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Tax Insights

VAT news - December 2017

Distance learning course is a single standard rated supply of education

Businesses and educational bodies that provide distance learning courses should check they are applying the correct VAT rate to their sales following the recent Upper Tribunal (UT) decision in the Metropolitan International Schools Limited case.

The issue in this case was whether the school was providing zero-rated supplies of printed matter, or a standard rated supply of educational services. The UT ruled that the First Tier Tribunal (FTT) had failed to give adequate weight to various features of the course, and that the books/manuals could not be considered the "principal" element of the supply, with the remaining parts considered ancillary support services. The UT stated that the FTT ignored several critical elements of the supply, such as the tutorial support, student progress reports, webinars, software, DVDs and access to virtual rooms; all of these were vital elements of the course, and the student would need these to attain the desired qualification.

Therefore, the FTT had "erred in law", the course was much more than a supply of printed matter; it was a single standard rated supply of education services.

If you have any concerns following this decision, please contact our Indirect Tax Team for assistance.

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Sale and leaseback of a relevant residential building – VAT self-supply required

Businesses and charities involved in property transactions which qualify for zero-rating should seek professional advice before entering into transactions which may affect the interest they hold. They could be subject to a change in use VAT charge if the qualifying use changes or the building is disposed of.

In HMRC v Balhousie Holdings Limited (Balhousie), the UT found that a sale, which was followed by a leaseback, was the disposal of an 'entire interest' in an asset (which had benefited from the zero-rating relief where a building is acquired for a relevant residential purpose). Therefore, it triggered a deemed standard rated self-supply.

Balhousie was an operator of care homes, and had been supplied with a care home which benefited from the zero-rating. Balhousie then entered into a sale and leaseback agreement. If it was found that Balhousie had disposed of an 'entire interest' in the property then it would fall within the 10-year change of use/disposal provisions, and it would be liable in effect to payback to HMRC the VAT on the property which was relieved due to zero-rating upon the property's acquisition.

The UT considered whether the transaction could be viewed as a composite transaction, the net result of which resulted in Balhousie retaining a relevant interest in the building, or whether each individual transaction was to be looked at separately.

The UT disagreed with Balhousie's argument that it enjoyed the same rights before and after the transaction. The UT decided that the crucial difference was that Balhousie no longer derived its right of occupation from the original zero-rated supply, but instead from the lease. Balhousie therefore had disposed of its 'entire interest' in the care home. Consequently, Balhousie was liable to account for the VAT due upon the care home by means of a self-supply.

Our Indirect Tax Team can assist if you need any guidance in this area.

Mercedes-Benz Financial Services UK Ltd – rental agreement is a supply of services

The recent Court of Justice of the European Union (CJEU) decision in the Mercedes-Benz Financial Services UK Ltd (MBFS) case could have significant ramifications for motor trade businesses providing hire-purchase and leasing arrangements to customers as well as in other industries where such contracts are commonly used to finance the acquisition of assets.

For VAT purposes, a lease is generally treated as a supply of services, whereas a hire-purchase agreement is treated as a supply of goods (as it expressly envisages that title to the goods will pass at the end of the hire term). The Agility agreement however, contained features associated with both lease and hire-purchase agreements, and was aimed at customers who were unsure whether

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they wanted to own the vehicle at the end of the lease period. This made it hard to classify.

HMRC argued that the Agility agreement, in line with the 'Hire Purchase' agreements, represented a supply of goods within the meaning of Article 14(2)(b) of the VAT Directive. HMRC therefore demanded full payment of VAT from MBFS upon the handing over of the vehicles at the start of the Agility agreements.

MBFS challenged this, contending that the Agility agreement, which does not necessarily provide for a transfer of ownership, had to be regarded as a supply of services and that, therefore, VAT only needed to be accounted for when each monthly instalment was paid.

The CJEU determined that if the "only economically rational choice" is to exercise the option at the end of the lease and take ownership of the vehicle, the agreement shall be considered a supply of goods. Since the final instalment payment was so large under the Agility contracts, the customers had a genuine choice, so it appears likely that the referring court will find that the agreement was for a supply of services.

Businesses in the motor trade or those that provide hire-purchase/leasing arrangements should carefully review their contracts to ensure that the VAT treatment is correct. Please contact our Indirect Tax Team if you have any queries on this matter.

United Biscuits - Pension fund management services provided by non-insurers

The High Court (HC) has ruled that pension fund management services to Defined Benefit schemes, which are provided by non-insurers should be subject to VAT. This decision coincides with the recent HMRC Brief discussed in our November edition, which announced the removal of the VAT exemption for supplies of pension fund management services by insurers. This ruling will have implications for businesses that provide pension fund management services, and trustees who will now be charged VAT on these services.

The trustees of the United Biscuits pension funds sought to recover VAT directly from HMRC which they were charged on pension fund management services provided by non-insurers.

It has long been HMRC's policy to treat supplies of pension fund management by insurers as falling within the insurance exemption contained within the Principal VAT Directive Art 135(1)(a). The trustees argued that this exemption should be applied to pension fund management services provided by insurers and non-insurers alike, otherwise it breached the principle of fiscal neutrality.

The HC rejected the contention that pension fund management services amounted to an exempt supply of insurance. It stated that insurance involves indemnifying a person against a risk, something that is absent from the management of pension funds. As a result, the fiscal neutrality argument was not relevant.

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Since the HC considered the case *'acte clair'*, there was no need for the matter to be referred to the CJEU. The HC also mentioned that the trustees did not have a case to seek a refund of overpaid VAT directly from HMRC; they should have requested this from the managers, had the VAT been erroneously charged.

Businesses providing pension fund management services should check they are applying VAT correctly following this decision. Trustees may wish to discuss this matter with our Indirect Tax Team, to ensure they are recovering as much VAT as possible.

Introduction of domestic reverse charge in construction sector

Following HMRC's consultation into fraud in construction sector labour supply chains, HMRC has decided to proceed with the introduction of a domestic reverse charge. This will mean the customer who receives a supply of construction workers will be required to account for the VAT. The Government believes this is the most appropriate form of action to take to combat this issue, and it should come into effect from October 2019.

Our Indirect Tax Team can assist if you require any guidance in this area.

HMRC clarifies zero-rating relief for construction services

HMRC has published an information sheet clarifying their policy on how VAT is applied to the construction of buildings that keep or make use of, parts of a building that previously stood on, or were adjacent to, the site where the works of construction took place. This notice will be of importance to owners and developers of buildings that are being constructed on sites previously occupied by buildings, those making a first grant of a major interest in the building, those in receipt of construction services or those making a claim under the DIY House Builder Scheme.

For further information on the implications, please contact our Indirect Tax Team.

Bridge is not a sport for VAT purposes

Not for profit bodies involved in the regulation and development of games such as bridge may need to review the nature of the activity to check whether it can benefit from the VAT exemption.

The recent CJEU decision regarding English Bridge Union Limited (EBU) provided clarity as to what constitutes a sport for VAT purposes.

The EBU organised tournaments and charged players a fee to participate, plus VAT. The EBU contended that bridge was in fact a sport for VAT purposes, and should be exempt under Article 132(1)(m) of the VAT Directive 2006/112. The EBU therefore believed it was due a repayment of this VAT for participating in the tournaments.

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A referral was made to the CJEU to provide guidance as to what constitutes a sport according to the VAT Directive. The Court ruled that, although there was no definition of what a 'sport' is in the Directive, its usual meaning in everyday language should be considered, whilst taking into account the context of its use.

The CJEU found that the concept of sport was characterised by a physical element, whereas bridge involved logic, memory and planning and could not be considered physical enough to constitute a sport. The CJEU did suggest that card games such as bridge could fall under the cultural exemption, if a member state listed it as a 'cultural service'.

Following this decision, it is possible that similar games/sports currently treated as exempt from VAT may be challenged by HMRC. Not for profit bodies involved in similar areas who are concerned about this ruling should contact our Indirect Tax Team for assistance.

Di Maura - Bad Debt Relief timing

A recent CJEU decision could lead to changes to the rules for bad debt relief (BDR) for businesses across the EU where these are ultra vires EU VAT law. However, the current UK rules would appear to comply.

Generally, BDR rules are set by the EU, but member states have some flexibility in setting the conditions that need to be satisfied for a claim to be made. The condition queried in Di Maura which was referred to the CJEU, was timing. The taxpayer made an adjustment to its VAT return after a customer failed to settle an invoice. Italian VAT rules prior to 2017 state that BDR is available only after insolvency proceedings have been concluded (and the payment obligation remains unsettled) in order to ensure any possibility of payment is exhausted.

The CJEU decided that the Italian rules were disproportionate to achieving their objective. The taxpayer should instead demonstrate a reasonable probability that the obligation of payment will not be fulfilled. The UK imposed an "insolvency condition" on claims for bad debt relief prior to 31 March 1989 at which point this condition was withdrawn as it was thought then to be ultra vires.

Member states should make sure that the conditions for BDR are proportional and in line with the principle of fiscal neutrality, so as not to disadvantage businesses.

Please contact our Indirect Tax Team if you have any concerns following this judgment.

New VAT rules for e-commerce sales

With internet sales increasing rapidly year on year, the European Council is putting measures into place to simplify VAT for online businesses and to combat VAT fraud.

The new rules include extending the existing 'mini one-stop shop' portal (MOSS) so that it applies to the distance selling of goods, and the creation of a new portal for distance sales of goods from third countries with a value below €150. For B2C sales, VAT will be paid in the member state of the consumer, which is expected to ensure a fairer distribution of tax revenues amongst member states.

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The changes also plan to create a level playing field between businesses by making online platforms (such as Amazon and eBay) liable for the collection of VAT on the distance sales facilitated by them. They will be treated as having received and supplied the goods themselves.

At present, goods imported from outside the EU can benefit from a low value exemption, if the goods are valued at less than €22. This exemption entitles traders to import goods VAT free. The new changes have called for the removal of this exemption, to combat abuse of the system.

Moreover, start-ups and SMEs will be able to continue to apply the VAT rules used in their home country, up to a limit of yearly cross-border online sales of €10,000. This new simplification is due to come into effect on 1 January 2019.

The European Council adopted the new rules on 5 December 2017, with the aim of making it easier for online businesses to comply with their VAT obligations, providing cost savings for businesses, and increasing tax revenues for member states. The rules are also expected to allow for improved administrative cooperation between member states. The new MOSS system will also relieve online traders of the burden of having to register for VAT in each member state in which they operate.

With the exception of the simplification measure for electronic services these measures will come into force from 1 January 2021.

Please contact our Indirect Tax Team if you have any queries in relation to this.

HMRC publishes VAT Grouping consultation responses

HMRC has published the responses following its consultation into the scope of VAT Grouping. The aim of the consultation was to consider the need for changes to the VAT Grouping provisions in light of recent VAT case law – such as *Skandia America Corporation* and *Larentia + Minerva and Marenave*. The consultation also examined the options concerning eligibility requirements for VAT group registration. HMRC has stated that it will continue to review the scope of VAT grouping, the issues raised, and it will consider the impact the UK's exit from the EU will have on such changes. HMRC will also clarify its current approach to certain types of partnerships through a policy paper, providing greater clarity to businesses.

Please contact our Indirect Tax Team if you have any concerns about this.

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Autumn 2017 Budget - VAT

Online VAT fraud

The Government has strengthened its powers to crackdown on tax fraud, where foreign companies warehousing products in the UK are selling them, VAT free, via internet market places such as Amazon and eBay.

Online marketplaces will now be jointly and severally liable for any unpaid VAT that businesses selling through their platforms fail to account for. There will also be a requirement for the marketplace to display the sellers' VAT numbers and check that they are valid.

These tough measures are good news for UK traders who have suffered a competitive VAT disadvantage because of non-compliant online sellers.

In line with these changes, HMRC has also published the responses following its consultation on Split Payments. This mechanism aims to collect VAT from online sales and transfer this to the tax authorities in real time, with no involvement from the seller and removing the difficulty of enforcing compliance.

The responses indicate that the split payment model is feasible, and HMRC will continue conducting user research over the next few months, including holding workshop-style sessions for those interested in participating.

Please contact out Indirect Tax Team if you have any queries regarding this matter.

VAT and vouchers

The Government is planning to legislate in Finance Act 2018-19 to ensure businesses account for the same amount of VAT when customers pay with vouchers compared with other means of payment, in order to bring UK legislation in line with the EU VAT Directive. It is envisaged that the changes will come into force from 1 January 2019.

To prepare for this, HMRC has launched a consultation on VAT and Vouchers, seeking comments from UK businesses (mainly in the retail sector) who buy, sell, and redeem vouchers and gift cards. This offers businesses an opportunity to highlight any concerns they have about the proposed changes. The deadline for responses is 23 February 2018.

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Freeze to VAT registration and deregistration thresholds

The threshold at which businesses need to register for VAT will be maintained at £85,000 until at least 31 March 2020.

This is the highest threshold in the EU and is favourable for small businesses wishing to price competitively and to those where the administrative burden would exceed the tax savings that being VAT registered can bring.

The deregistration threshold will also remain at £83,000 until 31 March 2020.

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