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VAT RELEVANT SALES MASTER DATA IN SAP

Customer and material tax classifications in your SAP master data explained

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WHAT ARE YOU SELLING?
- AN INTRODUCTION TO THE MATERIAL TAX CLASSIFICATION (MTC):

If a customer wants to buy goods or services from you, your sales department will create a sales order in SAP. The goods and/or services will be represented in the sales order with a 'material number' (or 'article number' as some would call it).

Each material number in SAP needs to be identified for tax purposes, so that the correct taxable status can be recognized in the system.

For example, are the materials you selling goods or services?
Are these goods or services standard rated, reduced rated, zero-rated, or perhaps exempt, etc.?

The taxable status of each material number in the SAP system is captured within the master data under the '**m**aterial **t**ax **c**lassification' ('**MTC**').

TO WHOM ARE YOU SELLING?
- AN INTRODUCTION TO THE CUSTOMER TAX CLASSIFICATION (CTC):

When a customer buys goods or services from you, your sales department will create a sales order in SAP. Each sales order will contain several 'partner roles', including a:

- 'sold-to' partner (generally refers to the legal partner for VAT purposes*)
- 'ship-to' partner (represents the physical location where the goods are delivered to or services are performed)
- 'payer' (the partner that will pay for the goods and/or services received)
- 'bill-to' partner (the physical address to where the invoice will be sent)

(*) The determination of the legal partner for VAT purposes has been discussed in one of our video articles and can be accessed here-> https://www.meridianglobalservices.com/insights-who-is-my-legal-partner-for-VAT-purposes/

Each partner number in SAP (that is regarded as the legal partner for VAT) needs to be identified for tax purposes, so that the correct taxable status can be recognized in SAP.

For Example: is the customer liable for VAT, not liable for VAT, does the customer belong to a VAT group or a fiscal unity, does the customer have a special exemption certificate etc?

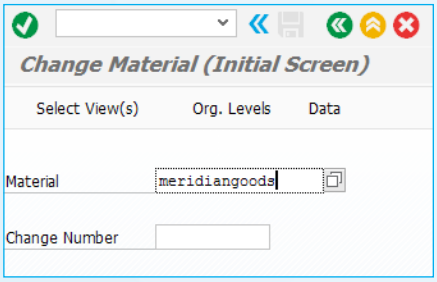
The taxable status of the legal partner for VAT purposes in the SAP system is captured within the master data under the '**c**ustomer **t**ax **c**lassification' ('**CTC**').

WHERE IN SAP IS THE MTC DEFINED?

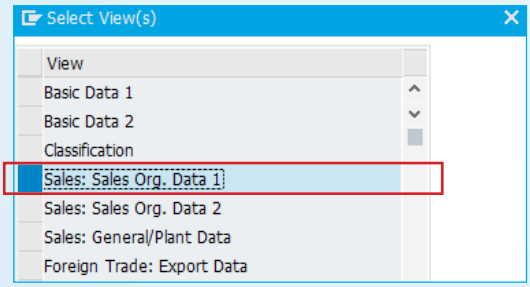
The MTC is stored within the material master data view 'Sales org. data 1'.
The figures below will show you the path to the MTC settings:

1. Start-up transaction MM02 (change material master data) or MM03 (display material master data)

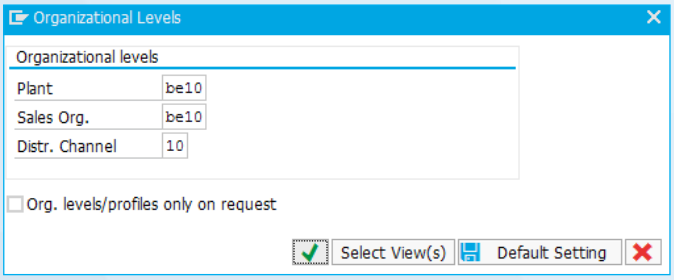
2. Fill in the material number and 'enter':



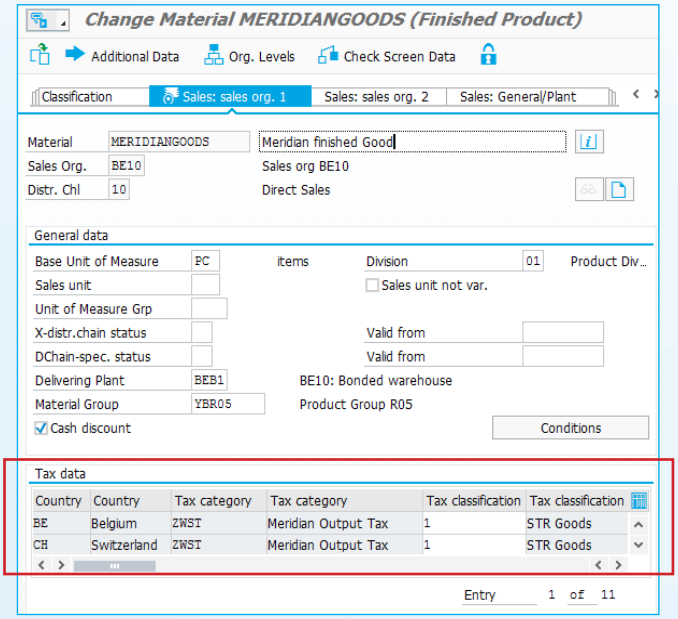
3. Select the view 'Sales: Sales Org. Data 1' and 'enter':



4. Fill in the organisational levels and 'enter':



5. On the bottom part of the screen, the MTC's are defined per combination of 'country code' and 'tax category':

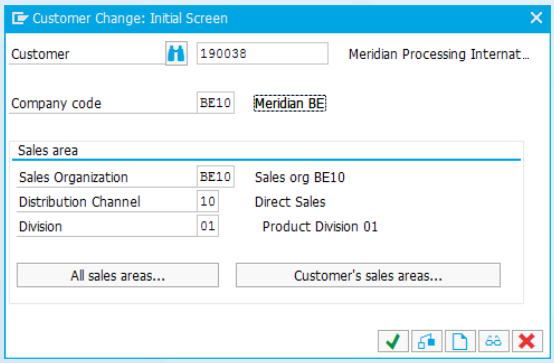


WHERE IN SAP IS THE CTC STORED?

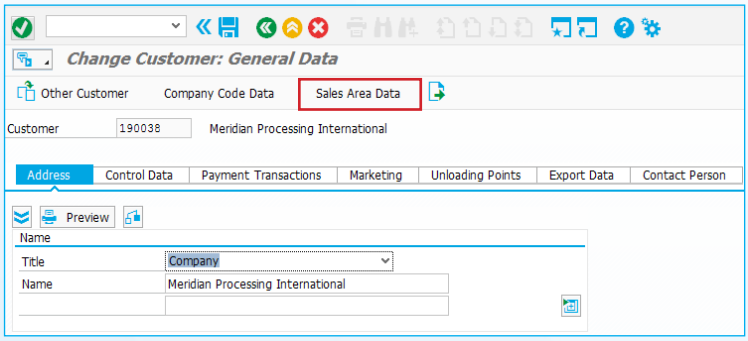
The CTC is stored within the customer master data view 'Sales org. data 1'.
The figures below will show you the path to the CTC settings:

1. Start-up transaction XD02 (change customer master data) or XD03 (display customer master data)

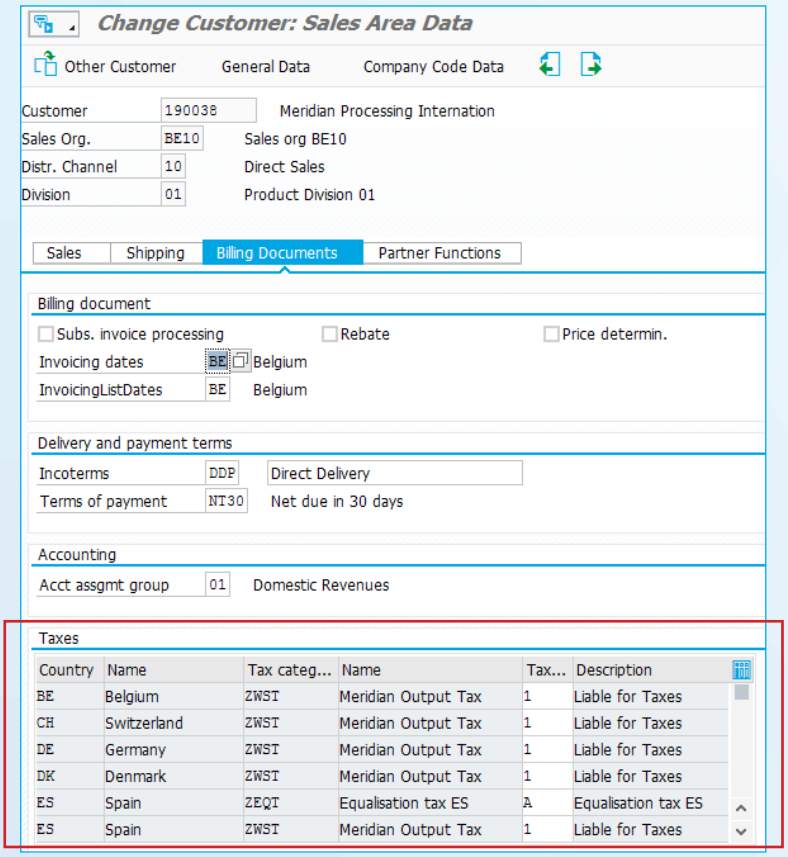
2. Fill in the customer number and the Sales Area data and 'enter':



3. Select 'Sales Area Data'

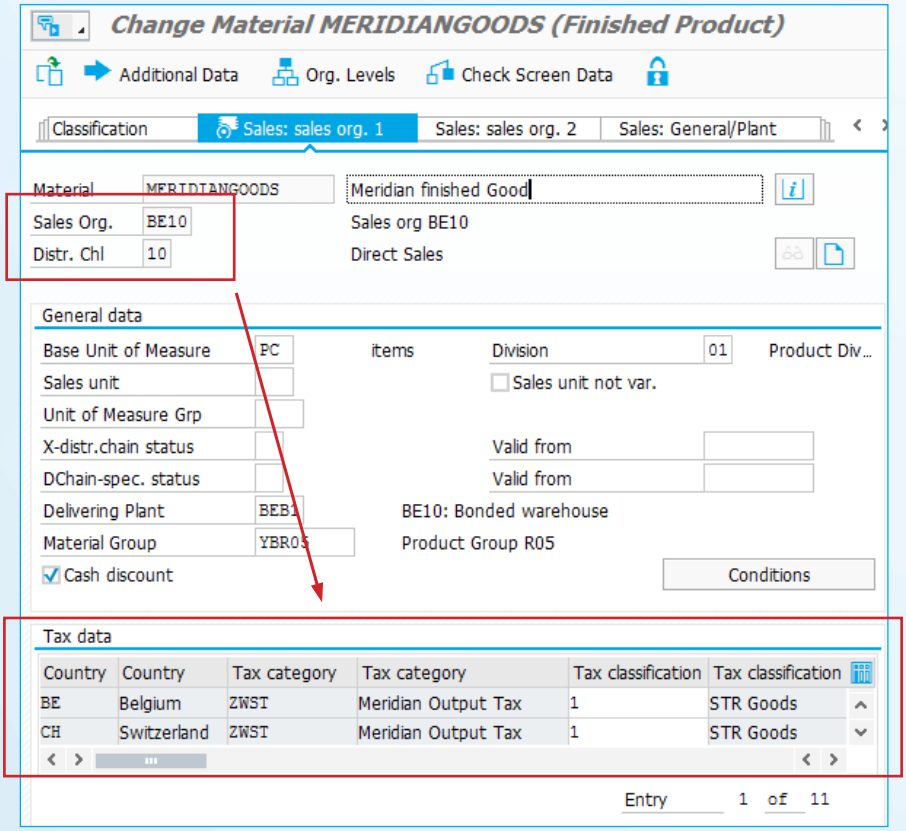


6. Select the tab 'Billing' documents. On the bottom of the screen the CTC's are defined per combination of 'country code' and 'tax category':



IS THE MTC 'SALES ORGANIZATION DEPENDENT' DATA?

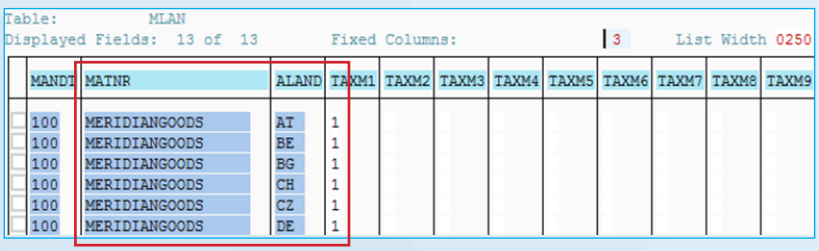
The screen on which the MTC's are displayed shows the sales organization (see figure below):



This (incorrectly) indicates that each sales organisation can define its own MTC.

This is however not true. What is displayed on the screen is misleading because the table in which this data is stored does not contain any organizational data. The table only contains:

- The material number (MATNR)
- The country code (ALAND)
- The MTC (TAXM1 u/i TAXM9)



One should be aware of this, as whenever a sales organization changes its MTC for a country, it affects all other sales organizations that use this same material number!

Consider the following example:

Your company sells children's clothing. You have a sales organization in the UK that sells children's clothing to the UK market and a sales organization in Belgium that sells the children's clothing to the Belgium market.
All goods are manufactured, stored and shipped directly from the UK.
In the UK, children's clothing is zero rated for VAT, whereas in Belgium it is standard rated for VAT.

The MTC can be specified according to the above per country code. In the system we can therefore assign the following:

- for country code BE a MTC 'Standard rated goods'
- for country code GB a MTC 'Zero rated goods'

At first sight it looks like you won't have a problem when determining VAT for each country, but looking closer into SAP VAT determination, you discover a nasty issue with the set-up:

- The country code in the material master data represents the so called 'tax departure country'. The 'tax departure country' in SAP is defined as 'the country of the delivering plant'.
- The sales order created by the UK sales organization will be created with the delivering UK plant. As the UK delivering pant is within the UK, SAP will look up the MTC according to country code 'GB' and will correctly zero-rate the transaction for VAT.
- However the sales order created by the Belgian sales organization will also be created with the delivering UK plant. As the UK delivering pant is within the UK, SAP will again look up the MTC according to country code 'GB' and will incorrectly zero-rate the transaction for UK VAT.
- The transaction in Belgium should have determined Belgian Standard VAT rate at 21%!
- Because standard SAP will determine an incorrect tax departure country for the Belgian sales order, the MTC will be incorrect as well.

A common mistake that companies make when trying to solve this issue, is requesting the material master data team to go into the material master data, enter the sales organization and then change the MTC for country GB to 'Standard rated goods'. This is because they are under the impression that the MTC is defined per sales organization.
But, because the table in which the MTC is stored (see above) does not contain a sales organization, the master data team would in effect also change the MTC for the UK sales organization.
As a result, the next transaction performed by the UK sales organization will incorrectly determine 'Standard rated VAT', which would be incorrect.

A recommended approach to solve this problem is to ensure that:

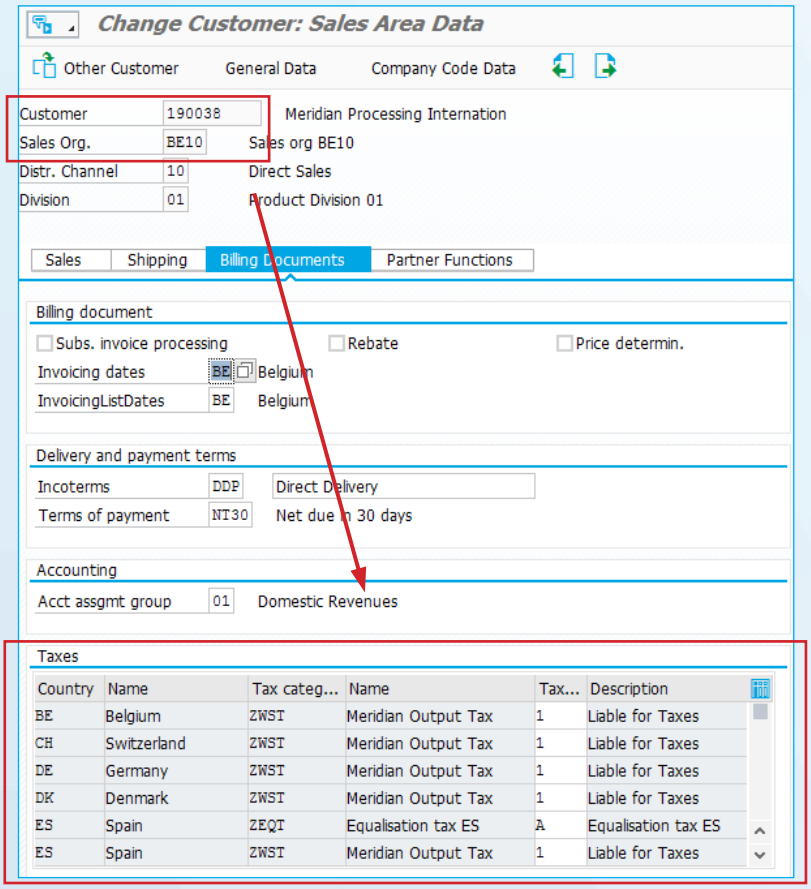
a) the system is modified to determine the correct tax departure country; and
b) the MTC is re-determined whenever the tax departure country is changed

Within SAP note 10560 **(http://service.sap.com/sap/support/notes/10560)**, a correction is suggested by SAP for this issue. These corrections work fine if your business flows are not too complicated.

However, within 90% of our customers we encounter various scenarios in which the tax departure country should be determined in a more flexible way.
Click **here** to learn more about the correct determination of the tax departure country

IS THE CTC ALSO 'SALES ORGANIZATION DEPENDENT' DATA?

Also within the customer master data screen, it looks like the CTC is sales organization dependent data:



This, too is misleading as the table that stores the CTC's does not contain any sales organization:

Table: KNVI
Displayed Fields: 5 of 5 Fixed

MANDT	KUNNR	ALAND	TATYP	TAXKD
100	0000190038	BE	ZWST	1
100	0000190038	CH	ZWST	1
100	0000190038	DE	ZWST	1
100	0000190038	DK	ZWST	1
100	0000190038	ES	ZWST	1
100	0000190038	FR	ZWST	1
100	0000190038	GB	ZWST	1
100	0000190038	IE	ZWST	1
100	0000190038	IT	ZWST	1
100	0000190038	NL	ZWST	1
100	0000190038	PL	ZWST	1

Although one could assume that a custumer should always have only 1 taxable status (no matter which sales organization is selling to this customer), there are many reasons why multiple status are indeed required, even within 1 country!

Consider the following example:

- you are a multinational company within Germany;
- you have 3 separate legal entities;
- Legal entity A and B belong to a German VAT group ('Organschaft');
- Legal entity C however is not included in this VAT group;
- Legal entity A and C both issue intercompany invoices to legal entity B.

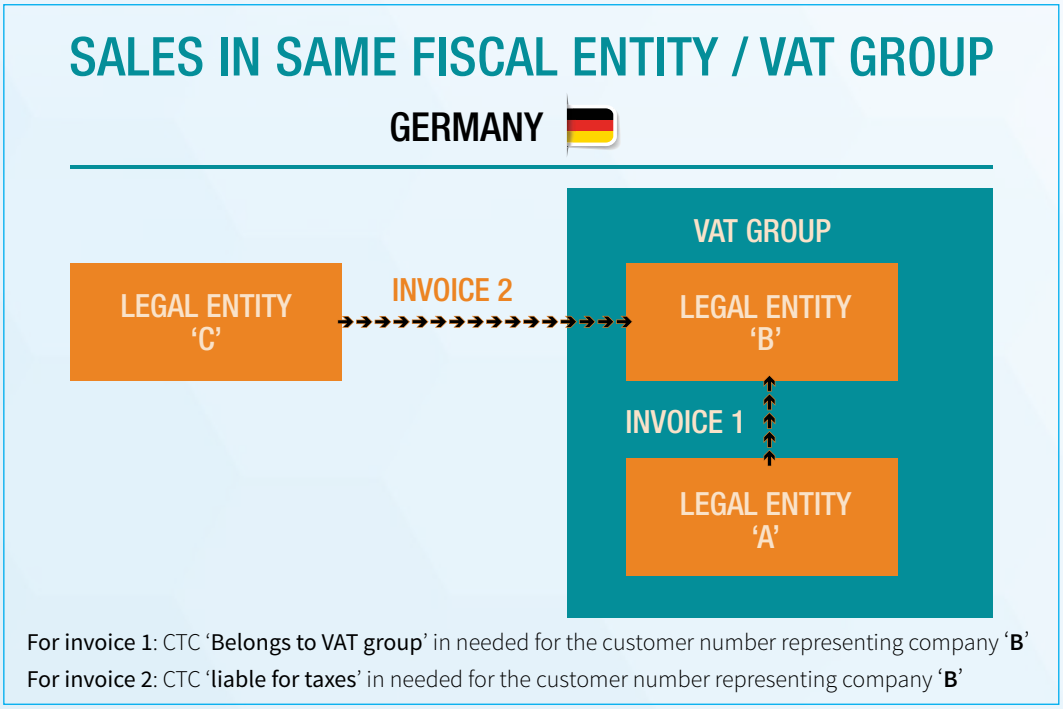
CASE 1:

An invoice from legal entity A to legal entity B should not contain VAT, as they belong to the same VAT group. To achieve this, you would like to set the CTC within the customer master data (representing legal entity B) as 'Belongs to VAT group'. This could be used to derive a specific tax treatment in the condition records.
The tax departure country (the country in which the invoice is reported for VAT) within the invoice is 'DE' (Germany).

CASE 2:

An invoice from legal entity C to legal entity B should contain VAT, as they do not belong to the same VAT group. To achieve this, you would like to set the CTC within the customer master data (representing legal entity B) as 'Liable for taxes'. As above, this could be used to derive a specific tax treatment in the condition records.
The tax departure country (the country in which the invoice is reported for VAT) within the invoice is 'DE' (Germany).

- **Case 1** needs to assign CTC 'Belongs to VAT group' to the customer representing legal entity B for country 'DE' (tax departure country)
- **Case 2** needs to assign CTC 'Liable for taxes' to the customer representing legal entity B for country 'DE' (tax departure country)



For invoice 1: CTC '**Belongs to VAT group**' in needed for the customer number representing company '**B**'
For invoice 2: CTC '**liable for taxes**' in needed for the customer number representing company '**B**'

Within the customer master data, only 1 CTC can be assigned for country 'DE' as this data is NOT sales organization independent. Therefore, you need to choose between 'Belongs to VAT group' or 'Liable for taxes'.

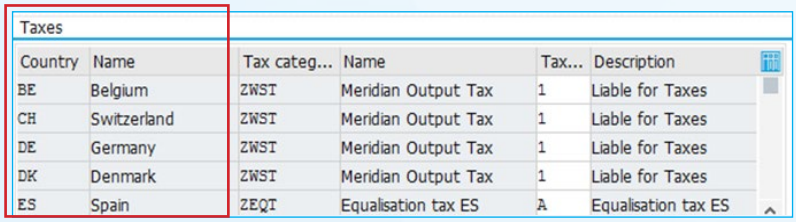
Taxes

Country	Name	Tax categ...	Name	Tax...	Description
BE	Belgium	ZWSI	Meridian Output Tax	1	Liable for Taxes
CH	Switzerland	ZWSI	Meridian Output Tax	1	Liable for Taxes
DE	Germany	ZWSI	Meridian Output Tax	1	Liable for Taxes
DK	Denmark	ZWSI	Meridian Output Tax	1	Liable for Taxes

As a result of this restriction, one of the 2 cases above cannot be handled via the customer master data and requires another solution. This could be either via a so called 'user exit' (customer specific coding) or via an additional access sequence within the VAT condition records (adding additional characteristics into the condition records).

HOW DOES SAP DETERMINE THE VARIOUS COUNTRIES FOR THE MTC AND CTC?

As we already have seen in various examples above, within the MTC and CTC definitions on the master data, several countries are shown.



Taxes

Country	Name	Tax categ...	Name	Tax...	Description
BE	Belgium	ZWST	Meridian Output Tax	1	Liable for Taxes
CH	Switzerland	ZWST	Meridian Output Tax	1	Liable for Taxes
DE	Germany	ZWST	Meridian Output Tax	1	Liable for Taxes
DK	Denmark	ZWST	Meridian Output Tax	1	Liable for Taxes
ES	Spain	ZEQI	Equalisation tax ES	A	Equalisation tax ES

These countries cannot be added manually to the master data. They are determined via a specific logic in SAP and are made available in the master data for:

- the country of the sales organisation;
- the country of the plants from which this sales organisation can deliver goods (note: these are not only the plants that BELONG to the sales organisation),

When this logic was originally designed by SAP, the determination of the countries as explained above was sufficient. But with today's business complexity, this logic is insufficient for various reasons.

LET'S HAVE A LOOK AT AN EXAMPLE OF DISTANCE SALES.

Your company sells children's clothing via a web shop. The UK sales organization sells children's clothing to the UK market and also (via the web shop) to the Belgium market.
All goods are manufactured, stored and shipped directly from the UK.
No Belgium entity / plant / warehouse exists.

In the UK, children's clothing is zero rated for VAT, whereas in Belgium it is standard rated for VAT.
Normally the MTC can be specified according to a country code.
But as we do not have any plant in Belgium, the system will only make the following countries available in the master data:

- The country of the sales organisation => UK
- The country of the plants from which this sales organisation can deliver goods => UK

In the system we can therefore only assign the following:

- for country code GB a MTC 'Zero rated goods'

As country Belgium ('BE') is not available in the system, we cannot specify for country 'BE' a MTC 'Standard rated goods'.
As a result, SAP will try to incorrectly 'zero rate' children's clothing that is sold to the Belgium market.
As this issue cannot be solved within the Standard SAP master data set-up, an custom solution needs to be built into the system, for example:

- Additional access sequences to the VAT condition records (which will create high maintenance as one would need to include sales organisation and material number);
- Create a 'dummy' or 'virtual' plant in Belgium and assign this to the UK sales organization (this option is almost universally blocked by SAP solution architects);
- Create a 'user exit' (customer specific program modification) that adds additional countries into the master data.

To access more articles from Meridian detailing VAT in SAP, check out our website and click on "resources":
https://www.meridianglobalservices.com/tax/technology/

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