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Electronically Supplied Services and Value Added Tax: The European Perspective

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Abstract

This paper is aimed to provide an in-depth analysis of the European VAT regime applicable to electronically supplied services (e.s.s.), and it will assess, in particular, what kind of services can be considered to be e.s.s. and where they are taxed, taking into account B2B and B2C transactions. The provision of services and software over the Internet and other electronic networks, in fact, is governed by a particular VAT regime that affects businesses operating in all the Member States of the European Union. Apart from the provisions currently applicable, an analysis of the regime introduced by Directive 2008/8/EC (in force from 2010-2015) will be provided.

Keywords: **Taxation, Value Added Tax, Electronically Supplied Services**

INTRODUCTION: FROM MATERIAL GOODS TO ELECTRONICALLY SUPPLIED SERVICES

The European system of Value Added Tax (VAT) is based on the dichotomy goods/services and different rules, mainly as regards the place of taxation, are applicable according to the object of the transaction (i.e. good or service). Without entering into further details, and just to give a basic idea of the different applicable regimes, we see that, pursuant to the VAT Directive[1], the (very) basic rule for goods is that "where goods are not dispatched or transported, the place of supply shall be deemed to be the place where the goods are located at the time when the supply takes place" (Article 31), while "the place of supply of services shall be deemed to be the place where the supplier has established his business or has a fixed establishment from which the service is supplied, or, in the absence of such a place of business or fixed establishment, the place where he has his permanent address or usually resides" (Article 43).

Provided this different regime, and without further analyzing the general provisions regarding the place of supply of goods and services, this article will be focused on the European rules applicable to electronically supplied services (thereinafter e.s.s.), in the light of the fact that "the application of the VAT system to electronic commerce is now considered to be the most significant VAT challenge" (Doernberg et al., 2001). Before providing the reader with a comprehensive list of e.s.s., it is necessary to highlight the importance of such a category of services, which really lies at the crossroad between taxation and technology. The use of informatics, computers and networks brings as a consequence that many goods are transformed into 'virtualized' and 'dematerialized' goods. In other words, "a number of goods which in the past could be supplied physically only, can now be transferred in digitalized form ('virtual goods') and become competitive substitutes on a global market" (Kogels, 1999). As a principle, according to the European lawmaker and to the Organization for Economic Cooperation and Development (OECD)[2], such virtual goods are deemed to be services (OECD, 2003; Doernberg et al., 2001; Westin, 2007; Alexiou & Morrison, 2004; Hargitai, 2001) and, as it will be showed *infra*, a special regime is applicable to them.

Just to make a few examples, everybody is used to read newsletters and magazines on-line, downloading them in *pdf* format. From the VAT point of view, the printed copy of this magazine would be a good, while the virtual, on-line version, with exactly the same content, is deemed to be a service (Doernberg et al., 2001).

From a general perspective, the need to reduce costs of production and the diffusion of the Internet, at least in the highly-developed countries, has the consequence that many traditional physical items are transformed, virtualized, dematerialized, in other words become services. Software is another very good example of this phenomenon. Until a few years ago, buying computer programs on a physical support (CD, disk, etc) was common practice, while now the era of the Software as a Service (SaaS) is definitely open (Parrilli et al., 2008; Turner et al., 2003; Greschler & Mangan, 2002). This means

[1] Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax [OJ L 347, 11.12.2006, pp. 1-118].

[2] The European Commission stated the same principle in the 1998 Communication to the Council, the European Parliament, the Economic and Social Committee and the Committee of the Regions, Electronic Commerce and Indirect Taxation, COM/98/0374 final.

that the user can buy the desired software online and he downloads it from the Internet directly on his computer. Yet, for the European lawmaker the software stored on a physical support is, to the ends of VAT, a good while the SaaS is deemed to be a service.

A third example is computer storage capacity. In this field the monopoly of physical devices (servers, hard disks, etc) is challenged by the provision of Internet-based services, so that many companies prefer to buy extra capacity on-line instead of acquiring expensive physical machines (Gibson & Van Meter, 2000). Even if the purposes and objectives of the two possible transactions are the same, i.e. having more computing capacity, the applicable VAT regime is conceptually different as well as, in some cases, the practical consequences arising from the application of the two sets of rules.

The scope of this article is to show the content of the European provisions currently applicable to e.s.s., with a particular attention to the prescriptions set forth by the VAT Directive together with the effects of the reforms recently introduced by Directive 2008/8/EC[3]. This source, in fact, brings many new elements (that will enter into force progressively in a time frame of 5 years, between 2010 and 2015) to the regime applicable to services (including e.s.s.). At the end of our analysis, then, we will propose the question whether the dichotomy goods/services is still useful, one of the alternatives being the merge between the two concepts and the implementation of a single treatment for both material and virtual goods.

THE NOTION OF ELECTRONICALLY SUPPLIED SERVICES

The first issue to analyze is undoubtedly the notion of e.s.s., starting from the VAT Directive, which does not provide a clear and general definition of e.s.s. but only an indicative list of them in Annex II (Van der Merwe, 2004). Before entering into further details, we have to say that such a list comprises the following items:

(1) "Website supply, web-hosting, distance maintenance of programmes [sic] and equipment;
(2) Supply of software and updating thereof;
(3) Supply of images, text and information and making available of databases;
(4) Supply of music, films and games, including games of chance and gambling games, and of political, cultural, artistic, sporting, scientific and entertainment broadcast and events;
(5) Supply of distance teaching."

It is evident that the examples we mentioned in the introduction are included in this list, so that the provision of an online journal is a supply of text, the SaaS is a supply of software while the online provision of computing and storing capacity is basically comprised in the notion of web-hosting. The content of the list is pretty clear so that no further detailed explanation is needed at this stage. Nevertheless, it can be problematic to assess when a service is expected to be an e.s.s. To be more precise, the supply of software is deemed to be an e.s.s., but the Directive does not specify how the supply

[3] Council Directive 2008/8/EC of 12 February 2008 amending Directive 2006/112/EC as regards the place of supply of services [OJ L 44, 20.2.2008, pp. 11-22].

should take place: only over the Internet, or also over other networks or through other delivery systems, like Bluetooth?

The solution to this problem may be seen in the provisions of another European source, Regulation 1777/2005[4], which has been enacted to implement some measures contained in the Sixth Directive[5], recast and replaced by the VAT Directive in 2006. Before analyzing the relations between the Regulation and the VAT Directive, in particular whether the former can be considered to be still into force, we have to say that Article 11 (1) of the Regulation provides a comprehensive definition of e.s.s. that "shall include services which are delivered over the Internet or an electronic network and the nature of which renders their supply essentially automated and involving minimal human intervention, and in the absence of information technology is impossible to ensure."

This definition apparently captures the paradigm of the provision of 'virtual goods', as defined above, over the Internet or other networks, like an Intranet or a Bluetooth-based distribution system, and therefore it seems to be very comprehensive. However, the interpretation and the relevance of the indent "and in the absence of information technology is impossible to ensure" raises some doubts. Provided that information technology (IT) is "the study, design, development, implementation, support or management of computer-based information systems, particularly software applications and computer hardware" (Information Technology Association of America, n.d.), it is not always easy to identify the cases in which the provision of e.s.s. is not possible in an alternative, not IT-based, way. In theory, in fact, it is possible to print and deliver a *pdf* file, thus the online delivery of its content is not the only possible way (Kogels, 1999). The same applies to the provision of SaaS, given the fact that the software can be stored in a physical support (VAT Committee, 2003).

In order to clarify this point, we have to go through the list of e.s.s., "delivered over the Internet or an electronic network", provided by Article 11 (2) of the Regulation:

(a) "The supply of digitalized products generally, including software and changes to or upgrades of the software;
(b) Services providing or supporting a business or personal presence on an electronic network such as a website or a webpage;
(c) Services automatically generated from a computer via the Internet or an electronic network, in response to specific data input by the recipient;
(d) The transfer for consideration of the right to put goods or services up for sale on an Internet site operating as an online market on which potential buyers make their bids by an automated procedure and on which the parties are notified of a sale by electronic mail automatically generated from a computer;
(e) Internet Service Package (ISP) of information in which the telecommunications component forms an ancillary and subordinate

[4] Council Regulation (EC) no. 1777/2005 of 17 October 2005 laying down implementing measures for Directive 77/388/EC on the common system of value added tax [OJ L 288, 29.10.2005, pp. 1-9].
[5] Sixth Council Directive 77/388/ECC of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment [OJ L 145, 13.6.1977, pp. 1-40].

part (i.e. packages going beyond mere Internet access and including other elements such as content pages giving access to news, weather or travel reports; playgrounds; website hosting; access to online debates etc.)".

This list shows that the absence of human intervention, more than the impossibility to have such human intervention, is the criterion that must be taken into account in order to assess whether or not a service is an e.s.s. In case of e-bids, for instance, what is relevant is that the email of notification is automatically generated and sent by a computer, even if, in theory, the same operation can be accomplished by a human person.

Article 11 (2) (f) refers to other e.s.s. listed in Annex I, which is directed to explain the list of e.s.s. contained originally in the Sixth Directive[6]. Given the fact that such list has been entirely incorporated in the VAT Directive, and reading the VAT Directive and Regulation 1777/2005 together, we can provide the reader with the following (basically) exhaustive list of e.s.s.:

(1) Website supply, web-hosting, distance maintenance of programs and equipment (see Massbaum & Eicker, 2001):
- Website hosting and webpage hosting;
- Automated, online and distance maintenance of programs;
- Remote system administration;
- Online data warehousing where specific data is stored and retrieved electronically;
- Online supply of on-demand disc space.

(2) Supply of software and updating thereof:
- Accessing or downloading software (including procurement/accountancy programs and anti-virus software) plus updates;
- Software to block banner adverts showing, otherwise known as Bannerblockers;
- Download drivers, such as software that interfaces computers with peripheral equipment (such as printers);
- Online automated installation of filters on websites;
- Online automated installation of firewalls.

(3) Supply of images, text and information and making available of databases:
- Accessing or downloading desktop themes;
- Accessing or downloading photographic or pictorial images or screensavers;
- The digitalized content of books and other electronic publications;
- Subscription to online newspapers and journals;
- Weblogs and website statistics;

[6] As amended by Council Directive 2002/38/EC of 7 May 2002 amending and amending temporarily Directive 77/388/EEC as regards the value added tax arrangements applicable to radio and television broadcasting services and certain electronically supplied services [OJ L 128, 15.5.2002, pp. 41-44].

- Online news, traffic information and weather reports;
- Online information generated automatically by software from specific data input by the customer, such as legal and financial data (in particular such data as continually updated stock market data, in real time), travel and weather reports, online debates, etc;
- The provision of advertising space including banner ads on a website/web page;
- Use of search engines and Internet directories, in more general terms supply of online services automatically generated by a computer following specific data input by the user.

(4) Supply of music, films and games, including games of chance and gambling games, and of political, cultural, artistic, sporting, scientific and entertainment broadcast and events:

- Accessing or downloading of music on to computers and mobile phones;
- Accessing or downloading of jingles, excerpts, ringtones and other sounds;
- Accessing or downloading of films;
- Downloading of music on to computers and mobile phones;
- Accessing automated online games which are dependent on the Internet, or other similar electronic networks, where players are geographically remote from one another.

(5) Supply of distance teaching:

- Automated distance teaching dependent on the Internet or similar electronic network to function and the supply of which requires limited or no human intervention, including virtual classrooms, except where the Internet or similar electronic network is used as a tool simply for communication between the teacher and student;
- Workbooks completed by pupils online and marked automatically, without human intervention.

(6) Supply of e-procurement, e-auction, etc services regulated by a completely automated procedure.

The criterion that renders a service an e.s.s. is thus, at least generally, the fact to be automatically generated, without human control and interference. This aspect can be criticized for the very fact that it is in many cases cumbersome to separate the e.s.s. from other services that involve the use of the Internet and of computer equipment but that are not purely automated. In case of supply of distance teaching, in fact, it could be considered to be pretty irrational the applicability of two different regimes for (i) long-distance live classes (with the remote presence of a human teacher) and (ii) purely virtual classrooms with no human intervention[7] (Doernberg et al., 2001).

Apart from that, it is necessary to point out that “the use of the Internet or other electronic networks by parties to communicate with respects to transactions or to

[7] The case law of the European Court of Justice indicates that, in general terms, the modality used to provide a service is irrelevant. See the case C-2/95 *Datacenter* [ECR 1997, I-3017].

facilitate trading does not, any more than the use of a phone or fax, affect the normal VAT rules that apply" (VAT Committee, 2003). With this respect, Article 56 (2) of the VAT Directive, then, states that "where the supplier of a service and the consumer communicate via electronic mail, that shall not of itself mean that the service supplied is an electronically supplied service". Moreover, from a different perspective, it has been said that the VAT Directive and Regulation 1777/2005 "had not provided a comprehensive definition of what digital goods and services are covered. The list seems to be unsatisfactory in respect of the novel types of services" (Basu, 2002), e.g. co-location services and registration of domain names.

Before analyzing the regime applicable to e.s.s. it is very interesting to focus our attention on two issues. The first one regards the validity of Regulation 1777/2005, provided that it has been enacted by the European lawmaker to implement some measures contained in the Sixth Directive of 1977, which has been recently recalled by the VAT Directive. It could be arguable, in fact, that this Regulation is not applicable anymore due to the fact that the source on which it is grounded has been replealed. This interpretation, however, is not the most correct one provided that the content of the Sixth Directive and of the VAT Directive is, to a certain extent, homogeneous, and, in particular, the list of e.s.s. contained in both sources is exactly the same.

This means that the abovementioned clarifications introduced by the Regulation are now applicable to the VAT Directive and therefore these two pieces of legislation must be read together. This solution comes from the interpretation of the recitals of the VAT Directive, which state (no. 1-3) that "Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes — Common system of value added tax: uniform basis of assessment has been significantly amended on several occasions. Now that new amendments are being made to the said Directive, it is desirable, for reasons of clarity and rationalisation that the Directive should be recast…To ensure that the provisions are presented in a clear and rational manner, consistent with the principle of better regulation, it is appropriate to recast the structure and the wording of the Directive although this will not, in principle, bring about material changes in the existing legislation. A small number of substantive amendments are however inherent to the recasting exercise and should nevertheless be made. Where such changes are made, these are listed exhaustively in the provisions governing transposition and entry into force."

The second issue to take into account is whether the national legislations and practices of the Member States strictly adhere to the principles stated in the VAT Directive and Regulation 1777/2005. In other words, provided that dematerialized and virtualized (i.e. digitalized) goods are deemed to be services by the applicable European VAT legislation, is this principles followed in all European jurisdictions? Given the fact that "another difficulty arises in characterization of the software as goods or services" (Westin, 2007), we have to take into account that "the EU treats electronically delivered software as a service but member states may deviate from this characterization" (Westin, 2007).

Apparently it seems that there is a consensus in treating the digital goods as services. In the UK, for instance, the tax authorities stated that, in case of software, this has to be considered either as a good (if made up of the carrier medium, i.e. CD, hard disk, etc) or

as a service (the data itself and/or the instructions), and "when the goods and services are not identified separately, the whole importation is treated as an importation of goods[8]" (HM Revenue & Customs, n.d.). In general terms, we can say that the nature of goods prevails over that of services.

In France, yet as regards software, the local "Tax Administration ruled that software, downloaded onto a purchaser's computer, constitutes a service, irrespective of its customized development" (Doernberg et al., 2001). In particular, the downloading and installation of a computer program is deemed to be an intangible service as well as the assistance provided online (Powers et al., 1997). As regards Germany, the solution adopted is the same and, to be more precise, "according to the German tax authorities the electronic transfer of standardized software is considered not to be a supply of goods but supply of an 'other service'" (Massbaum & Eicker, 2001). The Belgian VAT Code, finally, provides a definition of e.s.s. which is consistent with the one of Regulation 1777/2005 (Baltus, 2007; Soriano & Noirhomme, 2003). The tax authorities, then, base the explanation and interpretation of the national legislative provisions on the applicable European sources, so that we can say that there are no differences in the approach taken by the EU lawmaker and by the Belgian legislator and fiscal administration[9]. It is interesting to point out, finally, that the latter recommends making a case-by-case analysis when assessing whether or not a service is an e.s.s.

THE REGIME APPLICABLE TO ELECTRONICALLY SUPPLIED SERVICES

After having assessed what e.s.s. are according to the European lawmaker, we will now analyse which regime is applicable to them, in other words we will find solutions to the following fundamental question: where a transaction involving e.s.s. is taxed? We will first take into consideration the legal framework currently applicable and then we will provide the reader with an overview of the changes introduced by Directive 2008/8/EC. As a preliminary remark, we have to say that two basic principles govern the overall applicable regime.

First of all, pursuant to Article 43 of the VAT Directive, as pointed out above, "the place of supply of services shall be deemed to be the place where the supplier has established his business or has a fixed establishment from which the service is supplied, or, in the absence of such a place of business or fixed establishment, the place where he has his permanent address or usually resides" (Westin, 2007). From a different perspective, then, e.s.s. "provided from third countries to persons established in the Community or from the Community to recipients established in third countries should be taxed at the place of the recipient of the services" (Recital 3 of Directive 2002/38/EC). Therefore, the criteria to take into account are basically the place of establishment (in the EU or not) of (i) the supplier and of (ii) the consumer. In light of these principles, we will go through a series of scenarios, both involving business to business (B2B) and business to consumer (B2C) transactions.

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[8] This statement is consistent with the position expressed by the European Court of Justice (ECJ) in the case C-41/04 *Levob Verzekeringen BV and OV Bank NV v Staatssecretaris van Financien* [OJ C 22, 28.1.2006, pp. 1-2] according to which in case of provision of software on a material carrier together with customization services, the transaction should be considered as a whole and it is a supply of services.

[9] See *Circulaire* no. 9/2003 of 12 August 2003.

(a) EU-established supplier and EU-established customer

In this case, it is necessary to separate B2B from B2C transactions provided that the relevant sets of rules are radically different. In the former case, thus, Article 56 of the VAT Directive will be applicable, and therefore "the place of supply of [e.s.s.] to customers established outside the Community, or to taxable persons established in the Community but not in the same country as the supplier, shall be the place where the customer has established his business or has a fixed establishment for which the service is supplied, or, in the absence of such a place, the place where he has his permanent address or usually resides" (see Alexiou & Morrison, 2004; Westin, 2007; Parrilli, 2008). Taxable person is, pursuant to Article 9 of the VAT Directive, "any person who, independently, carries out in any place any economic activity, whatever the purpose or results of that activity."

To make a concrete example, if *A* (company located in Italy) sells online software and solutions to *B*, business established in Belgium, the place of supply is deemed to be Belgium and therefore the place of taxation will be Belgium, according to Article 63 of the VAT Directive ("the chargeable event shall occur and VAT shall become chargeable when the goods or the services are supplied").

The situation is different in case of B2C transaction, regulated by the general rule of the abovementioned Article 43, and therefore the place of supply and taxation will be the country of the supplier. For instance, if *A* (Italian company) sells online music or videos to Mr. *B*, private consumer who lives in Belgium, the place of taxation will be Italy.

(b) EU-established supplier and non EU-established customer

The application of Article 56 VAT Directive implies that the place of taxation in case of supply of services to customers located outside the European Union (EU) is the place where the customer is established, therefore "EU suppliers are no longer obliged to levy VAT when selling on markets outside the EU" (European Commission, n.d.). Provided that VAT, pursuant to Article 2 (1) (c) of the VAT Directive, is levied only for supplies of services "for consideration within the territory of a Member State by a taxable person acting as such", no VAT will be charged for these transactions. Therefore, if *A* (German company) sells online capacity to customers located outside the EU, no VAT will be imposed.

(c) Non EU-established supplier and EU-established customer

The field of supplies of e.s.s. from non-EU countries to consumers established in the EU has been dramatically reformed in 2002 primarily by Directive 2002/38/EC. Provided that, as pointed out above, EU suppliers previously had to levy VAT on the provision of their services worldwide, while non-EU suppliers were not obliged to do so in case of services supplied to European customers, the consequence was "a tremendous competitive advantage to non-EU suppliers who could deliver goods electronically VAT free, while their competitors had to charge VAT when they supplied final consumers in the EU and elsewhere. For example, European exporters to the United States had to pay EU VAT, whilst American exporters were not under a similar obligation" (Van der Merwe, 2004). The final results were both competitive disadvantage for European

companies and distortions in the internal market (Raponi, 2000).

In light of such reforms, we can provide the reader with an overview of the regime applicable to supplies coming from non EU-established providers[10]. As regards B2B transactions, VAT will be owed in the customer's State, pursuant to Article 56 of the VAT Directive. Therefore, if *A*, Australian software company, sells digital equipment to *B*, German business, VAT will be owed in Germany at the rate applicable there. As pointed out by the Dutch tax authorities, then, "where a supplier provides electronic services to an entrepreneur based in the EU, the VAT is levied from the entrepreneur consuming the services. In that case, the supplier is not allowed to charge VAT. The consumer of the services owes VAT at the rate applicable in the Member State where he is based" (Belastingdienst, n.d.).

The situation is slightly different in case of B2C transactions. In this case Article 57 of the VAT Directive enters into play and therefore where e.s.s. "are supplied to non-taxable persons who are established in a Member State, or who have their permanent address or usually reside in a Member State, by a taxable person who has established his business outside the Community or has a fixed establishment there from which the service is supplied, or who, in the absence of such a place of business or fixed establishment, has his permanent address or usually resides outside the Community, the place of supply shall be the place where the non-taxable person is established, or where he has his permanent establishment or usually resides." In other words, VAT will be levied at the rate applicable in the country where the customer is located and therefore "a non-EU established taxable supplier now has to charge VAT on sales to private, non-taxable consumers in the EU, like EU registered suppliers have to do" (Van der Merwe, 2004).

As regards the place where the VAT is owed, things are more complex, as it is necessary to take into account the 'special scheme for electronically supplied services' provided for by Articles 359-369 of the VAT Directive. Non EU-based businesses that plan to provide e.s.s. to non-taxable persons located in the EU shall register and get a VAT identification number in a Member State, the so-called 'Member State of identification', unless "they are otherwise required to be VAT-registered anywhere in the EU" (Sinyor, 2002). Pursuant to Article 360, in fact, "the non-established taxable person shall state to the Member State of identification when he commences or ceases his activity as a taxable person, or changes that activity in such a way that he no longer meets the conditions necessary for use of this special scheme." The Member State of identification, then, must "allocate to the non-established taxable person an individual VAT identification number" (Article 362). The non-European company will deal only with the tax authorities of the Member State of identification, and in particular he "shall submit by electronic means to the Member State of identification a VAT return for each calendar quarter, whether or not electronic services have been supplied" (Article 364). Moreover, "the VAT return shall show the identification number and, for each Member State of consumption[11] in which VAT is due, the total value, exclusive of VAT, of supplies of

[10] Article 358 (1) of the VAT Directive defines the 'non established taxable person' as "a taxable person who has not established his business in the territory of the Community and who has no fixed establishment there and who is not otherwise required to be identified" for VAT purposes.

[11] Defined as "the Member State in which, pursuant to Article 57, the supply of the electronic service is deemed to take place" (Article 358 (4) of the VAT Directive).

electronic services carried out during the tax period and the total amount of the corresponding VAT. The applicable rates of VAT and the total VAT due must also be indicated on the return" (Article 365). As regards payment of the VAT owed, Article 367 states that "the non-established taxable person shall pay the VAT when submitting the VAT return."

This system basically implies that "non-EU suppliers will collect taxes based on the rates of all the EU Member States in which they have final consumers. The country of identification will reallocate the VAT revenue to the country of consumption (called the 'Member State of consumption') – the Member State in which the supply of electronic services is deemed to take place" (Van der Merwe, 2004). The literature reasonably highlighted that such requirements make the position of EU businesses, at least in principle, more advantageous in comparison with non-EU suppliers: provided that European e-business companies can charge the same VAT rate to every European non-taxable customer (see *supra*), this is not the case in point for non-EU suppliers (Van der Merwe, 2004). To give an example, "if a non-EU operator decides to register in Great Britain and makes sales to individuals in France, Germany and Sweden, the operator will need to know that the rates to be applied at the customer location are 19.6 percent, 16 percent and 25 percent, respectively" (Basu, 2002). The consequence of this system is that "in practice suppliers…chose that Member State for registration with the lowest tax rate applicable to the respective service to be supplied. In this respect, a new field of tax competition between the Member States…arises" (Massbaum & Eicker, 2001). To be more precise, the best solution for non-EU companies is to open a subsidiary or a fixed establishment in a European country with low VAT rates, like Luxembourg (see *infra*) so that they can operate in the European market under the same conditions as EU-based businesses.

Apart from that, the criterion of the place of establishment of the customer is pretty arguable due to the difficulties that can derive when assessing where the non-taxable customer is located (see, for further considerations, *infra*). We can, finally, summarize the above scenarios in the following tables:

Table 1: B2B transactions (until 31/12/2009)

Supplier	***Customer***	***Place of taxation***
EU-based business	Taxable person based in the EU	Customer's Member State
EU-based business	Taxable person based outside the EU	No VAT
Non EU-based business	Taxable person based in the EU	Customer's Member State

Table 2: B2C transactions (until 31/12/2009)

Supplier	***Customer***	***Place of taxation***
EU-based business	Non-taxable person based in the EU	Supplier's Member State
EU-based business	Non-taxable person based outside the EU	No VAT
Non EU-based business	Non-taxable person based in the EU	Member State of Identification at the rate of the customer's Member State

THE IMPACT OF DIRECTIVE 2008/8/EC: FORTHCOMING REGIME

The regime analyzed above will basically be in force until the end of 2009 and from 1 January 2010 the new principles set forth by Directive 2008/8/EC will be applicable. Such a Directive is aimed to rewrite some of the provisions of the VAT Directive and therefore contains Articles that will replace the corresponding actual prescriptions of the VAT Directive. It is therefore of great practical and theoretical interest to report and analyze the new rules that will regulate the supply of e.s.s. Some of the amendments, then, will enter into force only at the beginning of 2015, basically for economic reasons.

The principles that inspired the recent reform are the following:

1. "For all supplies of services the place of taxation should, in principle, be the place where the actual consumption takes place" (Recital no. 3 of the 2008 Directive);
2. "For supplies of services to taxable[12] persons, the general rule with respect to the place of supply of services should be based on the place where the recipient is established, rather than where the supplier is established" (Recital no. 4);
3. "Where services are supplied to non-taxable persons, the general rule should continue to be that the place of supply of services is the place where the supplier has established his business" (Recital no. 5).

Therefore we can summarize the forthcoming regime, as from 1 January 2010 (and for a time frame of 5 years), in the following tables:

Table 3: B2B transactions (2010-2014)

Supplier	***Customer***	***Place of taxation***
EU-based business	Taxable person based in the EU	Customer's Member State[13]
EU-based business	Taxable person based outside the EU	No VAT[14]
Non EU-based business	Taxable person based in the EU	Customer's Member State[15]

[12] One of the amendments introduced by Directive 2008/8/EC concerns the newly-introduced Article 43 of the VAT Directive (applicable from 1 January 2010), pursuant to which "for the purpose of applying the rules concerning the place of supply of services: 1. a taxable person who also carries out activities or transactions that are not considered to be taxable supplies of goods or services…shall be regarded as a taxable person in respect of all services rendered to him; 2. a non-taxable legal person who is identified for VAT purposes shall be regarded as a taxable person."

[13] Pursuant to the new version of Article 44 of the VAT Directive (applicable from 1 January 2010) which states that "the place of supply of services to a taxable person acting as such shall be the place where that person has established his business. However, if those services are provided to a fixed establishment of the taxable person located in a place other than the place where he has established his business, the place of supply of those services shall be the place where that fixed establishment is located. In the absence of such place of establishment or fixed establishment, the place of supply of services shall be the place where the taxable person who receives such services has his permanent address or usually resides."

[14] According to the new version of Article 59 of the VAT Directive (applicable from 1 January 2010) which states that "the place of supply of [e.s.s.] to a non-taxable person who is established or has his permanent address or usually resides outside the Community, shall be the place where that person is established, has his permanent address or usually resides."

[15] Pursuant to the new version of Article 44 of the VAT Directive (applicable from 1 January 2010).

Table 4: B2C transactions (2010-2014)

Supplier	***Customer***	***Place of taxation***
EU-based business	Non-taxable person based in the EU	Supplier's Member State[16]
EU-based business	Non-taxable person based outside the EU	No VAT
Non EU-based business	Non-taxable person based in the EU	Member State of Identification at the rate of the customer's Member State[17]

The above described regime will be valid until the end of 2014. From 1 January 2015, in fact, the 'new' Article 58 of the VAT Directive will replace the existing provisions regarding supplies of e.s.s. to non-taxable persons, and therefore "the place of supply of [e.s.s.] to a non-taxable person shall be the place where that person is established, has his permanent address or usually resides." The results of these changes are reported in the table below:

Figure 5: B2C transactions (2015-…)

Supplier	***Customer***	***Place of taxation***
EU-based business	Non-taxable person based in the EU	Member State of Identification at the rate of the customer's Member State
EU-based business	Non-taxable person based outside the EU	No VAT
Non EU-based business	Non-taxable person based in the EU	Member State of Identification at the rate of the customer's Member State

Directive 2008/8/EC brings some remarkable reforms also as regards the abovementioned 'special scheme'. In particular, starting from the beginning of 2015, two 'special schemes' will be applicable in the field of VAT and e.s.s. The actual 'special scheme' described above will be replaced by the 'special scheme for telecommunications, broadcasting or electronic services supplied by taxable persons not established within the Community'. The content of such scheme corresponds to the existing one provided by Articles 359-369 of the VAT Directive, therefore see *supra* for further details. The second 'special scheme', created by the 2008 Directive, is the 'special scheme for telecommunications, broadcasting or electronic services supplied by

[16] Pursuant to the new version of Article 45 of the VAT Directive (applicable from 1 January 2010) "the place of supply of services to a non-taxable person shall be the place where the supplier has established his business. However, if those services are provided from a fixed establishment of the supplier located in a place other than the place where he has established his business, the place of supply of those services shall be the place where that fixed establishment is located. In the absence of such place of establishment or fixed establishment, the place of supply of services shall be the place where the supplier has his permanent address or usually resides."

[17] Pursuant to the new version of Article 58 (1) of the VAT Directive (applicable from 1 January 2010) which sets forth that "the place of supply of electronically supplied services…when supplied to non-taxable persons who are established in a Member State, or who have their permanent address or usually reside in a Member State, by a taxable person who has established his business outside the Community or has a fixed establishment there from which the service is supplied, or who, in the absence of such a place of business or fixed establishment, has his permanent address or usually resides outside the Community, shall be the place where the non-taxable person is established, or where he has his permanent address or usually resides."

taxable persons established within the Community but not in the Member State of consumption'.

The implementation of this scheme is due to the fact that the place of supply of e.s.s. provided by European companies to EU-located non-taxable consumers will be the consumer's Member State, to be more precise the place where he is established, has his permanent address or usually resides. This means that EU-established e-businesses will have to deal with a plurality of applicable VAT rates, as actually non-EU companies do (thus removing the existing discrimination against extra-European suppliers of e.s.s.), but, at the same time, the European lawmaker created a special regime aimed to avoid red tapes for such firms. The scheme will be applicable to 'taxable person[s] not established in the Member State of consumption', i.e. "taxable person[s] who [have] established [their] business in the territory of the Community or [have] a fixed establishment there but [have] not established [their] business and [have] no fixed establishment within the territory of the Member State of consumption[18]".

We can imagine the following example: *A*, company established in Germany, provides on-line music to private customers around Europe. *A* is the 'taxable person not established in the Member State of consumption' and Germany is the 'Member State of identification', i.e. "the Member State in the territory of which the taxable person has established his business or, if he has not established his business in the Community, where he has a fixed establishment.[19]" *A* will sell music online to customers established in the whole Europe, and the applicable VAT rate will be that of the client's Member State. Thanks to the special scheme, *A* will deal only with the tax authorities of the Member State of identification, i.e. Germany, and it will submit to such authorities its VAT return in which it will show, "for each Member State of consumption in which VAT is due, the total value, exclusive of VAT, of supplies of [e.s.s.] carried out during the tax period and the total amount per rate of the corresponding VAT. The applicable rates of VAT and the total VAT due must also be indicated on the return.[20]"

This reform, nevertheless, will make even more dramatic one of the biggest issues that already arose for what concerns the existing 'special scheme' for non-EU businesses, i.e. the individuation of the place of establishment of the consumer. If technology will not be useful to find the solution in the coming years (Basu, 2002), EU-based companies will face the same problems that non-EU businesses must solve now. In other words, instead of creating legal tools able to reduce or abolish the difficulties linked to the implementation of the 'special scheme' for non-EU firms, the European lawmaker decided to extend them…to EU-established companies. It is therefore pretty evident that

[18] Article 369*a* (1) of the VAT Directive (applicable from 1 January 2015).
[19] Article 369*a* (2) of the VAT Directive (applicable from 1 January 2015). The second paragraph of Article 369*a* will state that "where a taxable person has not established his business in the Community, but has more than one fixed establishment therein, the Member State of identification shall be the Member State with a fixed establishment where that taxable person indicates that he will make use of this special scheme. The taxable person shall be bound by the decision for the calendar year concerned and the two calendar years following." The relevance of the concept of fixed establishment will therefore increase when the reform will enter into force, and it is possible to predict problems in the individuation of fixed establishments in the field of e-commerce. The main question to which the European lawmaker and the national tax authorities should provide a solution, which must be both practically feasible and correct from the technical point of view, is the following: can servers and websites be deemed to be fixed establishments of an e.s.s. supplier? See the consideratins developed by Parrilli (2008).
[20] Article 369*g* of the VAT Directive (applicable from 1 January 2015).

such distortion has to be removed, provided that (at least for the time being) it is very difficult, if not impossible, to determine with a great degree of certainty the place of establishment of a consumer and, on the other hand, it is not really feasible to assess whether or not technology will be able to solve this issue in the coming years.

CONCLUSION: THE NEED FOR FURTHER REFLECTION

In the previous paragraphs we addressed some of the most relevant issues regarding the VAT regime for e.s.s. at European level, namely we analyzed (i) what e.s.s. are in light of the applicable legislative framework and how and where they will be taxed (ii) until the end of 2009 and (iii) from the beginning of 2010.

As concluding remarks, we find useful to briefly mention few major problems that are linked to the implementation of the VAT Directive as regards the provision of e.s.s., starting from the enforceability of the solutions adopted by the European lawmaker, especially in connection with the individuation of the place of establishment of the consumer. It has been pointed out, in fact, that "enforceability is the Achilles heel of the…VAT system. Enforcement causes problems owing to the difficulties in identifying…customers in general within the digital world" (Basu, 2002).

Unless technology will solve this problem and new tools aimed to identify with absolute certainty the location of the customer will be invented, the European lawmaker should probably reconsider the solutions adopted in the VAT Directive and in Directive 2008/8/EC and investigate whether or not taxation at the supplier's place would be more feasible. From a legal perspective, in fact, the identification of the place of consumption can tell very little about the place of establishment of the consumer: just to make an extreme but realistic scenario, what about a customer who downloads software on his laptop or mobile phone while flying on an airplane? One could argue that the relevant information can be inferred from the credit card data of this client, but they are not always very reliable, as one can be established in a country and have a bank account in another one. In other words, technology is not likely to definitely solve the problem of the identification of the consumer's location.

Apart from that, another very sensitive issue concerns the rate of taxation of e.s.s. Without entering into a detailed comparative analysis of the VAT rates applicable in all EU Member States, in many cases it "appears that on-line taxes for downloaded items would be higher than the taxes, which were being applied to the same products when these are delivered through traditional ways" (Basu, 2002) The typical example regards the printed and the digital versions of a book: in many countries the former will be taxed at a reduced rate, if not at a zero rate, while the latter will be taxed at the normal rate (Van der Merwe, 2004). This implies a violation of the equal treatment principle, pursuant to which "similar goods and services [should] bear the same tax burden.[21]" From a non-tax (and innovative) perspective, such 'discrimination' of e.s.s. is not really understandable if we consider the need to save natural resources. In other words, if a book delivered online is supposed to have less impact on the environment (in terms of resources necessary to create it), why should it be taxed more heavily and thus should be (at least potentially - in our very basic model, in fact, we do not take into account the

[21] Recital no. 7 of the VAT Directive.

costs needed to produce a digital and a printed book) more expensive for the final user?

The issue of rates introduces a different, and more general, topic, i.e. the need to reconstruct the notion of goods and services since such traditional division has been dramatically altered by technological changes. In other words, it is not possible to deny that "electronic deliveries warranted a revision of the interpretation of the distinction between goods and services which is fundamental in the workings of VAT" (Basu, 2002). This point is undoubtedly crucial and needs to be carefully assessed by the European lawmaker in order to provide solutions which are both implementable and technologically viable. With this regard, it is possible to disagree with the position of the European Commission that, as reported in the literature, "refuted the argument that the differentiation between VAT on traditional articles and their electronic counterparts is inconsistent. The Commission believes that it is impossible to argue that there is direct equivalence between these items, as they are by their nature two fundamentally different products that need not necessarily be taxed identically" (Van der Merwe, 2004).

It would be necessary to better assess to what extent material and digitalized products are really different and, above all, if it is still advisable to have a plurality of different regimes applicable to items that, at the end, have the same content and the same function. Without entering into further discussions that would go beyond the scope of this article, we point out that such a reconstruction does not necessarily mean that the supply of e.s.s. should be treated as a supply of goods (see Alexiou & Morrison, 2004).

The last issue to mention regards the reform introduced by Directive 2008/8/EC, that will enter into force in 2015, for what concerns the 'special scheme' for EU-based companies and taxation at the rates applicable in the consumer's Member State. The actual regime, as we said above, created the conditions for competition between EU countries (Pastukhov, 2007), and apparently Luxembourg is the winner in this race, provided that it is convenient for many suppliers of e.s.s. to be established in this country for the very fact that B2C transactions are taxed in the supplier's Member State, and Luxembourg offers attractively low VAT rates (the standard rate is 15%, see European Commission, 2008). As soon as the planned reform will be implemented in 2015 (see table 5), thus, the conditions for competition between European jurisdictions will not exist any more (or at least will be dramatically reduced), and, in more general terms, this could lead to a potential increase in the costs sustained by e-suppliers and final users.

The way to create a European VAT system for e.s.s. which is enforceable and fully fair, both for companies and consumers, seems to be still long, and the reforms introduced by Directive 2008/8/EC, in particular, can be a very useful starting point for further discussion and analysis rather than the final harbor.

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