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Chief Tax Counsel

30 March 2011

Jeffery Owens

Head of Centre for Tax Policy and Administration

Organisation for Economic Co-operation and Development

2, Rue Andre Pascal 75775

Paris, Cedex 75016

France

Re: *Draft Guidelines for VAT Neutrality*

Dear Mr. Owens:

On 22 December 2010 Working Party Number 9 on Consumption Taxes of the Organisation for Economic Co-operation and Development (OECD) released a consultation document setting forth its *Draft Guidelines on Neutrality*. The final document will be incorporated as Chapter 1, Sections 1 and 3 of the *OECD International VAT/GST Guidelines*. As President of Tax Executives Institute, I am pleased to submit the following comments on the consultation document.

Tax Executives Institute

Tax Executives Institute was founded in 1944 to serve the professional needs of business tax professionals. Today the organisation has 54 chapters in North America, Europe and Asia. As the pre-eminent international association of business tax professionals, TEI has a significant interest in promoting tax policy, as well as in the fair and efficient administration of the tax laws, at all levels of government. Our 7,000 members represent 3,000 of the largest companies in the United States, Canada, Europe and Asia.

In 1999, TEI chartered a chapter in Europe, which today encompasses a cross-section of European and multinational companies. TEI members are accountants, lawyers and other corporate and business employees responsible for the tax affairs of their employers in an executive, administrative, or managerial capacity. The Institute espouses organisational values and goals that include integrity, effectiveness and efficiency, and dedication to improving the tax system for the benefit of taxpayers and tax administrators alike.

General Comments

TEI commends the OECD and Working Party Number 9 for the ongoing efforts to develop international VAT/GST guidelines. In today's highly globalised business environment — with many businesses, including

small and medium-sized enterprises and large multinational corporations, engaged in cross-border trade and with more than 150 countries implementing VAT or GST systems — international guidelines are essential. By aligning various countries' tax regime with core principles, both double taxation and unintentional non-taxation can be minimised. As important, administrative and compliance burdens can be eased. Hence we commend the release of the *Draft Guidelines on Neutrality*, and appreciate the opportunity to comment on it.

VAT (or GST) is a transaction-based tax that aims to tax final consumption. The fundamental principle is that the VAT is borne by the final consumer rather than any of the intermediaries in the supply chain. Thus, to the extent businesses are acting as the tax collector on behalf of governments (rather than as a consumer), neutrality is critical.

Overall, TEI believes the draft guidelines represent a significant and important contribution to global tax policy. The adoption and application of the draft guidelines as a whole will promote the neutrality of VAT systems worldwide, thereby minimising the costs to businesses to collect and remit VAT. Hence, we are pleased to support not only the OECD's ongoing work in developing International VAT/GST Guidelines, but also the guidelines on neutrality. They will help protect VAT revenues, increase legal certainty and efficiency, reduce double taxation, avoid unintentional taxation of exempt items (as well as unintentional non-taxation of taxable items), and make VAT/GST systems easier to administer and comply with. Since business and governments are expected to do ever more with ever-fewer resources, this is critical.

Comments on the Guidelines

Specific comments in respect of the draft guidelines are, as follows:

Guideline 1: The burden of value added taxes themselves should not lie on taxable businesses except where explicitly provided for in legislation.

Comment: Paragraph 16 of the draft neutrality guidelines explain that the words “except where explicitly provided” were added in the 2006 guidelines to permit countries to place a value added tax burden on business for specific policy reasons and in limited circumstances. As examples, the 2006 guidelines cite “transactions made by businesses [that] are exempt because the tax base of the outputs is difficult to assess (i.e., many financial services) or for policy reasons (health care, education, culture).” The draft neutrality guidelines explain that any “imposition of value added tax on business should be *clear and explicit* within the legislative framework for the tax.” (Emphasis added.) TEI concurs. VAT legislation should ensure that taxable businesses do not unintentionally suffer the cost of the VAT; moreover, compliance requirements (and, hence, business costs) should be reasonable and proportionate, especially requirements relating to tax recovery mechanisms including documentation of input tax deductions (or credits in an invoice credit system).

Guideline 2: Businesses in similar situations carrying out similar transactions should be subject to similar levels of taxation.

Comment: Again, TEI concurs. Discriminatory taxes must be avoided. Businesses carrying out similar transactions should be treated equally and the means of delivery of the same

(or substantially the same) items should not affect the level of tax applied. Where an item is taxed at a higher (or lower) level because it is delivered through different means (*e.g.*, electronically vs. physically), purchasing decisions are affected and competition is distorted.

Guideline 3: VAT rules should be framed in such a way that they are not the primary influence on business decisions.

Comment: TEI agrees generally with the thrust of the guideline. Ideally, business operating decisions should be based on commercial drivers rather than tax considerations. Paragraph 18 of the draft guidelines explains that a number of factors “can influence business decisions, including financial, commercial, social, environmental and legal factors. Whilst VAT is also a factor that is likely to be considered, it should not be the primary driver for business decisions.” To be more consistent with the tenor of paragraph 18, we suggest revising the guideline slightly. Specifically, we recommend that Guideline 3 state that “VAT rules should be framed in such a way that they *do* ~~are~~ not have a significant ~~the primary~~ influence on business decisions.”

Guideline 4: With respect to the level of taxation, foreign businesses should not be disadvantaged nor advantaged compared to domestic businesses in the jurisdiction where the tax may be due or paid.

Comment: TEI agrees. Discriminatory levels of taxation are a clear barrier to free trade that undermine and distort competition and limit consumer choice. Affected businesses will incur additional costs and burdens and make decisions to overcome or compensate for the discriminatory treatment; such costs will often be borne by the consumer directly or indirectly. Thus, in framing the substantive and administrative tax rules, countries should avoid discriminating against a business based on location.

Guideline 5: To ensure foreign businesses do not incur irrecoverable VAT, governments may choose from a number of approaches.

Comment: Paragraph 27 of the draft guidelines explains that the approaches countries have adopted to avoid irrecoverable VAT include:

- The operation of a system of applying for direct refunds of local VAT incurred;
- Making supplies free of VAT;
- Enabling refunds through local VAT registration;
- Shifting of the responsibility on to locally registered suppliers/customers; and
- The granting of purchase exemption certificates.

As long as the approach — or combination of approaches — selected by a country produces a level playing field for businesses regardless of where they are established, TEI agrees. Consumption taxes incurred in furtherance of business should be recoverable in nearly every

circumstance. Where a government decides as a policy matter to make the tax irrecoverable, the rules should be narrow in scope, clearly defined in the legislation or regulations, and nondiscriminatory in application.

Guideline 6: Where specific administrative requirements for foreign businesses are deemed necessary, they should not create a disproportionate or inappropriate compliance burden for the businesses.

Comment: TEI believes that this should be a guiding principle for *all* forms of taxation — whether consumption, income, or excise tax. Administrative burdens are an added cost and any increase in such costs will affect business decisions. Thus, administrative requirements should never be disproportionate to the tax levied nor should they impose inappropriate or discriminatory burdens. TEI acknowledges, however, that in dealing with foreign businesses with no “legal” presence in a jurisdiction, there is an element of risk for tax administrations and measures may be necessary to protect against VAT fraud or tax avoidance. Paragraph 34 of the draft guidelines properly cautions, however, that “[t]ax administrations should also seek to balance these appropriate measures with the need to prevent unjustified discrimination. In other words, specific rules applicable to foreign businesses should not result in a disguised form of discrimination.”

Conclusion

TEI’s comments on the Draft Guidelines on VAT Neutrality developed by Working Party Number 9 were prepared by the Institute’s European Indirect Tax Committee, whose chair is Jean-Daniel Rouvinez. If you have any questions about TEI’s comments, please contact Mr. Rouvinez at 41 21 729 2993 (or jeandaniel.rouvinez@tetrapak.com), or Jeffery P. Rasmussen of the Institute’s legal staff at 1.202.638.5601 (or jrasmussen@tei.org).

Respectfully submitted,

Tax Executives Institute



Paul O’Connor
International President

INVITATION TO COMMENT ON VAT NEUTRALITY

CONTACT INFORMATION

Contact for follow-up:

Name:

Organisation:

Country:

E-mail address:

Telephone:

Fax:

Please indicate whether you are responding to this questionnaire :

- As an academic or student
- As a corporate taxpayer
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Where you are replying on behalf of others please construe the term "you" to mean "your organisation" or "your clients" as appropriate.

Do you authorize the OECD to publish your contribution on our internet site?

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