VAT update

July 2018

In this month's update we report on the alignment of the period for recovery of VAT by exempt public sector entities; new guidance concerning VAT liability on goods supplied on approval; and HMRC's policy paper on a new regime for interest and penalties. We also comment on three recent VAT cases on whether VAT is payable on a transfer by a company to a shareholder on a buy-back of shares; input tax recovery on supplies wrongly treated as exempt; and whether certain claims for the return of overpaid VAT are to be treated as having been made by the "single taxable person" constituted by the representative member of the VAT Group.

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Policy paper on interest and penalties

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Skarbowej: CJEU confirms that VAT is payable on the transfer of immovable property by a company to a shareholder on a buy-back of its shares

In *SZEF Krajowej Administracji Skarbowej v Polfarmex Spółka Akcyjna w Kutnie* (Case C-421/17), the Court of Justice of the European Union (CJEU) has confirmed that the transfer by a company to one of its shareholders, on a buy-back of the company's shares, of ownership of immovable property, is a supply of goods for consideration subject to VAT provided the property is used in an economic activity by that company. more›

Any comments or queries?

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About this update

The VAT update is published on the final Thursday of every month, and is written by members of RPC's Tax team.

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Zipvit: No input tax recovery for supplies wrongly treated as VAT exempt

In *Zipvit Limited v HMRC* [2018] EWCA Civ 1515, the Court of Appeal, agreeing with the First-tier Tribunal (FTT) and the Upper Tribunal (UT), has held that the taxpayer was not entitled to reclaim VAT in respect of supplies of services which had been wrongly treated as exempt from VAT. more›

Taylor Clark: Claims for the return of overpaid VAT not to be treated as having been made by or on behalf of the "single taxable person"

In *HMRC v Taylor Clark Leisure Plc* [2018] UKSC 35, the Supreme Court has held that a company which claimed recovery of VAT is not to be considered to have made a claim for repayment, where another company, which had formerly been a member of its VAT Group, had made the relevant claims. The other company had claimed repayment in its own right and not on behalf of the first company. more›

News

Alignment of period for recovery of VAT by exempt public sector entities

On 25 June 2018, HMRC published "Revenue and Customs Brief 4 (2018): aligning time limits for VAT refund schemes". The Brief explains that bodies performing statutory functions, such as the Police and Local Authorities, which are outside the scope of VAT have the ability to claim refunds for associated VAT costs under section 33, VATA.

This has the effect of extending the time limit for claiming refunds from 3 to 4 years and reflects the time limits applicable to VAT recovery claims by taxable entities.

A copy of the Brief can be viewed here.

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Guidance on VAT liability on goods supplied on approval

On 18 June 2018, HMRC published "Revenue and Customs Brief 5 (2018): VAT liability on goods supplied on approval". The Brief explains HMRC's policy in circumstances where goods are supplied on approval and the liability in relation to delivery changes.

HMRC is of the view that its previous guidance (VRS9150), which stated that mail order retails "normally supply goods on approval terms", is incorrect. HMRC has indicated that this may be the case in certain circumstance but that this would be unusual.

In *Littlewoods Organisation plc* (VTD 14977), it was held that goods were supplied on approval where there is no contract of sale unless and until the recipient concerned adopted, or was deemed to have adopted, the goods. This is different from a supply of goods with a subsequent right to return the goods.

HMRC states that retailers may have wrongly accounted for VAT on approval terms and that this may have led to them accounting for VAT at the wrong time.

While not requiring any retrospective correction, HMRC has indicated that retailers will be expected to correct any anomalies within the next three months from the date of the Business Brief.

A copy of the Brief can be viewed here.

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Policy paper on interest and penalties

On 6 July 2018, HMRC published Policy paper: "Interest harmonisation and sanctions for late payment". The Paper outlines ways in which HMRC would like to modify the interest payment and penalty regimes applicable to the late payment, or repayment, of VAT.

HMRC proposes that the VAT interest rules should be aligned more closely with those applicable to income tax self-assessment and corporation tax, in order to make the tax system simpler.

Late payment interest will be charged from the date that the payment was due and repayment interest on sums due to the taxpayer will be calculated from the date HMRC should have repaid the taxpayer.

The current late payment regime is to be replaced with a new regime to apply for VAT from April 2020.

The new late payment penalty will consist of two separate charges. The first charge is payable 30 days after the VAT payment is due and will be based on a percentage of the sum unpaid. The exact sum to be paid will depend on what payments are made or any Time to Pay (TTP) arrangement which has been agreed during this 30 day period.

A second charge will apply for sums outstanding from day 31 until payment is made. If a TTP arrangement has been agreed, penalties under the second charge will also be suspended from the date the TTP arrangement was agreed.

A copy of the Policy paper can be viewed here.

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Cases

Skarbowej: CJEU confirms that VAT is payable on the transfer of immovable property by a company to a shareholder on a buy-back of its shares

In *SZEF Krajowej Administracji Skarbowej v Polfarmex Spółka Akcyjna w Kutnie* (Case C-421/17), the Court of Justice of the European Union (CJEU) has confirmed that the transfer by a company to one of its shareholders, on a buy-back of the company's shares, of ownership of immovable property, is a supply of goods for consideration subject to VAT provided the property is used in an economic activity by that company.

Background

Polfarmex, a limited company with its registered office in Poland, manufactures pharmaceutical products and as such is subject to VAT.

Polfarmex planned to restructure its share capital through the buy-back of part its shares held by a limited liability company, using one of the methods of "redemption" provided for by the Companies Code. The compensation due by reason of that redemption would be the transfer, in favour of the other company, of ownership of some land and the buildings (including equipment in the buildings).

Polfarmex made an application to the appropriate Minister for a tax ruling in order to determine whether the redemption of the shares held by the limited liability company and the transfer of ownership of immovable property in favour of that company, would be subject to VAT.

In his ruling, the Minister took the view that the transfer of immovable property in return for the redemption of shares should be regarded as a supply of goods for consideration subject to VAT. In the view of the Minister, there would be a binding relationship between the parties to the transaction. Polfarmex committed to transfer to the limited company ownership of immovable property and the shares redeemed constituted the consideration for that transfer. Accordingly, since there would be a supply of goods for consideration, the transaction would be subject to VAT.

Polfarmex brought an action before the Regional Administrative Court in Poland seeking annulment of that ruling.

The Administrative Court annulled the tax ruling. It was of the view that the transaction proposed by Polfarmex would not be a transaction carried out in the course of its economic activity and the examination of the applicability of VAT must cover the entire transaction. Polfarmex was proposing a single transaction, consisting of the redemption of shares combined with the transfer to a shareholder of consideration in kind in exchange for the shares redeemed. Redemption of the shares was therefore closely linked to the transfer of ownership of the assets as payment, those two aspects of the transaction being interdependent. It followed that the transfer of the immovable property to the shareholder could not be considered an autonomous and separate transaction subject to VAT.

The Minister appealed to the Supreme Administrative Court in Poland.

In the view of the Supreme Court, the transfer of immovable property to a company in consideration for the acquisition of the shares which it held in that company, constitutes a taxable transaction within the meaning of Article 5(1), point 1, and Article 7(1) of the Law on VAT. Despite the similarity between the redemption of equity and shares, the question of whether the proposed transaction is subject to VAT raised doubts regarding the condition of acting as a taxable person and the pecuniary nature of that operation since, following the redemption of shares, a company limited by shares receives nothing directly in return as the representative shares in part of its share capital are cancelled and that share capital is reduced on a pro rata basis.

The Supreme Administrative Court therefore decided to refer the following question to the CJEU for a preliminary ruling:

"Does the transfer by a public limited company of immovable property to a shareholder in connection with the redemption of its shares constitute a transaction that is subject to value added tax in accordance with Article 2(1)(a) of Council Directive 2006/112?".

CJEU's judgment
The CJEU concluded that Polfarmex would make a supply of goods for consideration subject to VAT, by transferring ownership of immovable property (the building) to a shareholder.

Article 2(1)(a) of the Principal VAT Directive provides that VAT is chargeable on supplies of goods for consideration. The CJEU stated that the building would be exchanged for shares and therefore there would be a legal relationship in which there would be reciprocal performance, with each being consideration for the other.

Comment
Whilst this judgment is interesting, UK company law requirements may limit the relevance of this decision in the UK. The CJEU's comments, based on *Kretztechnik AG v Finanzamt Linz* Case C-465/03, that share redemptions may not be an economic activity, may be of more interest, as buy-backs are generally regarded as exempt.

A copy of the judgment can be viewed here.

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Zipvit: No input tax recovery for supplies wrongly treated as VAT exempt

In *Zipvit Limited v HMRC* [2018] EWCA Civ 1515, the Court of Appeal, agreeing with the First-tier Tribunal (FTT) and the Upper Tribunal (UT), has held that the taxpayer was not entitled to reclaim VAT in respect of supplies of services which had been wrongly treated as exempt from VAT.

Background
Zipvit supplied vitamins and minerals using Royal Mail services to despatch mail orders. The relevant invoices from Royal Mail indicated that the supplies were exempt from VAT. The issue was whether Zipvit was entitled to input tax credit in respect of the supplies which, at the material time, were treated by Royal Mail and HMRC as VAT exempt, but were actually properly chargeable to VAT as the postal exemption did not apply to individually negotiated supplies (*TNT Post UK Ltd v HMRC* [2009] ECR I-3025).

Two questions required determination: (1) whether VAT was "due or paid" pursuant to Article 168(a) of the Principal VAT Directive, so that Zipvit was entitled to deduct input tax; and (2) whether the lack of invoices from Royal Mail to Zipvit was central to HMRC's exercise of discretion under Regulation 29 of the VAT Regulations 1995 to reject Zipvit's alternative evidence of it having received taxable supplies for the purposes of its trade.

FTT decision
The appeal was dismissed.

In the view of the FTT, the words "due or paid", referred to the payment of the relevant VAT by Royal Mail to HMRC. The Royal Mail had not declared VAT, issued an invoice showing the VAT, or been assessed to pay VAT by HMRC and there was no enforceable tax claim. As such, the VAT on the supplies was not "due or paid" by Zipvit and it therefore had no right of recovery.

Although HMRC's exercise of discretion had been flawed as it had not considered all relevant matters, the alternative evidence produced in an attempt to demonstrate that Zipvit had paid the VAT was rejected by the FTT because Zipvit did not suffer the economic burden of the VAT.

Zipvit appealed to the UT.

UT decision
The appeal was dismissed.

In a departure from the FTT decision on question (1), the UT held that the correct question was whether the relevant tax had been paid by, or was due from, Zipvit who sought to deduct it as input tax to Royal Mail. The UT accepted Zipvit's argument that sums paid by Zipvit to Royal Mail had to be treated as inclusive of VAT at the standard rate as no invoice detailing the VAT charged had been received by Zipfit from Royal Mail.

The UT agreed with the FTT that, although HMRC had failed to consider all relevant matters in exercising its discretion, the alternative evidence should still be rejected because Zipvit did not suffer the economic burden of VAT.

Zipvit appealed to the Court of Appeal.

Court of Appeal judgment
The appeal was dismissed.

Given the amount of tax liability at stake, £1bn, and the wider litigation, the Court was of the view that it was important for the facts to be investigated as fully as possible and it therefore admitted fresh evidence in the form of Royal Mail General Terms in order to achieve a more complete set of contractual documentation. The fresh evidence suggested that the postal charges excluded VAT, which was liable to be paid by the customer, Zipvit.

The Court held that in circumstances where Royal Mail had a contractual right to recover an amount equivalent to VAT from Zipvit, but took no steps to enforce that right, a reference to the CJEU would be needed in order to determine whether Zipvit was entitled to claim a deduction for the VAT element of the original purchase price which was now treated as VAT inclusive. The Court said the position would be the same if, contractually, the parties had expressly agreed for the supplies to be VAT-inclusive.

In respect of the invoices, Zipvit attempted to treat the original VAT exempt payments made as VAT inclusive with no more evidence than the original payments. Zipvit was unable to provide evidence that the VAT had been paid or accounted for by Royal Mail. The Court said that VAT invoices are essential to enable HMRC to check whether the correct entity or individual has paid the VAT required. In the interests of fiscal justice, even if Zipvit was entitled to re-characterise the original payment as VAT inclusive, there would be an obvious detriment to HMRC and the public purse if Zipvit succeeded without first evidencing that Royal Mail had paid the VAT.

Comment

This judgment provides helpful clarification as to the entity liable for VAT in respect of the postal exemption for individually negotiated supplies and provides a stark reminder of the need to have clear evidence of tax being paid before attempting to claim a tax credit. Given the amount of tax in issue, it is likely that Zipvit will seek permission to appeal to the Supreme Court.

A copy of the judgment can be viewed here.

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Taylor Clark: Claims for the return of overpaid VAT not to be treated as having been made by or on behalf of the "single taxable person"

In *HMRC v Taylor Clark Leisure Plc* [2018] UKSC 35, the Supreme Court has held that a company which claimed recovery of VAT is not to be considered to have made a claim for repayment, where another company, which had formerly been a member of its VAT Group, had made the relevant claims. The other company had claimed repayment in its own right and not on behalf of the first company.

Background

Taylor Clark Leisure Plc (TLC) was the representative member of the Taylor Clark VAT Group for the years 1973 to 2009, when the Group was disbanded. In 1990, TLC transferred its bingo business to Carlton Clubs Ltd (Carlton), a newly incorporated subsidiary entity. The transfer was effected by a letter dated 30 March 1990 (the Asset Transfer Agreement). Carlton was a member of the VAT Group from 1990 until 1998, when it was sold.

In November 2007, Carlton submitted four claims for repayment of VAT which TLC had overpaid in the period 1973 to 1998. The claims related to the VAT treatment of bingo. Following the CJEU's decision in *Rank Group PLC v HMRC* (Joined Cases C-259/10 and C-260/10) [2011] ECR I-10947; [2012] STC 23, HMRC issued Revenue and Customs Brief 39/11, which accepted that repayment would be due (subject to verification).

The claims issued by Carlton used the TLC Clark VAT Group registration number but they had not been authorised by the Group. TLC maintained that it was able to rely on Carlton's claims because it was the representative member of the VAT Group at the time the supplies were made.

HMRC rejected the claims on the following basis:

1. that the claims had not been made before the expiry of the time limit (because no claims had been made by TLC itself)
2. the claims predating 31 March 1990 had been assigned to Carlton by the Asset Transfer Agreement, and

3. because the VAT Group had since been disbanded, the claim for over-declared output tax must be made by the company whose activities gave rise to the over-declaration and Carlton had made that claim[1].

Carlton and TLC initially pursued rival appeals, however, Carlton withdrew three of its four appeals because HMRC had paid them. The remaining appeal was stayed. TLC maintained its appeals.

FTT decision
The appeal was dismissed.

The FTT found that:

1. the right to claim repayment for periods prior to 1990 had been assigned to Carlton under the Asset Transfer Agreement
2. the right to claim had been passed back to Carlton from the VAT Group when it left the VAT Group in 1998, and
3. TLC had not, itself, made a claim under section 80, VATA and could not rely on Carlton's claims; it was therefore out of time to make a fresh claim.

TLC appealed all three issues.

UT decision
The UT reversed the decision of the FTT in relation to issue 1. The UT found that the right to claim had not been transferred to Carlton. The UT also found that it was only TLC who could make a claim for repayment because it was the representative member of the VAT Group at the time.

With regard to issue 3, the UT agreed with the FTT that TLC had not made a valid claim under section 80, VATA, and accordingly, did not have a valid claim and was time-barred from issuing a new claim.

TLC appealed to the Inner House on issue 3.

Inner House judgment
The question for the Inner House was:

"Can the VAT Group, represented by [Taylor Clark], rely on the claims for repayment of VAT overpaid by the VAT Group, when the claims were made in time but were made by another member of the same VAT Group?"

The Inner House took the view that the actions of individual members of a VAT Group could be ascribed to the representative member of a Group where they related to VAT. By adopting a purposive interpretation of the relevant legislation, the Inner House concluded that the claims made by Carlton were deemed to have been made by TLC as the representative member.

HMRC appealed.

1. HMRC's policy in relation to claims from disbanded VAT Groups has since changed and as it currently stands, HMRC considers that such claims vest with the last representative member of a disbanded VAT Group.

Supreme Court judgment
The appeal was allowed.

The Supreme Court reversed the judgment of the Inner House. It did not accept that Carlton's claims had been made by or on behalf of TLC.

Firstly, they were made after Carlton had left the VAT Group. Secondly, the use of the Group VAT registration number was not determinative since it was necessary to use that number in order to identify the relevant VAT payments. Thirdly it was clear that Carlton was not acting as TLC's agent. Carlton had asserted its own belief that claims which existed before its incorporation in 1990 and related to periods going back to 1973, had been assigned to it in 1990 under the Asset Transfer Agreement.

Carlton relied on the case of *Triad Timber Components Ltd v HMRC* [1993] VATTR 384, which supported its position that it had the right to make a reclaim in relation to a period when it was in a VAT Group, when it left the Group and the Group ceased to exist. This position also reflected HMRC's policy at the time.

Comment
The position can become complicated when entities join and leave existing VAT Groups or the Group as a whole ceases to exist.

The effect of the Supreme Court's judgment is that where there has been an overpayment of VAT from a VAT Group, the entity entitled to make a claim for recovery is the Representative Member, or a person acting as agent for the Representative Member, unless the claim has been assigned.

In circumstances where corporates are intending to issue claims which relate to VAT Groups it is important that appropriate advice is sought at an early stage in the process so as to avoid the possibility that a claim which is valid on the issue of substance is not lost due to a deficiency in form.

A copy of the judgment can be viewed here.

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