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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 Judgment of the Court of Justice of the European Union (CJEU). The case concerns the place of supply of goods being sold by a Polish company to a Hungarian customer and considers whether the transactions are liable to a very modest 8% VAT rate in Poland (as maintained by the taxpayer) or a rather less attractive 27% rate in Hungary (as argued by the Hungarian tax authorities).

In particular, the Court considers whether European law permits Member States to determine unilaterally the VAT treatment of particular supplies. Further, whether Member States are required to co-operate to reach agreement as to the correct VAT treatment of a supply and if so, whether the taxpayer is entitled to a refund of VAT it may have overpaid.

The Court goes on to consider whether KrakVet, as the supplier, 'dispatched or arranged the transport of goods', thereby resulting in the place of supply being Hungary (where the transport ends). Alternatively, whether a binding ruling that the place of supply was in the Member State of dispatch (and therefore liable to the lower rate of VAT in Poland), the taxpayer's arrangements were, in effect a tax avoidance measure and as such an abuse of tax law.

The Court has determined that, whilst Krakvet's arrangements do not constitute abuse, if the referring court, on consideration of the facts, concludes that Krakvet had a predominant involvement in the making of transportation arrangements its supplies will be made in Hungary and therefore liable to Hungarian VAT.

VAT Payment Deferral

As the VAT payment deferral period reaches an end, we consider what businesses need to do to ensure their VAT accounting remains on track.

VAT and dispute resolution

We consider the role of Alternative Dispute Resolution (ADR) in light of the Practice Statement issued this week by Greg Sinfield, Chamber President.

Court of Justice of the European Union – Judgment KrakVet Marek Batko sp. K

Place of supply – whether Poland or Hungary

KrakVet Marek Batko sp. K. (KrakVet) is an online retailer of pet food established and registered for VAT in Poland. It has no establishment in Hungary. KrakVet obtained a binding ruling from the Polish tax authorities that its supplies to retail customers in Hungary were made in Poland and therefore liable to VAT at 8%. Following a tax inspection the Hungarian authorities took the view that the supplies to Hungarian customers were made in Hungary. Accordingly, it registered KrakVet for Hungarian VAT and raised an assessment.

When placing an order, KrakVet's Hungarian customers had the option to have their goods delivered by KrakVet's recommended transportation company. Alternatively, they could arrange to collect the goods or use their own choice of courier and arrange transport themselves. Where the customer chose to use KrakVet''s recommended supplier, they entered into a contract with Krzysztof Batko Global Trade (KBGT). KBGT is a Polish company owned by the brother of KrakVet's owner. KrakVet itself did not contract for delivery with the customer. KBGT arranged transport from the Polish warehouse to the Polish border. Transport from the Polish border to the Hungarian customer was sub-contracted by KBGT to an unconnected courier. On delivery of the goods, the customer had the option to pay the courier in full (goods plus delivery) or pay KrakVet directly.

The Hungarian Court referred five questions and the Court of Justice has now issued its judgment (18 June 2020). In answering the first three questions together, the Court considers that Member States are not precluded from being able, unilaterally, to subject transactions to value added tax treatment different from that under which they have already been taxed in another Member State. Furthermore, whilst there is provision within EU law for co-operation between Member States this does not extend to a requirement to negotiate and agree specific tax treatment of transactions. The Court of Justice has the powers to determine in cases where a difference of treatment exists between Member States and these differences cannot be resolved. The fourth question concerned the phrase in the first sentence of Article 33(1) of [Directive 2006/112] which refers to transport being carried out "by or on behalf of the supplier" and how this should be interpreted. The relevance of this sentence is that if the supplier has, in the words of the Court, predominant involvement in the dispatch and transport of the goods, Article 33(1) will be applicable and the place of supply will be where consumption takes place, ie. where the purchaser belongs. The Court considers that this issue is a matter for the referring court to determine based on the facts of each case. The Court indicates that in Krakvet's case, if the facts as presented are correct, Article 33(1) would be in point but this is for the referring court to determine.

The final question referred to the Court concerns the hallmarks of abusive tax practices. In particular, was the fact that KrakVet arranged transportation of its goods via a third party company and therefore benefitted from a lower rate of VAT, circumventing the Distance Selling rules, an example of artificially structuring transactions with the aim of achieving an unfair tax advantage. The Court considers that the key features, being a wholly artificial arrangement designed solely to achieve a tax advantage were not present in this case. The Court notes that the fact that differences in tax rates between Member States are a product of incomplete harmonisation of tax rates. In that context and in accordance with settled caselaw it is not a requirement that taxpayers choose to pay the highest amount of tax but are free to choose a structure that limits their tax liability. Taking the above into account, the Court considers that the fact that companies are connected was not necessarily determinative, providing there is genuine, independent economic activity in both entities. The fact that customers can go to an alternative supplier is also not determinative. In conclusion, structuring transactions in this way cannot be classed as an abusive practice.

Comment: Whilst Krakvet appears to be out of the woods with regard to abusive practice, it would appear likely that Article 33(1) will apply, bringing the place of supply to Hungary and therefore subject to the higher rate of VAT in Hungary. The point around Krakvet having obtained a 'binding ruling' from the Polish tax authorities was not directly addressed in the Judgment. It should be noted that from 1 January 2021 the new definition of transportation or arranging transportation is being extended to include 'intervention' by a supplier in the transportation of goods. This may make this decision somewhat irrelevant for future arrangements. What it does do, however, is to make clear the crucial importance of determining the place of supply and putting in place correct arrangements to account for VAT in the right Member State. Businesses involved in cross-border transactions may wish to review their own supply chains to ensure that any supplies are being correctly handled for VAT purposes, both before and after 1 January 2021.

HMRC publish guidance as the VAT payment deferral period reaches a close

VAT payment deferral period ends 30 June 2020

As the VAT payment deferral period reaches its end, HMRC has issued an update reminding businesses to take the necessary steps to ensure that ongoing VAT payments are made on time.

To avoid possible interest and penalties, businesses will need to ensure that any direct debits that were cancelled are re-instated in good time to allow payments falling due outside the deferral period (after 30 June 2020) to be made as normal.

VAT returns should continue to be submitted on time as normal. Deferred VAT will be due on or before 31 March 2021 and can be paid in full as a single payment before that date. Alternatively, if businesses prefer to spread the repayment, additional payments can be made with subsequent VAT returns.

For businesses that may need further time to pay, HMRC is advising those businesses to contact their 'time to pay' helpline for further advice, details of which can be found here.

Where this may be the case we would advise businesses to do this at the earliest opportunity with a view to ensuring any agreement is in place before VAT payments fall due.

Comment

The VAT deferral was a welcome easement for businesses in the early stages of the coronavirus pandemic.

As the government is now announcing a gradual lifting of lockdown, businesses are beginning to re-open so there has been no extension to the deferral period.

HMRC is expected to be particularly busy so we are encouraging any business that thinks it may need further time to pay to contact HMRC at the earliest opportunity as failure to make payments falling due after 30 June on time may be liable to interest and penalties. VAT returns should continue to be submitted on time as normal.

The First Tier Tribunal releases a Statement of Practice in relation to Alternative Dispute Resolution (ADR)

Chamber President encourages greater use of the ADR process to resolve VAT disputes without recourse to the VAT Tribunal

Alternative Dispute Resolution (ADR) is a process by which, with the agreement of both parties, a taxpayer and HMRC can enter into mediated discussions regarding an amount of VAT due or a decision that may be the subject of disagreement. An independent trained mediator facilitates a discussion between the parties with a view to reaching agreement or preparing for litigation.

ADR is not arbitration in that the mediator does not impose a decision. Nor does it replace the standard reconsideration process. Rather, it is a neutral space in which both parties can explore whether there are ways to resolve a dispute without recourse to an appeal to the VAT Tribunal. It can be particularly useful in long-running disputes.

The Practice Statement clarifies that ADR can, in certain circumstances, be entered into before an appeal is lodged with the Tribunal. Additionally, ADR may still be entered into after an appeal to the VAT Tribunal has been lodged. Providing it is anticipated that the process can be completed ahead of the hearing date, ADR can be entered into even after documents have been lodged with the Tribunal. Given that it can be some time from lodging an appeal to receiving a hearing date, this will, in many cases, give adequate opportunity for the ADR process to be completed.

ADR does not affect a taxpayer's right to appeal but is often a less costly and less stressful process than a Tribunal hearing. It does not prejudice the outcome of the taxpayer's case. It can, however, provide clarity around the dispute and reframe the arguments to be dealt with at Tribunal if ADR does not resolve the dispute.

The Practice Statement also emphasises that taxpayers may appoint an independent mediator to co-facilitate any discussions. With HMRC's agreement it may also be possible for a single independent mediator to be appointed outside HMRC.

The overarching thrust of the Statement is to encourage greater use of the ADR process. Whilst it cannot be used in all cases, it is a route worth considering if a dispute with HMRC would benefit from an independent, confidential discussion.

If you have an issue which you think may be suitable for ADR, we have trained mediators in the VAT practice who would be happy to discuss the ADR process and the options available.

Comment

Alternative Dispute Resolution (ADR) is not a widely known or utilised route to reaching agreement with HMRC and this appears to be borne out by the Practice Statement issued by Greg Sinfield, Chamber President.

Given that VAT Tribunals have been largely put on hold due to coronavirus, undoubtedly there will be a backlog of cases once the Tribunal returns to full operation. Even then of course, social distancing may mean that cases are not held in the familiar way.

In clarifying the route to ADR, its nature and the timeframe for engaging in the process, this Practice Statement is a welcome reminder and encouragement to seek earlier resolution of disputes with HMRC.

Taxpayers using ADR will almost certainly save money on the cost of appearing at the Tribunal as well as potentially reaching a speedier resolution to their dispute. It is understood that in around 88% of cases ADR has a positive impact, not necessarily removing a VAT liability but at least in moving matters forward in a positive way.

We encourage businesses, particularly where discussions with HMRC have stalled or become protracted, to consider this route. It cannot be used in all cases but can be a useful approach to dealing with disagreements with HMRC.

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