EUROPEAN COMMISSION
DIRECTORATE-GENERAL
TAXATION AND CUSTOMS UNION
Indirect Taxation and Tax administration
VAT and other turnover taxes

SUMMARY OF RESULTS

PUBLIC CONSULTATION ON FINANCIAL AND INSURANCE SERVICES

Summary
Public consultation on financial and insurance services

In the period between 14 March and 9 June 2006, DG TAXUD organised a public consultation of business on its intention to modernise the rules for the VAT exemption for financial and insurance services. The consultation was based on a paper which contained views on the current legal framework as set out in the Sixth VAT Directive (Directive 77/388/EEC), and options for change. It explained why there is a need to review Community legislation in this area. In particular, it looked at why there is a need to ensure that it reflects the world as it is today, taking account of the changes that have occurred in the intervening 30 years. This paper was addressed to stakeholders in the financial services industry, including insurance, their professional advisors and indeed to consumers of these services generally. The purpose of consulting the public on this issue was to provide input to the discussion, gather relevant feedback and assist Commission services in developing their thinking on the subject.

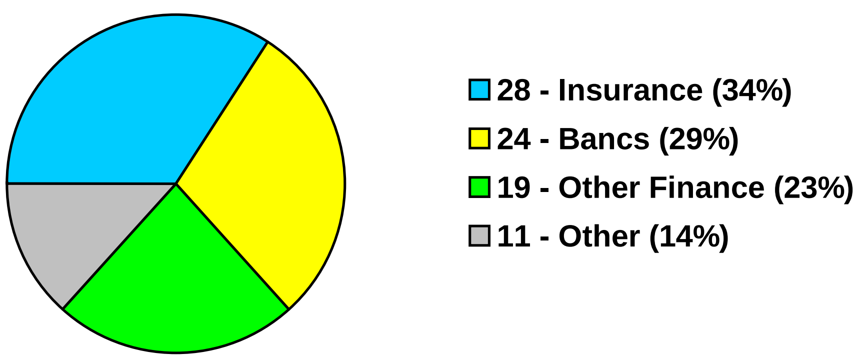
The public consultation was accompanied by a conference on the same subject organised on 11 May 2006 with the intention of familiarising economic operators and administrations with the different technical options available, conveying a realistic picture of what could be achieved by modernisation.

Despite the fact that many contributions were received after the official closing of the consultation period on 9 June 2006 – some of the contributions were only received in August 2006 - DG Taxud evaluated all 82 contributions received. These 82 contributions can be split into four different categories:

28 contributions from the insurance sector;
24 contributions from the banking sector;
19 contributions from the investment sector;
11 contributions from other sectors.

The detailed responses have already been made available to Member States in Working Party 1 on disc. They are now summarised in this paper.

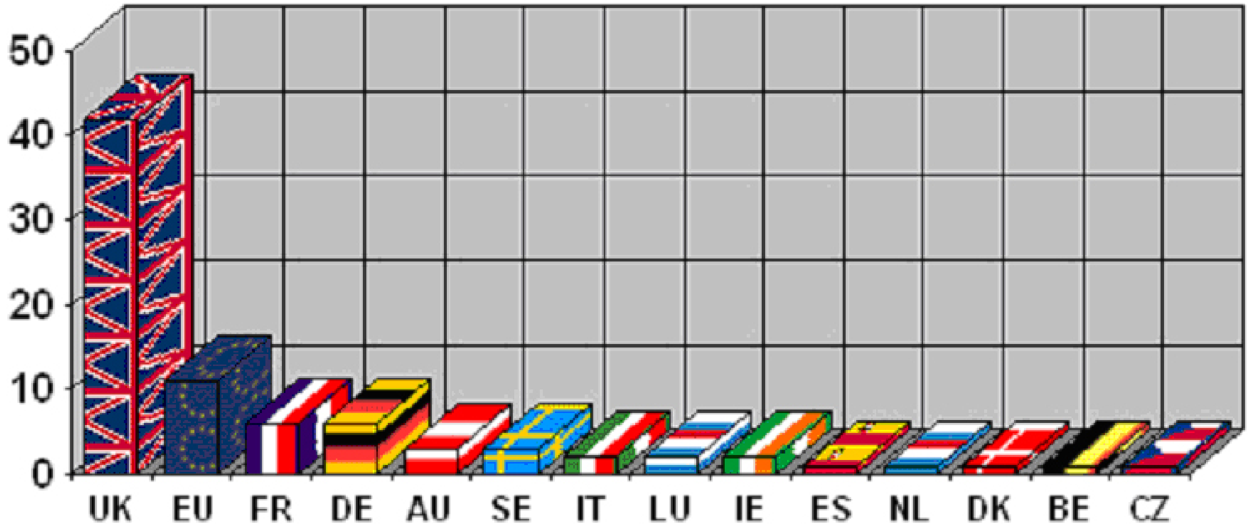
Distribution by sector (Figure 1)



The distribution of the consultations by Member States from which they originate is as follows:

42 contributions from the UK
11 contributions by organisations working at EU level
6 contributions from France
6 contributions from Germany
3 contributions from Austria
3 contributions from Sweden
2 contributions from Italy
2 contributions from Luxemburg
2 contributions from Ireland
1 contribution from Spain
1 contribution from the Netherlands
1 contribution from Denmark
1 contribution from Belgium
1 contribution from the Czech Republic

Notwithstanding the Member State from which they originated, many of the submissions were from organisations with a business presence in several Member States.



GENERAL RESULTS

At a more general level the contributions made by stakeholders in the public consultation on financial and insurance services has lead to three main conclusions:

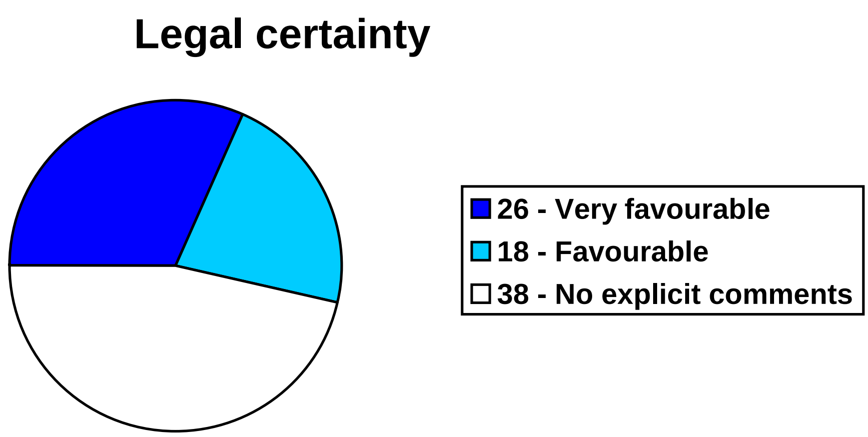
1. Whatever options are chosen for modernising the VAT treatment of financial and insurance services, they should lead to **more legal certainty and clarity** and **reduce the administrative charges** for economic stakeholders.

2. Economic operators from the **insurance sector** **and** those from the **financial** services **sector differ** considerably **in** their **interests**.

3. The **interests** of economic operators **for** "business-to-business" (**B2B**) **supplies differ** considerably **from** their **interests regarding** "business-to-consumer" (**B2C**) **supplies**.

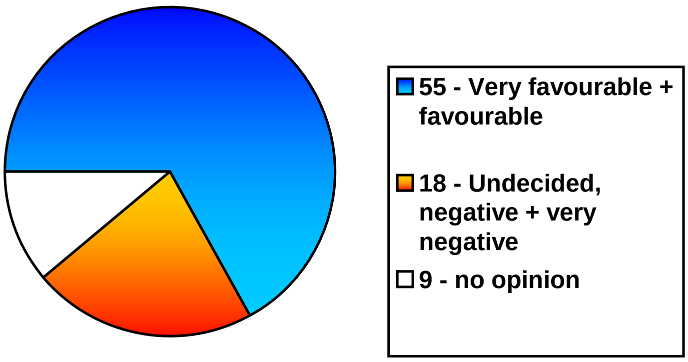
Legal certainty

54% of the stakeholders having taken part in the consultation, have explicitly expressed the need for clarity and the modernising of the vocabulary used for the VAT treatment of financial and insurance services.



Other stakeholders have more implicitly expressed their wish for more legal certainty and clarity by expressing certain choices:

- **67,07%** of stakeholders think that the definitions of exempt financial and insurance services should be extended for covering also outsourced activities. In their view outsourcing is the main problem which should be addressed. For them the modernising of definitions is the key priority.



- On the other hand **none** of the participants in the consultation has expressed a favour for keeping the current provisions as they are. All are of the opinion that modernisation is inevitable.

- **Many** stakeholders expressed that the terminology for exempt financial and insurance services used in the different language versions of the legislation differs substantially and should be aligned.

- A **majority** of stakeholders supports the Commission's suggestion to base the definitions of exempt financial and insurance services on the primary functions of the various services because this would create less future need to adapt the definitions of these services at the level of the 6th VAT Directive.

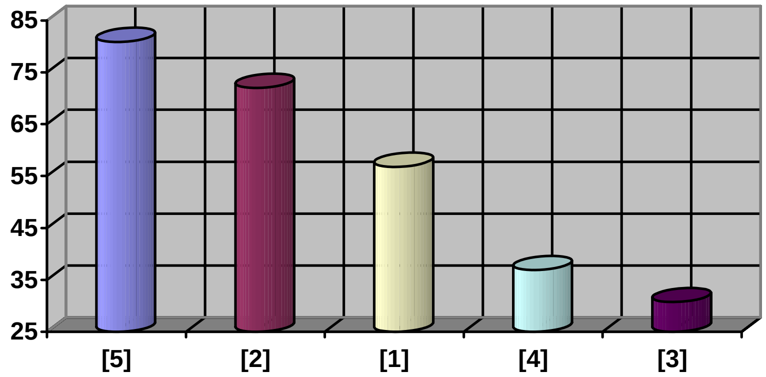
- A **majority** of stakeholders is also of the opinion that more legal certainty will reduce the administrative charges of both, economic operators and administrations. However, there is no clear orientation of stakeholders on whether the definitions should be contained in the 6th Directive only or also in an implementing regulation.

Different interest of Insurances and Banks

The consultation results in the conclusion that the main interests and priorities for the insurance sector differs considerably from those of the banking sector:

Insurance

80,86 %[1]	of the insurance companies see a priority in cross-border groupings **[5]**
71,98 %	of the insurance companies see a priority in the modernising of definitions **[2]**
56,76 %	of the insurance companies see a priority in the introduction of 0-rating **[1]**
36,88 %	of the insurance companies see a priority in an option for taxation **[4]**
30,71 %	of the insurance companies see a priority in the limited input tax deduction **[3]**

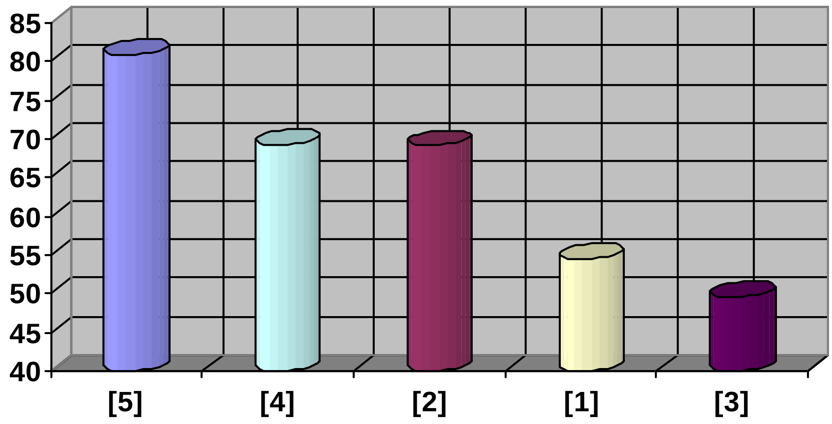


Banking

80,75 %[2]	of the Banks see a priority in cross-border groupings **[5]**
69,29 %	of the Banks see a priority in the option to tax for B2B supplies **[4]**
69,09 %	of the Banks see a priority in the modernising of the definitions **[2]**
54,53 %	of the Banks see a priority in the introduction of 0-rating **[1]**
49,63 %	of the Banks see a priority in the limited input tax deduction **[3]**

[1] These are weighted percentages (M 4) which have been calculated in the following way: In a first step the percentages of very positive and positive opinions of the 82 contributions were calculated (M 1); in a second step the percentages of very positive and positive opinions were calculated on the basis of all opinions expressed (**annex**) (M 2); in a third step coefficients were given to the various opinions: Where "no opinion" was given the coefficient 0, "very negative" the coefficient 1, "negative" the coefficient 2, "divided" the coefficient 3, "positive" the coefficient 4 and "very positive" the coefficient 5 for the purpose of showing the preferences of business operators (M 3); in a fourth and last steps the results of all methods were weighted (M 4) by composing the results and dividing them with 3 ((M1 + M2 + M3)/ 3).

[2] dito



For the option to tax for B2B supplies the difference in the positions between insurances and banks appears to be generated by the fact that Member States apply national insurance premium taxes or other equivalent taxes. The option to tax would in these cases lead to double taxation of insurance premiums. It would also seem that the proportion of B2C supplies is higher in the insurance sector than in the banking sector.

Differences between B2B and B2C supplies

According to the results of the consultation there are economic operators in the sectors concerned by the VAT exemption for financial services and insurances carrying out predominantly B2C supplies. A strong minority of these operators is of the opinion that neither the option of zero rating nor the option for taxation would help in their case and seemingly not bring down their input VAT charges. It would also increase competitive distortions between retailers supplying predominantly B2C and those institutions carrying out predominantly B2B supplies.

These contributions ignore some fundamental elements of VAT taxation:

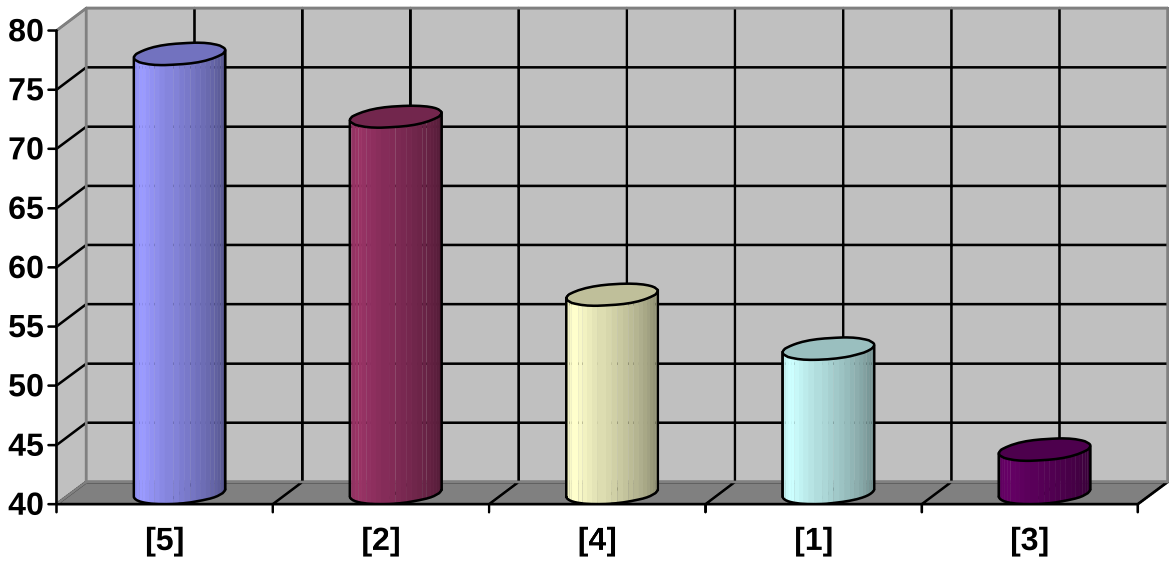
1. For B2C supplies there is no sticking VAT which is routed further down the supply chain. A B2C supply already leads to consumption with non-recoverable VAT incurred by the institution on inputs buried in the cost structure. There is no risk that another VAT is levied on the VAT included in costs routed further down the supply chain. There is thus also no risk of double taxation as there is for B2B supplies.

2. For B2C supplies the non-deductibility of input VAT is already more than compensated by the fact that no VAT is charged on the output margin, the latter usually being higher than the costs.

Result

Against this background, the key interests and priorities of the economic sector concerned as expressed in the consultation can be summarised as follows:

77,08 %[3]	of economic stakeholders see a priority in cross-border groupings **[5]**
71,78 %	of economic stakeholders see a priority in the modernising of definitions **[2]**
56,75 %	of economic stakeholders see a priority in the option to tax B2B supplies **[4]**
52,20 %	of economic stakeholders see a priority in the introduction of 0-rating **[1]**
43,67 %	of economic stakeholders see a priority in limited input tax deduction **[3]**

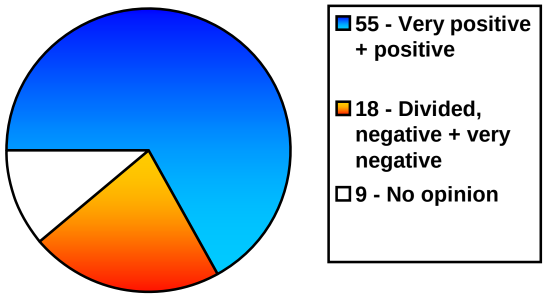


[3] dito

DETAILED RESULTS[4]

Modernising of definitions

67,07% of the participants in the consultation are in favour of modernising the definitions of exempt financial and insurance services:



Very positive: 36
Positive: 19
Divided: 10
Negative: 5
Very negative: 3
No opinion: 9

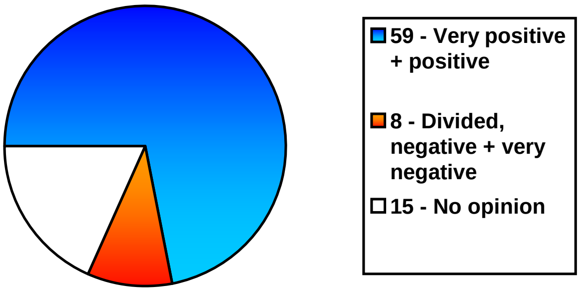
Most of the economic operators consulted, are in favour of modernising the definitions of exempt financial and insurance services in a way which reflects more the reality of commercial transactions in this area. This should also include outsourced services where they are vital to the business. Modernisation should also take account of other legislation (Directives or Regulations) which have been adopted by the Community in modernising the general regulatory environment for the business sectors concerned. Commercial decisions should not depend on fiscal (VAT) considerations. Modernising should also not lead to the transfer of problems to another level; the operators concerned stress the need for legal certainty. They are also of the opinion that possible budgetary losses at micro-economic level would be more than compensated at the macro-economic level. Another priority should be the long-term viability of VAT treatment of financial and insurance services. Many of the contributions also insist on the need to identify criteria which limit the application of the exemptions and prevent an extensive interpretation. It is also suggested to base definitions on the nature of the service, adopting the approach suggested by the SDC judgement of the European Court of Justice. Most of the economic operators are aware hat the modernising of definitions will not be able to resolve the outsourcing problem completely.

The Commission services conclude from these contributions that the modernising of definitions of exempt financial and insurance services is a priority.

[4] For the purpose of showing straightforward tendencies, the simple percentages of opinions are shown

Cross-border grouping vehicles

71,95% of the participants in the consultation are in favour of creating cross-border vehicles for VAT purposes:



No opinion: 15
Very positive: 37
Positive: 22
Divided: 4
Negative: 3
Very negative: 1

This is the element most wanted by the economic operators but also the most difficult to achieve because of Member States having very little experience with such vehicles and are cautious about their implications. Nevertheless for the majority of the economic operators concerned it is the key element of modernisation amongst all other elements.

Many operators mention the different treatment of branching and subsidiary structures. Branches are not independent persons. Consequently, supplies made between head-offices and branches are ignored for VAT purposes. This would also apply to supplies carried out within a "Societas Europaea" (SE). On the other hand subsidiaries are independent taxable persons and therefore supplies carried out between subsidiary and parent company will generally be taxable supplies. In many cases this leads to a more favourable tax (VAT) treatment for branch structures, favouring businesses which grow organically over those who grow through acquisition. Cross-border grouping vehicles would create a level playing field between branch and subsidiary structures.

A majority of operators is of the opinion that the creation of cross-border vehicles is the most important and efficient element to minimise unintended sticking tax (non-deductible VAT) which creates competitive issues for businesses. Cross-border co-operation between operators has reached a critical mass in some areas already, such as in the area of funds, where the main hubs in Luxemburg and Ireland have reached capacity limits which require cross-border co-operation. It would appear to the Commission that this development is confirmed by the increasing number of Member States introducing national grouping provisions under Article 11 of Council Directive 2006/112/EEC, the absence of which seems to have negative implications for inward investment.

In that context a majority of the operators is of the opinion that such cross-border vehicles would resolve some of the outsourcing problems and problems associated with shared cost centres which could not be resolved by the modernising the definitions only.

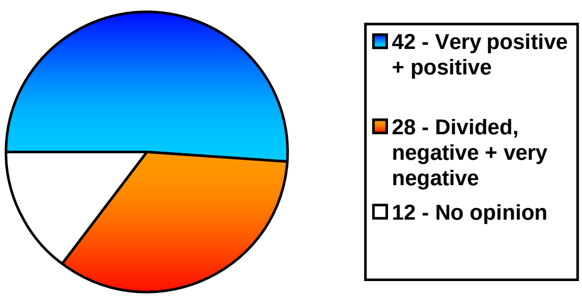
Some operators also note that the creation of cross-border vehicles at EU-level would have the advantage of a more harmonised application of grouping provisions and reduce their consultancy costs for complying with the various and different grouping provisions applied in several Member States and create more legal certainty and clarity. It would also give economic operators more flexibility in reacting at an organisational level to competitive pressures and thus finally strengthen the competitiveness of the European banking and insurance landscape as intended by the objectives of the Lisbon agenda. They also point out that the Commission and Member States are committed (through the Financial Services Action Plan) to encouraging consolidation in the industry and that facilitating grouping would be consistent with this objective.

Some operators add that the question of introducing cross-border vehicles can probably not be separated from the option to tax.

The Commission services conclude from these contributions that the introduction of cross-border vehicles is another priority for the Commission's work.

<u>Option to tax for B2B supplies</u>

It results from the consultation that 51,22% of the consulted economic operators are in favour of an option to tax for B2B supplies:



No opinion: 12
Very positive: 10
Positive: 32
Divided: 11
Negative: 14
Very negative: 3

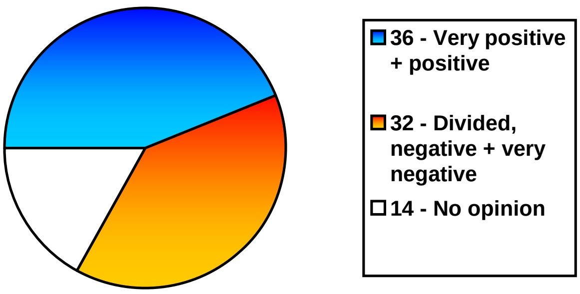
A majority of economic operators is of the opinion that the option to tax should be applied to financial as well as to insurance services; however, they realise that some Member States will be probably unwilling to do so, because they apply national insurance premium taxes already at national level. The option for insurances would lead to double-taxation. As they see it, the option should be with the economic operator and not with the Member State. This would give the industry the necessary flexibility to reduce the "sticking tax" (non-deductibility of VAT) in certain areas.

A key point in the opinion of the economic operators concerned will be whether the administrative charges for operators and fiscal administration can be contained within acceptable parameters which do not adversely affect the positive effects of applying the option. Some operators realise that the option to tax might be necessary to realise cross-border vehicles because economically such vehicles only make sense for taxable financial and insurance services which will lead in turn to maximising the VAT recovery opportunities and thus more neutrality in cross-border activities.

The Commission services agree that there is a link between the option to tax and cross-border vehicles and conclude from these contributions that the option to tax should be analysed in the framework of creating cross-border vehicles, even though this probably maximises the likelihood of revenue losses for Member States and may constitute a significant constraint on the range of realistic options.

Zero-rating

It results from the consultation that 43,90% of the consulted economic operators are in favour of zero-rating financial and insurance services:



No opinion: 14
Very positive: 19
Positive: 17
Divided: 19
Negative: 12
Very negative: 1

Most do not however consider the introduction of zero rating as a realistic option. It carries the benefit of simplicity at first sight, reducing the impact of sticking tax (non deductible VAT) through enhanced recovery as well as reducing the administrative compliance costs. The reduced tax bill for the industry is however a negative budgetary result for Member States who will be most reluctant to accept such a consequence.

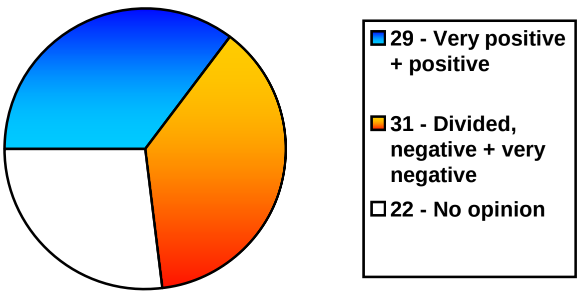
The operators also agree that such a solution would be inconsistent with the fundamental principles of VAT and in particular with the principle of neutrality. It would in fact create substantial competitive distortions between financial and insurance operators on one side and "normal" businesses on the other side which are difficult to justify.

Another point of criticism is that operators would be obliged to differentiate permanently and obligatorily between business clients and final consumers, which for some of them would be virtually impossible.

The Commission services conclude from these contributions that the introduction of zero rating is not a realistic option.

Limited input tax deduction

It results from the consultation that 35,37% of the consulted economic operators are in favour of granting a limited input tax deductibility:



No opinion: 22
Very positive: 11
Positive: 18
Divided: 9
Negative: 18
Very negative: 4

Most of the consulted economic operators are of the opinion that this approach would bring more disadvantages than advantages. The general view is that the business sectors concerned are so diverse that this approach would not be favourable to this Community industry. (Example: Labour costs vary so greatly across the Community that it would be impossible to determine common recovery percentages that accurately reflect payroll costs.) The fact that this model is operated in Australia and Singapore does not necessarily mean that it will work in Europe because the environment is not really comparable. Because of these differences the operators consider it almost impossible to agree on a common base for deduction of input VAT. In addition such a system would favour certain sectors like risk capital markets and create considerable competitive distortions. The creation of several different uniform amounts for various different sectors would render the system unmanageable.

Another disadvantage of this solution would be that it does not really resolve the outsourcing problem, because its vector of application is too narrow.
In the view of the consulted economic operators the implementing and managing of such a system would generate high administrative costs and these costs would not justified by a significant gain in legal certainty. In fact there would be a need for updating the system constantly and in the book-keeping of the economic operators there would be a need to distinguish between scenarios which benefit from that deduction and those which cannot. The operators are also of the opinion that this approach is not very consistent with the overall system of the 6th VAT Directive. They say that if this approach is pursued at all by the Commission services they would rather prefer the introduction of other methods for calculating the pro-rata under Articles 173-175 of Council Directive 2006/112/EEC.

The Commission services conclude from these contributions that the introduction of a standard or limited input tax deduction is not a priority.

Annex

Country / Region	0-rating (B2B)	clarify exemptions	Input credit	B2B option to tax	VAT bodies	update defintion
Austria						☺
United Kingdom	☺	😐	☺☺	☺☺	☺	
United Kingdom	☹	☹☹	☺☺	☹	☹	
Spain				☺	☺	
United Kingdom	☺	☺	☺	☹	☺	☺☺
France	☺☺	☺	😐	☹		
Europe	☺	☺	☺	😐	☺☺	☺☺
United Kingdom	😐	☺☺	☹☹	☹	☺☺	☺
France	😐	☺☺			☺☺	☺☺
United Kingdom	☹☹	😐	😐	😐	😐	☺☺
Germany	☺☺	☺☺	☺	☺	☺☺	☺☺
Germany	☹	☺☺	☺☺	☹	☺☺	
France	☹	😐	☹	☺☺	☺☺	☺
France	😐	☺			☺☺	
United Kingdom	☺☺	☺	😐	😐	☺	
Netherlands	☺	☹	☹	☺☺		
United Kingdom		☺☺				
Europe	☺☺	☺☺	☺	☺	☺	
United Kingdom		☺☺		☺	☺☺	
Europe	☺	☺☺	☹	☺	☺☺	☺
Europe			☺☺		☺☺	☺☺
United Kingdom	😐	😐	☹	😐	☺	
Sweden	😐	😐	😐	😐	☺	☺☺
Austria				☺☺		☺☺
United Kingdom	☺	☺☺	☺	☺	☺☺	
Europe	☺☺	☺	☺☺			☺☺
United Kingdom	☹	☺☺	☹	☹	☺	☺
Germany	☺	☺☺	☹	☺	☺☺	
United Kingdom	☺	☺	☹	☹	☺	
Germany	☺	☹☹	☹	☹	☹	
Germany	☺☺	😐	☺	☹	☹	
Italy	☺	☺		☺		
United Kingdom	☺	😐	☹	😐	☺	☺☺
United Kingdom		☺		☺	☺☺	☺☺

United Kingdom	😐	☺☺	☹☹	☺	☺☺	☺☺
United Kingdom		☺☺			☺☺	☺☺
United Kingdom	☺☺	☹	☹☹	☺	☺	☺
Europe	😐	☺☺	☺☺	☹	☹☹	
United Kingdom	☺☺	☺	☹	☺	😐	
United Kingdom	☺☺	☺	☺☺	😐	😐	
Ireland	☺☺	☺	☺	☹☹	☺☺	
United Kingdom	☺☺	☺	😐	😐		
United Kingdom	☹	☺	😐	☺	☺	
Europe	😐	😐	😐	☺	☺☺	
Europe	😐	☺☺	☹	☺	☺☺	
United Kingdom	😐	☺☺		☺☺	☺	
Luxembourg	😐	☺☺	☹	☺	☺☺	
Ireland	😐	☺☺	☺☺	☺	☺☺	
United Kingdom	☹	☺☺		☹	☺☺	
Luxembourg	☹	☺☺	☺	☺	☺☺	
United Kingdom	☺☺	☺☺	☺	☺	☺☺	
United Kingdom	☺☺	☹☹	☹☹	😐	☺	
United Kingdom	☹	☺☺	☺	☺	☺	
United Kingdom		☺☺				
Germany	☺☺	☺☺	☺	☹	☺	
United Kingdom	☹	☺☺	☺☺	☹	☺☺	
Europe	😐	☺☺	😐	☺☺	☺☺	
France	😐	☺☺		☺	☺	
Austria		☺	☺☺	☺	☺	
Belgium	☺	☺☺		☺☺	☺☺	
Denmark	☹	☺	☹	☺	☺☺	
United Kingdom				☺☺		
Europe	😐	☺	😐	☺	☺	
Europe	☺	☺☺			☺☺	
Czech Republic				☺☺	☺☺	
Sweden	☺☺	☺	☺	☺		
United Kingdom	☺	😐	☹	☺	☺	
United Kingdom						
United Kingdom				☺☺		

United Kingdom	☺☺	☺☺	☺	☺	☺	
United Kingdom	☺	😐	☹	☺	☺☺	
United Kingdom	😐	☺☺	☺	☺	☺☺	
Sweden	☺☺					
United Kingdom	😐	☹	☹	☹☹	☺☺	
United Kingdom	☺☺	☺	☹	😐	☺☺	
Italy	☺	☺☺	☺	☺	☺☺	
United Kingdom	😐	☺☺	☺	😐	☺	
United Kingdom	☺	☺☺	☺	☺	☺☺	
United Kingdom	☺☺	☺☺	☺	☺	☺☺	
United Kingdom	☹	☹	☺☺	☹	😐	
United Kingdom	☹	☹	☹	☹☹	☺☺	
France	☹	☺☺				