

VAT opportunities and obligations

A number of changes in VAT law took effect from 1st January 2010, and several important VAT cases have also called into question HM Revenue & Customs' (HMRC) traditional treatment of certain items. In some cases, HMRC has yet to issue revised guidance but you should consider whether you wish to make a claim and, if so, when. This leaflet deals with some of the key opportunities.

Opportunities

- VAT recovery on entertainment and samples
- VAT recovery on postal charges
- VAT recovery by charities on investment managers' charges
- VAT recovery on buying and selling subsidiaries

Obligations

- The "VAT Package"
- Filing EU sales lists

If you have the opportunity to make a claim the sooner you do it the greater the amount you are likely to recover. So act quickly, seeking help where necessary.

VAT recovery on entertainment and samples

Entertainment

The UK has a general block on the recovery of VAT on entertainment. In two recent EU VAT cases – X Holdings and Danfoss/Astra Zeneca – the recovery of VAT on entertainment and certain staff costs was considered. In X Holdings the Dutch VAT authorities referred the question of VAT recovery on entertainment to the European Court of Justice (ECJ). In such cases, before the ECJ hands down its ruling the Advocate General (AG) issues its opinion, which the ECJ often, although not always, tends to follow.



Based on the decision of the Advocate General it was thought that the right of recovery of input tax on the costs of providing a range of items including the provision of food and drink to staff, business gifts and the provision of accommodation and recreation opportunities to staff, would be extended. Many businesses have waited for the decision of the ECJ although some have made claims and assumed that the judgment of the ECJ would follow the view of the Advocate General. The judgment of the ECJ was issued on 15th April and did not follow the opinion of the Advocate General. It therefore seems that the blocking of recovery by HMRC on most of the above items was within EU law and that retrospective claims will not be possible. The question of samples was the subject of a separate case.

Samples

The UK allows the recovery of VAT on the provision of samples and promotional items but blocks the recovery if there is a series of samples to the same recipient or by reference to the cumulative value of gifts. The case involving EMI was referred to the ECJ.

On 15th April the Advocate General issued his opinion. The AG defined a 'sample' as one that constitutes any supply by a taxable person for the purpose of promoting future sales of a product to an actual or potential customer or a person who, owing to his particular position, is able to influence the exposure to market of that product. 'Samples' can be one or several items of goods that serve as examples of that product by retaining all the essential properties of the product in terms of quality and characteristics, thus enabling recipients of the samples to assess or test the nature, properties, and quality of the product. The AG said that the monetary limit must not render the relief meaningless and that Member States may not apply the ceilings cumulatively to several gifts made during a defined period of time.

Therefore if the ECJ follows the opinion of the AG the law relating to VAT on samples will be relaxed.

What action should you take?

The ECJ will in due course decide on samples, which may mean opportunities for UK businesses to make retrospective claims for VAT in respect of samples.

There is a rolling 4-year cap on claims. This means that you should consider submitting claims as soon as possible.

If you would like us to review your recovery of VAT in this area, please contact Adrian Houstoun (email ajh@kingstonsmith.co.uk or telephone 020 7566 3802).

VAT recovery on postal charges

In the UK, supplies by the post office have been treated as VAT exempt, which means there is no VAT to recover on postal costs as none is charged. A recent EU VAT case involved TNT UK and took the view that the VAT exemptions given to Royal Mail provide it with an unfair competitive advantage.

TNT UK lost its case but the ECJ took the opportunity to clarify the extent of Royal Mail's exemption. The court confirmed that the VAT exemption is restricted to the national operator providing universal postal services at standard charges. However, where prices are individually negotiated, postal and delivery services are subject to VAT.

Most businesses have a postal tariff rate that is a penny or two less than the national rate. In many people's view this means it qualifies as individually negotiated and should therefore be standard rated for VAT rather than exempt.

It remains to be seen whether HMRC's view of the scope of the exemption is fully in line with that of the EU, but HMRC appears to be willing to consider retrospective claims.

What action should you take?

There is a rolling 4-year cap on claims. This means that you should consider submitting claims as soon as possible. Evidence of what you spent and that your rates were less than the national rate for a stamp should enable you to consider a claim.

If you would like us to review your recovery of VAT in this area, please contact Adrian Houstoun (email ajh@kingstonsmith.co.uk or telephone 020 7566 3802).

VAT recovery by charities on investment managers' charges

About a year ago, one of the Nuffield charities publicised the fact that they had succeeded in reclaiming VAT on investment management fees to the extent that its investment income was supporting the VAT-able activities of the charity.

This announcement followed the argument in the Children's Society case concerning VAT on fundraising costs and overturned the long-standing decision in the Wellcome case that the activity of managing investments was in itself not a business one. The result was that the input VAT on investment management fees was no longer disallowable, but partly recoverable depending on the circumstances.

Subsequent claims from other charities using the same arguments appear to have been referred to HMRC's Policy Division so that it can rule on the principle behind the claims. We understand that HMRC has finally agreed that such claims are valid and it will issue a briefing about it in due course. To date, no information has been published, although some of our clients have been paid recently in respect of claims already submitted.

The ability to recover a proportion of input VAT on investment management fees depends on the nature of the charity's activities and what its investment portfolio is used for. Provided that part of the charity's activities are subject to VAT, and the investment income is used to support these activities, then it should be possible to submit a claim now in respect of input VAT not previously claimed, in accordance with the charity's normal partial exemption calculation. Currently, it is possible to make a retrospective claim as far back as the VAT return period ending in spring 2006, but this cut-off date depends on the charity's circumstances and will move forward.

What action should you take?

If you think your charity may be affected by this new interpretation, it is worth making a claim as soon as possible to obtain the maximum benefit. You will need to obtain details of the amount of investment management fees and VAT thereon paid since the beginning of the claim period.

If you would like us to review your recovery of VAT in this area, please contact Adrian Houstoun (email ajh@kingstonsmith.co.uk or telephone 020 7566 3802), or James Cross (email jcross@kingstonsmith.co.uk or telephone 020 7566 4000).



VAT recovery on buying and selling subsidiaries

Two important cases (one acquiring, one selling) have helped clarify the position on recovering VAT on deal costs. It has been established that a holding company can carry on an economic activity for VAT purposes where it actively manages its subsidiaries in return for a fee – rather than being just a passive shareholder. However, the issue of when a corporate buyer or seller can recover any of the VAT incurred on a share purchase and sale has remained a point over which HMRC and businesses disagree.

The acquiring case involved a Spanish group that purchased BAA. The tribunal concluded that a representative member of the BAA VAT group could recover the VAT incurred by Bidco, a company set up for the purpose of the transaction. This was on the basis that Bidco carried on an economic activity from the moment it was incorporated, and despite the fact that it never made taxable supplies itself. The tribunal found that Bidco's activities went beyond the mere acquisition and holding of shares not least because Bidco negotiated and arranged finance for the benefit of BAA's operations.

In the selling case, known as AB SKF, the ECJ held that the sale of shares should be treated in the same way as the acquisition of shares. Therefore, it could be an economic activity, provided the selling shareholder takes an active role in the management of those companies. It is a complex case and leaves scope for HMRC to deny input tax recovery and argue that the costs relate to an exempt supply rather than the residual business.

What action should you take?

Correct structuring of future deals may be to your advantage.

HMRC is expected to resist claims, but for transactions since 1 April 2006 where input tax recovery was denied you should consider whether to make a claim.

If you would like us to review your recovery of VAT in this area, please contact Adrian Houstoun (email ajh@kingston-smith.co.uk or telephone 020 7566 3802).

The VAT package

Virtually all businesses that purchase or provide intra-EU services will be affected by the biggest change to the VAT system since the early 1990s. This has been termed the VAT package. Compliance obligations will be radically different, requiring changes in the way businesses account for VAT on certain sales and purchases, combined with new EU sales list (ESL) reporting requirements.

The change is now in the recent past, but how prepared are you for the new regime that came into effect on 1 January 2010? Under the new basic rule for services applicable from 1 January 2010:

- The place of supply of intra EU services to a relevant business person will be where the customer belongs. These are known as business-to-business supplies (B2B).
- The place of supply of intra EU services to a person who is not a relevant business person will be where the supplier belongs. These are known as business-to-consumer supplies (B2C).
- The revised legislation uses the term 'relevant business person' to determine how services are treated. A relevant business person is a person to whom one of the following applies:
- The person is a taxable person within the scope of Article 9 of the Principal VAT Directive.
- The person is registered for VAT in the UK, the Isle of Man or another EU Member State.

The definition is broad and means that any business in the EU is a relevant business person. The term also extends to organisations that are not necessarily in business but are registered for VAT, such as certain charities. The treatment of supplies to non EU people remain the same as before.

Filing EU sales lists

Part of the VAT package is a new requirement to submit ESLs in respect of services supplied to customers and clients in other EU states. The requirement already covered goods but it now covers goods and services. So many businesses in the service sector will now have to submit ESLs for the first time.



This is a statistical document on which you must show all the supplies made to each of your EU customers. It also provides a way for the customer's tax authorities to check that the VAT due on the reverse-charged service has been accounted for.

- ESLs for services normally cover calendar quarters, so some businesses may prefer to request that their quarterly VAT returns are aligned with their calendar ESL quarters.
- You have 14 days to submit paper ESLs and 21 days for those submitted electronically.
- You will need all your customers' EU VAT numbers in order to complete an ESL, so it is advisable that you request EU VAT numbers from all your EU customers as soon as possible. HMRC's website contains information on checking their validity.

How we can help

Our VAT team provides a comprehensive service advising on all aspects of VAT, whether contentious or advisory. We review your business and identify potential opportunities, and can review structures or advice from other advisers to give you comfort. To discuss anything contained in this leaflet or other possible claims or advice, contact:

Adrian Houstoun, partner, and head of VAT at Kingston Smith (tel 020 7566 3802, email ajh@kingston-smith.co.uk). Alternatively, speak to your usual Kingston Smith contact.



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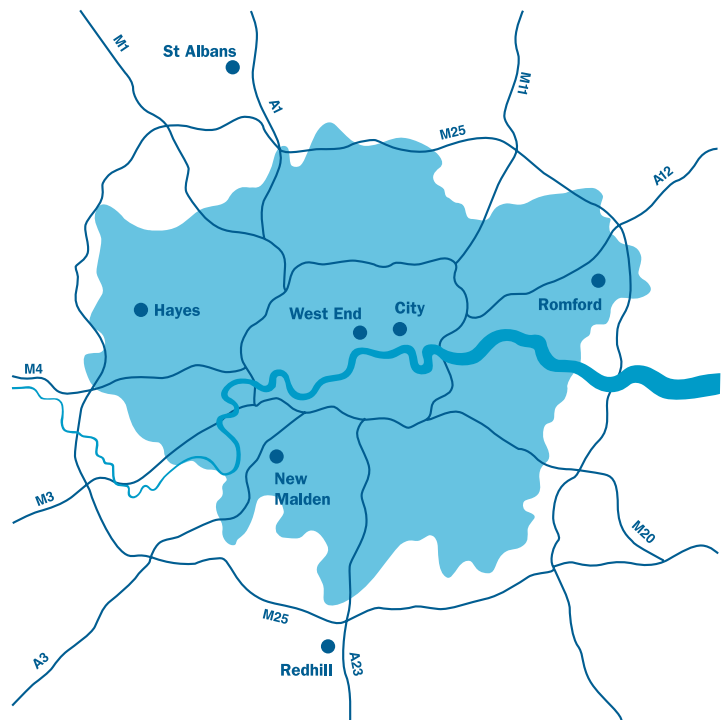
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