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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 two interesting cases from the Court of Justice and a decision from the First-tier Tax Tribunal.

In the case of Sonaecom, the Court has issued its judgment in relation to whether the company – a holding company – was entitled to recover input VAT it had incurred in relation to costs associated with an aborted acquisition of shares in a target company. The costs in question were consultancy fees paid in relation to a market study report and commission paid to a bank in relation to the raising of capital via a bond issue.

The company considered that it was entitled to reclaim the VAT incurred on these costs on the basis that it was an 'active' holding company and intended to provide taxable supplies of management services to the target company after acquisition. However, due to the financial crisis in 2008, the company ultimately abandoned its intended acquisition. The Portuguese tax authority refused the claim considering that, as no management services were supplied, there was no taxable supply of services against which the input VAT in question could be franked.

In the case of J.K., the Advocate General has issued his opinion in connection with whether take away meals provided by a McDonald's franchise in Poland should be treated as a supply of 'restaurant services' (8% VAT) or a supply of 'food' (5% VAT).

Finally, this week, we look at an interesting case from the First-Tier Tax Tribunal. The case of Netbusters concerns supplies of football pitches and netball courts in conjunction with the running of five-a-side and netball leagues. The case demonstrates that, despite HMRC's acknowledged acceptance of the Tribunal's earlier decision in the almost identical case of 'Goals', it still considers that the supplies made by Netbusters are not supplies of an interest in land and are not exempt from VAT.

Court of Justice – Judgment – Case C-42/19 – Sonaecom SGPS SA

Whether input VAT incurred on costs associated with an aborted acquisition of shares in a target company could be reclaimed

There have been many cases over the years on the topic of whether a holding company is entitled to reclaim input VAT that it incurs in relation to the acquisition of shares in a target company. This is another such case. To remind readers, the Court of Justice has stated in previous case law that the mere acquisition and holding of shares in a subsidiary is not an economic activity for VAT purposes. However, where the acquisition and holding of shares is accompanied by the provision of 'management services' by the holding company to the subsidiary company, that activity is an economic activity for VAT purposes. In simple terms, where the holding company's supply of management services is subject to VAT, that is a taxable economic activity and the holding company is, in principle, entitled to reclaim any VAT that it incurs in connection with that activity. The Court's case law has also confirmed that, to preserve the neutrality of the VAT system, that right of deduction is preserved even if, for reasons beyond the holding company's control, the intended taxable supplies of management services do not materialise.

In this case, the company (Sonaecom) wished to acquire the shares in a target company. It commissioned a market study and it paid VAT on the consultancy fees associated with the production of the market study report. Based on the Court's case law, it considered that it was an 'active' holding company as it had the intention to provide management services to the target company upon acquisition. Unfortunately, the financial crisis of 2008 meant that the acquisition of the shares had to be abandoned. The Portuguese tax authority argued that, as the intended supplies of taxable management services did not materialise, Sonaecom was not entitled to reclaim the input tax in question. The Court of Justice confirmed what it had ruled in the Ryanair case – essentially, the input VAT was reclaimable provided that there was objective evidence that the company intended to make taxable supplies of management services to the target company after the shares were purchased. This was a matter for the national court. The fact that the share purchase was abandoned did not change anything. The tax authority tried to argue that the financial crisis of 2008 was reasonably foreseeable such that the abandonment of the share acquisition was not 'beyond the company's control'. However, the Court disagreed confirming that it was not up to the tax authority to determine what was and what was not beyond the company's control.

As far as the VAT incurred on the commission payable to the bank in relation to the bond issue was concerned, again, the company argued that it was entitled to reclaim the VAT on the basis that it was an active holding company which had the intention of making taxable supplies of management services to the target after the acquisition. However, having raised the capital through the bond issue, but having then abandoned the acquisition of the target, the company decided to loan the capital to its parent company. The Court confirmed that, in the circumstances, whilst the intention was to make taxable supplies of management services which, ordinarily, would have provided a right of deduction of the related input tax, here the company actually used the services provided by the bank to make a supply of a loan to its parent company. Since the provision of a loan is an exempt supply under the VAT Directive, the company is not entitled to reclaim the input VAT that was incurred on the bank's commission.

So, the Court makes a distinction between the intended use of the costs and the actual use of the costs as, to do otherwise would probably breach the principle of fiscal neutrality and could lead to distortion of competition. Whilst, in this case, there would have been a right of deduction had the shares been acquired and had the management services materialised, in reality, that is not what happened. The services provided by the bank in relation to the bond issue were, in fact, used to make an actual supply of a loan. That supply was an exempt supply and, accordingly, the company was not entitled to deduct the VAT it had paid to the bank.

Comment – This case confirms that, in principle, holding companies have a right of a deduction if there is an objectively verifiable intention to make taxable supplies of management services to its subsidiary even if, due to circumstances beyond its control, that intention does not materialise. However, in cases where the inputs are first used for some other purpose that does not confer a right of deduction (as here with the exempt supply of the loan to its parent), the intended use is overridden by the actual use of the inputs. This makes sense and it preserves the neutrality of the tax and prevents distortion of competition.

Court of Justice – Advocate General's opinion – Case C-703/19 – J.K.

Whether supplies of 'take-away' food from a McDonald's outlet is a supply of 'restaurant services' or a supply of 'food'

In Poland, supplies of 'food' are liable to a lower rate of VAT (5%) whereas a supply of 'restaurant services' is liable to VAT at 8%. The question to be resolved in this case was whether a supply of a meal which was not consumed on the supplier's premises by the customer should be treated simply as a supply of food or whether, as the tax authority in Poland asserted, the supply should be regarded as one of 'restaurant services'.

The Advocate General has issued his opinion and has confirmed that the expression 'restaurant services' connotes something more than the mere provision of food. Indeed, the VAT Implementing Regulations (the regulations which help Member States to implement the substantive provisions of the VAT Directive in a uniform and consistent way) specifically states that restaurant services include the provision of prepared or unprepared food or beverages (or both), for human consumption accompanied by sufficient support services allowing for the immediate consumption thereof. The regulations also state that the provision of food is one component of the whole supply in which services shall predominate. In other words where food is supplied, but the provision of services such as the provision of facilities to consume the food (tables, chairs, cutlery, waitress service, etc) predominates, then that is a supply of restaurant services.

In the case in question, the McDonald's franchisee provided such services to 'eat-in' customers but did not in relation to supplies to 'drive-in' customers or 'walk-in' customers who consumed their meals off the premises. In the Advocate General's opinion, such supplies qualify as supplies of food liable to VAT at 5%. The full court will give its judgment in this case in a few months time. The Court does not always follow the Advocate General's opinion but it is difficult to see how, on the facts and in light of the regulations, the Court could come to any other conclusion.

Comment

In the UK, the supply of food for human consumption is zero-rated. However, there are a number of exceptions to that basic rule, one of which is food supplied in the course of catering which includes (since the introduction of the so-called fish and chip tax in 1984), supplies of hot food for consumption off the premises.

This case will not affect the UK's position. Although the AG has confirmed that the supply of take-away meals should be liable to the reduced rate of VAT in Poland (because they are merely the supply of goods and not 'restaurant services'), due to the special status of the UK's zero-rating provisions, the UK is not obliged to follow this approach.

The fish and chip tax seems, therefore, to be destined to remain payable in the UK for the time being.

First-tier Tax Tribunal – Netbusters (UK) Ltd

Whether supply one of an interest in land and exempt from VAT

Readers will be aware that the supply of an interest in, right over or license to occupy land is generally exempt from VAT unless the supplier has 'opted to tax' or the supply falls within a number of exceptions. In this case, the company hired land (five-a-side pitches and netball courts) from local authorities and schools. It then arranged and managed football and netball leagues and let the pitches and courts to participating teams.

Following the case of Goals Soccer Centre PLC (Goals) – a case on similar (but not identical) facts, the company submitted a claim for overpaid output VAT. It considered that its supplies were partly exempt from VAT (the supply of the pitch or court) and partly taxable (the supply of league management services). The claim was made in response to HMRC's Revenue & Customs Brief 8/2014 which expressly accepted the FTT's decision in Goals and which invited claims for VAT refunds from "all traders who operate in circumstances akin to Goals Soccer Centres plc". Having invited such claims, HMRC then rejected Netbusters' claim for overpaid VAT and, in effect, attempted to re-litigate the point of law established in Goals.

The Tribunal distinguished the facts of Netbusters from Goals on the basis that, in Goals, there were separate supplies of the pitch / court and of league management services. In Netbusters, the Tribunal found that the hire of the pitch / court and the league management services were a single supply for VAT purposes and the supply was of an interest in land to which the league management services were ancillary. Being a single supply of an interest in land upon which no option to tax had been exercised, the whole of the supply is exempt from VAT.

It does seem rather odd that, on the one hand, HMRC publicly stated in R&C Brief 08/2014 that it accepted the Tribunal's decision in Goals yet, on the other hand, it rejected Netbusters' claim arguing that Netbusters was, somehow, different to Goals!

Comment

The Goals decision concerned what was accepted by the Tribunal as two separate supplies of an interest in land and of league management. The Tribunal found that there were two separate supplies and, if there was only a single price paid by the customer, that the consideration should be apportioned on a fair and reasonable basis.

This is what Netbusters did but HMRC rejected the claim.

The Tribunal has found in Netbusters that there was, in fact, a single supply and that supply was an exempt interest in land with the league management services being regarded as ancillary to the main supply of the interest in land. Accordingly, the consideration for the supply need not be apportioned. Seems like something of an 'own goal'?

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