

The VAT treatment of vouchers: a comparative study between South Africa and the European Union*

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Abstract

For VAT purposes, two issues arise when vouchers are used namely whether the time of supply is when the voucher was issued and imported (in the case of vouchers issued outside the Republic) into South Africa, or, when a voucher is exchanged for goods or services; and, secondly, whether VAT must be accounted for on the discounted amount paid for the voucher or the stated monetary value of the voucher. This article critically examines the VAT treatment of vouchers under the VAT Act (as it currently stands) with reference to the draft Interpretation Note on the VAT treatment of vouchers at a discount. It further analyses the Draft harmonised EU proposals on the VAT treatment of vouchers in the EU with a view to seeking a solution to the current South African uncertainties in respect of the time and value-of-supply rules when vouchers are issued.

INTRODUCTION

In a competitive market, suppliers often reward customers for loyal and continued support by either issuing discount vouchers or adding additional products to the original supply at no cost. These vouchers are often issued electronically in terms of a loyalty scheme. Another modern business phenomenon, is the issuing of prepaid vouchers at a fee generally lower than the stated monetary value of the voucher. These vouchers can be exchanged either for specific predetermined goods or services, or for a range of goods and

* This article is largely based on the author's LLD thesis entitled 'The collection of value added tax on online cross-border trade in digital goods' submitted in fulfilment of the degree of doctor of laws at the University of South Africa.

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services at the choice of the consumer. For VAT purposes, two issues arise when vouchers are used namely, whether the time of supply is when the voucher was issued and imported (in the case of vouchers that were issued outside the Republic) into South Africa, or when the voucher is exchanged for goods or services; and secondly, whether VAT must be accounted for on the discounted amount paid for the voucher or on the monetary value stated on the voucher. Where the South African VAT Act¹ (VAT Act) regulates the treatment of vouchers for VAT purposes, the rules are unclear and cause confusion. Despite the fact that the South African Revenue Services (SARS) has recently issued a draft Interpretation Note on the VAT treatment for determining the value on which VAT must be levied on vouchers, determining the time and value of the supply of vouchers remain uncertain. This is an issue not restricted to South Africa. In the European Union (EU), neither the Sixth Council Directive, nor Council Directive 2002/112/EC provides rules for the treatment of prepaid vouchers, or vouchers entitling the holder to a discount or goods or services at no charge. As a result, EU member states have adopted their own rules which are described by the European Commission as ‘inevitably uncoordinated’.² To address these issues, the European Commission has prepared a draft proposal amending the harmonised VAT rules to provide for time-of-supply and value-of-supply rules in respect of vouchers.³ In this article I critically examine the VAT treatment of vouchers under the VAT Act (as it currently stands) with reference to the draft Interpretation Note on the VAT treatment of vouchers at a discount. This discussion is followed by an analysis of the Draft harmonised EU proposals on the VAT treatment of vouchers in the EU with the main purpose of seeking a solution for the current South African uncertainties.

THE VAT TREATMENT OF VOUCHERS IN SOUTH AFRICA

The time of supply

The general rule governing the time of supply, is either the date of the issuing

¹ Act 89 of 1991.

² Cowly ‘European Commission Review of VAT on Vouchers’ (2012) 25/3 *Irish Tax Review* 97.

³ European Commission *Draft proposal a Council Directive Amending Directive 2006/112/EC on the Common System of Value Added Tax, as Regards the Treatment of Vouchers* (2012) available at: [http://ec.europa.eu/taxation_customs/resources/documents/taxation/vat/key_documents/legislation_proposed/com\(2012\)206_en.pdf](http://ec.europa.eu/taxation_customs/resources/documents/taxation/vat/key_documents/legislation_proposed/com(2012)206_en.pdf) (last accessed 16 October 2012).

of an invoice, or the date of receipt of any payment in respect of the supply, whichever is the earlier.⁴ The required invoice is defined as any document notifying an obligation to make payment.⁵ In other words, it can take the form of any ordinary invoice, creditor's statement, contract, or any other document that notifies the recipient of an unconditional obligation to make payment.⁶ Where payment has been tendered before the issue of an invoice, *any*⁷ payment will trigger the VAT liability on the full amount of the goods or services rendered, unless payment was made in terms of an agreement for successive, or supplies deemed successive,⁸ or, where the payment constitutes a deposit.⁹

The question is whether a voucher constitutes an invoice when it is issued, or, whether payment for the voucher constitutes a returnable deposit until such time that the voucher is exchanged for goods or services? Generally, the issuing of a voucher does not amount to a supply of goods or services, but merely constitutes the issuing of a payment method that can be utilised by the recipient when he chooses.¹⁰ Accordingly, when the voucher is used as payment for goods or services, the time of supply would still be determined by the date of the issuing of an invoice, or the date of any payment for goods or services – whichever is earlier. The VAT Act primarily distinguishes between two types of voucher, namely, vouchers that entitle the holder to unspecified goods or services,¹¹ and vouchers which entitle the holder to specified goods and services.¹²

Vouchers: unspecified goods and services

Where a voucher, stamp, or token (excluding postage stamps) entitles the holder to goods or services to the extent of a monetary value stated on the voucher,

⁴ VAT Act s 9(1).

⁵ *Id* at s 1.

⁶ Silver & Beneke *VAT handbook* (2013) at par 4.4; De Koker & Kruger *VAT in South Africa: commentary* (2013 update) at par 10.2.

⁷ De Koker & Kruger n 6 above at par 10.3.

⁸ VAT Act s 9(3).

⁹ Proviso to the definition of 'consideration' in s 1 of the VAT Act.

¹⁰ 'Money' is excluded from the definitions of 'goods' and 'services' in section 1. Any bill of exchange, promissory note, bank draft, postal order, or money order is deemed to be 'money' in terms of the definition of 'money' in section 1 of the VAT Act.

¹¹ VAT Act s 10(18).

¹² *Id* at s 10(19).

VAT must be accounted for when the holder surrenders the voucher for goods or services.¹³ However, where the amount initially paid for the voucher exceeds its monetary value, VAT must be accounted for when it is purchased.¹⁴ Generally, these vouchers do not reflect a record of whether or not VAT was paid when they were issued. As such, VAT can potentially be levied on the amount initially paid for the voucher when it was issued and on the value of the goods and services when the voucher is redeemed. Unless the voucher is issued by and redeemed at the same institution, group of institutions, or in terms of a voucher scheme of which the institution is a member, the double taxation of the voucher cannot be avoided. This issue is further exacerbated by cross-border trade. For example, where X purchases a voucher from a foreign vendor (in a country that applies the origin principle of taxation¹⁵ online) and later redeems the voucher for goods, the voucher is taxed in the foreign jurisdiction upon issue, and the goods are again taxed in South Africa upon import.

In the case of e-commerce, it is often difficult to verify whether a transaction has occurred. When dealing with software updates, the recipient is often unaware that the electronic device has downloaded software from a local or foreign service provider. Invoices are rarely issued when updates are downloaded. These transactions often stem from a prior agreement with a service provider, seller, or manufacturer of the device, or with the software developer. Depending on the agreement, the recipient either pays a lump sum prior to commencement of the service from which the value of each upgrade or update is then deducted, or, the costs of the updates are deducted from the recipient's credit card account. In the case of a prepaid agreement for which a prepaid voucher has been issued, the payment was not made in respect of a specific service or digitised product.

¹³ *Id* at s 10 (18).

¹⁴ *Ibid.*

¹⁵ In terms of the origin basis, VAT is levied at the consumption level based on the origin of the goods, irrespective of where the goods are finally consumed. This means that imports are not taxed while exports are taxed. This system could be seen to encourage imports as imported goods from low VAT jurisdictions, are placed at an advantage over domestic goods in jurisdictions with a high VAT rate. For a full discussion on the origin principle of taxation see Metcalfe (1995) 'Value added taxation: a tax whose time has come?' (1995) 9/1 *The Journal of Economic Perspectives* at 130; Cnossen 'Design of the value added tax: lessons from experiences' in Khalilzadeh-Shirazi & Shah (eds) *Tax policy in developing countries* (1991) 73; Ebrill *et al The modern VAT* (2001) 179.

Instead, it could be argued that the payment constitutes a mere deposit of money into an account which the supplier may debit upon delivery of services or goods. The time of supply should, accordingly, be construed as the actual date on which the prepaid account is debited. In the absence of account statements or debit notifications, the recipient would be unaware of the time of supply. In many cases, service providers merely inform users of a low account balance. Records of actual transactions are not disclosed to users unless they are requested by the user, often at a fee.

De Koker and Kruger opine that the legal position of conditional contracts should be considered before a document is classified as an invoice.¹⁶ For example, where X and Y conclude an agreement in terms of which X will pay Y R1000 when Y has completed painting X's roof, the obligation to pay is deferred until Y completes the service. The agreement in itself cannot constitute an invoice because it does not reflect an obligation to pay as the obligation it reflects is conditional.¹⁷ Only when the service has been completed (the condition fulfilled), can it be said that the agreement constitutes an invoice.¹⁸

Similarly, where payment has been made in terms of a prepaid agreement for which a prepaid voucher has been issued, the payment has not been made to fulfil an obligation to pay. The recipient of the service could, in principle, cancel the agreement and have his money returned. The supplier would only be entitled to debit the account once it had commenced with service. It could, therefore, be argued that the agreement could constitute an invoice once the condition that would allow the service provider to debit the account, has been fulfilled. The recipient (where the reverse-charge mechanism is applied)¹⁹ is required to request account statements on a regular basis to allow him to determine the time

¹⁶ De Koker & Kruger n 6 above at par 10.2.

¹⁷ *Ibid.*

¹⁸ *Ibid.*

¹⁹ In terms of a reverse-charge mechanism the recipient taxpayer is required to self-invoice and levy VAT on the transaction. This is declared to the revenue authority concerned and VAT is paid to the revenue authority on the basis of the self-declaration. In terms s 14(1) the recipient of imported services must furnish the Commissioner with a VAT return within thirty days of the earliest issuing of an invoice or any payment. For further reading on the reverse-charge mechanism see Lovell *Understanding Vat* (1990) at 54–56; Weidenbaum, Raboy & Christian *The value added tax: orthodoxy and new thinking* (1989) 257–258; Ebrill n 15 above at 139–145.

of supply. The cost of acquiring these statements could in certain cases exceed the actual VAT liability.

Vouchers: specified goods and services

Where, on its surrender, a voucher, stamp, or token entitles the bearer to goods or services specified on the voucher, stamp, or token, the issuing of the voucher, stamp, or token attracts VAT.²⁰ The subsequent surrender of the voucher, stamp, or token attracts no further VAT.²¹ In these case, the voucher, although still a payment method, cannot be equated with money, cheque or, card payment, or an EFT. Since the voucher can only be redeemed for specific pre-determined goods or services from pre-determined suppliers, possible double taxation of the voucher can be avoided.

Value of supply

In terms of the general rule, the value of the goods and services on which VAT is payable is determined by the consideration paid in money, less so much of the value that represents VAT.²² Where the consideration is not a consideration in money, the open market of that consideration applies.²³ Consideration is defined to mean

... any payment made or to be made (including any deposit on any returnable container and tax), whether in money or otherwise, or any act or forbearance, whether or not voluntary, in respect of, in response to, or for the inducement of, the supply of any goods or services, whether by that person or by any other person, but does not include any payment made by any person as a donation to any association not for gain: Provided that a deposit (other than a deposit on a returnable container), whether refundable or not, given in respect of a supply of goods or services shall not be considered as payment made for the supply unless and until the supplier applies the deposit as consideration for the supply or such deposit is forfeited.²⁴

²⁰ VAT Act s 10 (19).

²¹ *Ibid.*

²² Section 10(2) read with s 10(3) of the VAT Act. See also De Koker & Kruger n 6 above at par 11.1; Silver & Beneke n 6 above at par 4.2.1.

²³ VAT Act s 10(3)(b). See also De Koker & Kruger n 6 above at par 11.2; Silver & Beneke n 6 above at par 4.2.1.

²⁴ VAT Act s 1.

In the case of prepaid vouchers where the payment is made in terms of a prepaid service agreement, the payment does not constitute consideration in respect of the said service until such time as the actual service has commenced. Therefore, despite the fact that the full prepaid amount can, in principle, be used to purchase goods or services, the value of the supply can only be determined once the actual supply takes place.

A further question that arises, is what value should be used where payment is made by a voucher issued by the supplier or by a third party – such as a credit card company – in terms of a loyalty scheme? In determining the value of the supply for VAT purposes, the VAT Act distinguishes between two types of voucher, namely, vouchers that entitle the holder to unspecified goods or services,²⁵ and vouchers which entitle the holder to specified goods and services.²⁶

Vouchers: unspecified goods or services

The supply of vouchers which entitle the holder to goods or services of his choice upon redemption, is not a supply as contemplated in section 7(1)(a), but is regarded as a medium of exchange similar to money.²⁷ VAT is, therefore, not levied on the intrinsic value of the voucher, but rather on the monetary value of the goods or services for which the voucher may be redeemed. Since the nature and the value of the future goods or services cannot be determined when the voucher is issued, VAT cannot be levied on the value of the voucher in terms of section 7(1)(a) when the voucher is issued.²⁸

However, where the voucher was issued for consideration exceeding the intrinsic monetary value of the voucher, the issuing vendor must account for VAT on the consideration that exceeds the intrinsic monetary value of the voucher.²⁹ This is in accordance with the principle of VAT as a tax on value added.

²⁵ *Id* at s 10(18).

²⁶ *Id* at s 10(19).

²⁷ SARS *Draft Interpretation Note: Vouchers supplied at a discount* (2012) at 2.

²⁸ *Ibid.*

²⁹ VAT Act s 10(18).

Vouchers: specified goods or services

In the case of vouchers that entitle the holder to specified goods or services, the value and nature of the supply can be determined when the voucher is issued. The issuing vendor is therefore able to determine the value of the supplies at the time of issue and to levy VAT in terms of section 7(1)(a). Therefore, in these cases, the consideration paid for the voucher constitutes the value of the voucher on which VAT must be levied.³⁰ The value of the goods or services that are subsequently supplied when the voucher is redeemed, is deemed to be zero.³¹ This applies irrespective of whether the value of the goods or services has increased by the time that the voucher is redeemed. In these cases, because of circumstances beyond the control of the issuing vendor, it cannot be said that the voucher was issued at a discount or discounted value.

Vouchers: issued at a discount

It is common for vendors to issue vouchers to customers at a discounted price while the voucher still entitles the customer to goods and services equal to, or in excess of, the intrinsic value of the voucher. In the case of vouchers for unspecified goods, the vendor must account for VAT on the value of the goods or services supplied upon redemption of the voucher, and not on the consideration paid for the voucher. This potentially leaves the issuing vendor out of pocket. For example, X issues a voucher to Y for which Y pays R90. In terms of the voucher, Y is entitled to goods to the value of R100. X must account for VAT on R100 (that is $R100 \times 14/114 = R12,28$) being the value of the goods for which Y has redeemed the voucher. However, X only received R90 consideration.

Generally, the VAT Act provides that where an unconditional discount has been granted, the supplier need only account for VAT on the gross amount of the supplies less discount (*ie* the amount in money received).³² However, as the voucher is regarded as a payment method rather than a supply, the vendor must account for VAT on the intrinsic monetary value of the voucher and not the amount in consideration that was paid for the voucher.

³⁰ *Id* at s 10(19).

³¹ SARS n 27 above at 2.

³² VAT Act s 10(3)(a).

Section 21(1) provides that the vendor may make certain adjustments to rectify the incorrect levying of VAT in respect of taxable supplies. These adjustments must, however, be evidenced by a debit or credit note issued in accordance with section 21(3). SARS points out that the supply of a voucher at a discount/discounted value does not constitute the rectifying of the incorrect levying of VAT in respect of a taxable supply of goods or services made by the vendor.³³ Therefore, the issuing vendor would not be entitled to an input VAT deduction on the amount of discount granted.

This results in an unfair differentiation between vendors who supply goods and services at a discount, and vendors who supply vouchers at a discount. Vendors who supply their goods and services by issuing a voucher at a discount would be financially worse off than vendors who discount the supply of goods or services directly. This said, where the voucher is only partially redeemed, the issuing vendor is still required to account for VAT on the value of the goods and services only. SARS notes that the part of the monetary value of the voucher that was not redeemed, but has either been paid out in cash or forfeited, does not attract VAT.³⁴ However, where the balance of the voucher is carried over, the vendor must account for VAT on the value of any subsequent supplies of goods and services upon redemption of the balance carried over. For example: X issues a voucher to Y with a stated monetary value of R500 but charges him only R450. Y tenders the voucher for goods or services to the value of R430. The balance of R70 is paid out in cash. X does not account for VAT on the amount of consideration (R450) received for the voucher. X cannot claim an input VAT deduction for the R50 discount on the voucher. X must account for VAT on the value of the goods and services rendered ($R430 \times 14/114 = R52.81$). The balance of R70 paid out in cash, has no VAT consequences.

Vouchers: issued by third parties

It is a common modern retail phenomenon for third parties to issue vouchers that may be tendered as payment or partial payment for the supply of goods and services by retailers. These vouchers should be distinguished from vouchers

³³ SARS n 27 above at 3.

³⁴ *Id* at 4.

which entitle the holder to a stated discount upon redemption of the voucher.³⁵

Typically, a third party supplies a voucher with a stated monetary value to a customer at a discounted price. The voucher may be redeemed for goods or services from any participating retailer vendor. The retailer vendor thereafter claims a reimbursement of the total monetary value of the voucher. The issuing third party is not required to levy VAT on the monetary value of the voucher.³⁶ For the reasons discussed above, the issuing vendor would not be entitled to claim an input VAT deduction for any discount granted on the voucher. Since the voucher is deemed to be a payment method, the retailer vendor must account for VAT on the value of the goods and services supplied. When the retailer vendor applies for reimbursement of the monetary value from the issuing third party, it does not constitute a supply in terms of section 7(1)(a).³⁷ Therefore, the reimbursement does not attract VAT.³⁸ However, where the retailer redeems the voucher for reimbursement, the issuer of the voucher would, in terms of section 16(3)(i), be entitled to claim notional input VAT on the monetary value expressed on the voucher.³⁹

Discount vouchers

Where vouchers which entitle the holder to a discount on specific purchases are issued for no consideration, the consideration paid for the goods or services so supplied is deemed to include the monetary value/discount awarded stated on the voucher, token, or stamp.⁴⁰ The monetary value is further deemed to include VAT.⁴¹ The redemption of the voucher by the retailer constitutes a financial service as defined in section 1, and does not attract VAT.⁴²

What if a voucher was issued for no consideration, but it entitles the holder to goods or services at a 100 per cent discount? In other words, a free voucher is

³⁵ See 'Discount vouchers' below.

³⁶ VAT Act s 10(18).

³⁷ Section 12(a) read with s 2(1)(c) of the VAT Act.

³⁸ SARS n 27 above at 5.

³⁹ Editorial 'Claiming VAT on discount vouchers' 2009 Nov/Dec *The Professional Accountant* 26; Silver & Beneke n 6 above at par 10.9.5.

⁴⁰ VAT Act s 10(20).

⁴¹ *Ibid.*

⁴² Editorial n 39 above at 26.

issued which entitles the user to free specified goods and services. As no consideration was paid when the voucher was issued, no VAT can be levied.⁴³ However, where the supplier and the recipient are connected persons, the open market value is generally used where no consideration is paid, or where the consideration paid is less than the open market value.⁴⁴ In the case where it cannot be established that the supplier and the recipient are connected persons, it is uncertain whether section 14(3) will prevail over section 10(3). In other words, can the open market value be applied in the case of the supply of goods or services upon redemption of a voucher for which no consideration has been paid and where the parties are not connected persons? Can it be said that a voucher issued to a loyal customer in terms of a loyalty scheme, connotes a transaction between connected persons? It should be noted that the provision in

⁴³ VAT Act s 10(19).

⁴⁴ Section 10(4)(a) and (b) of the VAT Act: ‘Connected persons are defined in section 1 as (a) any natural person (including the estate of a natural person if such person is deceased or insolvent) and – (i) any relative of that natural person (being a relative as defined in section 1 of the Income Tax Act) or the estate of any such relative if the relative is deceased or insolvent; or (ii) any trust fund in respect of which any such relative or such estate of such relative is or may be a beneficiary; or (b) any trust fund and any person who is or may be a beneficiary in respect of that fund; or (c) any partnership or close corporation and – (i) any member thereof; or (ii) any other person where that person and a member of such partnership or close corporation, as the case may be, are connected persons in terms of this definition; or (d) any company (other than a close corporation) and – (i) any person (other than a company) where that person, his spouse or minor child or any trust fund in respect of which that person, his spouse or minor child is or may be a beneficiary, is separately interested or two or more of them are in the aggregate interested in 10 per cent or more of the company’s paid-up capital or 10 per cent or more of the company’s equity share capital (as defined in section 1 of the Income Tax Act) or 10 per cent or more of the voting rights of the shareholders of the company, whether directly or indirectly; or (ii) any other company the shareholders in which (being shareholders as contemplated in the definition of “shareholder” in section 1 of the Income Tax Act) are substantially the same persons as the shareholders in the first-mentioned company, or which is controlled by the same persons who control the first-mentioned company; or (iii) any person where that person and the person referred to in subparagraph (i) or his spouse or minor child or the trust fund referred to in that subparagraph or the other company referred to in subparagraph (ii) are connected persons in terms of this definition; or (e) any separate enterprise, branch or division of a vendor which is separately registered as a vendor under the provisions of section 50 and any other such enterprise, branch or division of the vendor; or (f) any branch, division or separate enterprise of an association not for gain which is deemed by subsection (5) of section 23 to be a separate person for the purposes of that section and any other branch, division or separate enterprise of that association, whether or not such other branch, division or separate enterprise is a vendor; or (g) any person and any superannuation scheme referred to in section 2 (2) (vii), the members of which are mainly the employees or office holders or former employees or office holders of that person.’

section 10(3) is essentially an anti-avoidance provision. It is aimed at combating transactions entered into at a cost lower than market value with the intention of avoiding VAT or donations tax. In my view, the relationship between the issuing vendor and the customer is not one of connected persons as defined. As a result, where the supplier delivers goods or services to the recipient at no cost, and the parties are not connected persons, the transaction should be treated as a gift. This means that the value for VAT purposes should be nil.

Where a voucher issued for no consideration entitles the holder to goods and services equal to a monetary value as specified on the voucher, the issuing vendor will not levy VAT on the monetary value of the voucher on issue.⁴⁵ However, VAT must be levied on the total value of the goods and services supplied to the customer upon redemption of the voucher. For the reasons explained above, the issuing vendor would not be entitled to claim an input VAT deduction on the value of the discount (in this case the monetary value of the voucher) irrespective of whether the voucher was issued in terms of a loyalty scheme or as a *bona fide* gift. It therefore appears that the most beneficial VAT treatment of the transaction can be ensured where vouchers issued in terms of a loyalty scheme entitle the holder to specified free goods and services, as opposed to unspecified goods and services equal to a stated monetary value.

THE VAT TREATMENT OF VOUCHERS IN THE EUROPEAN UNION

Time of supply

In terms of the Sixth Directive, VAT becomes chargeable when the tax authority becomes entitled to claim tax from the person liable to pay, notwithstanding that the time of payment may be deferred.⁴⁶ The chargeable event occurs when the goods are delivered, or once the services have commenced.⁴⁷ Where payment has been received before the goods are delivered or the services performed, the chargeable event occurs when such payment is made.⁴⁸ Member states were

⁴⁵ VAT Act s 10(18).

⁴⁶ Article 10(1) of the Sixth Directive 77/388/EEC; also see re-casted version in article 62 of the Council Directive 2006/112/EC.

⁴⁷ Article 10(2) of the Sixth Directive 77/388/EEC; also see re-casted version in article 63 of the Council Directive 2006/112/EC.

⁴⁸ Article 10(2) of the Sixth Directive 77/388/EEC; also see re-casted version in article 65 of the Council Directive 2006/112/EC.

allowed to derogate from the general rule under certain circumstances, or in the case of certain transactions. This was achieved by deeming the date of issuing of an invoice or document serving as an invoice, to be the time of the supply.⁴⁹

In the case of vouchers such as prepaid phone cards, there is no clarity on the time of supply. Should VAT be paid when the voucher is purchased or when the actual service has begun? It should be noted that in Europe, as is increasingly the case in the rest of the world, the credit on vouchers such as a prepaid phone card can be applied to purchase various other goods and services and is not restricted to the use of telecommunication services. In contrast to the South African VAT system, different VAT rates apply in the case of different supplies of goods or services in EU member states. To further complicate matters, different VAT rates apply in different member states. The absence of harmonised rules has further forced member states to develop their own – unsynchronised – rules on the treatment of vouchers.⁵⁰ The complexity of the issue can best be described by way of example –

X who is resident in the Netherlands, purchases a prepaid phone card voucher in the Netherlands. He uses some of the credit on the phone card on 1 December 2012 in Germany to inform his family of his safe arrival. From Germany, X travels to Luxembourg where he uses some of the credit on the phone card to inform his family of his safe arrival and to download various applications, games, and useful software for his phone. On his return to the Netherlands, the credit remaining on the phone card is used to make donations to charitable organisations by sending text messages to a short service number.

Should the value of the phone card be taxed when X purchased the card in the Netherlands, or should the individual type of services acquired by the credit on the phone card, be taxed in the jurisdiction and at the time and rate applicable in the jurisdiction when the credit was exchanged for the specific services?

Similarly, where a consumer purchases vouchers in one country and redeems

⁴⁹ Article 10(2) of the Sixth Directive 77/388/EEC; also see re-casted version in article 66 of the Council Directive 2006/112/EC.

⁵⁰ European Commission n 3 above at 2; Van Vught & Edie 'That's the card to play to treat prepaid telephone cards' (2007) 18/3 *International VAT Monitor* 166.

them in another country, the question arising is whether the voucher should be charged with VAT when it was issued or when it was redeemed?⁵¹ Some member states tax the most common vouchers on issue, whilst others tax them at redemption.⁵² These mismatches between member states could lead to double taxation or the failure to tax at all.⁵³ In the example above, X could be taxed in the Netherlands on issue of the phone card and taxed again on the redemption of the credit on the phone card in Germany, Luxembourg, and the Netherlands.

To address these issues, the European Commission has prepared a draft proposal amending the harmonised VAT rules to provide for time-of-supply rules in respect of vouchers. The proposal draws a distinction between payment methods on the one hand, and single and multiple purpose vouchers on the other.

Payment methods

Innovation in payment methods has blurred the distinction between vouchers in the strict sense, and instruments akin to vouchers which are used to make payments. It is proposed that the instruments that are currently used to make payments at different unrelated outlets, and which are not treated as vouchers, should retain their current status.⁵⁴ So, for example, where a shopping mall voucher is issued entitling the user to spend the amount of credit on the voucher card at any of the shops in the mall, the voucher is treated as a payment instrument similar to a bank card. For VAT purposes, the intrinsic nature of the voucher should be determined in order to classify it as either a voucher or a mere payment instrument.⁵⁵ A stored value card or prepaid credit card, entitles the holder to goods and services upon the payment of such goods or services by means of the stored value card or prepaid credit card, thus rendering it a mere payment method.⁵⁶ In contrast, the redemption of a voucher is not a substitutive

⁵¹ Directorate-General for Internal Policies *Simplifying and modernising in the digital single market* (2012) 44 available at: <http://www.europarl.europa.eu/document/activities/cont/201209/20120924ATT52130/20120924ATT52130EN.pdf> (last accessed 15 October 2012).

⁵² *Ibid.*

⁵³ *Ibid.*

⁵⁴ European Commission n 3 above at 4.

⁵⁵ *Id* at 6.

⁵⁶ *Ibid.*

payment, but the exercise of a right to goods and/or services.⁵⁷

Modern technology, in particular in the cellular phone industry, has made the distinction between vouchers and payment methods increasingly difficult to establish. Traditionally, prepaid airtime vouchers are treated as vouchers because the voucher entitles the holder to a right to claim airtime against the value of the voucher.⁵⁸ Currently, the holder of the voucher can use the airtime to purchase music, software, make money transfers, pay for parking, or purchase goods from a vending machine.⁵⁹ Where the voucher facilitates both the right to goods and services and is also a payment instrument, it becomes difficult to classify it as a voucher.⁶⁰ It is suggested that where an instrument bears the characteristics of a voucher but is predominantly designed as a payment system, it should not be treated as a voucher.⁶¹

Single-purpose vouchers (SPV)

A single-purpose voucher is a voucher that carries a right to receive the supply of goods or services where the supplier's identity, place of supply, and the applicable VAT rate for the supply of goods or services is known at the time of issue of the voucher.⁶² In the case of an SPV, the issuing of the voucher and the supply of the goods and services, are regarded as a single transaction.⁶³ Simply put, the transaction is not taxed when the voucher is issued *and* when it is exchanged for goods or services. The proposed amendment to article 65 of Council Directive 2006/112/EC, provides that the SPV shall be taxed when it is

⁵⁷ *Ibid*; Van der Corput 'Astra zeneca – the VAT treatment of vouchers' (2010) 21/5 *International VAT Monitor* 368.

⁵⁸ European Commission n 3 above at 7; Van der Corput n 57 above at 368.

⁵⁹ European Commission n 3 above at 6–7; Van der Corput n 57 above at 368.

⁶⁰ European Commission n 3 above at 7.

⁶¹ *Ibid*; Van der Corput n 57 above at 368–369.

⁶² European Commission n 3 above at 20; Rodrigues & Lambourne 'Towards clarification of the EU VAT treatment of vouchers' (2012) 23/4 *International VAT Monitor* at 239; Cowly n 2 above at 98.

⁶³ European Commission n 3 above at 20; Shaw 'VAT on face value vouchers – the Lebaracase' (2012) 14/6 *Tax Planning International European Tax Service* vol 14 4 available at: [YPERLINK"http://ibfd.ent.sirsidynix.net.uk/custom/web/SD_PDF/scans/2012/T/TPETS/622-25.zip"](http://ibfd.ent.sirsidynix.net.uk/custom/web/SD_PDF/scans/2012/T/TPETS/622-25.zip) blank"http://ibfd.ent.sirsidynix.net.uk/custom/web/SD_PDF/scans/2012/T/TPE/TS/6_22-25.zip (last accessed 23 January 2013).

issued and paid for.⁶⁴ This means that when the voucher is exchanged for goods or services, the supply of the goods and services is not taxed as tax has already been levied when the voucher was issued. The proposal is consistent with the decision in *Lebara Ltd v The Commissioners for Her Majesty's Revenue and Customs*⁶⁵ where the ECJ ruled that in case of an SPV, the operator of telecommunications services does not carry out a second supply of services for consideration when the purchaser of the voucher exchanges it for telecommunication services.⁶⁶ This is a departure from the current treatment of SPVs in many member states.⁶⁷

Since SPVs are taxed up-front, any subsequent distribution thereof will not create any tax issues. Where the voucher and the subsequent goods and services are not supplied within the same organisation (for example a prepaid telecommunication voucher), the proposal could lead to double taxation: The voucher is taxed by the issuer and the supply is taxed by the supplier.⁶⁸ Should the voucher be treated as a payment method, only the subsequent goods or services would be taxed when the voucher is exchanged.⁶⁹ Revenue losses could, however, result where the voucher is never redeemed or is lost.⁷⁰ However, in these cases no goods or services were supplied, and the result would be similar to when cash is lost or not exchanged for goods and services. The current proposal does not provide for an adjustment when the voucher is lost or not redeemed.⁷¹ Clearly, when the voucher is not redeemed, an adjustment should be allowed as the consideration received was not in respect of goods or services supplied.⁷² Suppliers could rely on *Société thermal d'Eugénie-Les-Bains v Ministère de l'Economie, des Finances et del'Industrie*⁷³ where the ECJ ruled that the forfeiture of a deposit for future services does not constitute

⁶⁴ European Commission n 3 above at 20; Rodrigues & Lambourne n 62 above at 238.

⁶⁵ *Lebara Ltd v The Commissioners for Her Majesty's Revenue and Customs* Case C520/10 (2012) ECR I-00000.

⁶⁶ *Id* at par 43; Rodrigues & Lambourne n 62 above at 238.

⁶⁷ Cowly n 2 above at 98.

⁶⁸ Van Vught & Edie n 50 above at 170.

⁶⁹ Van der Corput n 57 above at 369.

⁷⁰ *Id* at 368.

⁷¹ Rodrigues & Lambourne n 62 above at 240; Cowly n 2 above at 99.

⁷² *Ibid.*

⁷³ *Société thermal d'Eugénie-Les-Bains v Ministère de l'Economie, des Finances et del'Industrie* Case C-277/05 (2007) ECR I-6415.

consideration for goods or services for which VAT must be levied.⁷⁴

Multi-purpose vouchers (MPV)

The proposed amendment to the draft Council Directive defines a multi-purpose voucher as ‘any voucher, other than a discount or rebate voucher, which does not constitute a single-purpose voucher’.⁷⁵ The holder of an MPV is entitled to a right to the supply of goods and services, but, in contrast to an SPV, the supplier, place of supply, and applicable VAT rate cannot be identified upfront when the voucher is issued.⁷⁶ An example is a hotel chain that issues breakfast vouchers to patrons which can be redeemed at any of the hotels or restaurants within the chain.⁷⁷ A further example is where a prepaid airtime voucher is issued which can be redeemed for telecommunication services or for public transport.⁷⁸

VAT will not be charged when the MPV is issued or during the supply chain when the voucher changes hands.⁷⁹ VAT is levied only when the voucher is redeemed or partially redeemed.⁸⁰ In other words, the goods and services supplied in redemption of the voucher, are taxed at the right place and at the correct rate when the goods or services are supplied. Any profit or margin during the distribution chain of the MPV, will be subject to VAT each time a distribution service is supplied, *ie* each time the MPV changes hands.⁸¹ The advantages of treating vouchers as money, are that retailers can account for VAT in accordance with the tax regime that applies to the supplies, and no adjustments are required if the vouchers are lost or used for goods or services that are subject to a VAT rate other than that envisaged when the voucher was issued.⁸²

⁷⁴ *Id* at par 36.

⁷⁵ European Commission n 3 above at 20; Cowly n 2 above at 98.

⁷⁶ European Commission n 3 above at 6.

⁷⁷ *Ibid.*

⁷⁸ *Ibid.*

⁷⁹ *Id* at 13; Shaw n 63 above at 4 available at: http://ibfd.ent.sirsidynix.net.uk/custom/web/SD_PDF/scans/2012/T/TPETS/6_22-25.zip (last accessed 23 January 2013).

⁸⁰ European Commission n 3 above at 13; Van Vught & Edie 48 above at 168–169.

⁸¹ European Commission n 3 above at 13.

⁸² Van der Corput n 57 above at 368.

The proposal does not require that a physical voucher be issued to the customer. In other words, a voucher can be issued as a physical document or card, a text message, or a mere acknowledgment that the customer's account has been credited with a certain amount.

From a compliance perspective, the general time-of-supply rules, and the draft amendments in respect of vouchers, are fairly simple to apply. However, the proposals in their current form still do not resolve all the problems and contain too many loose ends.⁸³

The value of supply

The general rule in the case of the supply of goods and services, provides that the taxable amount is everything that constitutes consideration obtained, or to be obtained, by the supplier in return for the supply to the customer or any third party, and includes any subsidy directly linked to the price of the supply.⁸⁴ The taxable amount includes taxes, duties, levies and any other charges but excludes the VAT itself.⁸⁵

At present, neither the Sixth Directive nor Council Directive 2006/112/EC provides for rules to determine the value for VAT purposes where vouchers are used. For example, where a telecommunication voucher is issued to a customer for consideration of Euros 80, but the intrinsic value of the voucher is Euros 100, which value should be used to determine VAT? Similarly, where the credit on the voucher can be exchanged for different goods and services, should the value of the voucher be taxed, or should the value of the goods and services that are acquired be taxed? In this case it is necessary to discuss the proposals on the VAT treatment of vouchers in the draft Council Directive 2006/112/EC.

In the case of an SPV, VAT is levied on the amount paid for the voucher at the time of issue, irrespective of the intrinsic value of the voucher.⁸⁶ Where the voucher is further distributed against a fee or commission, the value of the fee

⁸³ Rodrigues & Lambourne n 62 above at 241; Cowly n 2 above at 99.

⁸⁴ Article 73 of Council Directive 2006/112/EC.

⁸⁵ Article 78(a) of Council Directive 2006/112/EC.

⁸⁶ European Commission n 3 above at 20.

or commission is subject to VAT.⁸⁷ This proposal is similar to the treatment of vouchers for specified goods as contemplated in section 10(19) of the VAT Act.

In the case of an MPV, the type of supply and applicable VAT rate cannot be determined upfront when the voucher is issued. The value of the goods and services acquired in exchange for the voucher are used to calculate VAT.⁸⁸ This can, however, create a problem when the MPV reaches the customer through a distribution chain. Each time that the voucher changes hands, a taxable service occurs. The distribution can be spread over several member states, and calculating the value of the added service in the absence of an intrinsic value for the voucher (the value of which is determined on redemption), is extremely cumbersome. For this reason, the European Commission proposes that a nominal value be established when the voucher is issued.⁸⁹ The value of the goods and services acquired when the voucher is redeemed, is then limited to the nominal value attached to the voucher when it was first issued.⁹⁰ Simply put, the nominal value represents the taxable value irrespective of the value of the goods and services supplied in exchange for the voucher. The value of the margin/commission or service fee added to the voucher, is taxable in its own right when the voucher exchanges hands.⁹¹

Discount vouchers and discounted vouchers

Discount vouchers, other than vouchers acquired against payment, entitle the holder to goods and services at a discounted price. At present, Council Directive 2006/112/EC provides that the value of any price reduction, discount, or rebate should be deducted from the value before VAT is levied.⁹² Consequently, VAT should be levied on an amount that reflects the actual consideration received.⁹³ Where one person both issues and redeems the voucher, the calculation for VAT purposes is fairly uncomplicated. For example, where X grants Y a Euro 5

⁸⁷ *Ibid.*

⁸⁸ *Id* at 5.

⁸⁹ *Ibid*; Cowly n 2 above at 98.

⁹⁰ European Commission n 3 at 20.

⁹¹ *Id* at 5; Cowly n 2 above at 98.

⁹² Article 79 of Council Directive 2006/112/EC in the case of the supply of goods and services, and art 87 in the case of imported goods.

⁹³ Bijl ‘VAT: “money off vouchers” and “cash back schemes” – what are the problems and how can they be solved?’ (2012) 21/5 *EC Tax Review* vol 21 at 263.

discount on a Euro 100 garment, X only accounts for VAT on Euro 95. In practice, however, discount vouchers are often issued by the manufacturer or wholesaler and are redeemed by the customer at a retailer. In addition, the vouchers are often redeemed in member states other than the member state of issue.

In *Elida Gibbs Ltd v Commissioner of Customs and Excise*,⁹⁴ the court ruled that where a customer presents a voucher that was issued by a person other than the seller, entitling him to a rebate or a discount on submitting proof of purchase of specific items, the value of the goods for VAT purposes shall be the value paid for the goods less as much as represents the discount. This principle was confirmed in *Commission of the European Communities v The Federal Republic of Germany*⁹⁵ where the court ruled that the value used to calculate VAT cannot be more than the consideration paid by the customer. This position is, however, inconsistent with the harmonised VAT laws.⁹⁶ The European Commission is of the view that the ECJ interpretation results in cumbersome administration and is difficult to follow.⁹⁷ It is further of the view that the ECJ's interpretation offers no easy solution, especially where the voucher is issued in one member state but redeemed in another.⁹⁸ What happens where the issuer is not the source of the refund? The European Commission proposes that the voucher should not be seen as third party payment, but should be treated as part of the consideration.⁹⁹ Rather than reducing the consideration by the value of the voucher, the manufacturer or issuer thereof deducts the input VAT thereon on redemption of the voucher.¹⁰⁰ In other words, the purchase price is still reduced by the value of the discount voucher and VAT is paid on that value only, but instead of issuing an invoice for the full amount reflecting the payment by voucher and cash, the invoice is only issued for the reduced amount.¹⁰¹ This is

⁹⁴ *Elida Gibbs Ltd v Commissioner of Customs and Excise* Case C-317/94 (1996) ECR I-05339.

⁹⁵ *Commission of the European Communities v The Federal Republic of Germany* Case C-427/98 (2002) ECR I-08315.

⁹⁶ Bijl n 93 above at 266.

⁹⁷ *Id* at 270.

⁹⁸ European Commission n3 above at 9.

⁹⁹ *Ibid*.

¹⁰⁰ *Ibid*; Bijl J n 93 above at 266, 269.

¹⁰¹ *Ibid*.

similar to the provisions of section 10(20) of the VAT Act.

In the case where an SPV is issued at a discount, because VAT is levied at the time of issue, the issuer only accounts for VAT on the payment (discounted value) received for the voucher. Where an MPV is issued at a discount, the issuer does not account for VAT upon issue because the issuing of the voucher does not constitute a taxable supply. VAT is levied on the monetary value of the goods and services supplied subsequently. The issuer of the discounted voucher cannot claim an input VAT deduction on the discount granted. This is because the discount was not granted in respect of and at the time of the making of a supply.¹⁰² The European Commission is aware that an ostensible right to a VAT deduction exists, but that neither the Sixth Directive nor Council Directive 2006/112/EC provides for this type of deduction.¹⁰³ Further technical changes to the VAT Directive would be required to remedy this issue. It is unfortunate that the European Commission did not attempt to address this issue adequately in the proposed amendments. However, in *Argos Distributors Ltd v Commissioner of Customs and Excise*,¹⁰⁴ the court ruled that

when a supplier has sold a voucher to a buyer at a discount and promised subsequently to accept that voucher at its face value in full or part payment of the price of goods purchased by a customer who was not the buyer of the voucher, and who does not normally know the actual price at which the voucher was sold by the supplier, the consideration represented by the voucher is the sum actually received by the supplier upon the sale of the voucher.¹⁰⁵

In this case Argos, who issued the voucher at a discount, was able to identify the voucher, voucher holder, and the discounted price that was paid for the voucher, based on the serial number printed on the voucher and the corresponding information on their database. Generally, this information is not available and no records exist reflecting the discounted price at which the voucher was sold. Where the issuer of the voucher and the retailer who redeems the voucher are one and the same entity, the solution proposed by the ECJ in

¹⁰² Article 79(b) of Council Directive 2006/112/EC.

¹⁰³ European Commission n 3 above at 5.

¹⁰⁴ *Argos Distributors Ltd v Commissioner of Customs and Excise* Case C – 288/94 (1996) ECR I–05311.

¹⁰⁵ *Id* at par 23.

Argos can practically be executed and neutrality can be restored. In all other cases the ECJ's ruling poses no solution at all.

Free vouchers for free goods and services, forfeited vouchers, and cashed vouchers

In principle, VAT cannot be paid on a value greater than the consideration paid by the customer.¹⁰⁶ Where no consideration is paid, or where the consideration is lower than the open market value, the open market value of the supplies may be used to calculate VAT to prevent tax evasion or avoidance in respect of the supply of goods and services involving family or other close personal ties, management, ownership, membership, or financial or legal ties.¹⁰⁷ In contrast to the provisions in the South African VAT Act, the Council Directive provides for a wider range of connected persons. Where, for example, X receives every third software update free as a result of his membership of a loyalty scheme, the discount so offered could be classified as an agreement between connected persons (members of a loyalty scheme). In this case, however, where no intention exists to avoid or evade taxation, the value of the free digital supplies should be regarded as nil for VAT purposes. It should further be noted that member states are allowed to limit the scope of the meaning of connected persons for purposes of article 80.¹⁰⁸ Basu points out that, generally, where no consideration is paid, VAT is not levied.¹⁰⁹ As a result, VAT cannot be collected where a free voucher was issued which entitles the holder to free goods or services (whether specified or unspecified) where no intention exists to avoid or evade tax.

Under the current harmonised VAT rules, no provision is made for where the balance of a partially redeemed voucher is forfeited or redeemed for cash. The European Commission, further, did not attempt to address this issue in the

¹⁰⁶ *Commission of the European Communities v The Federal Republic of Germany* Case C – 427/98 (2002) ECR I–08315; *Staatssecretaris van Financiën v Coöperative Aardappelenbewaarploaats GA* Case C154/80 (1981) ECR I–00445.

¹⁰⁷ Article 80(1) of Council Directive 2006/112/EC.

¹⁰⁸ Article 80(2) of Council Directive 2006/112/EC.

¹⁰⁹ Basu 'European VAT on digital sales' (2002) 3 *Journal of Information, Law and Technology* available at: <http://elj.warwick.ac.uk/jilt/02-3/basu.html> (last accessed 5 October 2012).

proposed amendments.¹¹⁰ In the *Lebara*-case the ECJ ruled that the payment (by way of the voucher) must be directly linked to the goods and services supplied for the transaction to attract VAT.¹¹¹ Consequently, the balance of the value on a voucher that is either forfeited or paid out in cash, cannot attract VAT as no direct link exists between the supply and payment. In fact, no supply was made.

CONCLUSION

Vouchers are increasingly being used as modern business tools. The distinction between vouchers in the strict sense, and vouchers as payment systems is becoming more difficult. Neither the South African VAT Act, nor the current harmonised European VAT rules, provides for a clear distinction between vouchers as payment systems and vouchers in the strict sense. However, the definitions of single-purpose vouchers and multi-purpose vouchers put forward by the European Commission in its draft proposals in respect of the treatment of vouchers, appear to make this distinction easier. Definitions of single-purpose vouchers and multi-purpose vouchers should be included in section 1 of VAT Act that read –

“single-purpose voucher” means a voucher that carries the right to receive the supply of goods or services where the supplier’s identity, place of supply, and the VAT rate applicable to the supply of goods or services is known at the time of issue of the voucher.

“multi-purpose voucher” means any voucher, other than a discount or rebate voucher, which does not constitute a single-purpose voucher.

Unlike the EU VAT rules, the VAT Act provides for value-of-supply rules when a single-purpose voucher is issued against the payment of consideration. VAT is levied on the value of the consideration paid for the voucher. The value of the goods and services supplied upon redemption of the voucher, is nil. The European Commission’s draft amendment proposals on the determination of the value of supplies in the case of single-purpose vouchers, provide for similar

¹¹⁰ Borec *EU vouchers developments – Lebara, UK SPV legislation and voucher directive proposal* (2012) available at: <http://ebiz.pwc.com/2012/05/recent-eu-vouchers-developments/> (last accessed 24 June 2013).

¹¹¹ *Lebara Ltd v The Commissioners for Her Majesty’s Revenue and Customs* n 65 above at par 40.

deemed value-of-supply rules.

In the case of multi-purpose vouchers, the VAT Act provides that the value of the goods so redeemed must be accepted as the value for VAT purposes. In terms of the European Commission's draft amendment proposals, the deemed value in the case of multi-purpose vouchers should be the nominal value at the time when the voucher was issued. Since the value of the goods or services supplied cannot always be determined with certainty, especially in the case of automated transactions, I suggest that the EU proposal of a nominal value should be adopted.

Difficulty arises in restoring tax neutrality where vouchers are issued at a discounted price. Under the VAT Act, the issuing vendor would not be entitled to claim an input VAT deduction on the discount granted. In the EU, in accordance with the *Argos*-case, VAT should only be levied on the monetary value paid for the voucher. However, as I have pointed out, this is impractical where the issuer and redeemer of the voucher are different entities. Tax neutrality can be restored by providing for a specific notional input VAT deduction where a discounted voucher was issued. However, in the absence of a sound accounting system such as was the case in *Argos*, a notional input VAT deduction provision can be abused to commit VAT fraud. How tax neutrality can be restored in these cases without creating the opportunity for VAT fraud, therefore, remains unanswered.

However, where no consideration is paid for a voucher in terms of a *bona fide* loyalty or similar reward scheme, which either entitles the holder to specific goods or services, or, to unspecified goods and services equal to a stated monetary value, the value of the supplies should be nil. Since no consideration was received, these transactions should be treated as *bona fide* gifts. It should, however, be noted that while *bona fide* gifts do not attract VAT, the transaction could still attract donations tax.