

# VAT Newsletter

Important VAT, GST and  
sales tax news from around  
the world

Issue No. 8, October 2015

## Introduction

Welcome to the eighth issue of Ernst & Young LLP's 2015 *VAT Newsletter* for the US and Canada. These newsletters cover a variety of topics, as valued added tax (VAT) can impact businesses in many ways. Approximately 160 countries now have a VAT, goods and services tax (GST), consumption tax, service tax or similar VAT, and the laws and regulations are constantly changing. We use this newsletter to inform you of significant changes taking place.

At the end of this newsletter, you will find contact details for the senior members of our teams in the US and Canada who can help answer any questions you may have about the articles in this newsletter or any other VAT questions.

We are interested in your feedback on the items covered and what topics you would like to see covered in the future. Please provide any feedback to Howard Lambert at [howard.lambert@ey.com](mailto:howard.lambert@ey.com).

If you would like to subscribe to EY's other Indirect Tax updates, please click [here](#).



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EY's *Indirect Tax Briefing*, 12th Edition

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## Global

EY's *2015 Worldwide VAT, GST and Sales Tax Guide*

You can access the latest guide [here](#).

EY's *Indirect Tax Briefing*, 12th edition

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*Managing indirect tax controversy: dealing with audits and disputes*

*Managing indirect tax controversy* is our new Global Indirect Tax thought leadership report, providing insights into how companies can anticipate and deal effectively with tax audits and resolve disagreements with tax administrations. You can access the report [here](#).



## Americas

### Bahamas – VAT position of overseas insurance companies providing services in the Bahamas

As of 1 July 2015, only life insurance and insurance-based annuities and savings plans will remain exempt from VAT (up to that date insurance will remain generally exempt). Effective 1 July 2015, VAT will become chargeable on non-life insurance services at the standard rate of 7.5% (in a local-to-local context) or 0% (in a local-to-non-resident context). Based on Ministry of Finance communications so far, the general understanding has been that insurers without local physical operating presence should not be required to register and charge VAT, even in respect to services falling within the VATable scope as of 1 July (e.g., Bahamian property, motor or liability insurance). Based on the latest Ministry of Finance communications, however, we understand that insurers without local physical presence were also required to register for VAT by 1 July 2015, especially those holding a local insurance license and generating premium over US\$100k/year on Bahamian non-life policies. Therefore, it seems that the Ministry of Finance is diverting from its previous guidelines regarding residency considerations and this shift in their interpretation may require swift reaction from the affected insurance companies.

### Canada – Newfoundland and Labrador introduce transitional rules and new rebate for HST increase of 2%

#### Executive summary

In his fiscal 2015-16 provincial budget released on 30 April 2015, Newfoundland and Labrador Finance Minister and President of Treasury Board Ross Wiseman announced a 2% increase in the provincial component of the harmonized sales tax (HST) from 8% to 10%, effective 1 January 2016. The new combined HST in the province will be 15%.

The province recently released a notice, *Transitional Rules for the Newfoundland and Labrador HST Rate Increase*, outlining transitional rules in respect of the rate change.

The Minister also announced certain measures to mitigate the effect of the HST rate increase in the budget.

#### Detailed discussion

##### Transitional rules

Transitional rules are required to determine whether the existing Newfoundland and Labrador HST rate of 13%, or the new rate of 15%, will apply to transactions that straddle the 1 January 2016 implementation date. These rules apply to transactions that, for purposes of the Excise Tax Act, would be considered to be taxable supplies made in Newfoundland and Labrador.

Similar transitional rules were introduced when the federal GST rate was reduced from 7% to 6%, effective 1 July 2006, and

further reduced to 5%, effective 1 January 2008 (accompanied by corresponding decreases in the HST rate – from 15% to 14% to 13%, respectively) and when Nova Scotia increased the provincial component of the HST by 2% in 2010. These rules are necessary to ensure equity for transactions straddling the effective date.

The transitional rules generally operate on the basis of the earlier of when consideration for a supply becomes due and when it is paid without having become due.

Under the **Excise Tax Act**, consideration for a supply generally becomes due on the earliest of the following:

- ▶ The day the supplier first issues the invoice
- ▶ The date of the invoice
- ▶ The day on which the invoice would have been issued if not for a delay
- ▶ The date on which the amount becomes due under an agreement in writing

#### **How the transitional rules will apply**

The transitional rules are dependent upon the nature of the supply, as outlined below.

**Sale of goods:** HST will apply at the rate of 15% on goods, including subscriptions to periodical publications, where consideration is due without having been paid, or is paid without having become due, on or after 1 January 2016. The 13% rate will apply where consideration is due, or is paid before 1 January 2016. Thus, if a business invoices a customer, or receives a payment before 1 January 2016 for the sale of goods, HST would be collected at the rate of 13%.

If, instead, the business issues the invoice on or after 1 January 2016 for the same sale, the 15% HST rate would apply unless payment is made before 1 January 2016. Also, if the business receives payment on or after 1 January 2016, the 15% HST rate would apply unless the invoice is issued before 1 January 2016.

**Services:** Where consideration for a supply of services becomes due without having been paid, or is paid without having become due, on or after 1 January 2016, HST will apply at the rate of 15%. The 13% rate will apply to any consideration for a supply of services that becomes due or is paid before 1 January 2016.

For example, in January 2016, a person is invoiced for unpaid maintenance services, which are performed between 22 December 2015 and 10 January 2016. The HST rate of 15% would apply to the invoiced amount. If the person had been invoiced or had paid for the same services on 22 December 2015, the 13% rate would have applied.

Unlike the transitional rules that applied in Nova Scotia when the province increased the provincial component of the HST by 2% in 2010, the moment when the services are performed will have no impact upon the determination of the HST rate. Also, there are no special transitional rules applicable to funeral and cemetery services, passenger transportation services and freight transportation services.

**Leases and licenses:** Where consideration for a supply of property (including goods, intangible personal property and real property) by way of lease, license or similar arrangement becomes due without having been paid, or is paid without having become due, on or after 1 January 2016, HST will apply at the rate of 15%. The HST rate of 13% will apply to any consideration that becomes due, or is paid before 1 January 2016.

For example, on 10 December 2015, a person makes a car lease payment for a lease interval that runs from 10 December 2015 to 9 January 2016. The HST rate of 13% would apply to that lease payment. The HST rate of 15% would apply to the lease payment that becomes due on 10 January 2016, unless the lease payment is made before 1 January 2016.

**Intangibles:** HST will apply at the rate of 15% to any consideration that becomes due without having been paid, or is paid without having become due, on or after 1 January 2016 for a supply of intangible personal property (e.g., intellectual property or contractual rights) by way of sale which includes memberships (including lifetime memberships), admissions and passenger transportation passes.

For example, on 28 November 2015, a vendor sells tickets to a concert that will take place in April 2016. The HST rate of 13% would apply to the payment for the tickets.

There are no special transitional rules for lifetime memberships, or passenger transportation passes, as was the case in the transitional rules applicable in Nova Scotia when the province increased the provincial component of the HST by 2% in 2010.

**Sales of real property:** HST will generally apply at the rate of 15% to a supply of real property by way of sale (including sales of newly constructed or substantially renovated housing) in Newfoundland and Labrador, if both ownership and possession of the property are transferred to the purchaser on or after 1 January 2016. The HST rate of 13% would apply to a supply of real property by way of sale, if either ownership or possession of the property is transferred to the purchaser before 1 January 2016.

For example, in July 2015, a land developer enters into an agreement to sell a small commercial mall to an individual. Ownership and possession of the mall will transfer to the individual in February 2016. The HST rate of 15% would apply to the payments for the purchase of the mall.

If certain conditions are met, the supply of new homes under written agreements entered into on or before 15 July 2015 will be grandfathered and the 13% rate will apply even if the ownership and possession of the property is transferred on or after 1 January 2016. Grandfathering would generally not apply to traditional apartment buildings and deemed taxable supplies of real property by way of sale.

Specific disclosure rules apply to builders who enter into written agreements for the supply of newly constructed, or substantially renovated homes (e.g., a single-unit home, or residential condominium unit) after 15 July 2015 and before 1 January 2016. In summary, if ownership and possession of the property transfer on or after 1 January 2016 and the builders do not disclose in the written

agreement the fact, *inter alia*, that the increased tax rate of 15% will apply to the sale of the property, the builders can be liable for the uncollected additional amount of HST.

### Other transitional rules

The notice outlines special transitional rules for the following:

- ▶ Returns and exchanges
- ▶ Property and services brought into Newfoundland and Labrador
- ▶ Imported goods
- ▶ Imported taxable supplies
- ▶ Financial institutions
- ▶ Pension plans
- ▶ Taxable benefits, passenger vehicles and aircraft
- ▶ Streamlined accounting methods

### Other rebates and credits

Effective 1 January 2016, Newfoundland and Labrador will provide a 25% rebate on the provincial component of the HST for eligible purchases made and eligible expenses incurred by municipalities and local service districts. Effective 1 January 2017, the rebate will be increased to 57.14%. The notice provides transitional rules for the municipal rebate amendments.

Also, the HST credit will be enhanced beginning with the October 2016 payment.

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## Costa Rica – Government submits to Congress two bills to replace the Income Tax Law and substitute the current Sales Tax Law with VAT

### Executive summary

On 10 August 2015, the Costa Rican Executive Branch sent two significant bills to Congress, one of which is to substitute the existing Sales Tax Law with a Value Added Tax Law (the VAT Law). The bills are, to a large extent, based on drafts submitted by the Tax Authorities earlier this year for public comment.

The VAT Law will tax services that are currently not taxed under the Sales Tax Law.

### Detailed discussion

#### The VAT Law

The current Sales Tax Law would be repealed and replaced by the VAT Law.

According to the background section of the VAT Law, the Government intends to tax the most dynamic sector of the Costa Rican economy (i.e., services), which is, for the most part, not affected by sales tax under the current system.

Under the proposed VAT Law, services would generally be taxable, and only a certain amount of goods and services would be exempted.

The key features of the VAT Law include the following:

- ▶ VAT would generally apply to the sale of goods and the supply of all types of services within Costa Rica, as opposed to a very limited number of services under the current sales tax system.
- ▶ The recovery of input tax, i.e., VAT charged on goods and services supplied to the taxpayer for business purposes, would be regulated by a new set of rules.
- ▶ The VAT rate would gradually increase from the current 13% to 14% for the first year following the entry into force of the VAT Law, and to 15% for the second and subsequent years.

- ▶ A reduced rate of 5% would apply to certain items, including: (1) the purchase of packing materials, as well as raw materials used in the production of packing materials, (2) services used in the production of agricultural or agro-industrial products and (3) plane tickets for flights initiating in Costa Rica (domestic or international).
- ▶ Exemptions from VAT include: (1) certain basic foods listed in the VAT Law; (2) exported goods; (3) commissions and interest derived from loans and financings granted by entities regulated, or supervised, by certain local public authorities (e.g., SUGEF), or the stock market regulator; (4) rental income for real estate exclusively used for housing, provided that the monthly rent does not exceed a base salary; (5) private education services; and (6) self-consumption of electric power produced from solar panels.
- ▶ The transfer of all of the taxpayer's assets, or one, or several lines of its business, by means of a corporate reorganization, a stock purchase, an in-kind contribution, a merger or a bulk sale would not be subject to VAT when the transferee continues the activities of the transferor.





## Asia-Pacific

### Australia – Levying of GST on electronic services purchased from abroad and low-value imported goods

The Australian tax authorities have announced that the *de minimis* threshold below which GST does not have to be paid on goods imported into Australia will be reduced from the current level of AU\$1,000 to AU\$0 with effect from 1 July 2017 (i.e., the threshold will be eliminated). Accordingly, all goods imported into Australia on or after 1 July 2017 will be subject to GST. The mechanism for levying and collecting the GST remains unclear at present, but this may involve overseas businesses registering for Australian GST. It is also proposed that the supply of electronic services by an overseas business to Australian consumers (i.e., B2C supplies) will be subject to GST from 1 July 2017.

### New Zealand – Consultation: Levying of GST on electronic services purchased from abroad and low-value imported goods

The New Zealand Inland Revenue has published a consultation document seeking views on proposed new rules that would apply GST to cross-border supplies of electronic services. The proposed rules would require offshore suppliers to register and account for GST when they supply electronic services to New Zealand resident consumers.

The paper also contains some discussion on the collection of GST on low-value imported goods but does not, at this time, propose extending any registration system to offshore suppliers of low-value goods. It does, however, acknowledge the issue around the *de minimis* threshold under which GST does not have to be paid on imported goods and the wider issue of the cost of collecting GST on low-value imported goods. Submissions are sought on both the electronic services proposals, and on the collection of GST on low-value imported goods. The consultation ran until 25 September 2015. The consultation document can be accessed by clicking [here](#).



## Europe

### Court of Justice of the European Union Judgment – Potential VAT implications for intermediary arrangements

On 3 September 2015, the Court of Justice of the European Union (CJEU) released its judgment in the Lithuanian case of *Fast Bunkering Klaipėda UAB (FBK) (C-526/13)*. The case concerns the application of the exemption (zero-rating in the UK) of fuel for ocean-going vessels.

During the case, the Lithuanian tax authority argued that only the final supply, in a chain of intermediaries acting in their own name, but on behalf of a third party, to the ship owner/operator qualified for the VAT exemption. However, the CJEU decision confirms that since FBK delivered fuel directly into the vessel's tanks and the value of the supply could not be known until the fuel was delivered to the ship, the exemption may apply even though FBK's supply was to an intermediary and not the ship owner/operator. Nevertheless, the exemption would only apply if the transfer of title to the intermediary took place either at the same time, or after the operators of ocean-going vessels were entitled to dispose of those goods as owner and not before.

### Implications

Even though the judgment deals with the exemption of fuel supplies to ships, viewed more broadly, the judgment could have significant implications for supply chains where an intermediary does not, in practice, acquire the right to dispose of the goods as owner. This could apply to certain call off and consignment arrangements, to commissionaire structures and principal structures, particularly where flash title arrangements occur. It could also apply to existing and new limited risk distributor structures and procurement structures. This ruling is something that should be understood by anyone looking to implement a new supply chain.

The full implications of the judgment will depend on how the tax authorities implement it in practice. However, businesses involved in intermediary supply chains, or using simplifications such as call off stock may wish to consider the implications of the judgment further.

## European Commission – “Destination Study” Final Report

The European e-commission has now published EY’s Final Report “Implementing the ‘destination principle’ to intra-EU B2B supplies of goods; Feasibility and economic evaluation study.” The report is available [here](#).

## Latvia – Referral to the European Court of Justice: the cost sharing exemption and transfer pricing

A recent Latvian referral to the European Court of Justice (CJEU) relates to the interaction between the cost-sharing exemption of article 132(1)(f) of Directive 2006/112 and the requirement for mark-ups on certain intra-group allocations as a result of transfer pricing policies. While the full details of the referral have not been published, the issue is whether such mark ups can bar the application of the cost-sharing exemption.

### VAT cost-sharing exemption

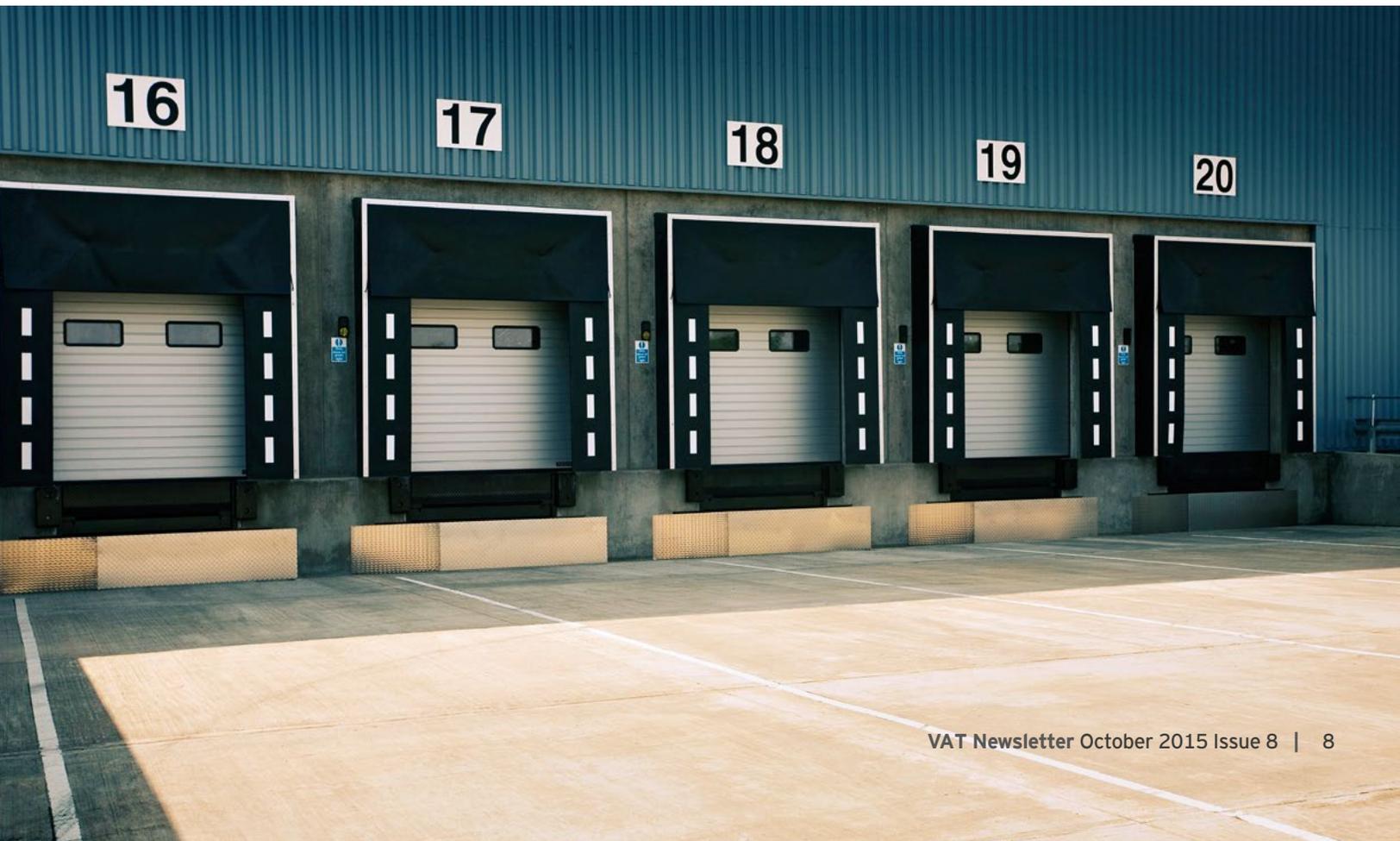
The VAT cost-sharing exemption applies when two or more organizations (whether business or otherwise) with exempt and/or non-business activities join together on a co-operative basis to form a separate, independent entity – a cost-sharing group (CSG) – to supply themselves with certain qualifying services at cost and exempt from VAT.

## The issue

For the exemption to apply, the consideration for supplies made by the CSG to its members has to be an “exact reimbursement” of the members’ share of the joint expenses (i.e., no margin or mark-up can be factored into the cost of providing the services). Transfer pricing allocations, by their nature, include a certain mark up. Therefore, the question remains whether this mark-up results on one of the fundamental conditions of the cost sharing exemption not being met.

## Implications in practice

For VAT purposes, transfer pricing allocations need to be assessed on a case-by-case basis, based on the specific facts and circumstances, to determine whether or not they fall within the scope of VAT. If they do and allocations are subject to VAT, group entities with a limited, or zero, VAT recovery right are faced with increased costs in the form of irrecoverable VAT. In these cases, the cost sharing exemption can be an interesting solution. However, the cost sharing exemption is only applicable to the extent that there is no mark-up on the allocations. The judgment of the CJEU will hopefully bring more clarity on the applicability of the cost sharing exemption in such cases.





## Middle East, India and Africa

### Egypt – Proposed introduction of VAT now in doubt

Egypt previously announced that it was planning to replace the country's existing general sales tax regime with a full VAT system. However, the EY member firm's Cairo office reports that the proposed introduction of VAT is now in doubt. Specifically, Egypt is now considering making various amendments/additions to the existing sales tax law, instead of introducing a VAT. However, no official announcement has been made to date in this regard.

### Israel – Reduction in the standard rate of VAT

With effect from 1 October 2015, the standard rate of VAT in Israel was reduced from 18% to 17%. No further changes have been announced.



## EY newsletters and alerts

If you would like a copy of a green paper, newsletter or alerts covering some of the topics mentioned below, please click on the link or contact Howard Lambert at [howard.lambert@ey.com](mailto:howard.lambert@ey.com).

**Canada:** *Tax Matters* – September 2015: The September issue of Canada's *TaxMatters@EY* is now available. From an indirect tax perspective, this issue includes an item regarding a recent Tax Court of Canada decision on a carousel scheme involving unremitted GST.

**Czech Republic:** Ernst & Young s.r.o. has recently issued the July 2015 edition of its regular client newsletter. From an indirect tax perspective, this edition includes the following items:

- ▶ Excise duty VAT amendments
- ▶ Latest VAT news – expansion of reverse change regime, real estate, VAT groups and the VAT control report
- ▶ Challenging right to deduct or effort to secure unpaid VAT in cases of alleged carousel fraud

**Latvia:** SIA Ernst & Young Baltic has issued the June/July 2015 edition of its regular client newsletter. This edition includes an item regarding excise duty changes.

**Latvia:** *EY Tax Newsletter* – August 2015: SIA Ernst & Young Baltic has issued the August 2015 edition of its regular client newsletter. This edition includes details on the following items:

- ▶ Amendments to the procedure for calculating and paying Natural Resource Tax, issuing authorizations to use natural resources and auditing management systems.
- ▶ Draft amendments on natural gas turnover and the procedure for applying excise duty.
- ▶ Amendments to the law on taxes and fees

**Romania:** *Standard VAT rate to be reduced:* Ernst & Young S.r.l. has advised that the standard VAT rate will be reduced from 24% to 20% from 1 January 2016 VAT rate and then to 19% from 1 January 2017.

**UK:** *EY VAT News* – Weeks of 27 July 2015; 5 August 2015; 10 August 2015; 24 August 2015; 31 August 2015; and 7 September 2015.

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ED None

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