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V@

Welcome to the January 2022 edition of RPC's V@, an update which provides analysis and news from the VAT world relevant to your business.

News

- HMRC has published **Revenue and Customs Brief 15 (2021): Repayment of VAT to overseas businesses not established in the EU and not registered in the UK.** The brief explains the outcome of the review of the policy, which was outlined in **Revenue and Customs Brief 10 (2021)**, issued in July 2021 (which we reported on in the **July 2021 edition of V@**). The change allows overseas (non-EU established) businesses to claim VAT refunds where they have been experiencing difficulties in obtaining a certificate of status, where the delay is due to the official authority dealing with a rare and exceptional one-off event, for example a global pandemic.

- HMRC has published a **Summary of Responses** in relation to its Call for Evidence on Simplifying the VAT Land Exemption, made in May 2021. The Call for Evidence sought views on the current VAT rules relating to land and property and explored potential options for simplifying them. In response to the evidence received, HMRC has set up a working group with the aim of producing guidance for HMRC compliance officers, which will also provide some certainty for businesses.

- HMRC has published **Revenue and Customs Brief 1 (2022): reviewing how to claim VAT when charging electric vehicles for business purposes.** HMRC is considering the situation where an employee is reimbursed by their employer for the actual cost of electricity used in charging an electric vehicle for business purposes. HMRC is, amongst other things, considering a number of simplification measures which it is hoped will reduce administrative burdens in terms of accounting for VAT on private use. The Brief indicates that, once HMRC's review is completed, HMRC will publish guidance confirming its policy.

Case reports

Ventgrove – Court of Session decides that no VAT is due on payment under a lease break clause

In *Ventgrove Ltd v Kuehne + Nagel Ltd* [2021] CSOH 129, the Court of Session held that a payment made by a tenant, Kuehne + Nagel Ltd (**KNL**), to its landlord, Ventgrove Ltd (**VL**), to exercise an option to end the lease, was not subject to VAT.

KNL had exercised a break option to terminate its lease. The lease required KNL to make a payment to VL, plus any VAT "properly due" on such amount. KNL did not include an amount of VAT in its payment and VL argued that the lease was not validly terminated as (1) it had opted to tax; and (2) HMRC had changed its policy on termination payments and now considered such payments to be subject to VAT.

The Court of Session held that the lease had been validly terminated as no VAT was in fact properly due on the break clause payment. This was because:

- at the time the break option had been exercised, HMRC had updated its guidance (**Revenue and Customs Brief 12 (2020): VAT early termination fees and compensation payments**), such that the change of policy had been postponed indefinitely;

- HMRC's policy on termination payments, prior to publication of Brief 12, was based on the decision in *Lloyds Bank plc v Customs and Exercise Commissioners* (VATD 14181). There had been no further relevant case law on the issue. The judgments of the Court of Justice of the European Union

(**CJEU**) which had influenced HMRC in the run-up to publication of Brief 12 were, in the view of the Court of Session, not in point, as the CJEU's judgments concerned payments that amounted to compensation for failure to complete a minimum contractual term. In this case, the minimum period under the lease had already expired by the time KNL exercised the break clause; and

- the requirement for KNL to pay to VL any VAT "properly due" on the break payment did not provide VL with a means to frustrate the exercise of the break option.

Why it matters: The Court commented that there had been no case in which a court or tribunal had considered whether the exercise of an option to terminate within an original lease was a taxable transaction. This case therefore represents a significant development in this area of VAT law. It is particularly notable that the Court commented that the CJEU cases of *MEO* (Case C-295/17) and *Vodafone Portugal* (Case C-43/19) are not directly in point, given these cases underpin the (currently postponed) change of policy set out in Revenue and Customs Brief 12 (2020).

The judgment can be viewed **here**.

Mandarin Consulting – UT decides that evidence of place of supply is inadequate

In *Mandarin Consulting Ltd v HMRC* [2021] UKUT 292 (TCC), Mandarin Consulting Ltd (**Mandarin**) supplied career coaching and support services to students of Chinese origin (the **Services**), which would be outside the scope of VAT if supplied to persons whose usual residence was outside the EU. Mandarin did not take the steps required by Council Implementing Regulation 282/2011/EU (the **Implementing Regulation**) to establish the usual residence of its customers before the time it made supplies to them. The First-tier Tribunal (**FTT**) decided that these failings precluded Mandarin from establishing that its supplies were outside the scope of VAT. We reported on the decision of the FTT in the **July 2020 edition of V@**.

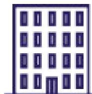
Mandarin appealed to the Upper Tribunal (**UT**). The UT concluded that the decision of the FTT contained an error of law, on the basis that, even though Mandarin did not satisfy the requirements of Article 23 of the Implementing Regulation, it was entitled nevertheless to seek to establish that its customers had their usual residence outside the EU. The UT decided that, when doing so, Mandarin was not limited to evidence that it gathered at, or before, the time of supply and there was no limitation in principle on the nature of evidence that Mandarin was entitled to deploy in support of its claim. The UT regarded the error of law as material to the FTT's decision and therefore set the FTT's decision aside (under section 12, Tribunals, Courts and Enforcement Act 2007).

The FTT had found that the services Mandarin was supplying constituted the services of consultants, falling within Article 59, Principal VAT Directive (**PVD**) rather than educational services falling within Article 54. This conclusion was not appealed to the UT. Because Mandarin was supplying consultancy services, its services were treated by Article 59 as supplied where the recipients of those supplies, who were non-taxable individuals, had their permanent address, or usually resided. Accordingly, establishing the place of supply of Mandarin's consultancy services involved determining (i) who the recipients of those services were; and (ii) where those recipients had their permanent address or usually resided. The answer to issue (i) changed over periods relevant to the dispute, largely because, from July 2016 onwards, Mandarin contracted with students' parents, rather than with students themselves (which the FTT found was the position until July 2016).

The UT was not satisfied that Mandarin could demonstrate, on the evidence that was before the FTT, that supplies to all of its students were made outside the EU pursuant to Article 59, PVD. The UT therefore remade the FTT's decision to leave the result unchanged in relation to periods prior to July 2016.

Why it matters: This decision serves as a cautionary tale regarding the need to obtain and keep appropriate documentary evidence to support the place of supply for VAT purposes. If Mandarin had been able to provide evidence in support of its claim that the Services were outside the scope of VAT, it may have avoided a substantial VAT bill.

The decision can be viewed **here**.



Hotel La Tour – FTT decides that VAT on professional fees in connection with a share sale is recoverable as input tax

In *Hotel La Tour Ltd v HMRC* [2021] UKFTT 451 (TC), the FTT held that VAT incurred by a seller, Hotel La Tour Ltd (**HLT**), on professional fees in connection with the sale of its subsidiary, Hotel La Tour Birmingham Ltd (**Target**), was recoverable as input tax.

HLT had provided management services to Target and the two companies formed part of a VAT group. Target owned and operated a luxury hotel and the purpose of the sale of Target was to fund the acquisition and development of a new hotel by HLT.

HMRC refused HLT's claim for the input VAT which HLT incurred on the relevant professional fees, on the basis that the sale of Target was an exempt supply for VAT purposes. HMRC argued that the share sale (an exempt transaction) severed the required "direct and immediate" link between the input tax that was being claimed and HLT's taxable activities.

Following *Frank A Smart & Son Ltd v HMRC* [2019] UKSC 39, the FTT noted the general position that there is a difference between the "initial fundraising transaction" (the fundraising activity, or sale, itself) and the "downstream transactions" (the activities the funds raised were to be used for; here, the acquisition and development of a new hotel). Further, the FTT found that the share sale did not break the chain, following *Frank*, which was authority that input tax incurred on costs associated with a share disposal will be deductible if:

> **(a)** the sale is a fundraising transaction objectively entered "for the purpose of an economic activity";
>
> **(b)** the funds are used for taxable supplies; and
>
> **(c)** the costs on which the input tax was incurred are not incorporated into the share price on sale, but are cost components of downstream taxable supplies (this will be satisfied even where the relevant costs are incurred to maximise the sale price).

The FTT found that, objectively ascertained, the purpose of the share sale of Target was to fund HLT's taxable general activities, namely the construction and future management of a new hotel. The FTT observed that it was crucial that HLT's financial position was that it could not afford to develop the new hotel without selling Target. There was no suggestion that the net proceeds of the sale would be used for any other purpose.

The FTT noted the professional fees were not incorporated in the price of Target's shares. The professional fees were paid out of the share sale proceeds. The fees could therefore be regarded as a "cost component" of HLT's taxable activities (construction of the new hotel) and not a "cost component" of the exempt share sale.

Why it matters: In cases where VAT recovery is a major concern, this case provides some helpful guidance on the appropriate way to draft share sale documentation in order to maximise VAT recovery.

The decision can be viewed **here**.

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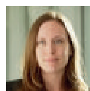

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