

VAT Working Party for Tax Questions
Council Secretariat
LEX Building Rue de la Loi 145
1048 Brussels

Brussels, 9 November 2010

Dear Madam,
Dear Sir,

Re.: Proposed Council Directive and Regulation for the VAT Treatment of Insurance and Financial Services

As the representative of the European factoring and commercial finance industry, the EUF once more wishes to comment on the further changes to proposed Council Directive and Regulation amending Directive 2006/112/EC in respect of the VAT Treatment of Insurance and Financial Services. We last wrote to you on 25 November 2009 and to assist you we attach a further copy of that letter.

In particular we wish to focus on the terminology, explanations and interpretation set out in the Council documents 13577/10 FISC 92 and 13578/10 FISC 93, both dated 16th of September 2010.

FISC 93

This document attempts to explain in detail the mechanisms of factoring and its VAT treatment. The purpose and benefit as well as the main features and constituent elements of factoring are examined according to the views of the Spanish Presidency. At the same time examples of factoring situations have been provided. This document also presents a compromise legal text for the proposed amended Directive and Regulations with specific comments regarding factoring.

Document FISC 93 attempts to give a short yet concise and all-encompassing overview of factoring in Europe. This concept is welcome in principle. Unfortunately, the resulting document contains a number of serious inaccuracies about both the theory and practice of factoring.

We would like to draw your attention to a selection of the more serious errors:

- Generally, factoring and invoice discounting are applied in B2B-relations. We therefore suggest that the examples given should better reflect B2B situations.
- The use of the terminology of “factoring with recourse” and “factoring without recourse” is not used correctly and consistently.



- Other legal concepts are not stated correctly (e.g. "cession" instead of "assignment").
- We also strongly suggest that the Council cease using the terms "true factoring" and "quasi-factoring". These are never used either in commercial practice or in legal documents and not understood in the EU market place nor in most legal jurisdictions. The correct and readily understood phrases are "recourse factoring", "non-recourse factoring" "recourse invoice discounting" and "non-recourse invoice discounting".
- The factor's client, as the assignor, is generally charged a "factoring fee" as the consideration for the composite financial service provided by the factor, which can include the assumption of the risk of debtor default (as in non recourse agreements) as well as the administration and management of account receivables and debtors. In practice, one notes the difficulty of equating which elements of charges correspond to which elements of services.
- Factoring services are not limited to the "recovery" of the receivables assigned, but cover a wide range of administrative and credit management services to the client. The very word "recovery" may also be misleading, as it assumes that every receivable assigned is bad or doubtful. In reality, the majority of debts assigned are not overdue and involve credit-worthy debtors. The debt management process, whether by the factor's administrative actions or through legal proceedings in respect of overdue debts, is only one of the activities performed by a factor and usually not the principal one. It is therefore more accurate to refer to the "management" of debts instead of their "recovery".
- Factoring without recourse is not an insurance service, as wrongly stated in FISC 93. It involves the assignment and purchase of receivables which are not features of any insurance contract. Even though the factor, as purchaser, accepts liability to pay the purchase price, whatever the position of the debtor, this does not turn the purchase into an insurance contract. This also reflects the legal classification of factoring in the EU member states. Therefore, factoring should not be mentioned in the context of insurance and reinsurance services, especially not in Art. 2 para. 1 (j) of the proposed Regulation, as shown on page 9 of FISC 93.
- Factoring and invoice discounting cannot simply be treated as agreements for the granting of credit. In some countries agreements do not contain any provisions for pre-payment. The legal approaches to qualify this service vary considerably from one country to another and have automatic consequences on the legal forms of factoring companies.

As you can see, factoring and invoice discounting are complex sui generis and unique products, which cannot be equated to just one of their alleged components which are inextricably linked to create a single indivisible economic supply. . This is in line with the most recent VAT decision of the ECJ: In case C-175/09 (AXA UK PLC v Her Majesty's Customs and Excise re Denplan), the ECJ stated that:

"in certain circumstances, several formally distinct services, which could be supplied in isolation and thus give rise, separately, to taxation or exemption, must be considered to be a single transaction when they are not independent. This is particularly true where two or more elements or acts supplied by the taxable person to the customer are so closely linked that they form, objectively, a single, indivisible economic supply, which it would be artificial to split."

Until now, the implementation of the VAT regime in respect factoring and invoice discounting transactions in accordance with the VAT Directive appears satisfactory amongst most EU Member States, although we recognise that in some countries uncertainties remain about its interpretation.

If the above inaccuracies are followed then there will be unexpected EU wide consequences on both the legal and fiscal front.

EUF's viewpoint and proposal

In our letter dated 25th of November 2009, which we attach for your information and convenience, we presented you with an overview of what factoring as a financial service comprises. Moreover, we referred to certain points in the proposed texts with regard to the VAT-treatment of factoring. In response to the working document from the Presidency numbered 7889/09 and dated March 20th 2009 and 13055/09 dated September 9th 2009, we outlined our analysis and suggestions for clarification and improvement. We regret to note that our suggestions have not been accepted and endorsed.

We repeat the suggestions in our letter of 25 November 2009 and submit that our approach therein has merit.

We believe that any modification to the current VAT regime should take into account and clarify any possible uncertainties that still remain in some EU-member states, thus creating a level playing field for all factoring and invoice discounting companies in the EU. Any modification of the current status quo must take into account that factoring and invoice discounting are sui generis products comprising single and indivisible supplies. Its constituent elements are so closely linked that only a single service is provided for VAT-purposes.

The EUF therefore restates its opinion that if there is to be a change in the status quo then the correct approach in the revised Directive and Regulations should be::

1. To correct any unclear definitions and concepts capable of misinterpretation. In particular the use of the phrases "true factoring" and "quasi-factoring" must be abandoned and replaced by recourse and non-recourse factoring and invoice discounting.
2. To abandon the artificial fragmentation of the constituent elements of the single services of factoring and invoice discounting, which should be treated as a single indivisible supply.
3. To mention in the Regulation factoring and invoice discounting activities as examples typically included in the definition of exempt services provided by art. 135 of the Directive provided that at the same time Article 137 of the Directive gives an option, directly to the financial institution, to tax such exempt supplies. The result will then be that all charges and fees relating to factoring and invoice discounting can, at the option of the financial institution, ultimately be subjected to VAT. This was included in an earlier draft of Article 137 in COM/2007/747-Final which stated that:

From 1 December 2012 Member States shall allow taxable persons a right to opt for taxation in respect of the services referred to in points (a) to (g) of Article 135(1)

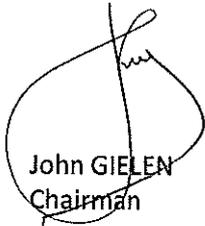
This would harmonise the VAT regime throughout the EU without the intervention of Member States.



Any different approach, especially if not built upon a correct and widely accepted description of the factoring and invoice discounting services, will damage the industry, affect the competitive position between EU factoring companies negatively and hence deprive many SMEs of a vital simple and well established method of financing their daily working capital needs.. Should these changes not be possible, then the EUF would prefer to retain the current situation in the European VAT regimes for factoring.

Please do not hesitate to contact us should you require further explanations of our viewpoints, be it in written form or through a personal meeting.

Yours sincerely



John GIELEN
Chairman