TAXE Committee and MNCs

The TAXE Committee gives multinationals 'one more chance' to turn up.

Back in June and July of this year, the European Parliament TAXE Special Committee called a wide range of multinational companies from Google and Facebook to HSBC and IKEA to appear at hearings to discuss their tax practices. Unlike the Public Account Committee in the UK, the TAXE Committee does not have the power to compel people to attend. So it comes as little surprise that many have chosen not to appear. In fact, only four of the 18 have faced the Committee, being Airbus, BNP Paribas, SSE and Total.

On 16 October, the Committee announced that it would give the remaining companies 'one more chance' to appear before them on 16 November. Committee chair Alain Lamassoure said: 'I hope that, this time, multinational companies will seize the opportunity to share their views with us on current developments in the corporate tax world.'

What is clear is that the Parliament is really riled by not having been able to question these companies.

Someone close to the Brussels debate has suggested to me that the recent BEPS announcements might make now the right time for these companies to come forward, 'blinking into the sunlight'. It is likely they would face some predictable questions. BEPS might provide some of the answers for them. Indeed, it could be the opportunity to diffuse some other challenges. Beyond the usual names on the list, companies like McDonalds are already facing tax challenges in France, Italy and possibly elsewhere, as well as being on the periphery of the state aid work by DG COMP. Perhaps the time has come to extract the thorn?

In reality, the hands of the TAXE Committee are quite firmly tied. They cannot force companies to appear, but have taken the step of writing to Martin Schulz, president of the European Parliament, calling on him to impose restrictions on those who refuse. This could include removing access to the European Parliament for them and their lobbyists. Although Schulz cast some doubt over whether such sanctions are within his power, he echoed the frustrations of the TAXE Committee.

It will be interesting to see whether those companies on the list choose to attend in November, and what the European Parliament's response might be if they choose not to. At a time when Brussels is setting out its stall in terms of BEPS adoption, and considering the impact on businesses, companies may think that now is the time to be at the table.

The TAXE committee was set up in the wake of Luxleaks to investigate tax rulings afforded to multinational companies. ■

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Sveda UAB and input tax recovery

In which 'Little Red Riding Hood' defeats the Lithuanian VAT Wolf.

The Lithuanian story of *Sveda UAB* (C-126/14) (reported at page 4) has a somewhat fairytale overtone. It starts with a commercial company which keeps a shop, deep in a dark wood. People travel to the shop, but the route is hard and wearisome. The company cannot afford improvements, but one fine day a government quango visits the shop and agrees to meet 90% of the company's cost, in order to create a delightful woodland pathway – all the better to let people visit it.

Brimming with gratitude, the company spends the money, reclaims all the VAT on the entire budget, and invites everyone to visit the shop. Of course, there are many visitors who, so enchanted with the path, stay on it, and never enter the shop. But both the company and the quango are happy with this, since the people benefit, and the shop sales increase to some extent.

Along came the Lithuanian VAT Wolf. It tried to eat up all of the input tax. It said the people did not pay to use the lovely new path, so there was no direct link to the supplies in the woodland shop. It said that the company had not born the cost, except for 10%, so it should not reclaim all of the VAT. It ate up all the VAT, and lay down to sleep, licking its lips.

The company ran to the CJEU to get help. The CJEU had to decide whether the Wolf was right that the costs related to something that was simply given away, and had insufficient connection with the shop; or right that the company had not born the true economic cost so could not reclaim the VAT. The company faced up to the Wolf. The Wolf called on his friend, HMRC, to help defeat the company in this trial of strength.

The CJEU decided that the VAT was all recoverable. It did not matter that the company did not charge the people for using the path, or that a direct purpose of the cost was to create a free-to-use facility. The fact that it also created better access to the shop meant the cost was directly and immediately linked to the sales from that shop. The question of how the money had been found to afford the improvement was irrelevant. All of the VAT initially claimed on this basis could be kept by the company as long as it continued to use the facility in connection with the shop, irrespective of whether free access was allowed to the public.

The Lithuanian VAT Wolf was slain, along with its friend, HMRC. And everyone lived (walked, and shopped) happily ever after.

And, in very real terms, this story has a happy ending for businesses and for charities. For some time, HMRC has tried to press forward with an ungenerous theory whereby input tax recovery should be directly referable to the commercial success achieved (or intended to be achieved) from the costs incurred. This has threatened to disturb the neutrality of the tax. The CJEU has reasserted the point that, as long as there is a sufficient link with the making of taxable supplies, the fact that there is a further ancillary benefit which was not necessarily paid for does not invalidate full input tax recovery. HMRC's restless search to disallow VAT on costs which they believe have benefited non-commercial activities, despite having a clear link with taxable supplies, should now be regarded as having reached its end. ■

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Tax credits: possible consequences

Has the tax credits defeat left the tax system vulnerable?.

George Osborne has been dealt a hefty blow this week after peers voted against a decision by government to make major changes to the tax credits system. Mr Osborne has said he will now review his decision, but has made it very clear he will press ahead with changes that will save billions in welfare payments.

So what's the chancellor to do next?

Firstly, let's make one thing clear. It's very likely that tax credit changes will be enforced at some later stage, but probably later than scheduled and with less severity. But with one month to go before a spending review that could have complemented his Budget last July, he has just a few weeks to plug the shortfall and prevent his austerity plans derailing.

There is a possibility that he will change the way they are introduced by ensuring that the restriction only applies to new claimants, but this will result in a shortfall in closing the deficit gap. We can also be fairly certain that he won't want to increase borrowing, and it's unlikely he will be able to raise any of the income tax rates because of the triple lock. I also don't think he'll use the proposed new high corporation tax rate on interest supplement to plug the gap either, as that exists to reduce the outflow of public funds in the form of interest payments

More worryingly, it's possible that the chancellor may now look to use the tax system to do exactly this. Some of the options he may be exploring could include:

- tinkering with the starting point of income tax rates;
- aligning NICs and income tax which could mean and extra £300 a year in the pocket of someone at the lower end of the pay scale, potentially paving the way for the inevitable changes to tax credits at a slightly later date;
- delaying the increase to personal allowances;
- increases to CGT;
- delays to the IHT enhancement to main residence (less likely I think as it is a key Conservative pledge). But increasing the 45% rate to 50% looks unlikely as this is unlikely to be sufficient.
- delaying the reduction in the corporation tax;
- a greater focus on tax avoidance and evasion.

It's likely that if there are any tax increases then they'll be introduced next month, which is going to make for an interesting Autumn statement. ■

George Bull, RSM (Weekly Tax Brief)

EU reduced VAT rates review

The European Commission has a change of heart on reduced VAT rates.

The EC is planning to allow member states more freedom to set their reduced VAT rates for various goods. This was announced on 27 October 2015 as part of the EC's 2016 Work Programme.

The review is backed by EC President Jean-Claude Junker. It will include an assessment of the impact of reduced VAT rates on new technologies, including e-books, and will commence in 2016.

EC U-turn on VAT rates: The review represents a reversal of the position of the EC on reduced VAT rates. Since as recently as 2013, the EC had been calling for a full withdrawal of the use of reduced VAT rates based on them being a distortion of the single market for goods and services.

Currently, the 28 member states are free to set their standard VAT rates with the single proviso that they are above 15%. The current lowest rate is 17% in Luxembourg. The highest rate is 27% in Hungary. Under the EU VAT Directive, article 98, Directive 2006/112/EC, countries may have one or two reduced VAT rates, the lowest of which must be 5% or above. Member states can only use the reduced VAT rates for the goods and services in an exhaustive list in Annex III of the Directive.

E-book VAT rates challenges: This has created friction recently between the member states. The EC was forced into referring France and Luxembourg to the CJEU in March over their use of the reduced VAT rates on e-books – printed books currently are listed in Annex III. The CJEU ruled that e-books were a service, and not a good like printed books, and so could not enjoy reduced rate. This forced France and Luxembourg to raise VAT on e-books from their reduced rates (5.5% and 3%, respectively) to their standard VAT rates (20% and 17%, respectively).

Other countries such as Germany, Italy and Poland subsequently backed France and Luxembourg in their view that this breached the EU concept of fiscal neutrality, which requires that EU tax rules do not distort the operation of the single market.

On October 20 2015, Poland challenged the e-book vat rate ruling at the CJEU.

Differences on VAT rate derogations: In addition to the Annex III rules, new member states used to be able to gain the right to apply the reduced rates on any goods that were already in place prior to accession to the EU. This has meant countries like the UK have a very long list of goods at nil rates, including food and children's clothing. However this loophole was withdrawn over ten years ago. This meant, for example, that Poland had to hike its reduced VAT rate on children's clothing to its standard rate of 23% following a CJEU ruling in 2008.

The EC had a similar 'victory' against Spain over the use of the reduced VAT rate on medical goods. It also blocked the UK applying 5% reduced VAT on energy saving products in June 2015.

In a number of states, the issue of nil rating of women's tampons has been hotly debated in recent weeks. Member states have limited powers to cut their rates without majority backing of all other member states. ■

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