VAT update

January 2020

In this month's update we report on (1) changes to the rules relating to distance selling; (2) changes to VAT for intra-EU chain transactions and zero rated goods; and (3) HMRC's guidance on proposed changes to the VAT treatment of call-off stock arrangements. We also comment on three recent cases which consider (1) whether VAT zero rating is available for electronic editions of newspapers; (2) the scope and meaning of "services of consultants", for the purposes of Article 59(c), Principal VAT Directive; and (3) the deductibility of input tax on fees incurred in implementing a tax scheme.

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On 2 December 2019, Council Directive 2019/1995, which seeks to introduce changes to the rules relating to distance sales, was published in the Official Journal. This publication follows the formal adoption by the Education, Youth, Culture and Sport Council on 22 November 2019. more›

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On 23 December 2019, HMRC published new guidance on the proposed changes to the VAT treatment of call-off stock provided for by Council Directive (EU) 2018/1910 (the Directive) and Council Implementing Regulation (EU) 2018/1912. more›

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News Corp – digital newspapers are "newspapers" for VAT purposes

In *News Corp UK & Ireland Ltd v HMRC* [2019] UKUT 0404 (TCC), the Upper Tribunal (UT) has reversed the decision of the First-tier Tribunal (FTT) and held that digital versions of newspapers fall within item 2, Group 3, Schedule 8, VATA 1994 and are zero-rated for VAT purposes. more›

Any comments or queries?

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About this update

Our 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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Gray & Farrar International – the services supplied by a matchmaking business did not fall within the "services of consultants"

In *Gray & Farrar International LLP v HMRC* [2019] UKFTT 684, the First-tier Tribunal (FTT) has held that the matchmaking services supplied by the taxpayer went beyond the provision of "services of consultants", for the purposes of Article 59(c), Principal VAT Directive 2006/112. **more›**

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News items

Changes to the rules relating to distance sales

On 2 December 2019, Council Directive 2019/1995, which seeks to introduce changes to the rules relating to distance sales, was published in the Official Journal. This publication follows the formal adoption by the Education, Youth, Culture and Sport Council on 22 November 2019.

The changes to the distance sales provisions were first laid down and approved in 2017 and are due to enter into force in 2021. They clarify which member state will be administratively competent for a specific sale, and when an online platform (such as Amazon, E-bay or Alibaba) is to be considered as having a role in a sale and therefore ultimately responsible for ensuring the VAT is collected.

Following publication in the Official Journal, the Council Directive will enter into force on the 20th day after its publication (and the changes will apply from 1 January 2021). Member States will have to adopt and publish, by 31 December 2020 at the latest, the laws, regulations and administrative provisions necessary to comply with the Directive.

The Directive can be viewed here.

Changes to VAT for intra-EU chain transactions and zero rated goods

On 19 December 2019, the Value Added Tax (Place of Supply of Goods) Amendment Order 2019 (SI 2019/1507) (the Amendment Order) and the Value Added Tax (Amendment) (No 2) Regulations 2019 (SI 2019/1509) (the Amendment Regulations) were made, introducing changes to UK law required by Council Directive (EU) 2018/1910 (the Directive).

The Directive made certain "quick fix" amendments to Council Directive 2006/122/EC (the Principal VAT Directive) to improve the functioning of VAT in EU cross-border transactions.

The Directive makes provision for chain transactions (which occur where a number of businesses successively buy and sell the same goods but the goods themselves are transported directly from the original supplier and delivered to the final purchaser).

The Amendment Order amends the Value Added Tax (Place of Supply of Goods) Order 2004 (SI 2004/3148), as required by the Directive, identifying the transaction in the chain that is to be treated as the intra-community supply and, therefore, zero-rated, and specifying how the place of supply of goods provisions in section 7(2), VATA 1994, are to apply to supplies of the goods after that supply.

The Amendment Regulations amend the VAT Regulations 1995 (SI 1995/2519), to reflect in legislation the conditions for the application of zero-rating to intra-community supplies.

On 20 December 2019, HMRC published guidance on the practical application of the changes, noting that the new chain transaction rules will achieve the same end result as the UK's current policy.

HMRC's guidance can be viewed here.

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HMRC publishes guidance on the proposed changes to the tax rules for call-off stock arrangements

On 23 December 2019, HMRC published new guidance on the proposed changes to the VAT treatment of call-off stock provided for by Council Directive (EU) 2018/1910 (the Directive) and Council Implementing Regulation (EU) 2018/1912.

Call-off stock arrangements refer to goods that are transported by a supplier from one member state to a customer in another, in circumstances in which the supplier already knows the identity of the person to whom the goods will be supplied. Currently, the rules applied by member states differ across the EU. Although the UK allows the customer to account for the acquisition when the goods first arrive into the UK and before being called-off, some member states require the supplier to register for VAT and account for the acquisition and subsequent supply to the customer.

The changes to EU law are intended to simplify the position and avoid the need for the supplier to register for VAT in the destination member state. Instead, subject to certain conditions, the new rules will treat the intra-community supply of the goods as occurring when the goods are called-off and the final supply is made to the customer. The conditions include the following requirements:

- there must be a call-off stock agreement between supplier and customer and the maintenance of detailed records
- the supplier must not have a business or other fixed establishment in the destination member state
- the customer must be registered in the destination member state and the supplier must know the identity of the customer and the customer's VAT registration number, and include this on its EC sales list.

Taxpayers who do not meet the conditions fall outside the new rules and will continue to be subject to the current VAT accounting treatment afforded in the relevant member state.

The changes provided for in the Directive will be enacted into UK law through amendments to VATA 1994 and the VAT Regulations 1995 (SI 1995/2518). The government intends to include this measure in the next Finance Act. The measure will apply, subject to the conditions in the legislation, in cases where goods are removed from an EU country on or after 1 January 2020 (the legislation will therefore have a retrospective element). This means businesses can take advantage of the new arrangements from 1 January 2020.

HMRC's guidance can be viewed here.

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Cases

News Corp – digital newspapers are "newspapers" for VAT purposes

In *News Corp UK & Ireland Ltd v HMRC* [2019] UKUT 0404 (TCC), the Upper Tribunal (UT) has reversed the decision of the First-tier Tribunal (FTT) and held that digital versions of newspapers fall within item 2, Group 3, Schedule 8, VATA 1994 and are zero-rated for VAT purposes.

Background

News Corp UK & Ireland Limited (News Corp) is the representative member of a VAT group that publishes, principally, *The Times*, *The Sunday Times*, *The Sun* and *The Sun on Sunday*.

The main issue for determination was whether digital versions of these newspapers are "newspapers", within the meaning of Item 2, Group 3, Schedule 8, VATA 1994, and are therefore zero rated.

News Corp and HMRC could not reach agreement on this issue and the dispute came before the FTT for determination. The FTT concluded that although the digital versions are equivalent to the newsprint editions, they are not "newspapers" within the meaning of Item 2, News Corp appealed to the UT.

Whilst recognising that the concept of a supply of digital versions of newspapers was not within the contemplation of the drafter of the legislation in 1972, News Corp contended that the meaning of "newspapers" was broad enough to include digital versions which were now available. In the alternative, it relied on the "always speaking" doctrine of statutory interpretation.

UT decision

The appeal was allowed.

The UT addressed the interpretation of "newspapers" in Item 2 in the round, having regard to all relevant rules of construction, including (i) the requirement for strict interpretation of an exception to the general rule as to standard rating, and (ii) the "always speaking" doctrine.

The UT observed that in order to conclude that "newspapers" included digital newspapers, it was necessary to find that digital newspapers were within the legislative purpose, as a consequence of the characteristics they shared with physical newspapers that existed at the time the legislation was enacted. The legislative purpose of Item 2 was a matter of common ground in the case, namely, to promote literacy, the dissemination of knowledge and democratic accountability by having informed public debate.

The FTT's conclusion was based on its conclusion that Group 3 was concerned only with goods and services. This was fatal to News Corp's case given it was common ground that digital versions of the newspapers were services and not goods. The UT disagreed with the FTT's conclusion that on its proper construction Group 3 was intended to be limited to items that were goods.

Having concluded that the FTT's reasoning was flawed, the UT went on to consider whether, applying the principles of construction (including the "always speaking" doctrine), the word "newspapers" is to be interpreted as including the relevant digital versions of *The Times*, *The Sunday Times* and *The Sun* newspapers in this case.

In the view of the UT, it was not sufficient to simply demonstrate that a particular service satisfied the legislative purpose. It was also necessary that the service shared the essential characteristics of a "newspaper". For this reason, a rolling news website, which furthered the legislative purpose, would not satisfy the test as it did not provide edition-based news.

The UT concluded that both the purpose and the characteristics of the print and digital editions were identical. This was particularly true of the e-reader version, which consisted of an exact facsimile of the printed newspaper made available for downloading. The UT added that the invention of a digital form of newspaper was the type of technological development (not contemplated at the time the legislation was enacted) that the "always speaking" doctrine was intended to address.

Comment

This is an important decision which has implications beyond the realm of newspapers. If, as the UT found, Group 3 is not limited to physical goods then this may alter the VAT treatment of other electronic services that satisfy the essential characteristics of the other items listed in Group 3, such as, maps, charts, booklets, brochures, leaflets and books.

Given the importance of this decision, HMRC may seek to appeal to the Court of Appeal.

The decision can be viewed here.

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Gray & Farrar International – the services supplied by a matchmaking business did not fall within the "services of consultants"

In *Gray & Farrar International LLP v HMRC* [2019] UKFTT 684, the First-tier Tribunal (FTT) has held that the matchmaking services supplied by the taxpayer went beyond the provision of "services of consultants", for the purposes of Article 59(c), Principal VAT Directive 2006/112.

Background

Gray & Farrar International LLP (G&F) provided an 'exclusive' matchmaking service to clients in various jurisdictions. G&F's manager interviewed clients and used her expertise to identify potential matches. The client would then be provided with information about potential partners, together with the manager's advice, express or implied, as to their compatibility. The manager was supported by a small liaison team who sought feedback from clients on how meetings, dates and relationships were going and provided post-date support, coaching and counselling.

G&F considered its services fell within Article 59(c) of the Principal VAT Directive (implemented in the UK by paragraph 16(2)(d), Schedule 4A, VATA 1994) as they constituted "services of consultants". Accordingly, when it supplied its services to non-taxable persons residing outside

the EU, it treated the supply as being outside the EU and therefore outside the scope of VAT. HMRC disagreed and raised assessments on G&F. G&F appealed to the FTT.

It was agreed that the services provided by G&F should be compared to services "principally and habitually" provided by consultants and that services "principally and habitually" provided by consultants tend to be based on a "high degree of expertise". It was also agreed that G&F supplied a single composite supply.

The only issue before the FTT for determination was whether G&F's services were, or were similar to, the services provided by consultants, or fell within "data processing and the provision of information" within Article 59(c).

FTT decision
The appeal was dismissed.

The FTT adopted the same approach as the CJEU in *Maatschap MJM Linthorst, KGP Pouwels and J Scheres cs v Inspecteur der Belastingdienst/Ondernemingen Roermond* (Case C-167/95) [1997] STC 1287 and considered the principle components of the supply and whether it fell within the provision. In this respect, the labelling of the services provided by G&F as "matchmaking" was irrelevant.

In determining the nature of what is done, the FTT said that the perspective must be from that of the typical consumer, as the issue is what he or she receives not how it is supplied. In the present case, this was from the point of view of a client seeking a person with a view to a long-term relationship and so the question was, what was supplied in pursuance of that purpose.

In the FTT's view, the way in which G&F provided or created advice was not part of what it was providing. In regular telephone calls G&F sought information from its clients. In addition, it provided coaching or counselling. The seeking of information does not, of its self, satisfy the customer's purpose; to do that, the information had to come with G&F's advice. Together, these were the constituents of the supply.

The information provision clearly fell within Article 59(c). The question was whether the advice was expert advice, based on a high degree of expertise.

The FTT accepted that the managing partner had extensive match making experience. However, the ongoing advice and role of the liaison team was more difficult to categorise. The FTT considered whether the role of the liaison team was merely incidental to the provision of information and the expert advice provided by the managing partner, or ancillary to those supplies. It narrowly concluded (with the presiding member's casting vote) that the liaison team provided support in the development of a relationship, which was in addition to the provision of information and expert advice. On this basis, the FTT concluded that the service went beyond the provision of information and expert advice and therefore did not fall within Article 59(c).

Comment

This was a finely balanced decision and the two members of the FTT were unable to agree on the role of the liaison team and the correct categorisation of the services provided by G&F. Ms Wilkins regarded the role of the liaison team as ancillary to the expert advice provided by the managing partner, which would have meant the services did fall within Article 59(c) and would have been outside the scope of VAT in appropriate circumstances, but Judge Hellier disagreed and, as president, he had the casting vote and the taxpayer's appeal was therefore dismissed. The lack of consensus between the members, illustrates how difficult it can be to determine whether particular services fall within "services of consultants", for the purposes of Article 59(c).

The decision can be viewed here.

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Taylor Pearson – input tax on fees incurred in implementing a tax scheme was deductible

In *Taylor Pearson (Construction) Ltd v HMRC* [2019] UKFTT 691 (TC), the First-tier Tribunal (FTT) has held that input tax on fees incurred in implementing a tax scheme, intended to remunerate directors in a tax efficient manner, was deductible.

Background

Taylor Pearson (Construction) Ltd (the company) made supplies of construction goods and services, which were all taxable supplies for VAT purposes.

In March 2012, following a profitable trading year, the company decided to reward its three directors with bonuses of £50,000. The company engaged tax advisers to do so in a tax efficient manner. The fee was 11.5% of the total amounts paid to the directors. The scheme devised by the tax advisers included an issue of shares to the directors.

In HMRC's view, the company's case was similar to *Customs and Excise Commissioners v Rosner* [1994] STC 228 and *Finanzamt Köln-Nord v Becker* (Case C-104/12), in which input VAT incurred in defending a sole trader or individual employees personally, in criminal proceedings entirely unconnected to the business, was held not to be deductible.

HMRC issued a VAT assessment to the company pursuant to section 73, VATA 1994, in relation to the company's VAT periods ending 31 December 2012 and 31 March 2014. The company appealed.

The substantive issue was whether the company was entitled to deduct input VAT in relation to services provided by the tax advisers. There were two specific issues to be considered by the FTT:

1. whether the services supplied were used for the purpose of the company's business, within the meaning of section 24, VATA; and
2. whether the services supplied could have a direct and immediate link with taxable output supplies even though they had a direct and immediate connection with exempt supplies, being the issue of share capital in the company.

FTT decision
The appeal was allowed.

HMRC withdrew its first argument during the hearing, as the first issue of shares is not a supply for VAT purposes, and it is only the subsequent sale of shares that is exempt.

In the view of the FTT, the economic and commercial reality was that the services provided were tax advice in relation to the provision of employment rewards.

Referring to *Kretzchtechnik AG v Finanzamt Linz* (C-465/03), the FTT noted that the ultimate purpose of the arrangements, from the perspective of both the company and the employee, was to incentivise the employee in a tax efficient manner. It therefore had to consider whether that objective was for the purposes of the company's business.

HMRC argued that the incentivisation of employees did not have a direct and immediate link with the purposes of the business. The FTT disagreed and was highly critical of HMRC, commenting:

"I do not consider this argument has any merit whatsoever and do not understand why HMRC put it forward. This concerns me ... Perhaps of more concern to me is that this case is materially identical to the relatively recent case of *Doran Bros* ([2016] UKFTT 829), which was decided in favour of the appellant. HMRC did not appeal Doran Bros".

Applying *Doran Bros*, the FTT concluded that the incentivisation of employees, even when they were directors and shareholders of the company, had a direct and immediate link to the purposes of the business and it therefore allowed the appeal.

Comment
It is perhaps surprising that HMRC litigated this case, given its similarities to the FTT's decision in *Doran Bros* and the fact that case law in respect of *Kretcztechnik* is also well-established.

Following this decision and the FTT's criticism, HMRC should perhaps give careful consideration before adopting a position which has already been firmly rejected by the FTT.

Although this can be a difficult area, it is generally the case that VAT incurred on expenditure which is designed to increase staff morale and performance is a business expense.

The decision can be viewed here.

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- Shortlisted – Insurance Team of the Year – Legal Business Awards 2018
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