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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 three important VAT cases. The first is a judgment from the Court of Justice in the case of Blackrock Investment Management (UK) Ltd (BIM) which concerns the VAT liability of services provided by Blackrock Financial Management Inc (BFMI, a US Corporation).

BFMI supplies a software based investment platform (called Aladdin) which BIM uses as part of its own service of investment management which includes the management of both special investment funds (SIFs) and non-SIFs. The question for the Court of Justice to resolve was whether the consideration paid by BIM for the single supply of the software platform should be apportioned with the portion attributable to the SIFs being exempt from VAT.

The Advocate General issued an opinion in March 2020 confirming that, in the circumstances, the single price paid by BIM could not be apportioned and, as a consequence the whole of the amount paid was subject to UK VAT under the reverse charge.

The full Court has now delivered its judgment.

The second case concerns an Advocate General's opinion in the case of Wellcome Trust Ltd (WTL). Again, this case concerns the VAT position in relation to investment management services. WTL buys in investment management services from investment managers established outside the UK and it uses those services to manage the substantial investment portfolio of the Wellcome Trust. That activity was found to be a 'non-economic' activity by the Court of Justice in 1996 and the question to resolve in this referral by the UK's Upper Tribunal was whether WTL acted as a 'taxable person' when it procured the investment management services. If it did not, then the place of supply of the management services it purchased was not the UK and the services were not subject to UK VAT under the reverse charge. The Advocate General has issued his opinion.

Finally, we look at a Supreme Court judgment in the case of KE Entertainments Ltd v HMRC which concerns a claim for overpaid output VAT on bingo participation fees.

Court of Justice of the European Union – Judgment - Blackrock Investment Management (UK) Ltd

Whether single supply of services can be apportioned

Blackrock Investment Management (UK) Ltd ('BIM'), is a company incorporated in the UK and is a Member of the Blackrock VAT Group. BIM manages Special Investment Funds (SIFs) and other funds. However, SIFs do not represent, either by number or by value of the assets managed, the majority of the funds managed.

For the management of all of its funds, BIM receives supplies of services from BlackRock Financial Management Inc. ('BFMI'), a company incorporated in the United States. Those services are provided through a software platform named Aladdin and comprise a combination of hardware use, software and human resources. Aladdin provides portfolio managers with market analysis and monitoring to assist in the making of investment decisions; it monitors regulatory compliance and enables portfolio managers to implement trading decisions. Those services constitute a single supply, whichever funds are being managed. As BFMI is established outside the UK, BIM accounted for UK VAT under the reverse charge mechanism on the full value of that single supply. However, as it considered that the Aladdin services applicable to SIFs should have been exempt from VAT, for the period 2010 to 2013, it only accounted for VAT in relation to the proportion of the price paid that was attributable to the other non-SIF funds.

HMRC disagreed with that approach and raised assessments. BIM appealed to the First-tier Tax Tribunal which dismissed its appeal and so BIM appealed to the Upper Tribunal. The Upper Tribunal decided to refer the case to the Court of Justice as it relates to the interpretation of EU VAT law. In essence, the Upper Tribunal asks whether, in the circumstances, a single supply of management services, provided by a software platform belonging to a third-party supplier for the benefit of a fund management company, which manages both special investment funds and other funds, comes within the exemption from VAT laid down in the VAT Directive. In other words, should the service provided by BFMI be exempt from VAT and not subject to the UK reverse charge.

The Advocate General issued a negative opinion back in March 2020 and the Court has now issued its judgment on 2 July 2020. The Court has agreed with the Advocate General.

On the basis that there is a single supply of management services provided by BFMI to BIM, the Court considers that a single rate should apply to the supply and that it is not permissible to apportion the single supply between an exempt element (here the supply of fund management services supplied to SIFs) and a taxable element (the supply of management services to non-SIFs). That would go against the grain of the Directive which stipulates that a single supply should attract a single rate. Accordingly, the Court has concluded that in circumstances such as those in this case, the tax treatment of the supply of services cannot be determined according to the nature of the majority of the funds managed by the company concerned (ie no apportionment based on value of funds managed).

Furthermore, in order to be classified as exempt transactions within the meaning of Article 135, the services provided by a third-party manager must, viewed broadly, form a distinct whole fulfilling in effect the specific, essential functions of the management of special investment funds. In this case, the parties were in agreement that the Aladdin service was designed for the purpose of managing investments of various kinds and that, in particular, it may be used in the same way for the management of SIFs as for the management of other funds. Therefore, that service cannot be regarded as specifically for the management of special investment funds and, as a result cannot therefore benefit from exemption from VAT.

In light of the above, the Court concludes that the answer to the question referred by the Upper Tribunal is that Article 135(1)(g) of Directive 2006/112 must be interpreted as meaning that a single supply of management services, provided by a software platform belonging to a third-party supplier for the benefit of a fund management company, which manages both SIFs and other non-SIF funds, does not fall within the exemption provided for in that provision.

Comment – one can understand the logic of Blackrock's case – had it bought in a separate supply of Aladdin services from BFMI specifically for the SIFs, it might have qualified as an exempt supply. However, as the Aladdin service is used to manage all types of funds it cannot apportion the consideration and ascribe a value to the SIF element based on the value of SIF funds under management. There is a single supply for a single consideration.

CJEU – Advocate General's opinion – Wellcome Trust Ltd (WTL)

Whether the taxpayer acted as a taxable person when procuring services

In 1996, the Court of Justice confirmed in a judgment that WTL's activities (of buying and selling shares and other securities) was not a business activity. The Court concluded that the activities were more akin to those of a private investor rather than those of a trader. Accordingly, since 1996 WTL's main investment management activity has been treated as outside the scope of VAT. However, WTL does have other business activities and is registered for VAT in relation to those activities.

To enable it to conduct its own (outside the scope of VAT) investment management services, WTL buys in investment management services from third party investment managers some of which are based outside the European Union. The question to resolve in this case was whether, when it procures those services, WTL acts as a taxable person. If it does, then the provisions of Article 44 of the VAT Directive – which determine the place of supply of the bought in services as being the place where WTL is established would apply and render the services liable to UK VAT. In essence, WTL argued that in line with the 1996 judgment, it did not act as a taxable person and that, accordingly, Article 44 did not apply to the services it bought in. Unfortunately, the Advocate General disagrees. Whilst the court has clearly ruled (in 1996) that WTL is not a taxable person in relation to its own activities, for the purposes of Article 44, it does act as a taxable person when it procures the third party services. As a consequence the services are deemed to take place in the UK and are liable to VAT which WTL must account for in the UK under the reverse charge mechanism.

As WTL's outputs are outside the scope of VAT, it is unable to reclaim the VAT it is required to account for in this way. The full court will deliver its judgment in due course (likely to be September / October 2020).

Comment

The AG considers that the 1996 ruling of the Court (that WTL is not a taxable person in relation to its own investment management activities) cannot be 'read-across' to the place of supply rule contained in Article 44.

It is necessary to consider the context and objectives pursued by the place of supply rules and it is necessary to also consider the wording of Article 43(2) of the Directive.

Article 43(2) specifically states that non-taxable legal persons identified for VAT (which WTL is) are to be regarded as taxable persons.

The AG, in effect, sees WTL as a 'final consumer' of the services and, as VAT is a tax on consumption, the place of supply is the place where WTL is established and 'consumes' the services it procures. This means that WTL is required to account for UK VAT on the supplies it receives but is unable to reclaim that VAT as input tax.

Supreme Court – Judgment – KE Entertainments Ltd v HMRC

Whether a claim for overpaid VAT was made in time?

This case concerns a claim for overpaid VAT during the period from 1996 to 2004 on Bingo participation fees. When a customer pays to play bingo, there are two elements to the amount paid. Firstly, there is the stake element, which is outside the scope of VAT as it is not regarded as consideration for the right to play. Secondly, there is the participation fee element which is subject to VAT. Bingo promoters are, therefore, required to apportion the payment received from customers and account for VAT on the proportion deemed to be in respect of participation fees. Until 2007, that apportionment was performed on a game by game basis. However, in 2007, HMRC published a Business Brief confirming that the correct method of apportionment was on a session by session basis (a session comprises a number of games). The company, along with many other bingo operators submitted three-year claims for VAT overpaid as a result of operating the game by game method of apportionment. These claims were settled in full.

In the meantime, in 2011, the First-tier Tax Tribunal issued a decision in the case of Carlton Clubs Ltd (another bingo operator) which accepted a retrospective claim. Carlton had argued that, in effect, the different basis of calculating the apportionment of participation fees meant that the customer had paid less for the right to play bingo and more for the stake. As a consequence, the correct method for reclaiming overpaid VAT was to claim under Regulation 38 of the VAT Regulations and, by doing so, there was no time limit as there is under the normal rule contained in section 80 of the VAT Act. In light of that decision, KE Entertainments made a Regulation 38 adjustment to its December 2012 VAT return which covered the period from 1996 to 2004. HMRC did not accept that adjustment and so the current litigation began.

As is normal, the case began at the First-tier Tax Tribunal which allowed the company's appeal. HMRC then appealed to the Upper Tribunal which came to the same conclusion as the FTT and so HMRC then appealed to the Court of Session. The Court of Session allowed HMRC's appeal and so the company appealed to the Supreme Court. The company argued that its claim for overpaid VAT did not fall into section 80 of the VAT Act. This was because, it argued, section 80 only applies where VAT has been brought to account that was **not** output tax due. However, under the pre 2007 game by game method of apportionment, the VAT it had accounted for on participation fees was, in fact, output VAT that **was** due. So, if the output VAT was due, section 80 could not apply and any claim for overpaid VAT could not, therefore, be subject to a time limit.

The Supreme Court has issued its judgment and has dismissed the company's appeal. The Court has ruled that there can only be one correct way of apportioning the VAT due on participation fees. This was accepted by HMRC in 2007 as being on the session by session basis. Accordingly, any method of apportionment other than the session by session basis brought into account VAT that was not output VAT due and, as a consequence, any VAT overpaid by using the game by game basis could only be reclaimed using the claim procedures set out in section 80. That section has a time limit attaching to it (three-years at the time the claim was made but now four years) and that time limit had long-expired by the time the company adjusted its VAT return in 2012.

This is the end of the road for the company as there is no appeal from the Supreme Court. It will be disappointing news for the bingo operators that had similar claims stood behind this litigation.

Comment

The First-tier Tax Tribunal set a hare running when it issued its decision in the case of Carlton Clubs. Prior to that decision, bingo operators had submitted their claims for overpaid VAT (and had them accepted by HMRC and repaid) under the provisions of section 80 of the VAT Act.

The decision in Carlton Clubs opened up an opportunity to extend the claims without being subject to the statutory three-year (now four-year) time limit. This was possible because, in Carlton Clubs, the FTT had been persuaded that the consideration for the right to participate in a game of bingo had decreased after the supply had been made (as a result of the different basis of apportionment introduced in 2007).

The Supreme Court does not agree. In essence, it considers that there has been no such decrease in consideration. All that has happened is that the taxpayer company has amended its method of apportionment. As the Court has found that there is only one correct method of apportionment (under the session by session basis) the VAT brought to account under the game by game basis of apportionment was correctly to be classed as 'output VAT due', the only route available to a taxpayer to reclaim any overpaid VAT was, therefore, under the provisions of section 80.

That section is subject to a time limit whereas an adjustment under Regulation 38 for a decrease in consideration is not. The Supreme Court's judgment means that that is the end of the road in this and any other cases that were 'stood behind' it.

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