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Indirect tax update

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Summary

Welcome to this week's Indirect Tax Update.

This week we look at a decision of the First-tier Tax Tribunal. The case concerns an option to purchase a plot of land and the subsequent surrender of that option for £1.4 million.

HMRC's published guidance states that the grant of an option to purchase land is to be regarded as a supply of an interest in the land. Accordingly, under UK VAT law, the supply is treated for VAT purposes as a supply of goods and is either exempt from VAT or is taxable at the standard rate of 20% if the person granting the option has opted to tax.

In this case, having obtained planning permission in relation to the land in question, the appellant company surrendered its rights granted by the option for a valuable consideration. HMRC was of the view that the surrender of the option to purchase was not a supply of an interest in land and was not, therefore a supply of goods but was a supply of services upon which VAT was due. HMRC considered that the surrender did not meet the conditions contained in the VAT Directive.

The Tribunal found against HMRC.

In other news, the UK Government has announced that it is to defer the full impact of border controls at the end of the Brexit transitional period. Originally, the Government had said that it would introduce full border controls from 1 January 2021. However, it recognises the difficulties that many affected businesses will have encountered in their preparation for Brexit caused by the Coronavirus pandemic. Accordingly, it has announced that border controls will now be introduced in stages. This is welcome news for those affected businesses.

Finally this week, we look at a Court of Justice judgment in the case of CHEP Equipment Pooling (a Belgian entity). In this case, the business transferred its own assets (pallets) to Romania in order to lease them to its Romanian subsidiary. The Romanian tax authority considered that the company should have been registered for Romanian VAT as a result of the transfer and, as a result, it refused to pay a claim for a VAT refund on the grounds that the company was a taxable person in Romania.

First-tier Tax Tribunal – Landlinx Estates Ltd

Whether the surrender of an option to purchase land is a supply of goods

This is an unusual case! – Unusual in two respects. Firstly, on the one hand, HMRC has, historically, accepted that the supply of an option to purchase land is a supply of an interest in the land and is, therefore, under UK VAT law, to be treated as a supply of goods. On the other hand, in this case, HMRC argued that the surrender of the option to purchase is not a supply of an interest in land and is not a supply of goods but is a supply of services. The second unusual element to the case was that, in an attempt to justify its position, HMRC relied on the provisions of the VAT Directive rather than on UK law. Any student of EU law knows that a State cannot generally rely on EU law in preference to its own domestic law but this is what happened in this case.

Landlinx Estates Ltd (Landlinx) was granted an option to purchase a plot of land and, following the published guidance in this regard, the grantor of the option treated the supply as the grant of an interest in land (ie a supply of goods). As the grantor had not 'opted to tax' the land in question, the supply of the option was treated as an exempt supply for VAT purposes. Landlinx then sought and was granted planning permission in relation to the land. It then surrendered the option to purchase and received a payment of £1.4 million as consideration for that surrender. HMRC took the view that the surrender was not a supply of goods but was a supply of services and, as a consequence, it issued an assessment against Landlinx for VAT of £237,000.

HMRC conceded at the Tribunal hearing that, historically, it had regarded the grant of an option to purchase as a supply of goods. However, it advised the Tribunal that it had reviewed its policy in that regard and now considered that that policy was incorrect and is to be revised. HMRC argued that the grant of an option does not meet the test set out in the VAT Directive to be regarded as a supply of goods. In other words, the grant of an option does not transfer the right to dispose of the goods as owner, it merely provides a right to be able to call for such a transfer at some future point in time. According to HMRC, that does not qualify as a supply of goods under EU VAT law. HMRC argued that, if it was correct, then a surrender of an option to purchase also cannot be a supply of goods but must be a supply of services.

In a long and complex decision, the Tribunal considers that HMRC's approach is incorrect. The provisions of UK VAT law dealing with what constitutes a supply of goods was originally enacted in the 1972 Finance Act. The UK provision in question therefore pre-dated the equivalent provisions of EU VAT law and so the Tribunal concluded that treating supplies of interests in land (including the assignment or surrender of such interests) as a supply of goods was, therefore, the intention of the UK Parliament at that time and there had been no change to the law in the interim.

Generally, in situations where a provision of domestic law fails to implement a provision of EU law or fails to implement it correctly, the Tribunals and courts will adopt the principle of conforming interpretation (known as the "Marleasing" principle after a Court of Justice judgment in a case of that name). This means that the courts can, in effect, interpret the domestic provision to achieve the result sought by the EU law provision. However, in some circumstances, the domestic courts will refuse to interpret the law in this way if, in their view, such an interpretation would go against the grain of the domestic law. In this case, the Tribunal rejected HMRC's request to adopt a conforming interpretation of the UK's domestic law. This was on the basis that the UK law pre-dated the EU provisions which reflected the clear will of Parliament in 1972. To interpret the provision in such a way as to comply with EU law would have meant going against that will. The Tribunal refused to undertake such an exercise. Accordingly, the grant of an option to purchase is, as a matter of UK VAT law, a supply of an interest in land and is, thus, a supply of goods. Similarly, the surrender of such an interest should be dealt with in the same way. Landlinx' appeal was allowed.

Comment – it is most unusual for a Member State to ask a court to interpret a domestic provision in a way that conforms with EU law. However, that is what happened here but the Tribunal refused to do so. It is concerning that HMRC seems to have performed a volte-face in relation to its long-standing policy on the nature and liability of a supply of an option to purchase land. Landowners and developers need to be aware of this hitherto unannounced change of policy. It is too early to know whether HMRC intends to seek leave to appeal this decision. If it does not, then it seems clear that UK law treats the grant (and surrender) of an option to purchase as a supply of goods. If HMRC considers that to be wrong and it wishes to bring UK law into line with EU law, then it seems clear that UK VAT law will need to be changed.

Cabinet Office announcement

Brexit: Border controls after the end of the transitional period

The Government announced in February this year that, at the end of the Brexit transitional period which expires on 31 December 2020, full border controls would be introduced to deal with both the import and export of goods to and from the remaining EU bloc. This involves the requirement to complete import and export declarations and to present goods for customs clearance and other customs formalities.

This week, however, the Cabinet Office has confirmed that the UK will not seek or accept any extension to the transitional period (even if that means that the transitional period ends without a trade deal with EU. This provides certainty for all affected businesses that the new border controls will actually become effective on 1 January 2021.

However, as the new border controls will require businesses to make significant changes to procedures and accounting functions, the Cabinet Office has acknowledged that, due to the Coronavirus pandemic, many businesses will not be prepared for these changes in time for 1 January 2021. Accordingly, the Government is to phase-in the new border controls in three stages. This flexible and pragmatic approach will give industry extra time to make the necessary arrangements. From January 2021, importers of 'standard' goods will have six months to lodge any customs declarations and pay any import duties. From April 2021, importers of products of animal origin (such as meat, pet food, honey, milk or egg products and all regulated plants and plant products) will require pre-notification of their arrival to Customs along with the relevant health documentation. From July 2021, traders moving all goods will have to make full declarations and pay tariffs at the point of importation. Full Safety and Security declarations will also be introduced.

The Government has also announced that it is to provide funding of £50 million as a support package to help customs intermediary businesses (such as customs brokers, freight forwarders and express parcel operators) prepare for the new customs requirements. This funding will support intermediaries with recruitment, training and supplying IT equipment to help handle customs declarations.

Comment

The Government has announced that the UK will not be seeking nor will it accept any extension to the UK's transitional period for leaving the EU.

This means that from 1 January 2021, the UK will have autonomy to introduce its own approach to goods imported to GB from the EU and, initially, the Government said that full border controls would be implemented with immediate effect on 1 January 2021.

However, as affected businesses have been impacted by the Coronavirus pandemic, the Government recognises that these businesses will require more time to prepare for the changes.

Accordingly, the new border control measures are to be phased in in three stages. Full border controls will now come into force from 1 July 2021.

Court of Justice Judgment – CHEP Equipment Pooling (CHEP)

Whether the transfer of own assets justified refusal of input VAT claim

Article 17 of the VAT Directive stipulates that the transfer by a taxable person of goods forming assets of the business to another Member State of the EU is to be regarded as a supply of those goods for VAT purposes. In other words, even though there is no transaction for valuable consideration, VAT law deems there to have been a supply. Accordingly, there is generally a requirement for the entity transferring the goods to register for VAT in the Member State of arrival and to account for any acquisition VAT due in that Member State.

In this case, the taxpayer company – an entity established in Belgium, transferred its own goods (pallets) from Belgium to Romania. The company had a Romanian subsidiary and transferred the pallets for the purposes of leasing them to that subsidiary. In the meantime, the company incurred Romanian VAT on various purchases in Romania and sought a refund under the EU's VAT refund system. The Romanian tax authority refused the refund on the basis that CHEP should have been registered as a taxable person in Romania on account of its movement of the pallets from Belgium. CHEP appealed against that decision and the Romanian court decided to refer the matter to the Court of Justice as it required assistance with the interpretation of the VAT Directive. Romanian VAT law stipulates that a taxable person not established in Romania but established in another Member State, who is not registered and not required to be registered for VAT purposes in Romania, shall be eligible for a refund of value added tax paid on imports or acquisitions of goods/services carried out in Romania. The requirement that the claimant is neither registered for VAT nor required to be registered is an additional condition imposed by Romanian law and is not a condition of the refund Directive. Accordingly, whilst the Court of Justice agreed that, in the circumstances, CHEP ought to have been registered for VAT in Romania (due to the acquisition of its own pallets), the failure to register was not sufficient grounds for the tax authority to refuse the refund.

Comment

It is not uncommon for businesses to transfer their own goods between Member States. Generally, such a transfer will trigger a deemed intra-community supply of the goods in the Member State of departure and a deemed acquisition of the goods in the Member State of arrival. To zero-rate the deemed intra-community supply, the business will need to provide a VAT number issued by the Member State of arrival.

There are a number of exceptions to this rule. In certain circumstances, the deemed supply / acquisition of the goods can be ignored. For example, goods that are transferred for temporary use in the Member State of arrival for the purposes of a supply of services by the business transferring the goods is deemed not to be a transfer of own goods for these purposes. Provided the goods are returned to the Member State of departure after their temporary use, no deemed supply or acquisition will occur.

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