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ACTION NEEDED TO IMPLEMENT THE VAT QUICK FIXES FROM 1 JANUARY 2020

The EU intends a comprehensive reform of the VAT system. The goal is to establish a VAT system for the EU that is both less complicated and less susceptible to abuse. As a first step to combat abuse and fraud, the EU Member States agreed on a number of amendments to the EU VAT Directive (the so-called "Quick Fixes"). These Quick Fixes were implemented into national law by the end of 2019 and apply from 1 January 2020 onwards.

The legislative process in Germany is concluded. Necessary changes of national law passed both chambers of legislation by the end of November 2019. In addition, the VAT committee at EU level prepares Explanatory Notes to facilitate implementation of the Quick Fixes by the Member States and businesses in the EU. A first draft of the Explanatory Notes was published on 26 September 2019. However, the Explanatory Notes merely take the form of recommendations. In cases of doubt, taxpayers cannot base an appeal on the interpretations contained in the Explanatory Notes.

DO THE QUICK FIXES ALSO AFFECT YOUR BUSINESS?

The Quick Fixes bring about changes with regard to

- the criteria by which intra-Community supplies qualify for tax exemption,
- the documentary evidence needed for cross-border movements of goods,
- the allocation of the movement of goods in chain transactions, and
- the simplifications provided for consignment stock arrangements.

Companies that maintain international trade relationships, or plan to do so in future, regardless of their business sector, have therefore to address the new legislation as a matter of urgency.

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CONTENT OF THE NEW LEGISLATION

1. CRITERIA FOR THE TAX EXEMPTION OF INTRA-COMMUNITY SUPPLIES

Commencing in 2020, the key criteria for tax exemption pursuant to Sec. 6a UStG (German VAT Act, hereinafter: "VATA-DE") are:

› a valid VAT Identification Number of the customer,
› evidence that the goods were moved across the border,
› submission of a recapitulative statement, and
› no "involvement" in tax evasion.

The substantive and formal requirements for intra-Community supplies currently applicable will be extended by the new Sec. 6a VATA-DE. Under the terms of the new law, the tax exemption requires that:

› the buyer (established in another Member State than the state of dispatch) has to be registered for VAT purposes at the time when the delivery is made, and
› the buyer actively uses his valid VAT Identification Number from the Member State of destination.

Moreover, the new Sec. 4 No. 1b VATA-DE requires the supplier to submit a recapitulative statement in order to obtain tax exemption.

PRACTICAL TIPS

VAT IDENTIFICATION NUMBER (VAT-ID)

Due to the fact that the VAT-ID is now a substantive legal prerequisite for the tax exemption of intra-Community supplies, the need to obtain a qualified confirmation of the VAT-ID from the Federal Central Tax Office and the documentation of the confirmation is even more important than it was until now.

The new regulation in Germany requires the VAT-ID to be "used" by the buyer in order to obtain tax exemption. The "use" of the VAT-ID requires taking action and therefore actively communicating the number (see Part B Special Section of the bill on the 2019 Annual Tax Act ("JStG") dated 31 July 2019). In other words, the VAT-ID printed on the letterhead of the buyer no longer suffices. However, this rule goes beyond the requirements of the EU VAT Directive, as this only requires the buyer to communicate its VAT-ID in any way. For example, according to the draft Explanatory Notes it is sufficient when the VAT-ID of the buyer is stated on the invoice, as it can then be assumed that the VAT-ID was communicated to the supplier beforehand. Moreover, the use of the term "use" in German law raises a number of questions, particularly with regard to the time of use. In its statement on the bill, the Federal Council called for a legal definition of the term "use" to

be included in the law. However, the cabinet considers such an addition to the law as superfluous and refers in its counterstatement to the German Administrative Guideline regarding VAT ("VAT-DE") which already defines how the term "use" has to be understood (Sec. 3.2 par. 10 sentence 2 et seq. VAT-DE).

Currently the issue of whether subsequent communication of a valid VAT-ID is sufficient to qualify for tax exemption remains open. The draft Explanatory Notes allow a subsequent communication in the case when a buyer has applied for a VAT-ID but did not receive it prior to the movement of the goods. This example also illustrates the need for a supplement to the law in Germany as the active "use" of the VAT-ID requires that it has already been issued before the goods are supplied.

RECAPITULATIVE STATEMENTS (RS)

If the company does not meet its duty to submit a RS or if the RS is inaccurate or incomplete with regard to the respective supply, the tax exemption for this intra-Community supply will be denied, even if all other prerequisites are met. The lawmakers have already understood that a RS can only be completed after the intra-Community supply has been executed. For this reason, this new criterion for the tax exemption of intra-Community supplies has been included in Sec. 4 No. 1b VATA-DE and not in the definition of Sec. 6a VATA-DE.

It remains to be seen how the fiscal authorities will handle incorrect RS. Generally, when all other criteria for the tax exemption according to the new Sec. 6a VATA-DE are met at the time of the sale, the intra-Community supply should be treated as tax exempt at this time. The invoice should therefore be issued without VAT. If the supplier submits an accurate RS at a later date or when he can suitably remedy or justify any errors or oversights, the tax exemption will remain in force. Both the bill issued by the cabinet as well as the draft Explanatory Notes allow any RS that is incorrect, incomplete or submitted late to be corrected. Such a correction should apply retrospectively to the time of the sale for the purposes of tax exemption.

2. DOCUMENTARY EVIDENCE FOR THE CROSS-BORDER MOVEMENTS OF GOODS

The new Sec. 17a of the German VAT Implementation Ordinance ("VIO-DE") includes another novelty relating to intra-Community supplies. This new rule simplifies the documentary evidence, depending on who undertakes the shipment. The documentation have to be kept on the basis of at least two sources from a given catalog that do not contradict each other. The rule constitutes a presumption, which the tax authorities may later rebut.

It should be noted that the new rule contained in Sec. 17a VIO-DE does not replace the current rule of Sec. 17a VIO-DE which will stay applicable as new Sec. 17b VIO-DE.

PRACTICAL TIP

The practical implications of the changes in the documentary requirements tend to be relatively minor in Germany, as the current regulation on documentary evidence (the Entry Certificate in particular) will stay applicable. This is the express wish of the lawmaker in addition to the uniform EU presumption rule, which was implemented in the new Sec. 17a VIO-DE by the Annual Tax Act 2019. The rules of the new Sec. 17a VIO-DE are based on Art. 45a of the EU VAT Implementing Regulation. Art. 45a constitutes the maximum requirements on transport papers that may be demanded by Member States. Nevertheless, businesses should address the new rules as it is possible that suppliers based in other EU Member States will be confronted with the new requirements and demand additional documentary evidence in future.

3. ALLOCATION OF THE MOVEMENT OF GOODS IN CHAIN TRANSACTIONS

With regard to chain transactions (several supply transactions with the direct movement of goods from the first supplier to the final customer) the place of supply and the applicability of the tax exemption of intra-Community supplies or export deliveries depends on the question to which section of the chain transaction the movement of goods is allocated to. Unfortunately, how this is decided is treated differently by the Member States of the EU. The court rulings by the European Court of Justice (ECJ) and the Federal Fiscal Court in Germany also differ on this point. This legal uncertainty is now supposed to be remedied by the amendment of uniform requirements to the EU VAT Directive.

The new Sec. 3 par. 6a VATA-DE incorporates the EU requirements into German law:

- If the first supplier in the chain transports/dispatches the goods, then the movement of goods is allocated to the first transaction.
- If the final customer in the chain engages the transport/dispatch of the goods, then the movement of goods is allocated to the supply to the final customer.
- If another party in the middle of the chain (buyer/seller) transports or dispatches the goods, then the movement of goods is allocated to the supply to this party.

Generally, the question of who moves the goods is decided on the basis of which party engages the transport.

If a party in the middle of the chain transaction ("interposed trader") engages the transport, then the movement of goods is allocated to the supply of the goods to this party (as mentioned above). However, if this party uses a VAT-ID of the Member State of dispatch, then the onwards supply by this party is deemed to be the supply to which the movement of goods is allocated to. This also applies in the case of exports if the interposed trader uses the VAT-ID or the tax number of the Member State of dispatch. In cases involving imports, the movement of goods will be allocated to the interposed trader if he registers the transaction with the customs authorities in its own name, or in case of indirect representation.

PRACTICAL TIPS

If the interposed trader engages the transport, the agreement of special incoterms loses its significance, as the allocation of the movement of goods only depends on the use of the VAT-ID. The interposed trader can therefore influence the allocation of the movement of goods by communicating or refusing to communicate its VAT-ID. In this regard, interposed traders in a chain transaction should take care. Based on the current interpretation of the new law, the "use" of the VAT-ID has to occur prior to the transport/dispatch of the goods. However, the draft Explanatory Notes state that the VAT-ID may also be communicated later and therefore does not necessarily have to be "used" prior to the beginning of the transport. It remains to be seen whether the lawmakers and fiscal authorities adopt this interpretation.

According to the draft of the Explanatory Notes, the party that engages the transport/dispatch is the party that enters into a contract with the freight forwarder and bears the risk of transport. Furthermore, it is stated that it would be harmful for the presumption of a chain transaction if multiple parties are involved in the transport and each engages for individual sections of the transport. This corresponds to the current administrative guideline in Germany (Sec. 3.14 par. 4 VAT-DE).

Cases where goods are picked up remain critical as another party engages the transport and the first supplier cannot be sure whether he is involved in a chain transaction or not. In such cases the first supplier should always check the freight papers to determine whether his customer engaged the transport or not and be aware of the VAT consequences (e.g. invoicing process).

4. SIMPLIFICATIONS PROVIDED FOR DELIVERIES TO CONSIGNMENT STOCKS

The new Sec. 6b VATA-DE introduces a simplification for the treatment of supplies to consignment stocks. The new regulation provides for a presumption that supplies are made directly to a customer (avoiding an intra-Community transfer of goods) if the following criteria apply:

- The goods are transported from one Member State to another Member State by the supplier.
- There is an agreement between the supplier and the customer by which the latter is entitled to the acquisition of property regarding the delivered goods.
- The supplier knows the full name and address of the customer at the time the transport/dispatch of the goods commences.
- The supplier does not have a permanent establishment in the Member State of destination.
- The customer uses the VAT-ID of the Member State of destination.
- The VAT-ID and identity of the customer are known to the supplier at the time the transport/dispatch commences.
- The supplier enters the customer's VAT-ID in its RS and marks the goods separately in the list to show that the goods were delivered in accordance with the new Sec. 22f VATA-DE.
- The goods are removed from the stock within 12 months.

If the above criteria are met, it is assumed that an intra-Community supply occurs when the goods are called off from the stock (with a corresponding intra-Community acquisition by the customer). There is no intra-Community transfer of goods beforehand. As a consequence, the supplier does not have to register for VAT purposes in the Member State of destination.

If the goods are stored in the consignment stock for more than 12 months, it is assumed that an intra-Community transfer of goods occurs on the day after the 12 month-period expires. In this case, the supplier has to register for VAT purposes in the Member State of destination.

PRACTICAL TIPS

Businesses do not have to apply the simplifications for consignment stocks. Based on the draft Explanatory Notes, it is sufficient to act consistently, when the criteria are not met, in order to avoid mandatory applications of the simplification.

The supplier is obliged to state the VAT-ID of the customer in the RS. According to the draft of the Explanatory Notes, it is not necessary to include any information (besides the VAT-ID of the customer) in the RS when goods are just transferred to the consignment stock. Furthermore, the draft states which values have to be reported in the RS when the stocks are used in a regular or harmful transaction.

With regard to the use of the VAT-ID, please see the comments under 1. "VAT-ID".

In its statement on the 2019 Annual Tax Act, the Federal Council addressed the issue of "Technical difficulties when amending the RS" and called for a change to the law, as it can be assumed that technical implementation of the RS will not occur before October 2021. The cabinet is currently reviewing how this issue can be handled.

If the supplier and the customer agree to apply the simplification, it would be advisable to enter into agreements on how the required data should be exchanged. For example, it would make good sense for the parties to mutually commit to providing the other party the corresponding information.

It is not clear whether the contractually agreed sequence in the use of the goods applies for VAT purposes when determining the use of the goods or whether an accounting fiction (e.g. FIFO) can be applied. The latter would apply especially for bulk goods, as it is impossible to check how long individual parts have actually been in stock.

If the time limit of 12 months is exceeded, or some other event occurs (e.g. destruction, accidental loss or theft of the goods) the supplier has to register for VAT purposes in the Member State of destination. In practice, this could lead to the situation that the supplier is not registered in the Member State of destination when the harmful event occurs. The supplier has to report an intra-Community transfer of goods in the Member State of dispatch that is equivalent to an intra-Community supply. This supply will not be tax exempt as the supplier does not have a VAT-ID in the Member State of destination. It remains uncertain whether input VAT can be deducted in such cases. In addition, in spite of being subject to VAT in the Member State of dispatch, there is still a duty to report an intra-Community acquisition in the Member State of destination. Due to the discussion relating to "use prior to delivery" or "mere communication" it is currently not certain that a retroactive correction will be possible. In case there is a risk that the 12-month storage limit might be excee-

ded, suppliers could choose to register for VAT purposes in the Member State of destination as a precautionary measure. However, this would run counter to the sense and purpose of the simplification. In addition, it appears that actual taxable supplies have to be executed in the Member State of destination as otherwise the registration cannot be maintained.

5. USE OF CONSIGNMENT STOCKS FOR DOMESTIC TRANSACTIONS AND FIXED CUSTOMERS

Currently the simplification only covers consignment stocks in cross-border structures. In domestic situations there is still need for regulation. There are also uncertainties with regard to supplies to a specific customer. In court rulings by the Federal Fiscal Court, which the fiscal authorities have followed, there is already a movement of goods when the goods are placed into the consignment stocks and not when they are called off by the customer. This perspective leads to a conflict between the German VAT Act and the Commercial Law. As the issue was not resolved by the lawmaker before the 2019 Annual Tax Act came into force, and the fiscal authorities did not prolong the non-objection rule, the entrepreneurs will be required to avoid differing dates under the VAT Act and the Commercial Law by entering into mutual agreements addressing the issue.

CONCLUSION

The amendments are driven by the goal of uniform European VAT regulations. Overall, this goal seems to be achieved. Unfortunately, there are already signs of there being some weaknesses in the new legislation. First and foremost, the fiscal authorities will be called on to offer a practical interpretation of the laws.

In spite of the existing uncertainties, entrepreneurs should place their priority on analyzing their internal processes as soon as possible and modifying them accordingly, where needed. We have already conducted a number of workshops with clients and would be happy to also assist you and your company in this endeavor.

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