Greenberg Traurig European VAT, Customs and Trade Alert

This edition of GT's *European VAT, Customs and Trade Alert* will consider:

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EU about to simplify VAT collection rules in relation to centralized customs clearance? The European Commission circulated a document for consultation to parties concerned in the context of a preparation of a possible legislative proposal on the simplification of VAT collection procedures in relation to centralized customs clearance. Bearing in mind the growing demand of companies to organize EU customs clearance cross-border, this is an important consultation. The current VAT rules do not provide clear and efficient solutions for centralized customs clearance. To facilitate the developments in the customs arena, it is crucial that the European Commission and the EU Member States implement a solution soon.

ECJ rules on excise duty consignments involving a customs suspension procedure. Recently, the European Court of Justice (ECJ) ruled in a case involving products subject to payment of excise duty. Excise duties are (indirect) taxes levied on the consumption or the use of certain products such as (manufactured) tobacco products, alcoholic beverages and mineral oils. The prejudicial questions put forward by the referring Court in the underlying case — *inter alia* — related to whether or not the product in question needed to be accompanied by an administrative accompanying document (AAD) during transportation.

EU Tightens Sanctions on Iran. With the adoption of Council Decision 2010/413/CFSP concerning restrictive measures against Iran, repealing Common Position 2007/140/CFSP, and its publication in the Official Journal of the European Union (EU) on July 27, 2010, the EU imposed new sanctions on Iran. It is anticipated that these sanctions will have an impact on many, if not all, companies doing business with Iran and Iranian companies. Even existing relations and agreements could be impacted.

VAT aspects combined services and supplies. The supply of services and goods can lead to a wide variety of VAT consequences. Several questions have to be answered. For example, where a service of a supply is considered to take place and whether an exemption is applicable or what VAT rate must be applied. These questions can be difficult, especially when there is a combination of services and/or goods.

The next edition of the *European VAT, Customs and Trade Alert* will be published around November 20.

WTO Panel issues reports on tariff treatment of certain information technology products by the EU and its Member States

By Erik Zietse

On August 16, 2010, the WTO issued the reports of the panel on the tariff treatment of certain information technology products by the EU and its Member States. The reports follow the complaints by the United States, Japan and Chinese Taipei against the EU and its Member States for failing to comply with their scheduled duty-free tariff concessions arising from the Information Technology Agreement (ITA).

The complaint was focused on three specific types of products: Flat Panel Displays (FPDs), Set Top Boxes which have a Communication function (STBCs) and Multifunctional Digital Machines (MFMs).

The complaining parties claim that the EU is required to accord duty-free tariff treatment to the aforementioned products under the European Communities Schedule of Concessions to the GATT 1994 pursuant to modifications therein to reflect the commitments it has made under the ITA. In its lengthy report of over 450 pages, the panel considers all aspects of these cases. For all products, the panel finds that the EU and its Member States have acted *"inconsistently"* with its obligations under the GATT 1994. The main conclusions are:

FPD

"The European Communities fails to accord treatment no less favourable than that set forth in its Schedule to the commerce of the other WTO Members, in particular certain flat panel display devices that are capable of receiving and reproducing video images both from an automatic data-processing machine and from a source other than an automatic data-processing machine, or that have a DVI interface, whether or not they are capable of receiving signals from another source. Thus, the European Communities is inconsistent with Article II:1(a) of the GATT 1994. This inconsistency is not eliminated by the duty suspension with respect to certain products in dispute falling within the scope of the FPDs narrative description or within the scope of CN code 8471 60 90 because the duty suspension measure does not eliminate the failure to accord treatment no less favourable to the commerce of the other WTO Members."

STBCs

"The measures (of CNEN 2008/C 112/03) *direct national customs authorities to classify under dutiable headings some set top boxes which incorporate a device performing a recording or reproducing function and retain the essential character of a set top box and that fall within the scope of the STBCs narrative description in the Annex to the EC Schedule. Because the concession calls for duty-free treatment of products falling within its scope, this dutiable treatment is inconsistent with Article II:1(b) of the GATT 1994.*

"The measures (of CNEN 2008/C 112/03) *direct national customs authorities to classify under dutiable headings some set top boxes which utilise ISDN, WLAN or Ethernet technology, and that fall within the scope of the STBCs narrative description in the Annex to the EC Schedule. Because the concession calls for duty-free treatment of products falling within its scope, this dutiable treatment is inconsistent with Article II:1(b) of the GATT 1994."*

MFMs

"The regulation(s) (517/1999 and 400/2006) *requires dutiable treatment of certain ADP MFMs that fall within the scope of the concession for "input or output units" in HS1996 subheading 8471 60 of the EC Schedule. Because the concession calls for duty-free treatment of products falling within its scope, this dutiable treatment is inconsistent with Article II:1(b) of the GATT 1994.*

"The regulation (517/1999) *requires dutiable treatment of certain non-ADP MFMs that fall within the scope of the concession for "facsimile machines" in HS1996 subheading 8517 21 of the EC Schedule. Because the concession calls for duty-free treatment of products falling within its scope, this dutiable treatment is inconsistent with Article II:1(b) of the GATT 1994.*

"Because the measure has guided and serves to guide the European Communities uniform application of the common customs tariff in a way that results in the application of duties to those ADP MFMs that fall within the duty-free concession, the measure is inconsistent with Article II:1(b) of the GATT 1994.

"Because the measure has guided and serves to guide the European Communities uniform application of the common customs tariff in a way that results in the application of duties to those non-ADP MFMs that fall within the duty-free concession, the measure is inconsistent with Article II:1(b) of the GATT 1994.

"The regulation (400/2006) *does not require the dutiable treatment of non-ADP MFMs with a facsimile function. Therefore, the European Communities has not acted inconsistently with Article II:1(b) of the GATT 1994 with respect to non-ADP MFMs with a facsimile function as the measure does not impose duties in excess of those provided for in the EC Schedule.*

"The three relevant CN2007 codes require that certain ADP MFMs which fall within the scope of the duty-free concession for input or output units of an ADP in subheading 8471 60 of the EC Schedule be charged a duty of 6 per cent. Therefore, with respect to these products, the measure is inconsistent with Article II:1(b) of the GATT 1994.

"The three relevant CN2007 codes require that certain non-ADP MFMs which fall within the scope of the duty-free concession for "facsimile machines" in subheading 8517 21 of the EC Schedule be charged a duty of 6 per cent. Therefore, with respect to these products, the measure is inconsistent with Article II:1(b) of the GATT 1994."

Pursuant to finding that the EU has acted inconsistently with the GATT 1994, the panel recommend *"that the Dispute Settlement Body request the European Communities to bring the relevant measures into conformity with its obligations under the GATT 1994."*

In previous issues of the *European VAT, Customs and Trade Alert*, we have discussed the developments in the field of the tariff classification of information technology products on multiple occasions. The tariff classification of these products is an ongoing source for discussion and disputes between the industry and the Customs Authorities. Now that the panel has concluded that EU and its Member States have acted in violation of their ITA obligations, it is anticipated that these ongoing discussions on, for example, flat panel displays and multi-functional printers, will soon enter a new phase. Although the report of the panel is not directly binding and will as such not have a direct effect, the conclusions are expected to have a positive influence on the ongoing classification discussions.

EU about to simplify VAT collection rules in relation to centralized customs clearance?
By Erik de Bie

The European Commission circulated a document for consultation to parties concerned in the context of a preparation of a possible legislative proposal on the simplification of VAT collection procedures in relation to centralized customs clearance. Bearing in mind the growing demand of companies to organize EU customs clearance cross-border, this is an important consultation. The current VAT rules do not provide clear and efficient solutions for centralized customs clearance. To facilitate the developments in the customs arena, it is crucial that the European Commission and the EU Member States implement a solution soon.

What is the problem? The Modernized Customs Code allows the customs authorities to authorize importers to declare and pay customs duties to the customs office that is competent for such importer, independent from where the goods are physically imported and where they are transported to within the EU.

An example: On behalf of a German company, Chinese goods enter the EU through the Barcelona harbor. The goods are to be sold to a Spanish customer. If the German importer obtained the appropriate license from German Customs, the German importer can declare and pay the customs duties to German Customs without physically transporting the goods to Germany. However, in this example, the German company will have to assess and pay the VAT in Spain, being the EU Member State of actual importation.

In other words, the current VAT rules "destroy" the centralization and simplifications that are offered by the Modernized Customs Code, since the German importer will still have to deal with Spanish VAT compliance obligations and VAT payments. The conclusion is obvious: the VAT rules should be amended to ensure that companies can have the full benefit of the centralized customs clearance.

The European Council, the European Commission and numerous experts acknowledged years ago that the VAT rules have to change. A number of possible solutions were developed, analyzed and discussed, but there is still no final decision and agreement. It is obvious that the centralized customs clearance options becomes much more interesting when a solution for the VAT compliance is in place. We therefore call on all parties involved to agree on real solution and to actually implement such a solution in the EU VAT legislation as soon as possible, instead of continuing discussions, as in many other VAT related cases, for many years.

Based on the "Consultation paper" of the European Commission, it can be understood that the Commission considers two possible solutions:

1) Centralization of import VAT obligations. In this scenario, importers will be allowed to declare both the customs and VAT to the authorities in the Member State in which the centralized authorization is obtained. It is considered that payment could be to the Member State of importation or through the Member State of authorization who on its turn will transfer the VAT to the Member State of importation.

2) Changed timing of the VAT obligations. This scenario provides for an option to deal with all VAT related import obligations in a supplementary declaration or on a periodical basis. In the Consultation paper, it is left open whether the VAT declaration should be lodged in the Member State of authorization or in the Member State of importation.

We believe that the Consultation paper does not outline the best possible solution in which all — in some Member States already applied — VAT facilitations and simplifications are taken into account. It is clear that the Commission is respecting the current VAT regime in a number of EU Member States that still require businesses to declare and pay VAT on an import declaration basis. We trust that the Commission and the Member States will agree on a much better solution, namely a combination of both scenario that are mentioned in the Consultation paper. We believe that only a solution that allows businesses to declare and pay both the customs duties and VAT on a periodical basis to the Member State of authorization would be a true solution.

If your company wants to contribute to the ongoing consultation of the European Commission, this needs to be done by 31 October 2010. Please feel free to contact us if you want to discuss more details.

ECJ rules on excise duty consignments involving a customs suspension procedure

By Martin Ouwehand

Recently, the European Court of Justice (ECJ) ruled in a case involving products subject to payment of excise duty. Excise duties are (indirect) taxes levied on the consumption or the use of certain products such as (manufactured) tobacco products, alcoholic beverages and mineral oils. The EU excise legislation is laid down in Directives, meaning that all Member States have the obligation to transpose the EU provisions into their national legislation. The initial EU excise legislation dates back to 1993,[1] as a result of the establishment of the Internal Market and includes general provisions, in particular concerning the production, storage and movement between the various Member States. The prejudicial questions put forward by the referring Court in the underlying case — *inter alia* — related to whether or not the product in question needed to be accompanied by an administrative accompanying document (AAD) during transportation.

Per the EU excise legislation, the "main rule" for transportation of excise products for which excise duties have not been paid is that these are accompanied by an AAD, drawn up by the consignor.[2] There are some exceptions to the rule — *inter alia* — for excise products that are coming from third countries and are placed under a customs suspension procedure.[3]

The case: An importer arranged for the importation of raw tobacco into the EU. The product was imported under a customs suspension regime, i.e., inward processing relief, suspension system, for which the importer obtained a customs authorization from the competent authorities. It is important to point out that raw tobacco is not subject to excise duty payment. The raw tobacco was subsequently processed into cut tobacco, the latter being subject to excise duty. Per the customs license, the importer was entitled to use delivery notes to accompany consignments of cut tobacco to other EU Member States. The recipient certified receipt of said delivery notes. At a certain moment, the importer was assessed by the competent customs authorities (Customs) as — according to Customs — the importer had not produced an AAD, certified by the competent authorities in the Member State of receipt. As a result, Customs took the view that the importer had failed to demonstrate delivery/receipt of the goods in the tax warehouse of the recipient. Hence, Customs sought excise duty payment from the importer. The complaints of the importer were rejected by Customs after which the importer challenged the decisions in an action before the competent Court.

[1] Council Directive 92/12/EEC.
[2] Article 18(1) of Council Directive 92/12/EEC.
[3] Article 5(2) of Council Directive 92/12/EEC.

The referring Court decided to stay the national proceedings and referred the following questions to the ECJ for a preliminary ruling:

"Must the first indent of the first subparagraph of Article 5(2) of [Directive 92/12] be interpreted as meaning that non-Community goods subject to excise duty which have been placed under an inward processing procedure within the terms of Article 84(1)(a) of [the Community Customs Code] are to be deemed to be subject to duty-suspension arrangements even if they are produced, under an inward processing procedure, from goods which are not subject to excise duty only after the importation of those goods and therefore, in accordance with the 15th recital in the preamble to Directive 92/12 …, when they are being moved there is no need for the accompanying document referred to in Article 18(1) of Directive 92/12 … to be used?

"If the first question is to be answered in the negative: must Article 15(4) of Directive 92/12 … be interpreted as meaning that proof that the consignee has taken delivery of the goods may also be provided otherwise than by means of the accompanying document referred to in Article 18 of Directive 92/12 …?"

Based on the fact that the Community Customs Code[4] lays down obligations with regard to the supervision and monitoring of the customs suspension regime (and the fact that supervision concerning movement is equivalent to that which results from the requirement of an AAD), the ECJ is of the opinion that the first indent of article 5(2) of Directive 92/12/EEC not only applies to products coming from third countries which are subject to excise duty but also to products such as those at issue in the main proceedings. As a result, the ECJ concludes that there is no need to determine whether such products must also be regarded as products going to third countries, within the meaning of article 5(2) of Directive 92/12/EEC.

In conclusion, products subject to excise duty (e.g., manufactured tobacco) that are manufactured from products not subject to excise duty (e.g., raw tobacco) and imported into the EU under the inward processing relief scheme are to be deemed to be subject to duty suspension arrangements, within the meaning of that provision, even though they have become products subject to excise duty only by virtue of having been processed within EU territory. This means that they can move between Member States without Customs being entitled to insist on production of AAD's or commercial documents. In view of the answer to question 1, the ECJ felt no need to address the second question.

As a side note: At the moment this case was pending (2003), Directive 92/12/EEC was applicable. Due to various developments, a new Council Directive entered into force in 2009[5] which applies across the EU effective April 1, 2010. The "new" Directive also provides a legal framework for the use of the Excise Movement Control System (EMCS), which is applicable from 1 April 2010. EMCS is a computerized system for monitoring movements of excise goods under suspension of excise duty within the EU, i.e., for which no excise duties have yet been paid. EMCS was developed as a result of the high levels of fraud in the Member States and the corresponding loss of national revenues, especially in the field of tobacco and alcohol.

Since April 1, 2010, EMCS replaces "paper" documents with electronic messages (e-AD) from the consignor to the consignee via Member State administrations. The period between 1 April and 31 December 2010 is considered a transition phase but as of January 1, 2011, EMCS becomes compulsory for all relevant movements of excise goods. It is noted that the transport must (still) be accompanied by a printed version of the e-AD or any other commercial document mentioning, in a clearly identifiable manner, the unique administrative reference code assigned by EMCS to the movement.

[4] Regulation (EEC) 2913/92.
[5] Council Directive 2008/118/EC, repealing Directive 92/12/EEC as of April 1, 2010.

EU Tightens Sanctions on Iran

By Erik Zietse, Erik de Bie and Kara Bombach

With the adoption of Council Decision 2010/413/CFSP concerning restrictive measures against Iran, repealing Common Position 2007/140/CFSP, and its publication in the Official Journal of the European Union (EU) on July 27, 2010, the EU imposed new sanctions on Iran. It is anticipated that these sanctions will have an impact on many, if not all, companies doing business with Iran and Iranian companies. Even existing relations and agreements could be impacted.

On June 17, 2010, the European Council underlined its concern about Iran's nuclear program and welcomed the adoption of United Nations Security Council Resolution 1929 (UNSCR 1929). In addition to the measures already imposed under UNSCR 1929, the Council of the EU was invited to implement accompanying measures targeted at the areas of trade, the financial sector, the Iranian transport sector, key sectors in the oil and gas industry and additional designations, in particular for the Islamic Revolutionary Guards Corps.

Following the adoption of these measures, the EU maintains a sanction regime even stricter than the UN sanctions under UNSCR 1929. With this step, the EU joins the United States, which already imposes comprehensive sanctions against U.S. citizens' involvement with Iran or Iranian entities and specifically implements UNSCR 1929, and Canada, which also already imposed similar measures. Given that the EU is Iran's largest trading partner, the new EU sanctions are expected to have a significant impact.

The New Sanctions

The most recent EU sanctions include sanctions in the field of the transfer of products and technology, financial measures, the transport industry and an update of the list of sanctioned persons, entities and bodies. The long list of sanctions includes, amongst others, the following measures:

- Ban on the sale, supply or transfer of key equipment and technology for certain key sectors of the Iranian oil and gas industry, including Iranian and/or Iranian owned enterprises in those sectors outside Iran;
- Ban on the provision of technical assistance or training and other services related to key equipment and technology, as well as financing or financial assistance for any sale, supply transfer or export of key equipment and technology;
- Ban on the direct or indirect supply, sale or transfer of goods and technology included in the list of dual-use items (i.e., items that can also be used for military purposes);
- Restrictions on financing of certain enterprises in the oil and gas industry;
- Restrictions on the transfer of funds to and from Iran;
- Restrictions on the operations of Iranian banks in the EU, including specific limitations on insurance deals;
- Increased inspection of Iranian cargo coming to the EU and going to Iran, including a ban on cargo flights from Iran to the EU; and
- Increased number of persons, entities and bodies subject to sanctions.

The Regulation implementing the new sanctions into EU legislation is expected in September. The lists of sanctioned persons, entities and bodies have already been amended and took effect on July 27. Many companies will be affected by the new sanction regime, including companies that have a longstanding history of business with Iran.

Potential Impact on Current Business

Based on the new sanctions, for example, service providers operating under existing contracts may have to stop providing services involving products that will be subject to the new list of restricted goods, services and technology. Even in situations where contracts existed prior to the sanctions coming into force, activities that are prohibited going forward will not be grandfathered, and must be halted. Additionally, regardless of a particular company's actions to comply with the sanctions, it should be noted that third parties in a transaction, including financial institutions, may take actions to block, freeze, reject or otherwise report the transaction to the EU enforcement Authorities.

New Licensing Requirements

The new provisions will impose certain licensing requirements as well. For example, where a commercial transaction involves anything other than foodstuffs, healthcare, medical equipment or humanitarian donations, and the transaction results in a transfer of funds to and/or from Iran exceeding €40,000, a license from the competent national authorities will be required prior to the transfer. The license application process will take time and companies are strongly recommended to allow sufficient time to obtain the required license prior to actually exporting the products to Iran. In addition, all transactions with a value exceeding €10,000, but not exceeding €40,000, must be reported to the Authorities.

Global Compliance and Enforcement

It is crucial to ensure compliance with the existing and new sanction measures against Iran. Compliance with the EU restrictions against Iran should be part of a global trade compliance program that includes compliance with all relevant laws such as U.S. and Canadian sanctions against Iran. Failure to comply with the sanction measures can have serious consequences for companies and individuals involved and may lead to significant financial damages and potentially even criminal prosecution. It remains to be seen, but we anticipate that with the heightened EU measures, EU authorities may refer, investigate and prosecute matters with U.S. officials related to Iran that run afoul of the various relevant export and sanctions restrictions.

If your company is currently doing business with Iran or considering new business with Iran, it is strongly recommended that you review the impact of both the latest and the previously existing sanctions prior to entering into any agreement or transaction.

VAT aspects combined services and supplies

By Martijn Kouffeld

The supply of services and goods can lead to a wide variety of VAT consequences. Several questions have to be answered. For example, where a service of a supply is considered to take place, whether an exemption is applicable, or what VAT rate must be applied. These questions can be difficult, especially when there is a combination of services and/or goods.

Particularly in the situation that the applicable VAT rates differ or when one or more of the items is VAT exempt it is important to determine the VAT consequences. Incorrect application of the VAT rate can for example lead to additional assessments or denial of the right to deduct input VAT for the buyer.

In case of a combination of supplies it must be determined whether such combination is considered to be a single supply for VAT purposes or not. According to case law of the European Court of Justice, in principle, each activity must be assessed individually, although a combination of services must not be separated artificially. The

leading argument is that the perception of the average consumer determines whether there are several supplies with their own VAT aspects or that the combination leads to a single activity for VAT.

If the conclusion is that there is one single supply, it must be determined which element is leading and thus what VAT rate is applicable. In a recent decision the Court's-Hertogenbosch had to decide on the VAT consequences of the supply of books that included CD-ROMs. Books are VAT taxable at the reduced rate, while on CD-ROMs the standard rate is applicable. The value of the CD-ROM was 15 percent of the total value. According to the tax inspector there were two separate supplies: the book and the CD-ROM. The Court, however, decided that in this case there was only a single supply of a book. The supply of the CD-ROM was not an individual supply as it had no separate meaning.

Another example is the supply of magazines with a novelty included. The novelty is included to make the magazine more attractive and has its own meaning. In such cases, it must be determined what amount of VAT is included in the consumer price. The price must then be split in two, based on the cost price of the individual items.

The conclusion is that when a combination of goods and/or services is supplied it must be carefully determined what the VAT consequences are. Sometimes there will be a single supply for VAT purposes with one applicable VAT rate while in other situations there will be separate supplies with their own VAT aspects.

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This *European VAT, Customs and Trade Alert* was prepared by:

- **Erik de Bie** **+31 (20) 30 17 315** debiee@eu.gtlaw.com
- **Martin Ouwehand** **+31 (20) 30 17 402** ouwehandm@eu.gtlaw.com
- **Martijn Kouffeld** **+31 (20) 30 17 326** kouffeldm@eu.gtlaw.com
- **Erik Zietse** **+31 (20) 30 17 405** zietsee@eu.gtlaw.com
- **Kara Bombach** **202.533.2334** bombachk@gtlaw.com