Tax Insights

VAT news - August 2017

Sporting exemption applicable to all not-for-profit bodies

Not-for-profit bodies governed by public law who supply sporting services may now be able to treat such supplies as exempt, following the Court of Justice of the European Union (CJEU) decision in the London Borough of Ealing (LBE) case.

In the UK, sporting services supplied to individuals by not-for-profit bodies are treated as exempt from VAT. However, this exemption does not extend to sporting services supplied by a local authority, on the basis that this could cause 'distortion of competition' with commercial providers.

The LBE challenged this interpretation, as other not-for-profit bodies could benefit from the exemption provided they could demonstrate there was no distortion of competition, and meet other conditions.

The CJEU agreed with the Advocate General (AG) that the UK had not interpreted the sporting exemption outlined in EU VAT law for not-for-profit bodies governed by public law correctly. The sporting exemption was not meant to make it harder for public bodies to be granted the exemption than it is for private bodies. The UK however, applied the provision in such way as to preclude public bodies from accessing the exemption automatically. Thus, the CJEU found that the UK domestic law was not compatible with the Principal VAT Directive.

Following this judgment, local authorities may wish to reconsider their position if they supply sporting services and satisfy the other eligibility criteria to benefit from this VAT exemption. The treatment of cultural services should also be

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considered as these are also subject to the same distortion of competition condition. Our Indirect Tax Team can offer guidance in this area, if required.

'Unreasonable' delays in tax repayments by tax authorities requires default interest to be paid

The recent CJEU case of Glencore Agriculture Hungary Kft, (Glencore) discussed the timeframe within which EU taxpayers can expect to be repaid any VAT due to them. Glencore had submitted a VAT repayment return and suffered a delay of more than two years in receiving the VAT repayment. On top of this, the Hungarian tax authorities issued Glencore with a number of penalties for providing information requested late, which ostensibly delayed the tax authorities' enquiry.

Following the conclusion of the enquiry, the tax authorities paid just over half the VAT due and Glencore made an application for interest on account of the prolonged delay. The tax authorities cited the penalties imposed as sufficient for the delay; however, they had requested a large quantity of data within the first two weeks of the claim and, upon each request, allowed only three working days to comply.

The CJEU held that while EU VAT law does not set out an obligation to pay interest, this does not mean member states can unnecessarily delay VAT repayments. Where a VAT repayment has been subject to an unreasonable delay, as in this case, the taxpayer is due a payment of default interest.

This ruling will be of interest to taxpayers who have VAT repayments delayed by the rules of an EU member state. In the UK, HMRC are not generally known for lengthy delays in making VAT repayments and any undue delay in repayment can be subject to default interest along with an ex gratia payment as compensation for any further delays caused by HMRC (although these payments will likely be below the current interest rate). Further, if HMRC delays a repayment from a VAT return submitted on time for more than 30 days (any enquiry time into the VAT return is disregarded here) then the taxpayer is entitled to a repayment supplement from HMRC.

As a separate, but related point, it is hoped that the Supreme Court's ruling in relation to compound interest claims discussed in the *Littlewoods* case will provide guidance in connection to interest claims. It is understood that questions may be referred to the CJEU on the time value of money in establishing the right to reimbursement which would further delay the Supreme Court's judgment.

If you have any queries in relation to delays in receiving VAT repayments, please contact our Indirect Tax Team.

Input tax incurred by developer on infrastructure works not recoverable

AG Kokott has released her opinion in the Iberdrola Inmobiliaria Real Estate Investments (Iberdrola) case which may have implications for charities which supply services free of charge, and for businesses such as developers/builders in the UK providing works under planning gain agreements.

In summary, Iberdrola planned to construct a holiday village on land it owned, which would then be leased out on a taxable basis. However, it transpired that in order to connect the holiday village to the existing municipal waste-water pump station, the pump station had to be extensively renovated. Iberdrola therefore agreed to carry out the repair of the waste-

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water infrastructure for the local authority at its own expense. Iberdrola sought to recover the related input tax on this work, but it was blocked by the Bulgarian tax authorities, on the basis that the work was supplied free of charge to the local authority.

The AG stated that a mere causal link between inputs and economic outputs is not sufficient for input tax recovery. Moreover, the fact that Iberdrola recorded the costs in its accounts as a 'cost of trade' was irrelevant. She concluded that EU VAT law does not permit the recovery of input tax for services which are supplied free of charge directly to a third party for its own purposes, even if motivated by business reasons.

Although there are similarities between this case and the *Sveda* decision, the AG emphasised that the two cases are distinguishable; in the latter, the construction of the trail on behalf of the Lithuanian state was to be used for *Sveda's* future business activities. In the Iberdrola case, the repaired water pump was provided free of charge to the local authority for its own economic use.

The CJEU decision is expected later this year, and it will be interesting to see whether the AG's opinion is followed. The AG prefaced her opinion by saying that the *Sveda* decision had created some uncertainty over the extent of the right to deduct input tax and that the CJEU has the opportunity to clarify its decision in that case.

Please contact our Indirect Tax Team if you require any assistance in this area.

Substantial but not complete demolition of building is standard rated alteration to an existing dwelling

In the case concerning J3 Building Solutions Ltd (J3), the Upper Tribunal overturned the First Tier Tribunal (FTT) ruling and concurred with HMRC that the existing building had never ceased to exist. This acts a reminder as to the complicated nature of VAT provisions in relation to work on property and that care should be taken when considering any works to existing property.

J3 carried out substantial construction works on a site where a former coach house (used as a dwelling) existed, and to which extensions had been added. Consent had been granted for the demolition of the extensions and part of the existing house. Since three walls were retained following the demolition, HMRC contended that the retained walls were more than a single façade, therefore it could not be argued that building had ceased to exist, as the building was not completely demolished. HMRC's view was that the FTT had failed to properly consider Note 18 of Group 5 of Schedule 8 of the VAT Act 1994 when reaching its decision. This includes the condition that a building only ceases to be an existing building when demolished completely to ground level or that the part remaining above ground level consists of no more than a façade.

The Upper Tribunal decided HMRC's analysis was correct. The FTT had erred in considering and interpreting Note 18. The construction work amounted to an alteration to the existing building and therefore the works were deemed to be standard rated rather than zero-rated. J3 had referred to the *Astral Construction Ltd* case in conveying its argument, but the Upper Tribunal stated that the principles established in this case were not relevant to the matter at hand.

Businesses concerned about the VAT treatment of its construction projects may wish to contact our Indirect Tax Team for clarification.

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No escaping VAT on overpayments where change was not issued

This case concerned the UK's largest parking provider, National Car Parks (NCP), appeal to the Upper Tribunal regarding the requirement to account for VAT on the whole amount of the payment made by customers to its car parking machines. Where customers did not have the exact change required to pay the parking fee they were required to pay in excess of the fee and the parking machines did not give change.

NCP argued that any overpayments which were paid into their machines were outside the scope of VAT as they were not in return for a supply. HMRC however, countered that the whole amount paid by customers was taxable as the terms were such that no change was given and the supply of parking was provided in return.

The judge agreed with the FTT and held that the whole amount paid by customers was in consideration for parking services. The over-payments by customers could not be seen as 'voluntary' and VAT is chargeable on the whole amount received.

If you have any questions in relation to this case please contact our Indirect Tax Team.

VAT exemption for providers of unregulated welfare services

Organisations providing welfare services which do not appear to fall within the VAT exemption at first glance, may now be allowed to treat their supplies as exempt.

As background, organisations which provide welfare services can treat these services as exempt if they are:

- A charity;
- A state-regulated private welfare institution or agency; *or*
- A public body.

In the case of The Learning Centre (Romford) Ltd (TLC) it was agreed that the organisation was providing welfare services in the form of educational and day-care services to vulnerable adults with learning difficulties. The business was run for profit. It was not regulated in England in the sense that the type of day-care it provided was not within the Health and Social Care Act 2008, which only regulated such care when provided in the recipient's own home. Consequently TLC charged standard rated VAT on its supplies and had to absorb a proportion of the VAT cost so as to remain competitive within the marketplace.

TLC argued that it was making exempt supplies because:

1. It was state-regulated on the basis that its staff were regulated by the Disclosure Barring Service (i.e. DBS checks);
2. Bodies located in Scotland and Northern Ireland making identical supplies were regulated and therefore qualified for exemption.

In answer to the first point, the FTT found that the entity required to be subject to state-regulation was TLC and so the status of its staff was irrelevant; the DBS had no control over the services TLC would provide. Therefore, TLC was not state-regulated.

In answer to the second point, the FTT found in favour of TLC stating that discrimination did arise between welfare institutions situated in England and Wales compared to those located in Scotland and Northern Ireland. The FTT found that the UK's implementation

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of the VAT welfare services exemption was unlawful as it infringed the principle of fiscal neutrality. TLC was entitled to rely upon the direct effect of EU VAT law meaning that TLC's supplies are exempt.

This case will be of interest to taxpayers who currently charge VAT on supplies of welfare services which they are not able to pass on to their customers in full. It is also a useful reminder that with the growth of devolution in Scotland over the past 20 years, and the possibility for more devolved power in Northern Ireland, there is potential for similar disparities between England and Wales and the rest of the UK.

It seems likely that HMRC will appeal against the decision. If you have concerns over the implications of this case, please contact our Indirect Tax Team.

Relevant Residential Purpose building can also be treated as a dwelling

The case of Summit Electrical Installations Ltd (Summit) was heard in the FTT and considered whether a building with planning permission for student accommodation could be considered a dwelling.

A developer and main contractor, Create Construction Ltd (Create), was granted planning permission to construct student accommodation. The accommodation was restricted to "no person other than a full time student attending the University of Leicester or DeMontfort University". Summit received a zero-rating certificate from Create, on the basis that the building was to be used by Create for a relevant residential purpose (RRP) (i.e. student accommodation). HMRC challenged the zero-rating as sub-contractors should not zero-rate their supplies on a building for a RRP (as discussed in the case of *J & B Hopkins Limited* in our June newsletter) and therefore VAT at 20% should have been charged by Summit.

Create refused to accept VAT-only invoices from Summit to remedy this enquiry and therefore Summit wanted the FTT to decide whether they were eligible to zero-rate their supply as they considered they were supplying services in the course of construction of a building which was also designed as dwellings.

HMRC argued, firstly, that the supply could not relate to a dwelling because of the restrictions set out in the planning application and, secondly, that as a certificate was issued, this indicated that the parties involved had elected that the building was for use as a RRP.

In relation to HMRC's first argument the FTT found that the terms of the planning condition were not restrictive enough to deny the zero-rating relating to dwellings; they related to students. "Such a vast class of people cannot … represent a prohibition of use" found the FTT. In that sense the construction of the student accommodation satisfied the conditions to be met for the rooms to qualify as dwellings and for the zero-rating provision to apply.

The FTT disagreed with HMRC's second point as the building was a qualifying building designed as dwellings.

It should be noted that HMRC's guidance in 15.1 of the VAT Notice 708 sets out that HMRC accepts that where a building qualifies for zero-rating as a building designed as a dwelling or for use for a RRP, the taxpayer can decide which zero-rating relief they wish to benefit from.

HMRC's guidance is of note here, as it seems that HMRC were arguing against the stance taken in their own guidance. Worryingly, this suggests that HMRC are trying to restrict the ability of taxpayers to benefit from the zero-rating for the construction of dwellings. Whilst this is the first case we have seen on these facts, we would encourage anyone who is

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considering building works to seek professional advice, as HMRC are very quick to challenge the zero-rating of a supply they do not agree with.

Victory for ambulance provider against HMRC

This case will be of interest to any taxpayers who carry out transportation services and are not currently making use of the VAT zero-rating.

A small family owned company, Jigsaw Medical Services Limited (Jigsaw), provided First Aid training, event medical cover and ambulance services. Jigsaw had been advised that they qualified for the VAT zero-rating for transportation services for the ambulance services provided and had recovered input VAT on the cost of the ambulances. The zero-rating extends to the transport of passengers in a vehicle designed or permanently adapted for the carriage of persons in wheelchairs and which, if it were not so designed or adapted, would be capable of carrying no less than 10 persons.

HMRC carried out a visit and advised Jigsaw that zero-rating did not apply; the supplies of ambulance services should be exempt (meaning that no input VAT recovery would be allowable on the cost of the ambulances).

The taxpayer appealed HMRC's decision to the FTT and the judge was left to decide whether the ambulance had the potential to hold at least 10 passengers. The judge considered the hypothetical question, if the ambulance was not designed or adapted to carry wheelchairs, is it still able to carry no fewer than 10 passengers?

The judge held that the ambulance would be able to hold at least 10 passengers, provided it was not designed or adapted to carry wheelchairs. The argument by HMRC that the ambulance should still be capable of fulfilling its contractual obligations as an ambulance, after its reconfiguration, was dismissed as this was not contained in the law. The FTT determined that the transport services qualified for both zero-rating and exemption; where this happens, the zero-rating takes precedence. The appeal was therefore allowed and zero-rating applied.

This case highlights that HMRC had been interpreting the law in relation to transportation too narrowly, and there is the opportunity for taxpayers who have vehicles adapted for wheelchair use to benefit from the zero-rating.

Changes to VAT rules for telecommunication services

It was announced in last year's budget that the existing VAT "use and enjoyment" rules for supplies of business to consumer (B2C) telecoms would be amended this year. The Value Added Tax (Place of Supply of Services) (Telecommunication Services) Order 2017 effects this change with effect from 1 November 2017 rather than 1 August 2017, the date originally announced.

The 'use and enjoyment' provision for supplies of telecommunications services currently provides that the place of supply is outside the EU if the user is outside the EU. This reduces the VAT liability on sales made to UK resident customers who use the services outside the EU.

B2C supplies will no longer be subject to the use and enjoyment rule and will be subject to the general rule for B2C telecommunications services. This means that the place of supply of telecommunication services will be the country in which the recipient of the supply belongs. The effect of the measure is to bring affected services used outside the EU within the scope of UK VAT where consumers belong in the UK.

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The place of supply rules will not change for business to business (B2B) supplies. This change will bring the UK VAT rules in line with international rules.

VAT unaffected by changes to the Making Tax Digital plans

HMRC announced on 13 July an update to its Making Tax Digital plans which has effectively given businesses another year before the scheme becomes compulsory. This means that businesses with a turnover above the VAT registration threshold will not be required to implement the Making Tax Digital provisions until April 2019. The rest of the wider Making Tax Digital plans will be enforced from April 2020 onwards. The changes envisaged for VAT requires businesses trading above the £85,000 registration threshold limit to keep digital records on top of filing their quarterly VAT returns online. Making Tax Digital will however be available on a voluntary basis for other taxes and for those trading below the VAT registration threshold, if they wish to move to the new system sooner.

As mentioned previously, the Making Tax Digital plans will not affect charities, who will continue to be exempted from these changes, although trading subsidiary companies operated by charities will not be covered by the exemption.

If you have any questions as to how your business may be affected by this, please contact our Indirect Tax Team.

HMRC to phase out VAT payable order cheques

HMRC has announced plans to start phasing out VAT payable order cheques. Businesses that receive their VAT repayments from HMRC using this medium will need to notify HMRC of their UK bank account details in order to receive VAT repayments via BACS. It is not yet clear whether businesses who operate solely with an overseas bank account will need to open a UK bank account to receive future VAT repayments.

EU VAT cross border rulings project extended

The pilot project set up in 2013 to enable taxable persons to obtain advance rulings for the VAT treatment of complex cross-border transactions has been extended again to 30 September 2018. Various EU member states are participating in this scheme, and further information can be found here.

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