The EU's New E-Commerce VAT Regime

by Peter Boerhof

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In this article, the author considers how e-commerce vendors and marketplaces will be affected by the VAT rules for e-commerce in the EU that take effect July 1.

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Change is coming to the EU's e-commerce tax rules, and businesses that don't understand the new regulations will almost certainly end up running afoul of the compliance regime. Unfortunately, the changing regime is based on complex EU rules consisting of several directives and implementation regulations that must be read together, and many of the rules still need to be transposed into the national legislation of the EU countries. The changes will potentially impact everything from how VAT is calculated and reported across the EU to the data that a vendor or marketplace must collect in the course of a transaction. It is important to stress that these changes only apply to business-to-consumer (B2C) sales and not business-to-business transactions.

This article focuses on how the new rules will affect e-commerce vendors and marketplaces with the goal of helping them prepare for the July 1 effective date. After discussing some of the reasons why the changes are needed, the article looks at some common situations and discusses how the new regime will change the status quo.

Why Do the Rules Need to Change?

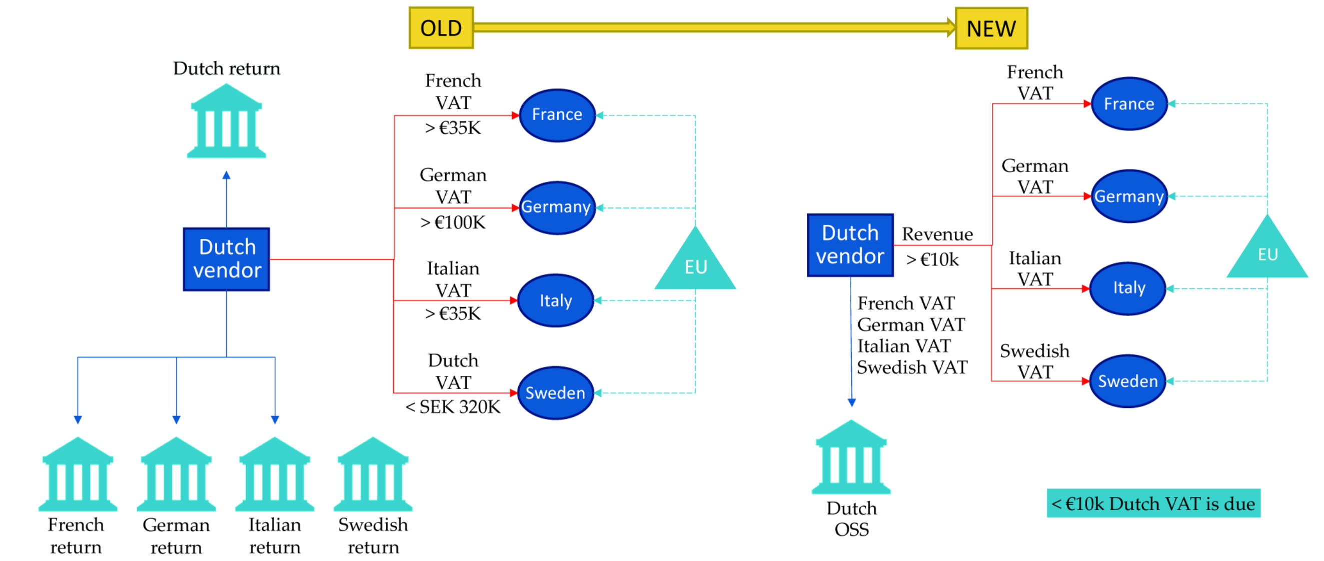
The e-commerce VAT rules need to change for several reasons, but ultimately they need to change because the market has changed.

The first reason for the changes is to address distorted competition with non-EU vendors. As consumers, most people know that they can buy low-priced products online from China and save money compared with a local brick-and-mortar shop or even an online EU vendor. One of the key reasons those products are more affordable is that VAT and import duties do not apply because there is an import exemption for goods with a value of €22 or less. In contrast, EU vendors must collect VAT when they sell the same products. The new regulations are meant to create a level playing field that allows them to compete with non-EU vendors.

The second reason for the new regime is to create a level playing field within the EU. If, for example, a Danish consumer buys a book in the local brick-and-mortar bookstore, the price of the book will include the 25 percent Danish VAT. If the same consumer buys the same book online through a small web shop in Ireland, there will be no VAT collected. Because VAT rates differ across the EU, you could buy the same item in person at 25 percent VAT, 15 percent VAT, or even without VAT. This distortion is caused by the fact that brick-and-mortar shops always charge local VAT. In contrast, e-commerce vendors from other EU countries only apply the VAT of the country of destination if their sales to that country exceed the distance sales threshold of €100,000 (or €35,000 for some countries). If the distance sales threshold is not exceeded, the EU e-commerce vendor would charge its own residence country's VAT.

And finally, changes are introduced to reduce the VAT compliance burden for larger EU e-commerce sellers that often exceed the €100,000 (or again €35,000) threshold in multiple EU states.

Figure 1. B2C Sales Within the EU



Under the existing rules, those companies must register and report VAT in each EU country where the distance sales threshold is exceeded.

Notably, under the new rules, even smaller e-commerce vendors will need to report VAT in multiple EU countries. To avoid a significant increase in the overall compliance burden for e-commerce vendors, the new regime introduces a one-stop-shop (OSS) VAT return. Using this special return, all EU VAT on distance sales can be reported to the seller's home country tax authority, which will distribute the VAT to other EU countries.

B2C Sales of Goods Within the EU

The first area of focus is sales to final consumers of goods that are already in free circulation in the EU. For these transactions, the first goal is to neutralize the differences in VAT treatment between cross-border sales and domestic sales. This is done by ensuring that the VAT of the country of destination is almost always applied when a final consumer buys from a foreign vendor. This can be accomplished by abolishing the existing distance sales threshold of €100,000 or €35,000. Indeed, this is almost always accomplished by the new regime; small vendors that incidentally sell cross-border and do not generate annual revenue of more than €10,000 from cross-border sales within the EU can still apply the VAT of their home country.

Because these rules mean a large increase in the number of vendors that must collect VAT in their customers' countries, the regime will ensure that VAT for all EU countries can be reported using a single OSS return in the vendor's country of establishment. A vendor reports all VAT on distance sales to the various EU countries on this OSS return and files it using the VAT filing platform of its home country tax authority. The local tax authority distributes the revenues to the various EU countries for which VAT was reported.

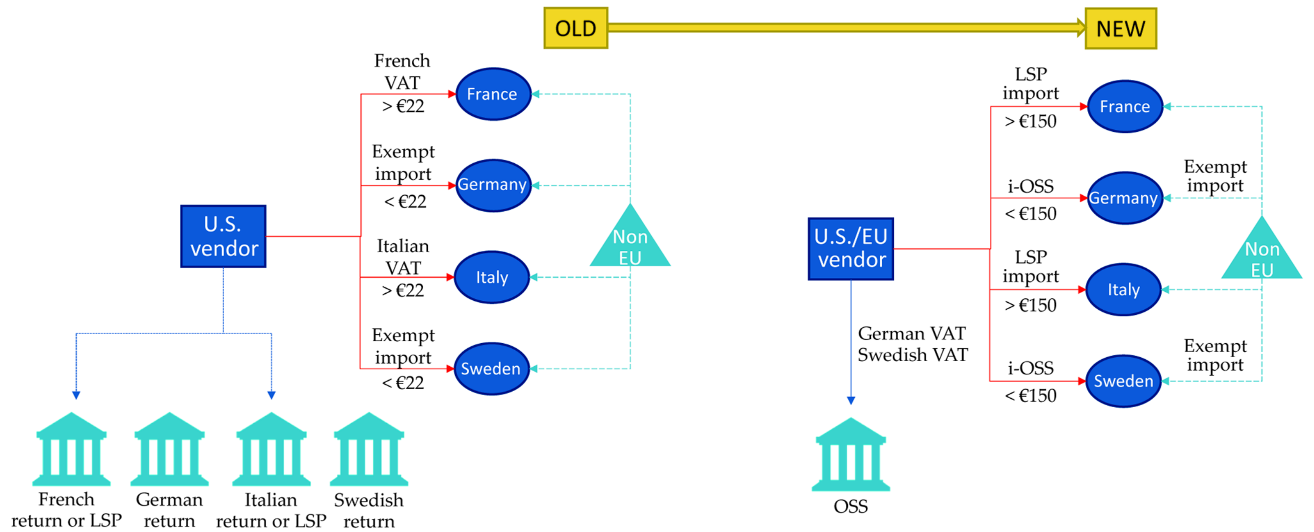
Existing Rules

An example can help reveal the practicalities of both the existing and new rules.

Consider a Dutch vendor selling to final consumers in France, Germany, Italy, and Sweden. The sales to Germany exceed the distance sales threshold of €100,000, so German VAT must be reported on those sales. France and Italy apply a lower distance sales threshold of €35,000, and the Dutch company's sales exceed that threshold in both countries. Thus, French and Italian VAT must be reported too. Only in Sweden do the sales stay below the local distance sales threshold.

Therefore, under the existing regime, the Dutch vendor must register for VAT in France, Germany, and Italy and file local VAT returns with those countries. This also means having to

Figure 2. B2C Sales of Imported Goods



communicate in the local languages and potentially be audited in each country, both of which can be quite challenging. For the sales to Swedish consumers, the vendor must apply and report Dutch VAT.

New Rules

Under the new rules, the position of the Dutch vendor will change. The vendor has an overall revenue of more than €10,000 for cross-border sales to final consumers in the EU. Therefore, it will need to calculate and report French, German, Italian, and Swedish VAT, but this will all be done using an OSS return filed in the Netherlands.

Some Considerations

Vendors will need to assess their supplies at an early stage to prepare for the transition. Under the new rules, the vendor in this example will also need to calculate Swedish VAT — something it does not do now. Not only does this need to be embedded in the enterprise resource planning platform, but the vendor may need to consider pricing because the VAT in Sweden is 4 percent higher.

The OSS return can only be used to report VAT on sales; VAT on purchases cannot be reported on this return. If the Dutch vendor incurred input VAT on the cost of renting a warehouse in Germany, it could choose to maintain its German VAT registration and file local VAT returns in Germany. In this example, he would probably be obliged to keep the local registration if he shipped goods to his German customers from the German warehouse because those sales would no longer qualify as distance sales.

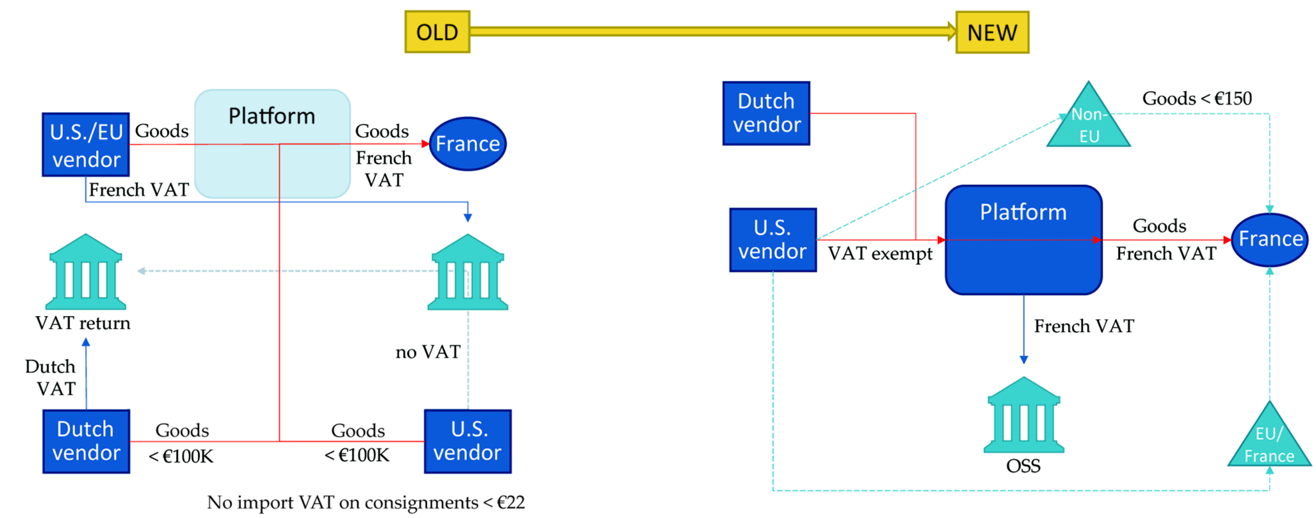
Many vendors that stayed below the per-country thresholds of €100,000 or €35,000 under the existing rules are likely to exceed the EU-wide €10,000 threshold. As a result, they will need to understand the taxability of all products they sell across the EU and calculate the VAT that applies in the countries of destination. This can become quite complicated because taxability and VAT rates for the same goods often differ in different states. For example, the VAT on bicycles is 5 percent in Malta, 12 percent in Sweden, and 25 percent in Denmark. Children's clothes incur 25 percent VAT in Sweden, but they are zero-rated in Ireland.

B2C Sales of Imported Goods

New rules will also apply for goods coming from outside the EU. Low-value parcels (that is, those with a value below €22) will no longer be exempt from import VAT, and a new €150 threshold will be introduced.

For goods with a value of over €150, standard import rules will apply. In general, the courier or postal company will pay the import duties and import VAT at the time of importation. Depending on what the parties have agreed to,

Figure 3. Marketplaces Become Deemed Sellers for VAT



the duties and import VAT may be charged onward to either the online vendor or the final consumer.

For goods with an intrinsic value that does not exceed €150, the new regime will introduce a special import one-stop-shop (i-OSS). The import will be exempt from VAT, and the VAT of the country of destination will be due. The i-OSS requires a special registration, and the registration number should be used during importation to benefit from the exemption. If the i-OSS is not used, then the import VAT will be collected by the courier or postal company.

Existing Rules

For this discussion, consider a U.S.-based vendor that sells into France, Germany, Italy, and Sweden. The goods shipped to France and Italy have a value exceeding €22, which means that import VAT is owed under the existing rule. The value of the products sold to German and Swedish customers does not exceed €22; therefore, those goods are exempt from VAT under the existing rules.

New Rules

Under the new rules, the vendor will need to monitor whether the value of the goods is above or below €150.

For the hypothetical U.S. vendor, the products shipped to French and Italian customers have a value exceeding €150, so import VAT will be collected by the courier or postal company. The products sold to Germany and Sweden, however, have a value not exceeding €150. If the U.S. vendor is registered for the i-OSS, those imports are VAT exempt, and German and Swedish VAT will need to be reported. If the U.S. vendor is not registered for the i-OSS, the courier or postal company will need to collect the VAT.

Some Considerations

These new rules are not limited to vendors established outside the EU; they also apply to EU vendors selling goods that are shipped from outside the EU directly to their customers. Thus, the physical flow of the products is the key, not the vendor's place of establishment.

It is clear that couriers and postal companies will have to perform a lot more activities under the new rules. This raises the question: Who is going to pay for this?

There are also some points that are not clear. For example, suppose products are imported into the Netherlands without applying the i-OSS and directly shipped to a consumer in Germany. This could trigger a regular distance sale from the EU country of import (the Netherlands) to the country of destination (Germany).

Multi-Seller Platforms as Deemed Sellers

The last significant area of change involves multi-seller platforms or marketplaces that facilitate the sales to final consumers in the EU.

Under the existing VAT rules, they only facilitate transactions — they are not involved in the actual transactions. Under the new rules, multi-seller platforms and marketplaces will be deemed sellers for VAT and will need to collect the VAT due in the countries of destination.

This rule only applies to imported goods with a maximum value of €150 and to sales by non-EU vendors to EU consumers. Other transactions that are facilitated by a multi-seller platform or marketplace will still trigger a VAT liability for the original vendor. Under the new rules, distance sales within the EU by an EU vendor that ships the goods from an EU location to an EU final consumer will be reported by the vendor in his OSS return, regardless of whether the sales are facilitated by the marketplace.

Existing Rules

To start, consider a large U.S.-based vendor that sells goods via a multi-seller platform or marketplace to final consumers in France. The large U.S. vendor is registered for VAT in France and reports French VAT.

There is also a smaller U.S.-based vendor that sells low-value goods to consumers in France. If the import threshold of €22 is not exceeded, an exception applies and that vendor does not pay any VAT.

However, a Dutch-based vendor that sells the same low-value goods using the same multi-seller platform to French consumers will need to report Dutch VAT on these sales.

New Rules

To tackle the differences in VAT treatment under the existing rules, the new rules will introduce VAT liability for multi-seller platforms. This can become quite complicated for the various vendors selling through the marketplace and for the marketplace itself.

Here are a few scenarios applying the new rules to a Dutch vendor selling to French consumers through a multi-seller marketplace:

- if the Dutch vendor sells to consumers in France from an EU stock point, French VAT should be reported on a Dutch OSS return;
- if the same Dutch vendor sells some of its products from a French stock point (or a drop shipment from a French vendor), the vendor will need to report French VAT on a French VAT return;
- if the Dutch vendor sells products that have been imported but have a value not exceeding €150, French VAT will need to be reported by the marketplace; and
- if this Dutch vendor supplies imported goods with a value above €150, then import VAT will be collected by the courier or postal company.

Applying the new rules to a U.S. vendor selling to French consumers through a multi-seller marketplace, different scenarios may apply:

- if the U.S. vendor sells products from an EU stock point (local fulfillment), French VAT will be collected by the marketplace;
- if the U.S. vendor sells from its U.S.-based stock and the value of the products does not exceed €150, then the multi-seller marketplace will collect French VAT; and
- if the U.S. vendor dispatches products from its U.S.-based stock with a value above €150, import VAT will be collected by the courier or postal company.

Some Considerations

Both vendors and multi-seller marketplaces will be confronted with various VAT regimes. At the line-item level, both need to assess which party will be liable for the VAT and in which return the VAT must be reported.

A few assumptions can be applied to facilitate these assessments:

- the underlying vendor selling via a multi-seller marketplace is assumed to be an entrepreneur for VAT purposes (the B in B2C);
- the buyer is assumed to be an end consumer (the C in B2C); and
- goods that are packed together, dispatched simultaneously by the same consignor to the same consignee, and covered by the same transport contract are considered a single consignment.

A multi-seller marketplace often does not know if goods will be dispatched in one or multiple consignments. This is why the multi-seller marketplace is permitted to assume that there is a single consignment when goods are ordered by the same customer, at the same time, and from the same supplier.

Conclusion

Both for marketplaces and online vendors, the impact of the changes to the EU VAT can be quite significant. Smaller vendors selling directly to consumers in the EU will need to maintain information regarding additional VAT rates and arrange for additional reporting through the OSS return.

Larger vendors will need to consider whether they will continue foreign VAT registrations or reduce their compliance burden by canceling some of those registrations.

Marketplaces will be pulled into VAT requirements for sales that they merely facilitated under the old system.

If they have not done so already, entities involved in online sales of products to final consumers in the EU should start assessing the impact of these new VAT rules on their sales transactions, systems, and processes. The July effective date is approaching rapidly, and businesses should not expect a grace period. ■