

PRESS RELEASE

International Tax Barometer

DOING BUSINESS ABROAD: VAT a Crucial Factor

Berlin, 24th July, 2014 – Growing numbers of businesses are taking the plunge and offering their goods and services for sale on markets abroad. “This means, of course, that small firms in particular are increasingly having to deal with issues involving international fiscal considerations,” says Peter Lüdemann, member of Ecovis' management board and an expert in international tax law. “Unfortunately, they often first become aware of the pitfalls when they attract the attention of foreign financial authorities if they have infringed fiscal regulations in the country they have exported to.” In the case of particularly types of transactions involving VAT, this may even happen to foreign enterprises supplying goods or services without a subsidiary or permanent establishment in the foreign country to perform the transaction. It is such problems which prompted Ecovis to investigate the issue in more detail by addressing the following questions to the firms which are partners in its international network: “When do foreign suppliers and service providers have to pay VAT in the country to which they are exporting goods or services and when do they have to register with the local finance authorities? And what are the consequences if they infringe VAT requirements?” Partners of Ecovis in 25 countries, ranging from Argentina to Japan, participated in completing the questionnaire. The answers to the question about VAT requirements in each of these countries were many and varied – even within the EU. “It is therefore sensible to seek expert advice on the VAT situation before commencing transactions with another country,” concludes Josef Debono, indirect tax advisor with ECOVIS Malta. There is, however, one exception: Hong Kong. Here there is no need to worry about VAT, because they have none. The answer to the question of what the consequences of late declaration or payment of VAT are is that, in all of the remaining 24 countries, businesses in default can expect to pay surcharges or penalties, most of which increase in relation to the delay incurred. However, there are considerable differences in the details to be observed.

Mandatory VAT registration differs from country to country but certain general tendencies can be deduced from the replies received. If a foreign company uses one of its permanent subsidiaries abroad to execute transactions in the country to which it is exporting, this company (or its subsidiary) generally needs to be registered. Conversely, this does not apply if the foreign company acts purely as an entity

exporting *goods* from abroad to the domestic customer; in this case, it is VAT exempt. Instead, the local fiscal authorities usually charge the importing company import sales tax.

The regulations are generally more complicated where applied to *services* supplied by foreign companies which do not have a subsidiary in the country in question. The conditions vary as to whether it is mandatory to pay VAT and thus be registered in that country. Lun Wang, a partner of Ecovis in Shanghai, gave the following answer, for example, for China as a whole. "Foreign companies which execute building projects or provide labour services here need to register with the corresponding local financial authorities within 30 days of the conclusion of a contract."

In New Zealand, any non resident business that carries on a taxable activity can register for GST (Goods and Services Tax) but can only claim a deduction for GST input if the taxable supply is made in New Zealand. Registration is mandatory if the turnover is more than NZ\$60,000 (roughly equivalent to 38,000 Euros). Under new legislation passed on the 1 April 2014 any non resident business who does not make taxable supplies in New Zealand can now register for GST and recover input tax incurred if they meet certain criteria. Wade Glass, a partner of Ecovis in Auckland, New Zealand's commercial capital, says that the new legislation provides economic equality for non resident businesses who no longer need to absorb the GST input.

In the Great Britain there are basically five different options:

- There is no mandatory registration for businesses supplying *trade customers* with goods, the reason being that such customers generally have to account for UK VAT on receipt of the goods under what is commonly known as the 'reverse charge' rules.
- If a supplier sends goods from another EU country to British *consumer customers*, the supplier only needs to be registered in the United Kingdom and pay VAT there if the turnover from those distance sales exceeds 70,000 GBP (roughly equivalent to 88,000 Euros).
- If a supplier sends goods from a non-EU country, the supplier may take responsibility for import duty and import VAT on behalf of the customer. If this does not occur, the customer will have to account for import duty and import VAT.
- If a foreign company sells and delivers goods to UK customers and makes the delivery from stocks kept in the country it will have to register and charge UK VAT on the sale.
- Where a foreign company without a business presence in the UK sells services to UK business customers there is generally no requirement to register for VAT as the customer will account for VAT under the 'reverse charge' rule. "However, there are special requirements for certain services," says Roger Morgan, head of the corporate tax department of ECOVIS Wingrave Yeats, in London.

Similar registration regulations relating to distance sales within the EU also apply in other EU member states, with various thresholds. In Cyprus, Italy, Latvia, Malta and Spain, it is 35,000 Euros, in Germany and France 100,000 Euros.

As in the United Kingdom foreign businesses without subsidiaries or permanent establishment are also exempt in other EU member states if they provide services and if the reverse charge principle applies to them, i. e. if their domestic customers are liable to VAT on such services. However, here too there are some exceptions where the foreign service supplier is obliged to pay the local VAT and therefore needs to be registered.

In every second country questioned, foreign businesses need to apply for registration as soon as they start to sell goods or services to local customers. In six of the 24 countries (25%) this is the case where a certain turnover threshold is exceeded. In six other countries either the one or the other principle is applied, depending on the nature of the transaction.

It is of interest to note that in two thirds of the countries even small businesses which exceed a certain turnover limit are VAT exempt. In many countries, however, this only applies to micro-enterprises which have their registered offices or a subsidiary in that country. The limits range from 7,000 Euros in Malta to the equivalent of 101,000 Euros in the United Kingdom. Many countries have higher turnover thresholds for supplies of goods than for services; for example, 82,200 Euros compared to 32,900 Euros in France and 75,000 compared to 35,000 Euros in Ireland.

VAT registration: formalities, times, penalties

In all the countries foreign businesses have to complete special registration forms. These have normally to be accompanied by the following evidence:

- VAT registration in the country where the company has its registered offices
- documents (for example an excerpt from the companies' register) proving that the person signing the application for VAT registration is entitled to do so as its manager or holds corresponding power of attorney
- a copy of the passport or ID card of the said representative
- and, in the case of companies, a copy of their articles of association

Information is also required about the nature of the business to be undertaken. In many countries, for example in France, Switzerland and the United Kingdom the financial authorities need an estimate of how high the foreign entity expects its monthly or annual turnover in their country to be. In Poland and the United Kingdom they also need to show that they have opened a bank account in the respective country.

As a general rule the documents to be produced need to have been translated into the language of the country in which the company is applying for VAT registration. Mexico and Uruguay also require certification by a notary in that country, too. Switzerland requires that foreign enterprises also appoint a local fiscal representative for the registration; in Poland and Cyprus, only enterprises from non-EU countries are obliged to do so, but in Cyprus it is possible to provide a guarantee instead. In contrast, in neighbouring Greece, the requirements for a VAT representative and local accounting according to Greek law were rescinded in May, 2013. "Foreign

businesses only need to apply for their VAT number and submit quarterly VAT reports,” says Panagiotis Vroustouris, Ecovis partner in Athens.

Another item of interest is that companies applying for registration in New Zealand are free to choose whether they wish to submit their VAT reports monthly, every two months or every six months, and on what basis they wish to determine the VAT (invoices, receipt of payments, or a mixture of both).

Depending on the country in question, initial registration can take between one and about 30 days to complete. The fastest, at one day after submission of the application complete with all requisite documentation, are the Japanese fiscal authorities. In Mexico too, according to information supplied by an Ecovis partner there, Ricardo Quibrera Saldaña, “It normally takes just one day once you have made an appointment and provided all the requirements are fulfilled.” In another six countries, registration is completed in one week at the most. At 30 days, the official procedure takes longest in Italy, Poland, Spain and the United Kingdom. “In Germany it depends on which financial authority is responsible,” says Ann-Christin Büscher, VAT expert with Ecovis, Düsseldorf, “but normally everything is tied up within one month.”

In most of the countries (20 of the 24), penalties are imposed for late application for registration. There are only four exceptions: Australia, Croatia, New Zealand and Poland.

However, the penalties charged vary widely. Cyprus and Argentina, for example, charge 85 Euros, respectively the equivalent of 50 Euros, for every month in default. In the United Kingdom there is a three-step time and percentage scale: 5% of the VAT due for notifications up to nine months after the application deadline, 10% for nine to 18 months late and 15% thereafter, but in all cases with a minimum penalty of 50 GBP.

In other countries there is a clear range of penalties imposed for late registration; in Luxembourg, for example, between 50 Euros and 5,000 Euros, in Mexico the equivalent of about 220 USD and 658 USD. In Ireland, on the other hand, the tax authorities are allowed to impose a uniform penalty of 4,000 Euros for late application, and in Japan it can be really expensive, ranging from 5% to 35% of the VAT owing.

What happens when VAT regulations are ignored: penalties per country

If businesses do not submit their VAT reports and returns punctually, they have to do penance in all 24 of the countries surveyed, albeit at different rates. Taken individually, most countries apply similar penalty structures to those imposed for late registration.

The most lenient tax authorities are to be found in Uruguay. Here the penalty for the late submission of VAT returns is the equivalent of just 10 Euros. New Zealand is satisfied with 50 NZ\$ on the basis of payment receipts and 250 NZ\$ on the basis of

accounts receivable and in hybrid cases. In Switzerland, in contrast, it lies with the fiscal authorities to decide whether a penalty should be imposed for late submission.

In Germany the financial authorities are entitled to impose a late charge of up to 10% of the VAT payable, with a maximum of 25,000 Euros. In France the penalty for the late submission of VAT reports is a uniform 10% of the VAT owing, and in Austria up to 10%. In the United Kingdom the penalty is between 5% and 15% of the VAT owing. Depending on the legal form and the company's list of transgressions for late filings, Greece can charge the defaulting company between 250 Euros and 30,000 Euros. In India, with its modest penalty of 500 rupees (the equivalent of 6 Euros), it is the interest payable on arrears at a rate of 15% p. a. (or a higher or lower rate of interest as determined by the government) which carries more weight.

The most drastic penalties are imposed by the Italian fiscal authorities for the late submission of VAT reports: the penalties range from 120% to 240% of the VAT withheld. Even if the tax return shows that no VAT is due, a fine of between 258 Euros and 2,065 Euros is still imposed for infringement of the deadline.

The financial authorities in the 24 countries questioned are also implacable in the case of late payment of any VAT due. Most of the countries impose at least corresponding interest on arrears or comparable penalties for late payment, and some countries also impose fines (in Luxembourg, for example, of between 50 Euros and 5,000 Euros, and in Latvia between 10% and 50% of the VAT owing).

In Germany the late payment penalty is 1% of the outstanding amount of VAT owing per month or part thereof. In New Zealand, a penalty of 1% of the VAT owing is due as early as the first day after the due date, with an additional 4% if the financial authorities still have unsettled receivables by the end of the seventh day, and 1% for every month delayed.

Switzerland calculates interest on arrears at a rate of 4% per year. In China the rate is 0.05% for every day in arrears, which is equivalent to 18% per year. If, however, the newly imposed payment deadline is ignored, the financial authorities can charge hefty fines of between 50% and 500% of the VAT owing.

Greece and Uruguay tighten the thumbscrews in stages, relative to how long a company takes to pay its VAT. In Uruguay, for example, the fine for payment delayed up to five days is 5% of the VAT owing, then 10% for delays between five and 90 days, and 20% thereafter.

Compared with its policy for late VAT returns, Italy is more lenient with delayed VAT payments, the fine being a uniform 30% of the VAT owing once a VAT report has been submitted. In both cases, however, the fines can be reduced if the tax offender pays any VAT due before a certain deadline. Nonetheless, should the unpaid VAT exceed 50,000 Euros, the matter is treated as a criminal offence.

There is a special feature in Poland, as explained by Marcin Milczarek, a lawyer and

partner of Ecovis in Warsaw. “Both missing the deadline for submission of a VAT return and making late payment are fiscal offences and as a rule it is not the financial authorities but a judge who decides on how high the fines should be.” However, in minor cases, if the circumstances of the offence are obvious and the taxpayer will accept the fine, the fiscal authorities may impose a fine that does not exceed the equivalent of 800 Euros (that is twice the minimum salary).

About Ecovis

Ecovis is a leading global consulting firm with its origins in Continental Europe. It has over 4,500 staff operating in 40 countries. Its consulting focus and core competencies lie in the areas of tax consultation, auditing, legal advice and accounting and management consulting services. The particular strength of Ecovis is the combination of personal advice at a local level with the general expertise of an international and interdisciplinary network of professionals. Every Ecovis office can rely on qualified specialists in its back offices as well as on the specific industrial or national know-how of all the Ecovis experts worldwide. This diversified expertise provides clients with effective support, especially in the fields of international transactions and investments - from preparation in the client's native country to support in the target country. In its consulting work Ecovis concentrates mainly on mid-sized firms. Both nationally and internationally- from preparation in the client's native country to support in the target country. In its consulting work Ecovis concentrates mainly on mid sized firms. Both nationally and internationally, its one-stop-shop concept ensures all-round support in legal, fiscal, managerial and administrative issues.

The name Ecovis, a combination of the terms economy and vision, express both its international character and its focus on the future and growth.

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