fact that these savings are difficult to measure, particularly on a global basis, does not diminish their value. Modernising the legislation and removing the likelihood of individual Member States implementing diverse or *ad hoc* solutions will bring definite compliance cost savings to businesses which operate in more than one Member State. The consequent reduction in uncertainty is likely to translate into cost savings for the businesses concerned generally.

5.2. Modernising the definitions of vouchers

There are currently no definitions of vouchers in the VAT Directive. The definitions being contemplated follow broadly the approaches taken by tax administrations with whom the Commission has had frequent discussions over the year.

To that extent therefore, any legislative change would merely bring the Directive into line with the practices which have evolved on the basis of pragmatic solutions.

No real evidence has emerged that businesses would have any difficulty with this although some concerns were expressed in the consultation process about future developments leading to obsolescence which in turn would create tension for new business models or innovations in technology. This however is unlikely given the very general and high level approach taken which would be unlikely to act as a constraint on innovation within any reasonable time perspective.

The economic impact here is not readily quantifiable. A reduction in compliance costs would however be expected from more consistent interpretations across all Member States, particularly for pan-EU businesses or those seeking to exploit single-market opportunities.

The maximum economic benefit would be expected from a legislation based solution. Soft law is unlikely to deliver the same degree of certainty and uncertainty about the taxing outcome is generally regarded as highly undesirable.

5.3. Distribution of vouchers through a chain and the distributor's margin

Distribution chains (typically for prepaid telecommunications vouchers but often described as a "credit top-up" or similar) operate on one of two broad bases. Either the distributor changes

⁵⁹ This is confirmed by the Deloitte study.

a stated fee for the distribution service or takes a mark-up in the process. The contemplated changes are predicated on the notion that these are economically equivalent and should be taxed in the same way.

Amending the VAT Directive to reflect this and to ensure neutral treatment should not in itself have any significant for most businesses or tax administrations. It should however facilitate cross-border distribution chains when the Directive sets common rules for the treatment of distributors' income.

It cannot however be excluded that this setting of common rules will be disruptive in a very small number of instances, particularly where small distributors of prepaid telecommunications vouchers are covered by specific local arrangements which would be difficult to incorporate in the Directive. These include concessional or *forfaitaire* schemes or high registration thresholds for small businesses.

By their nature, it is not always easy to get a clear picture of such local arrangements and it would be impossible to construct something at the level of the VAT Directive to take account of all local variations. In the unlikely event of this giving rise to insurmountable problems or having a disproportionate negative impact, the Commission would seek to find a solution on the basis of dialogue with the Member State concerned.

As the impact is uncertain (because in many instances, existing practices may be based on concessional arrangements which are often not documented), it is not practical to quantify it. The overall economic impact, particularly in so far as the outcome facilitates business, should however be positive and even extend to clear practical benefits such as the opening up of pan-EU distribution chains.

5.4. Taxable amount for transactions involving vouchers

Clarification of the taxable amount is not likely to have any significant impact on either business of tax administrations, beyond the benefit of clarifying the correct procedure to follow in chain transactions.

In so far as that the existing situation has been a source of litigation, and this has not yet solved all of the interpretation issues involved, positive economic benefits should be expected. These would include reduction in costs created by uncertainty and, in some circumstances, removal of barriers which hinder economic expansion.

Here, as elsewhere, litigated solutions are an expensive and often unsatisfactory in bringing clarification. Removing the need to have recourse to the Court puts an end to a potentially significant economic burden for both taxpayers and tax administrations.

5.5. Time of taxation

Where the purchase of prepaid telephone cards cannot be considered to be an advance payment for future supplies of certain goods or services and, on that ground, is not subject to VAT, the tax must become due at the time the holder of the card actually uses it for the purposes of making payment for specific supplies of goods or services (Article 63 of the VAT Directive). It normally remains the responsibility of the supplier of the service to ensure tax compliance in such circumstances.

In the most circumstances the likely changes will have little effect on the tax outcome. Acquiring telecommunications services by means of a voucher (prepaid credit) should not endanger the application of the rules of taxation. For B2C telecommunications services, these are currently taxed on the basis of where the supplier is established (provided this is within the EU). Uncertainty about the time of taxation can however lead to uncertainty about the place (Member State) of taxation where Member States have mismatched practices.

Following recent changes in the rules for place of taxation, from 1 January 2015 telecommunications services will be taxed where the consumer is established. For an essentially anonymous service, such as prepaid telephone credits, linking the place of taxation to where a sim card is issued would generally be a path to securing this result.

Achieving a correct taxing outcome will not be incompatible with the established operating model for most telecommunications service providers or sellers of prepaid telecommunications service. That the tax system might include measures to ensure that vouchers cannot be employed to frustrate normal tax rules or to sustain other mischief can never be seen as having a burdensome impact on compliant businesses.

By ensuring a clear and consistent tax outcome, the contemplated changes will give reassurance to both businesses and tax administrations, particularly where cross-border transactions are involved.

In most cases, this will not have any significant impact. The changes will however remove residual uncertainty about the time of taxation which may act a barrier to commercial arrangements.

Aligning the time of taxation for voucher-facilitated transactions will close opportunities to avoid taxation on certain types of transactions and which cause concern to tax administrations. This will have an economic impact on operators who currently exploit such loopholes. It is however impossible to quantify this. Even where tax-arbitraging or simple tax avoidance is the driving force behind a particular business model, it will usually be presented in such a way as to conceal or minimise such motivation. Identifying schemes which are created purely to generate a tax advantage (VAT or otherwise) is not always straightforward.

There is no measurable impact here but the economic benefits can be envisaged in more qualitative terms. Clear and consistent tax rules should provide a growing industry (and one which is increasingly pan-European) with an environment which enables them better to reap the economic benefits of the Internal Market.

5.6. Impact on Member States from modifying the VAT Directive

If a proposal from the Commission to amend the VAT Directive along the lines indicated above is adopted by the Council, Member States will be required to take the necessary steps to ensure their legislation is in conformity.

On the basis of the information and explanations available to the Commission, it does not appear that any Member State currently has legislation in place which reflects in full the particular measures envisaged for a proposal. The absence of any common rules has meant that Member States have found their own solutions over the years (as shown by the identified mismatches in section 2.2 above). The obligation to bring national legislation and practice

into line with EU provisions will probably involve all Member States in taking measures to achieve that.

Member States who have responded to problems through concessional or extra-statutory arrangements will have to ensure that these are placed in conformity with their EU obligations. As these practices are not always fully documented, it is not possible to indicate which Member States might face significant conformity issues. It is noticeable however that in the course of the discussions mentioned in section 1.1, not one of the Member States gave any indication that bringing their legislation in line with a common EU practice would be seen as unduly onerous.

Those Member States who have indicated that they suffer revenue losses because of mismatches in taxation under the current rules would see an end to those losses. As indicated elsewhere however, there is reluctance on their part to supply specific data on tax losses, making it difficult to quantify any beneficial impact.

There is however no reason to expect that any Member States will face negative revenue consequences because of these measures. Moreover, the removal of obstacles to intra-EU commerce is potentially beneficial for all.

5.7. Neutrality between competing payment systems

Defining vouchers has the consequence that some operations may cease to qualify as vouchers if they fall outside that definition. As MPVs acquire increased functionality, they become more like a mainstream payment service. The implications of this is analysed in section 2.2.1.

If the outcome is to qualify certain services now offered by telecommunications service providers as payment services and if these services are treated as exempt, there will be consequences associated with partial exemption including some restriction on recovery.

It is possible that some of the service providers concerned will see this as a negative consequence but it would be difficult to ignore the competitive imbalance that would result from any other treatment. Current uncertainty about what constitutes a voucher for VAT purposes and where the dividing line is to be drawn between vouchers and general payment systems may allow certain operations to benefit from a more advantageous tax regime. This is contrary to the notion of neutrality in competition which is central to the VAT system and cannot continue.

The Commission has however already made a proposal⁶⁰ which is currently under discussion in the Council which would allow providers of otherwise exempt financial services to opt to tax them. If this is accepted by the Council, there would then be no negative economic impact for businesses that are deemed as providing payment services.

6. COMPARING THE OPTIONS

Policy Objectives	1. Doing nothing	2. Soft law approach	3. Modification of the VAT Directive
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⁶⁰ Proposal for a Council Directive amending Directive 2006/112/EC on the common system of value added tax, as regards the treatment of insurance and financial services [COM(2007) 746].

Removing uncertainty from tax system.	The outcome would be continued reliance on the ECJ to overcome the legislative gaps. As already mentioned this is cumbersome and does not always deliver clarity.	As with option 1, litigated solutions would remain a feature. As there is really no clear rule at all in the VAT Directive, there is no core element of law from which guidance might be drawn.	The only certain way of meeting this objective would be to modernise the Directive by inserting new provisions dealing with vouchers.
Protect public revenue.	Revenue losses attributable to mismatches or aggressive tax planning will continue. Member States often find their options for dealing with the latter are limited.	Threats to revenue would persist and it is unlikely that Member States would accept this as a sufficiently robust response.	Clear legislation which assures correct taxation in all circumstances is the best way of protecting tax revenue.
Deliver neutrality in competition.	Existing absence of level playing field would persist.	Existing absence of level playing field would probably persist.	When VAT works properly, neutrality is assured. This can only be achieved by filling the gaps in the system, an outcome that can only be assured by legislative measures.
Deal with mismatches in place and/or time of taxation.	Mismatches would persist, leading to unintended double or non taxation.	Existing absence of level playing field would probably persist. This instrument is not really suited to solving conflicts of interpretation between different Member States.	Mismatches in taxation can be attributed to the shortcomings in the Directive. Clear comprehensive provisions in the Directive, applied consistently by Member States would end this.
Dealing with the consequences of ECJ judgements.	Litigation would remain the main way to deal with problems of application. Problems with existing jurisprudence which	Litigation would in all likelihood still be seen as a remedy. Guidance (say in the form of VAT Committee output) would only provide a remedy to minor interpretational problems or unevenness	Although it is impossible to rule out future litigation, some reduction could be expected from modernised legislation. In so far as it is

	can be difficult to apply or is applied unevenly would persist.	in application associated with existing ECJ jurisprudence.	necessary to deal with the consequences of ECJ decisions, this can best be achieved by updating the Directive.
Setting clear lines between vouchers and innovative payment systems.	Continued problems about neutrality in competition between similar services would persist with possible negative effects on business innovation.	Some clarification could be achieved through <i>e.g.</i> VAT Committee guidelines. However uncertainties arise from the application of specific provisions in the Directive (such as the rules on recovery) and it is not clear that these could be overcome through guidelines.	Definitions of the different types of vouchers in the Directive will give certainty about what is and what is not a voucher. Neutrality and consistency in the tax treatment should follow from this.

It is by now clear that the problems encountered and which this initiative seeks to address, are attributable to shortcomings in the Directive in so far as it has not kept abreast of more recent commercial developments.

Given that taxation requires absolute legal certainty and, as far as intra-EU commerce is concerned, this can only satisfactorily be achieved through Community legislation. None of the other options considered would deliver this outcome.

Moreover, in discussions with Member States and other stakeholders (notably in the public consultation), there were few voices raised in favour of a non-legislative solution. This reflects the reality of their limitations in taxation generally. The conclusion of this impact assessment has to be that a legislative solution is needed since none of the other options will assure the desired outcome.

7. MONITORING AND EVALUATION

It is established practice for the Commission to monitor the implementation by Member States of legislation of the kind envisaged. No particular additional measures are envisaged in that respect.

Beyond this it is likely, reflecting experience with other recent changes to VAT legislation, that technical or legal issues consequent to implementation will give rise to discussions within the VAT Committee. These will be scheduled as the need arises.

Depending on the views expressed by Member States, or by other stakeholders, consideration may also be given to holding a further Fiscalis seminar, to examine issues arising from implementation and possibly to share experiences of best practice. Although these seminars are aimed at bringing together officials from national tax administrations, the practice has developed that business expertise is also given a voice where this is appropriate.