# VAT treatment of gambling etc for off-shore operators

by **Dario Garcia**

In this article we conduct a review of the VAT treatment for gambling and the revenue protection measures available to Member States in the EU and in particular the approach adopted by the UK. We finish off with a short speculation on what Brexit might mean (perhaps not that much).

## EU Law

This is found primarily in Council Directive 2006/112/EC (the VAT Directive) and Regulation 282/2001/EU on VAT ("the VAT Regulation").

Article 135.1(i) provides for the exemption of

"Betting, lotteries and other forms of gambling, subject to the conditions and limitations laid down by each Member State;"

The apparently very wide discretion allowed to Member States to limit the scope of exemption (limited only implicitly by the obligation on each Member State to respect the general principles of EU law, in particular prevention of distortion of competition) coupled with the unlimited freedom allowed Member States to impose other gaming and gambling duties, makes the gambling sector possibly the least harmonised of any in the EU.

Notwithstanding the close fraternal relationship between EU Member States, each remains extremely jealous of its own tax base. Each is keenly aware of the threat posed to its tax base by cross border shopping, within and outside the EU, particularly in the digital age which in many sectors has made this strikingly easy. One such sector is the online gambling market.

EU law allows a surprising degree of national protection in a supposedly single market, particularly in the field of electronically supplied services. A consideration of the nature and effect of these protectionist measures, particularly as they affect the gambling sector, is therefore necessary.

## Place of supply: electronically supplied services

Article 2.1(c) of the Directive subjects to VAT:

"The supply of services for consideration within a Member State…"

Where a supply takes place is therefore fundamental in determining the proper VAT jurisdiction. Not surprisingly, there are detailed rules for determining this. We are focusing on gambling, so it will be assumed that the consumer is a private individual acting as such.

In such a case (business to consumer) or ("B2C") the basic rule respects the "origin" principle. Accordingly Article 45 of the Directive provides:

"The place of supply of services to a non taxable person shall be the place where the supplier has established his business…"

Application of such a rule encourages EU private consumers to shop in no or low VAT jurisdictions since if they do so at home they naturally suffer a permanent VAT cost. The easier it is to "VAT shop" the more damage will be done to both domestic operators and national exchequers.

Cross border shopping for digitally available services, like betting and gaming (but also such services as telecoms and broadcasting) present no real barriers. Little surprise then that the basic origin principle (Article 45) in the case of such services is replaced on a general basis by the "destination" principle. Accordingly Article 58 provides that the place of supply of "electronically supplied services" to non taxable persons (i.e. private consumers) is where the consumer is

"established, has his permanent address and residence or usually resides…"

Article 59a of the VAT Directives gives a discretion to Member States if application of the Article 58 destination rule leads to the place of supply being outside (not inside) the EU, for example because the consumer resides in a third country. If the Service is actually used and enjoyed in a Member State, then to that extent, the supply may be pulled into that Member State. The UK has exercised this discretionary power for certain services, including electronically supplied ones.

Let us return to what may be caught as an "electronically supplied service".

Annex II of the VAT Directive provides that it

"includes games of chance and gambling games…"

That does not mean that such gambling and games are always electronically supplied. The EU VAT Committee is of the view that not all distance gambling is necessarily electronically supplied.

It has to be remembered of course that the jurisdiction to the tax at the country of destination (Article 58) or of use and enjoyment (Article 59a), is of little consequence unless the gambling is removed from the scope of exemption. As has been seen, the exemption is particularly elastic, so Member States have moved to tax certain betting and gaming, including (not surprisingly in view of the protectionist policy drivers) by reference to whether it is supplied electronically. In the UK exemption remains in place, even if electronic supply is made.

### Is the gambling electronically supplied

The VAT Regulation provides more detailed guidance on implementation of the VAT Directive and provides at its Article 7.1 that

"Electronically supplied services [are] essentially automated and involving minimal human intervention…"

It follows that if human intervention is more than minimal and where the process is not automatic, then the service is not electronically supplied. The destination principle will not then apply so that the origin one (in Article 45) of the Directive remains in place. It follows then that where a gambling service is not electronically supplied, the place of supply remains where the operator is located so that the incentive to go VAT shopping remains.

Application of the electronic supply criterim is not itself without difficulty. It has, for example, been argued that fixed odds betting is not an automated process and requires significant human intervention.

It is quite unrealistic to expect detailed legislative/regulatory provisions of a binding nature to be promulgated to secure harmony at an EU level. The most that can realistically be hoped for is guidance from the EU VAT committee. However, whilst the EU Committee may give such guidance in due course, this is, at its highest, only ever of persuasive authority: it is not binding. Resolving the question requires a technical evaluation, itself allowing a degree of appreciation and so inevitably a difference in approach. Given also the margin of discretion allowed to Member States in the scope of exemption, there will remain differences in application between Member States. Test cases may be taken to the Court of Justice of the European Union (ECJ) but it should be remembered that the Court can only go so far as to lay down the principles of general application in determining the degree of discretion available to Member States and the right approach to its exercise. Matters of detailed factual and technical evaluation will be left to national courts. The decision of a Member State national court does not bind another Member State.

It will be remembered that for both non electronically supplied services and ones which are so supplied, including gambling, Member States have a power under Article 59(a) of the Directive to relocate the place of supply of services if that would otherwise be outside the EU. The relocation takes the

supply to where it is "effectively used and enjoyed" by consumers in the Member State. Of course, this only has any point if the gambling is not exempt in the particular Member State in question, but in that regards one comes back to the wide measure of national discretion given.

In concluding this part of our discussion it may therefore be concluded that in terms of the VAT liability treatment of gambling services, the road to anything like EU harmonisation is likely to be long and difficult, with no certainty as to what would be at its end.

### Other Issues

There are other issues which merit consideration:

- The measure of taxable turnover;
- Other applications of the use and enjoyment relocation technique;
- Compliance/registration issues.
- We take each of these in turn.

### Taxable Turnover

The orthodox view is for a gross profits basis of assessment. This requires VAT (where it is due) to be paid not on nominal receipts (i.e. total stakes) but rather on such receipts less winnings, where there is a legal obligation to pay them out.

There is EU case law, guidance (from the EU VAT Committee) and, in the case of the UK, national guidance from HMRC (VAT Notice 701/29).

In *Town and County Factors Limited*, Case C-498/99 the ECJ found that the taxable turnover for the organiser of the UK "Spot the Ball" competition was the full amount received, without deduction of prize money paid out. This was, however, on the basis that there was no legal obligation to pay out such prizes, the operator being bound in honour only. The operator therefore, as a matter of law, had the full amount of entry fees freely at its disposal so that the full fee was to be regarded as the consideration.

In contrast, in its earlier decision in *H J Glawe Spiel*, Case 38/93, the ECJ had found differently. In Germany the operator of gaming machines was legally obliged (by statute), through the internal mechanism of the gaming machine, to pay out a certain proportion of receipts as winnings and keep them separate in the machine until paid out. The operator's taxable turnover was found to exclude winnings paid out.

The majority view of the EU VAT Committee is that the two decisions can be reconciled on the basis that a legal obligation to pay prizes (statutory or contractual) is sufficient for their exclusion from the taxable amount. UK HMRC guidance advances the same treatment.

### Use and Enjoyment

Mention has already been made of this tax base protection measure, available under Article 59(a) of the Directive, in specified factual circumstances. This measure also extends to services supplied business to business (B2B), where they are supplied from an EU business to a non EU business recipient.

Let us say that, for example, an offshore (outside EU) gaming operator supplies gambling services (electronic or otherwise) to a UK payer. To attract other customers it will buy UK advertising services. The basic rule for B2B services is not the origin principle (i.e. taxation in the country where the supplier belongs) but the "destination" principle (i.e. tax in the country where the gambling operator belongs): Article 44 of the VAT Directive. This would mean, where the offshore destination country has no VAT, that the advertising will be obtained VAT free. If the gambling operator were located in the UK, it would have to pay VAT which, because gambling is generally exempt in the UK, would represent a permanent cost to the operator (as irrecoverable input VAT).

The UK can under Article 59(a) (as it has signalled it may do) alter the basis for taxation of services supplied to offshore operators by substituting the destination principle for an effective use and enjoyment one. The UK could then say that the offshore operator itself uses and enjoys UK provided advertising services in the UK so that the advertising provider will be required to charge UK VAT.

The use and enjoyment relocation facility can be applied to most services made to a non EU business customer. However, the use and enjoyment test, being a factual one (so in principle to be determined by national courts, not the ECJ), is not without difficulty (so allowing for a considerable degree of variation in application). Again, an operator offering its services in various countries could advertise through its sponsorship of a major sporting event in one country only, which would televised in all its markets. Plainly the advertising service in used in all those markets even

though the event takes place in one of them only. An apportionment would be expected, though the basis for that is not determined under EU law so that effectively each Member State is in competition for a share of the VAT revenue with no binding basis for apportionment on EU wide basis being in place, and no Member State being bound by the decisions of the Courts in another.

### Compliance

In principle, a gambling operator would have to register for VAT in each country in which it has private consumers, unless of course that country exempts the gambling in question. That requirement presents a considerable compliance burden. This can be somewhat mitigated by the One Stop Shop ("OSS") registration facility. Put simply, this allows registration in one Member State only, through which VAT for each other Member State is collected (at the rate in each such Member State) and accounted for to the host country. The OSS host Member State then passes the VAT collected to the other Member States via a clearing/settlement system to be operated by the EU. The operator still has to deal with various VAT rates and have in place auditable systems to ensure proper accounting and linkage of customers to the right country.

### Brexit

As has been explained, the rules at EU level are somewhat elastic: they allow considerable latitude for Member States in terms of the scope of exemption for betting/gambling and in taking measures to protect national VAT revenues.

EU law also allows national gambling taxes, Brexit itself therefore has no indications for UK national policy in this regard.

As a matter of national policy, the UK has applied the VAT exemption very widely: Group 4 of Schedule 9 to the VAT Act 1994 provides for exemption, without limitation, of

"The provision of any facilities for the placing of bets or the playing of any games of chance for a prize".

Brexit itself has no discernable impact on this policy, but neither did EU membership. The UK has signalled that it may apply "use and enjoyment" measures to ensure taxation of services provided to offshore gambling operators but, again, Brexit itself is unlikely to impact this policy, though the UK could extend its effect to EU based operators. This will of course depend on the UK's relationship with the single market following Brexit.

One clear implication for Brexit will be that the UK will not be able to host the OSS registration for an offshore operator. They will therefore have to find another Member State home in the EU and register the OSS there.

### Conclusions

The landscape is complex. At present EU law allows for significant diversions of approach in Member States, particularly as to the scope for exemption and also for protectionist supply relocation measures to safeguard national revenues. The broad range of discretions available to Member States mean that harmonisation of the EU market is someway off and, of course, following Brexit the UK is unlikely to be a full member of that market.

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