

*The following is a translation of a letter sent from the Confederation of Swedish Enterprise to the Swedish Tax Agency on 26 December 2013. The original letter is available online on:*  
[http://www.svensktnaringsliv.se/multimedia/archive/00034/Stora\\_brister\\_i\\_SKV\\_34917a.pdf](http://www.svensktnaringsliv.se/multimedia/archive/00034/Stora_brister_i_SKV_34917a.pdf)

## Major shortcomings in the guidance and practice regarding the distinction between single and composite supplies

Should a toy enclosed in the supply of a meal be taxed separately at a 25 % VAT rate or should it be deemed ancillary to the supplied meal and be taxed at the 12 % VAT rate for food? Should the supply of a spare part used in a repair be treated as a separate supply of a good or as ancillary to the repair service? Is the lunch served as a part of a conference arrangement to be taxed at the 12 % reduced VAT rate for food or at the 25 % standard VAT rate as for the conference arrangement?

### Summary

VAT is often considered one of the most complex and burdensome taxes for business to deal with. Over the years, the VAT system has grown increasingly difficult to understand and to handle for business as well as tax authorities and courts. One of the most complex issues is how to assess transactions consisting of several elements. For the purpose of VAT, one must determine whether a transaction consisting of several elements is to be deemed one single supply or two or more distinct supplies. In case the transaction is deemed one single supply, one must characterize the supply for the purpose of identifying the correct VAT treatment.

Although this is one of the most important issues concerning VAT, neither the Swedish VAT Act nor the VAT Directive provides any guiding provisions in this respect. Instead, business is dependent on guidance from the Swedish Tax Agency and the courts. Case law from the Swedish courts and the ECJ and a large number of statements from the Swedish Tax Agency has been filling this gap in the legislation. Unfortunately, the case law and statements lacks coherence.

We have done a survey of statements and references to case law regarding single or composite supplies made by the Tax Agency in its VAT Manual for 2012. Overall, it is impossible to discern any clear guidelines and criteria for how the assessment should be made for determining if a transaction consist of only one supply or not. The assessments in the numerous statements and court cases are based on inconsistent criteria and the outcome seems to be more or less random. Often, the assessment is based on outdated Swedish case law which has not been tested against the current EU law. In some cases, the assessment lack sufficient reasoning, leading to different outcomes for similar transactions and to different treatment for different industries. These shortcomings put the practice by the Swedish Tax Agency in conflict with EU law. Also, they increase the already high administrative and material burden that the VAT system entails on business. The Swedish Tax Agency must overcome these problems and provide uniform guidance and practise in accordance with the EU law.

Furthermore, we believe that there may be reason to revise the VAT Directive with regard to the treatment of supplies consisting of several elements. This would facilitate the application of the VAT Directive in this respect and reduce unnecessary administrative burdens for business. As a part of the work on the future VAT system within the European Union, this issue has been brought to the attention of the European Commission by Confederation of Swedish Enterprise as well as BUSINESSEUROPE.

The main aim of this letter is to alert the Tax Authorities on the urgent need for clear and coherent guidance, such as a test or at least a clarification of criteria to take into account in the assessment. Such clarification would increase predictability and lead to a more uniform practice.

Furthermore, this letter aims to summarize and highlight the shortcomings of current guidance and practice. Urgent measures in order to deal with these shortcomings on a national level as well as a European Union level are thus needed.

## Background

The VAT is often considered one of the most complex and burdensome taxes to deal with. The EU harmonized VAT systems is among the most difficult set of rules and entails the heaviest administrative burdens on business, in both Swedish and European measurements. Unlike the income tax, VAT is a consumption tax and not a tax on enterprise. Enterprises are merely an unpaid tax collector for the authorities, which is reason enough to require VAT to be easy to understand, manage and administer. This has unfortunately not been the case. Over the years, the VAT system has grown increasingly difficult to understand and to handle for business as well as tax authorities and courts.

One of the most complex issues of VAT compliance is how to treat transactions consisting of several elements. A transaction which comprises several elements may, for the purposes of VAT, either be regarded as a single supply or as two or more distinct supplies to be assessed separately. This distinction is decisive for VAT treatment, for example when determining applicable VAT rates or the place of supply. If the transaction is deemed a single supply, an exemption, a VAT rate or a place of supply provision is applicable for the whole transaction. The distinction between single or composite supplies is also decisive when determining whether a special provision is applicable, such as the reversed charge mechanism for the construction sector. In case the transaction is deemed one single supply, one must characterize the supply for the purpose of identifying the correct VAT treatment.

Even though this is one of the most important issues in VAT context, neither the Swedish VAT Act (SFS 1994:200) nor the VAT Directive (2006/112/EEG) provides any guiding provisions in this respect. Instead, business is dependent on guidance from the Swedish Tax Agency and the courts. Case law from the Swedish courts and the European Court of Justice (ECJ) and a large number of statements from the Swedish Tax Agency has been filling the gap in the legislation. However, the case law and statements lack coherence. We also see that these shortcomings are passed on to the administrative courts in Sweden.

A statement from the Swedish Tax Agency (dnr: 131 729629-10/111, of the 13<sup>th</sup> of December 2010) explains the meaning of the principle of rule of law, the principle of fiscal

neutrality, the principle of equal treatment and the principle of proportionality as follows [*our translation*].

Within the EU law, there are various general legal principles – principles of interpretation – such as the principle of rule of law, the principle of fiscal neutrality, the principle of equal treatment and the principle of proportionality. Often, these principles occupy a superior position and can best be characterized as primary legislation. These general principles generally aim to protect the rights of individual's.

The principle of equal treatment establishes that comparable situations must not be treated differently unless there are factual reasons for a diverse treatment. (215/85, Balm, p. 23)

The principle of fiscal neutrality protects free market competition and establishes that all economic activity should be taxed in a neutral manner. This principle aims to stop diverse VAT treatment between similar, and therefore competing, situations. (C-216/97, Gregg, p. 20)

The Swedish Tax Administration makes, conscious or unconscious, choices about which statements and case law to pick and refer to in the Tax Agency's VAT Manual for 2012. We have done a survey of statements and references to case law regarding single or composite supplies made by the Tax Agency in its VAT Manual for 2012. We have found that there is not only a lack of coherent guidance, but also contradictory and outdated statements. The lack of uniform guidance and practice results in non-compliance with the union law and its fundamental principles to which the Swedish Tax Administration itself refers to. These shortcomings increase the already high administrative burden that the VAT system entails.

## EU law

As mentioned above, neither the Swedish VAT Act nor the VAT Directive provides any guiding provisions in the regard of single or composite supplies. However, the issue has been subject to a large number of judgments from the ECJ (for instance in cases C-349/96, C-497/09, C-499/09, C-501/09, C-502/09 etc.). The Supreme Administrative Court in Sweden recently summarized the ECJ case law as follows [*our translation*].

Firstly, an overall assessment of the circumstances characterizing the transaction in question must be made in order to determine whether there are two or more distinct supplies or one single supply. The Court has also held that every transaction must normally be regarded as distinct and independent and that a transaction which comprises a single supply from an economic point of view should not be artificially split, so as not to distort the functioning of the VAT system. There is a single supply where two or more elements or acts supplied are so closely linked that they form, objectively, a single, indivisible economic supply, which it would be artificial to split. There is also a single supply where one or more elements are to be regarded as constituting the principal supply, while other elements are to be regarded, by contrast, as one or more ancillary supplies which share the tax treatment of the principal supply. In particular, a supply must be regarded as ancillary to a principal supply if it does not constitute for customers an end in itself but a means of better enjoying the principal service supplied.

In our study, we have noticed a number of references to the ECJ case law in the Swedish Tax Agency's statements and guidance. However, the Swedish Tax Administration has failed in taking essential steps to update statements and references in this regard. Contrary, our observation shows a remarkable number of references to old Swedish case law, leaving business with unnecessary ambiguity and inconsistencies.

Furthermore, we believe that there may be reason to revise the VAT Directive with regard to the treatment of supplies consisting of several elements. This would facilitate the application of the VAT Directive in this respect and reduce unnecessary administrative burdens for business. As a part of the work on the future VAT system within the European Union, this issue has been brought to the attention of the European Commission by Confederation of Swedish Enterprise as well as BUSINESSEUROPE.

## Survey of the treatment of single or composite supplies in the Swedish Tax Agency's Manual for 2012

Appendix 1 to this letter contains a study of more than 120 statements and references to case law regarding single or composite supplies found in the Swedish Tax Agency's Manual for 2012. Our survey of these statements and references to case law has been done in order to clarify and comprehend the considerations made. We have identified the following issues.

### Obsolete references

A large number of statements contain references to obsolete case law; some even refer to case law from the time before the Swedish membership in the EU. In the light of the development of the ECJ case law, we find such obsolete statements seriously questionable.

### Lack of reasoning

Often, there is an inadequate reasoning regarding the factors that have been taken into account in the considerations made (e.g. contracts, price, working hours, cost of material, cost of labour, etc.). Complex issues are often assessed by sweeping and insufficient reasoning and omission of details of importance. A sweeping explanation is common, leaving room for suspicions that a certain tax result has been the aim. All this on the expense of equal treatment.

### Lack of a test

There is no general test based on the EU law for how to assess whether a transaction that consist of two or more elements is to be deemed one single supply or composite supplies. We have, however, found some practical methods regarding certain goods of certain services, e.g. for supply of a magazine and good in one package.

### Diverse treatments for different industries

Swedish preparatory legal documents, statements of the Swedish Tax Agency and Swedish case law gives the impression that certain kinds of transactions always should be treated as one single supply. For example, this is the case for construction services. Furthermore, the fact that the reversed charge mechanism applies for construction services seems to contribute to a tendency to deem the service element (rather than the supply of goods) the principal element of the construction transaction, and thus apply the reversed charge mechanism on all elements in the transaction. The presumption in practice seems to be that the whole transaction is to be deemed a service and not a supply of good. It could be argued

that this view simplifies the application of the reversed charge provisions for construction services, but the compliance of this view is highly questionable. On the other hand, for the real estate sector the tendency seems to be the opposite. Instead of assuming that the transaction is a single supply, two distinct supplies are often considered to be at hand. An example is leasing of property combined with a franchise agreement; such a supply is most often considered as two different supplies for the purpose of VAT.

#### Diverse treatment for comparable transactions

In the study, we have noticed that a number of similar transactions have been treated differently. On the one hand, both school lunch and food and accommodation supplied at a dormitory in a boarding school have been deemed ancillary to the exempt education service. On the other hand, food and accommodation served at a riding camp (which is considered a sport activity and subject to the reduced 6 % VAT rate) was not deemed ancillary to the sporting activity and thus tax at the normal VAT rate. Another example is hotel services (VAT rate 12 %), where breakfast have been separated and taxed at the standard 25 % VAT rate. When the VAT rate on restaurant and catering services was reduced from 25 % to 12 %, the tendency to separate food from other services seems to have changed. Instead, the Swedish Tax Administration now considers food supplied in conjunction with conference arrangements (VAT rate 25 %) subordinate the conference arrangement.

Overall, it is impossible to discern any clear guidelines and criteria for how the assessment should be made for determining if a transaction consist of only one supply or not. The assessments in the numerous statements and court cases are based on inconsistent criteria and the outcome seems to be more or less random. Often, the assessments are based on outdated Swedish case law which has not been tested against the current EU law. In some cases, the assessments lack sufficient reasoning, leading to different outcomes for similar transactions and to different treatment for different industries. These shortcomings put the practice by the Swedish Tax Agency in conflict with EU law. Also, they increase the already high administrative and material burden that the VAT system entails on business. The Swedish Tax Agency must overcome these problems and provide uniform guidance and practise in accordance with the EU law.

## Survey of the treatment on single or composite supplies in EU, Norway and Switzerland

VAT is a harmonized tax within the EU, thus a survey of the treatment of single or composite supplies in the Europe is of interest. Ernst & Young AB have, on behalf of The Confederation of Swedish Enterprise, made a survey on the treatment of single or composite supplies in EU member states, Norway, and Switzerland (see appendix 2-3).

In summary, the survey shows that no general and uniform practise regarding the treatment of single or composite supplies exist within the EU, Norway or Switzerland. Numerous countries have no or very little national legislation, guidance or case law in this regard. Many countries rely on ECJ rulings. Countries with an established and general guidance often build there legislation on principles established by the ECJ. Several countries apply an assessment based on percentage of the price. This means that a composite supply of goods and services is deemed a supply of goods if the price of the good exceeds a certain proportion of the total price. The rates do however vary significantly between countries, from 33 % (Greece and Spain) and 50 % (Belgium and Austria) to 67 % (Ireland).

We believe that a general test similar to the UK practise is interesting and deserves further study. There are publically available guidelines from UK as a result of the ECJ ruling in C-349/96.

## Conclusions

The Swedish Tax Agency must address the major shortcomings that currently exist in the guidance regarding the treatment of single or composite supplies and apply a uniform practise based on ECJ case law.

The main aim of this letter is to alert the Tax Agency on the urgent need for clear and coherent guidance, such as a test or at least a clarification of criterions to take into account in the assessment. Such clarification would increase predictability and a lead to a more uniform practise.

Furthermore, this letter aims to summarize and highlight the shortcomings of current guidance and practice. Urgent measures in order to deal with these shortcomings on a national level as well as an EU level are thus needed.

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**Annex 1** Survey: VAT Treatment of Single or Composite Supplies in the Swedish Tax Agency's Manual, 2012 (available in Swedish only)

**Annex 2** E&Y Pan-European Survey: Questionnaire - VAT treatment of composite supplies

**Annex 3** Ernst & Young Pan-European Survey: VAT treatment of composite supplies