AAT VAT update 14 May 2015

In this month's edition of the VAT update we look at:

1. The HMRC leaflet on new VAT recovery for certain charities
2. Court of Justice of the European Union (CJEU) rules utilities supplied by landlord are separate from the rent
3. Partnership dispute legal fees denied input VAT recovery
4. Property transfer held not to be a TOGC but HMRC out of time to assess

1. HMRC leaflet on new VAT recovery for certain charities

HMRC have issued **VAT Notice 1001** which explains the VAT rules that apply to charities eligible for refunds of VAT under sections 33C and 33D of the VAT Act 1994. The VAT refund scheme was introduced from 1 April 2015 for palliative care charities, air ambulance charities, search and rescue charities, and medical courier charities. The refund scheme enables these charities to reclaim the VAT incurred on their 'non-business' activities. The notice includes details on what charities are covered by the scheme, the VAT that can be claimed, and how to recover the VAT incurred, for both VAT registered and non-registered charities.

2. Court of Justice of the European Union (CJEU) rules utilities supplied by landlords are separate from the rent

Judgement has been given in a Polish case which considered whether the supplies by the landlord of various utilities such as electricity, water and waste disposal were parts of a single composite supply with the VAT treatment following the supply of the major component. The judgement is available **here**.

The detailed differences between Polish VAT and that of the UK do not really matter because the underlying point concerns the principle of whether supplies by the landlord of measured utilities are separate supplies or part of a composite supply made under the rental agreement. In Poland the rental supply would have carried Polish VAT of 23% whereas, for example, the supply of water would have been taxed at 8%, so the difference was material. Here in the UK, the rental might have been exempt or standard rated at 20% depending on whether an option to tax had been exercised but, for example, the metered supply of water from a utility company would be zero rated.

In *Wojskowa Agencja Mieszkaniowa w Warszawie,* judgement was delivered on 16 April 2015 about the VAT treatment of charges for supplies of electricity, heat, water and refuse disposal that were made by a landlord to its tenants. The individual properties had separate meters for the supplies of utilities but the landlord charged the tenants for the utilities which the tenant used and the landlord paid the utility companies. The Polish Minister Finansów took the view that there was a single composite supply of the property that included the supplies of electricity, water, etc., and that the charges for them attracted the same VAT (23% in Poland) treatment as the rent.

The CJEU decided at line 39 of the judgement that:

…if the tenant has the right to choose his suppliers and/or the terms of use of the goods or services at issue, the supplies relating to those goods or services may, in principle, be considered to be separate from the letting. In particular, if the tenant can determine his own consumption of water, electricity or heating, which can be verified by the installation of individual meters and billed according to their consumption, supplies relating to those goods or services may, in principle, be considered to be separate from the letting. As regards services, such as the cleaning of the common parts of a building under joint ownership, such services should be regarded as separate from the letting if they can be organised by each tenant individually, or by the tenants collectively and if, in all cases, the supply of those goods and services is itemised separately from the rent on invoices addressed to the tenant.

The Court concluded that:

– The VAT Directive must be interpreted as meaning that the letting of immovable property and the provision of water, electricity and heating as well as refuse collection accompanying that letting must, in principle, be regarded as constituting several distinct and independent supplies which need to be assessed separately for VAT purposes, unless the elements of the transaction, including those indicating the economic reason for concluding the contract, are so closely linked that they form, objectively, a single, indivisible economic supply which it would be artificial to split.

– It is for the national court to make the necessary assessments taking into account all the circumstances of the letting and the accompanying supplies and, in particular, the content of the agreement itself."

In the UK, landlords who supply utilities such as electricity water and sewage should note to itemise these charges separately in the invoice and wherever possible meter such charges separately. Organised properly, these utility supplies can obtain the benefit of zero and reduced rates of VAT.

3. Partnership dispute legal fees denied input VAT recovery

Generally, VAT is only reclaimable if it is charged on a supply to the claimant (VATA 1994, s. 24(1)) and the expense has been incurred with a view to making taxable supplies. Care is needed when deciding to whom and for what legal fees have been incurred. In many enquiries, HMRC are likely to seek an analysis and an explanation of legal and professional fees. It is in practice a well known risk area for errors to occur.

In an anonymised case heard by the FTT, the judge, Barbara Mosedale decided that the input tax could not be recovered because the dispute and therefore the legal fees had not been incurred by the partnership with a view to the partnership making taxable supplies. The partnership consisted of four persons (A,B,C,and D) and D wished to retire but sought to wind up the partnership with the sale of assets and goodwill. Legal proceedings were started and A&B engaged solicitors and a different solicitor was engaged for C. The dispute was resolved and the partners A,B and C submitted their legal fees invoices to the partnership for reimbursement with the three individuals continuing as the ABC partnership.

The firm of solicitors which acted for Messrs A and B addressed their invoices to Messrs A and B jointly, showing each of their names and home addresses on the front of the invoice. The invoices were paid by Mr A and Mr B personally. The engagement letter made it clear that the solicitor's clients were A&B. Similarly, the other firm of solicitors had Mr C as the client and Mr C paid the bill personally.

On the basis of *Airtours* and *Redrow* it is not enough for the appellants to show that the partnership of Messrs A,B and C benefited from the solicitors' services. The case of *Redrow* requires the partnership to show that the partnership was a party to the contract and in particular that it was liable to pay for the services. The FTT found as a fact that the partnership was not liable to pay for the services. The individuals were the clients and the individuals were personally liable to pay the legal bills.

The legal bills were not paid for taxable supplies to be made by the partnership. There was not a valid tax invoice to support the claim to input tax and so it is inevitable that the FTT upheld the HMRC decision to refuse the recovery of input tax on the legal fees incurred by the individuals. The partnership did not hold invoices sufficient for regulation 13 because they did not hold the required document with the name and address of the partnership. This distinguished the case from the *Hartridge* case.

The case is available **here** and worth a read as it clarifies the right to recover input tax.

4. Property transfer held not to be a TOGC but HMRC out of time to assess

With the election confirming that a Conservative Government will be appointed, we can expect continuing budget purdah and few announcements from HMRC until after the next budget. This does not mean that tax will not change because the law can alter with decisions of precedent made by the Upper tribunal and higher courts.

There is an interesting decision from the Upper Tribunal which addressed two questions: whether there had been a transfer of a going concern (TOGC) on the sale of a building; and, whether the assessment made by HMRC was out of time because HMRC had all the information it needed to decide the issue but took too long to raise the assessment. That last issue is very interesting because HMRC presented a case and argument but failed to introduce the necessary evidence to support their argument.

In **Revenue and Customs v Royal College of Paediatrics and Child Health & Anor [2015]** UKUT 38, the sale of the building at 5-11 Theobalds Road, London WC1X 8SH for £17,445,000 was agreed on 16th November 2007 and completed on 15th January 2008. The vendor had opted to tax the building so if it was not a TOGC the VAT potentially payable was substantial.

The Royal College is a registered charity whose activities are predominantly nonbusiness or exempt. It was registered for VAT in 1996. Its premises were at 50 Hallam St, London. The Royal College let space in its premises at Hallam St to two further organisations, the British Association of Perinatal Medicine (BAPM) and the British Association for Community Child Health (BACCH). The latter two organisations are registered charities, with aims similar to each other and related to those of the Royal College.

Advice was sought and if BAPM were to enter into an agreement for a lease with the vendor, paying a premium of £1000 before the Royal College agreed to buy the property then, since the vendor was carrying on a property business, the transfer would be a TOGC. The First tier tribunal ruled that this arrangement worked and it was a TOGC.

The sale was completed on 15th January 2008. As it was treated as a TOGC, no VAT was charged on the sale. In March and then May 2008 the Royal College granted 15 year leases to BAPM and BACCH respectively each for a single room in the property.

On 18th November 2008 the Royal College's advisers wrote to the Commissioners about the use of the property in order to clarify the treatment. This letter stated, amongst other things, that the transfer was treated as a TOGC. The next critical event was on 5th July 2010 when the Commissioners decided that the transfer was not a TOGC and assessed the vendor for VAT.

Taxpayers are entitled to a degree of certainty if they make full disclosure of the relevant facts. In 2004, the Court of Appeal effectively changed the law in relation to discovery assessment for direct tax when they ruled in favour of HMRC in Langham v Veltema. The rules in VAT are different and the time limits for assessment are to be found in s73 VATA 1994.

Finding in favour of HMRC, the upper tribunal (UT) overturned the FTT decision on whether there had been a TOGC. However here the agreement for a lease was not part of the seller's business at all. The putative tenants were never part of the vendor's business, they came from the purchaser. The agreement arose directly from and was simply part of the sale transaction. No part of seller's business was transferred to the buyer. For this reason the transfer was not a transfer of a going concern.

This makes the decision of the UT interesting because the issue of time limits became critical. These time limits are, 2 years after the end of the prescribed accounting period; or one year after evidence of facts sufficient in the opinion of the Commissioners to justify.

There is no doubt that the assessment was outside the two year period provided for in s73(6)(a) since the prescribed accounting period ended on 29th February 2008 and the assessment was on 5th July 2010. Before the FTT HMRC relied on the one year period and contended that the relevant evidence was only received on 24th November 2009. This was within the one year period and so within s73(6)(b).

The Royal College and the vendors contended that a file of the documents was given to Mr Lewis of HMRC in May 2009. HMRC contended that the documents were only provided in November 2009. At the FTT, Judge Denmack found as a fact that the documents were given to the relevant officer, Mr Lewis, in May 2009. On that basis he found that the Commissioners had all the information they needed to make the assessment on 14th May 2009 and so the assessment was out of time.

HMRC argued for a later date in January 2010 when the officer who made the assessment received all of the information but HMRC had failed to produce evidence to support this argument. There was no evidence to overturn the FTT decision of fact on the time limit and so the UT rules the appeal by HMRC must fail because the assessment was out of time.

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The views expressed in these podcasts are Derek Allen's personal views and do not necessarily represent AAT policy or strategy.

This podcast concentrated on VAT. There will be a general tax podcast updating AAT members on recent developments and decisions available on the website on 31 May 2015.