VAT focus

The 2015 VAT review

Speed read

Key developments in VAT during the last 12 months include: the fallout from *Skandia*, which includes the UK confirming it would, from 1 January 2016, apply a 'two-tiered' approach, differentiating between member states with Swedish-style VAT grouping rules and everyone else; a surprising departure from HMRC guidance in assessing whether a transaction is a TOGC; a rejection of HMRC's restrictive view on VAT recovery by holding companies; the introduction of a new 45% rate of corporation tax on restitution interest, following the taxpayer's continuing victories in *Littlewoods Retail*; and further developments in VAT on debt collection, with a CJEU referral in *National Exhibition Centre*.

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2015 was a good year for the VAT aficionado (not that one can recall too many bad years), but rather than enumerate everything interesting that happened – for fear of producing a list that would rival Santa's – I have decided to focus on five topics that I believe will still be water cooler worthy come the New Year, if not beyond.

VAT groups

Skandia America Corp (C-7/13) pushed the subject of grouping back to the top of the VAT agenda. Although the ruling of the CJEU was handed down in 2014 (and not 2015), much of the debate to determine the extent of its blast radius took place this year.

The CJEU held that services provided by a non-EU company to its Swedish branch – i.e. services provided within the same legal entity – rather than being a 'nothing', gave rise to a supply by virtue of the fact that the branch was in a VAT group (and was thus a different taxable person from its headquarters). The controversy was whether this ruling was restricted to member states which, like Sweden, only allowed in-country establishments to be included in VAT groups; or whether it extended to member states which, like the UK, included entire entities (even their establishments outside the territory).

The VAT Committee and the VAT Expert Group both published working papers on the subject this year (*Working paper 845* and *VEG No. 47* respectively), analysing the arguments from both sides. Despite all the discussions, however, there is no consensus, and we are still some way off from a uniform approach across the EU.

From 1 January 2016, the UK will apply a 'two-tiered' approach, differentiating between member states with Swedish-style VAT grouping rules and everyone else (see *Revenue & Customs Briefs 2/2015* and *18/2015*). It remains to be seen whether this would bring with it its own complications.

Before we leave this topic, I should mention that not all the questions around VAT grouping derive from *Skandia America Corp*. The ruling of the CJEU in *Larentia + Minerva* (C-108/14 & C-109/14) raises the possibility of including partnerships in VAT groups. A door long thought sealed has now been opened, and it will be interesting to see where it leads.

TOGCs

Another area where long held preconceptions were revisited to surprising effect is the transfer of a business as a going concern (TOGC).

Far too often (on real estate transactions in particular), the question of whether a transaction is a TOGC (and thus a non-supply) has been answered not by reference to the law, or the rulings of the CJEU, but by reference to HMRC's guidance (as set out in *VAT Notice 700/9*). Over the years, HMRC's prescriptive examples of what is or is not a TOGC have taken on an authority that, in many cases, was simply unwarranted. Yet few would challenge the *status quo*.

Then, three years ago, came the decision of the UT in *Robinson Family* [2012] UKFTT 360. This led to HMRC revising its policy on whether the grant of a lease (as opposed to the sale of the superior interest), and the surrender of a lease, could be TOGCs (see *Briefs 30/12* and *27/14*).

This year, the UT held in *Intelligent Managed Services* [2015] UKUT 341 that the transferee of a business would be carrying on the same kind of business as previously carried on by the transferor – so that the transfer would be a TOGC – even where the supplies made by the transferee in the course of this business would be disregarded by virtue of it being in the same VAT group as its customer.

This cuts across yet another of the prescriptive examples set out in *VAT Notice 700/9*.

The focus on substance, ascertained from all the facts, is a welcome change from dogmatic adherence to prescriptive 'guidance'. This may be the beginning of a sea change in how one assesses whether a transaction is a TOGC. Who has not wondered whether a series of immediately consecutive transfers could ever be a (non-supply) TOGC?

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VAT recovery by holding companies

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HMRC insists that in order for input tax to be recoverable, the cost of the input transaction must be a component of the price of the taxable output transaction. It also took the view that even a holding company that only made taxable supplies to its subsidiaries should suffer some input tax disallowance where it received dividends (on the basis that such receipt was a non-economic activity).

Both of these positions came up for consideration by a court this year, and both were rejected: the first by the Court of Appeal in *Volkswagen Financial Services* (*VWFS*) [2015] EWCA Civ 832; the second by the CJEU in *Larentia + Minerva*.

This was welcome news to taxpayers who have argued

for years that HMRC's stance was simply wrong. While it is tempting to think that HMRC would use this opportunity to draw a line and transition to a more sensible position, it is (I understand) in fact seeking leave to appeal the decision of the Court of Appeal.

There is also the question of HMRC's policy on holding companies that are in VAT groups. In such a case, it requires not only that the cost of the input transaction is a cost component of the services supplied by the holding company to the subsidiary (within the VAT group), but also that the supplies from the holding company are used by the subsidiary to make its own (taxable) supplies to third parties outside the VAT group. This has not come before a court yet, but like the 'component of price' and the 'dividend' arguments mentioned above, it is considered by many taxpayers to be wrong.

Irrespective, therefore, of whether HMRC is granted leave to appeal *VWFS*, the story is nowhere near over.

Restitution

The story is definitely not over on where restitution sits in the world of VAT.

The biggest VAT story this year is probably the decision of the Court of Appeal in *Littlewoods Retail* [2015] EWCA Civ 515. In short, the taxpayer prevailed, and it was held that the interest due from HMRC should be calculated on a compound (rather than simple) basis. It is generally understood that this would result in an award in excess of £1bn.

In what many believe to be a desperate move, the government (in a late amendment to the Finance Bill) introduced (with retrospective effect) a special 45% rate of corporation tax that would apply only to interest payable pursuant to a restitution claim and only where it is calculated on a compound basis. The new tax is to be collected at source, so HMRC does not even have to pay the full amount and then wait for the tax return to be filed to receive 45% of it back.

There is doubt as to whether the provisions are lawful under European law, and a challenge is not unexpected. Therefore, just as one controversy (compound or simple) appears to be nearing a conclusion, another rears its head.

Littlewoods was not the only case this year where the Court of Appeal had to consider the interaction between restitution and taxation. The other case was *Investment Trust Companies* (*ITC*) [2015] STC 1280.

The issues in *ITC* are complex. In a nutshell, the question was whether the recipient (rather than the supplier) of a supply (i.e. the tax bearer, rather than the taxpayer) was entitled to claim repayment from HMRC of VAT that had been paid to them, which subsequently transpired not to be due. The Court of Appeal held that the tax bearer was so entitled, but only in relation to the net amount of tax actually paid to HMRC by the taxpayer (i.e. the amount of output tax less the amount of deductible input tax). Perhaps surprisingly, it also held that the tax bearer would have a claim even where the taxpayer himself was time-barred.

In the past, it would have been rare to refer to the law of restitution when dealing with VAT. The leading cases on the subject (at least insofar as it relates to tax) were all direct tax cases (see, for example, *Woolwich* [1992] STC 657, *Sempra* [2007] STC 1559 and *Deutsche Morgan Grenfell* [2007] STC 1, among others). After this year, I would not be surprised if the focus on the interaction between restitution and taxation shifts to the sphere of VAT.

Debt collection

Article 135(1)(d) of the Principal VAT Directive exempts transactions concerning payments, transfers or debts, but it specifically excludes debt collection from the exemption.

What constitutes taxable debt collection was considered in *AXA* (C-175/09), but the wide reading the CJEU gave to 'debt' and 'debt collection' (which blurred – if not entirely eliminated – the line between an agent who actively chased delinquent or bad debts, and one who passively received payments, on behalf of another) led to a number of controversies, a particular uncertainty being whether services only amount to taxable debt collection when supplied to the creditor (but not when supplied to the debtor).

Although the question was thought settled (see *Bookit* [2014] UKFTT 856, for example), the controversy never went away.

Finally, this year, a referral was made to the CJEU in *National Exhibition Centre* (C-130/15). In essence, it asks the CJEU to explain what exactly it meant in *AXA* – i.e. what constitutes a 'debt', what amounts to 'debt collection' and whether the VAT treatment of the service depends on its nature or the status of its recipient.

Will the CJEU provide sufficient clarity for taxpayer and HMRC alike to operate the exemption (and exclusion) with certainty? We shall see.

(The referral also contains questions echoing the referral made in 2014 in *Bookit* (C-607/14) – in particular, whether the mere transmission of information that would cause a transfer to be made has the effect of transferring funds, so that it amounts to a transaction concerning payments or transfers.)

What else?

As with all 'top five' lists, the above is highly personal. Readers are likely to have lists of their own, which may be vastly different. I can see some including *Kumon, Newey* and *Pendragon*, or *Astral Construction*, or possibly e-books, or pensions. *Earl Redway* may make some lists, or a military housing agency in an Eastern European country. Or perhaps *Sveda*, or one of the *Colaingrove* cases. Or *Mapfre*. Or the fact that HMRC felt it necessary to remind businesses that the sale of carrier bags was taxable (and the VAT on 5p was 0.83p).

Whatever VAT developments caught your imagination in 2015, enjoy the holidays and here's to 2016 being just as exciting. ■

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