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**EBF and E&Y examine models for an optional application of VAT
on financial services**

Satya Poddar, who designed in the 1990s a theoretical model aimed at applying VAT to financial services is back with a report on 'Design and Impact of the Option to Tax System for Application of VAT to financial services', published today by Ernst & Young (E&Y) at the request of the European Banking Federation (EBF).

The EBF invited the recognised industry expert from the audit and consulting firm Ernst & Young to conduct a study investigating into the possible variants of a system providing financial institutions with discretion to apply VAT on financial services.

"In the 90s, we had not supported the Poddar model, because it was technically too sophisticated. Ten years on, we thought it interesting to ask Mr Poddar to have a fresh look at the possible modalities of an option to tax as envisaged in the European Commission's proposed Directive", said Guido Ravoet, Secretary General of the EBF.

Since 2006, the EU has indeed been working on a three-pillar reform of the VAT treatment of financial services. The reform first includes an update of the definitions of exempt financial services, aimed at increasing legal certainty. In addition, two complementary solutions aim to address the economic distortions caused by the blockage of input VAT inherent to the exemption, which leads to cascading of the tax.

One of these two solutions would consist of an option to tax, which would allow VAT to be added to financial services, thus permitting the recovery of any related VAT expenses. This solution would prevent irrevocable VAT from flowing into the supply chain, thus reducing the negative consequences of the exemption system.

So far, Member States have the discretion to take up the option to tax. The proposal is to move this discretion from the Member States to the financial institutions. So far the European Commission has however left a number of questions unanswered.

The Report is a thorough analysis of the possible combinations for an option to tax, addressing all the open questions.

"Amid the possible combinations, European banks remain in favour of a very straight-forward system to be applied on a transaction-by-transaction basis, but we would be ready to support zero-rating of B2B transactions in a wider and more radical overhaul of the way VAT is applied to financial services", Guido Ravoet said.

Contacts

European Banking Federation
Fédération Bancaire Européenne (aisbl)
10 rue Montoyer B- 1000 Brussels

Guido Ravoet, Secretary General
+32 (0)2 508 37 26
Florence Ranson, Communications Adviser
+32 (0)2 508 37 34 f.ranson@ebf-fbe.eu

Note to the Editor

Set up in 1960, the European Banking Federation is the voice of the European banking sector (EU and EFTA countries). The EBF represents the interests of some 5000 European banks: large and small, wholesale and retail, local and cross-border financial institutions