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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 an order issued by the Court of Justice in the case of Weindel Logistiks Service.

Normally, the court issues judgments but, if the court considers that the issue in question has either been dealt with in a previous judgment or is sufficiently clear, it may 'skip' the judgment and simply issue an order. Where the court goes into some detail as to the reasons for the order the order is referred to as a 'reasoned order'.

The issue in this case was whether the company was entitled to reclaim VAT paid on the importation of goods where it was not the legal owner of the goods and it did not incorporate the cost of the goods into its own downstream taxable supplies.

The court has confirmed that, in such circumstances, the company is not entitled to reclaim the VAT paid on importation as input tax.

The Court of Justice has also issued a judgment this week in the case of Kaplan International Colleges (UK) Ltd (KIC). This was a referral to the court by the UK's First-tier Tax Tribunal. The matter concerns the exemption from VAT for supplies by cost sharing groups and whether, in Kaplan's case, supplies by the cost sharing group qualified in circumstances where the recipient of the supplies (KIC) was not a member of the cost sharing group but was the representative member of a VAT group. The Court has ruled that the services provided by the cost sharing group do not qualify for exemption from VAT.

Finally this week, we look at HMRC's updated policy paper in relation to the VAT accounting rules that will apply after 1 January 2021 for goods moving from GB to the EU via Northern Ireland and vice versa. HMRC has issued updated guidance which seems to impose an additional 20% VAT cost where goods move between GB and the EU (including the Republic of Ireland) via Northern Ireland.

Court of Justice – Reasoned Order: Weindel Logistik Services

Whether VAT paid on importation of goods into the EU can be reclaimed

The Court of Justice has issued a reasoned opinion (as opposed to a judgment) in this case. Under the court's procedural rules, if it considers that the matter referred to it by the referring court has been considered previously or, if it considers that the matter is 'acte clair' and does not require a judgment, it can issue an order rather than a judgment. This case is one of those cases. Rather than issue a judgment, the court has issued a reasoned order. Such an order has, however, the same binding force as a judgment.

The case in question concerns the recovery of VAT paid on the importation of goods into the EU by a business that did not own the goods in question. Weindel Logistik Services (Weindel) acted as the importer of record in relation to a quantity of goods owned by its Swiss customer. Weindel was contracted by the owner to perform a service on the goods and to then return them to the customer in Switzerland. Weindel paid the import VAT that was due on the goods when they arrived at the Slovakian border and reclaimed that VAT as input tax on its periodic Slovak VAT return. Unfortunately, when the Slovak tax authority investigated the return, it denied the company's claim considering that the company had no entitlement to recover the VAT paid on importation. The tax authority argued that Weindel had not acquired the right to dispose of the goods as owner nor had it incorporated the cost of the goods into its downstream taxable supplies. According to the tax authority, therefore, there was no direct link between the VAT paid on importation of the goods and the company's own taxable supplies of services.

The company appealed to the Slovakian courts and, ultimately, the Supreme Court in Slovakia referred the issue to the Court of Justice for a preliminary ruling on the correct interpretation of the VAT Directive.

In simple terms, the court agrees with the Slovakian tax authority. One of the golden rules governing the right of deduction is that there must be a direct link between the transaction upon which VAT is charged (the upstream transaction) and the taxable transactions of the claimant (the downstream transactions). A right to deduct is, however, also permitted in favour of the taxable person, even in the absence of a direct and immediate link between a particular upstream transaction and one or more downstream transactions, when the costs of the upstream transactions are part of the general overhead expenses and are, as such, components of the price of the goods or services that it provides downstream. In this case, the Slovak Supreme Court confirmed that Weindel acted only as a service provider, without having acquired the imported goods or bearing the import cost. As such, there was no direct or immediate link with its downstream taxable supplies of services which meant that the VAT that had been paid on importation of the goods into Slovakia was not reclaimable.

In essence, the court concludes that import VAT can only be reclaimed by someone that has either acquired the right to dispose of the goods as if it were the owner (which does not necessarily mean that legal ownership or title in the goods must pass) or, alternatively, if the cost of importing the goods has been incorporated into the price of the importer's downstream taxable transactions. The court specified that persons who import goods without owning them are not in a position to benefit from the right to deduct VAT, except where it can be established that the cost of importation is incorporated in the price of the particular downstream operations or in the price of the goods or services provided by the taxable person in the course of his economic activities.

Comment – this order of the court confirms HMRC's policy in the UK. HMRC announced in April 2019 (Revenue & Customs Brief 02/2019) that it was to amend its policy on the recovery of import VAT by non-owners. At the time, there was some conjecture as to whether or not HMRC had correctly interpreted the provisions of the VAT Directive. This order from the Court of Justice confirms that HMRC's change of policy was correct.

With Brexit almost upon us in the UK, the number of imports into the UK is set to increase significantly. Businesses importing goods which they do not own should heed this case and, where necessary or appropriate consider alternative arrangements and consider amending existing contractual obligations and terms of trade.

Businesses importing goods into the UK in order to perform a service on the goods before re-exporting them may also wish to consider inward processing relief as an alternative procedure on importation.

Court of Justice – Judgment – Kaplan International Colleges (UK) Ltd (KIC).

Whether supplies by a cost sharing group (CSG) qualify for VAT exemption

Provided that certain conditions are met, the VAT Directive provides an exemption from VAT for supplies of services by a CSG to its members. In this case, prior to 2014, KIC, as representative member of a UK VAT group, was required to account for UK VAT (under the reverse charge mechanism) on services received from student recruitment agents based in China, India, Hong Kong and Nigeria. However, In 2014 KIC's subsidiaries, which were also members of the UK VAT group, formed a CSG along with a newly formed Hong Kong company (KPS). KPS took over responsibility from KIC in relation to student recruitment and it contracted directly with the overseas agents. KPS then invoiced each of the members of the CSG for their respective share of the costs and claimed VAT exemption in relation to these charges. KIC was not a member of the CSG but was the representative member of the VAT Group.

Under UK VAT law, any supply of goods or services to a member of a VAT group is deemed to be a supply to the representative member. In addition, a VAT group is regarded as a single taxable person with the members effectively losing their identity for VAT purposes. In this case the supply of services by KPS was, therefore, a supply to KIC (as representative member of the VAT group). This meant that the services were not supplied by KPS to the members of the CSG and, as a result, the exemption provided for such supplies by Article 132(1)(f) of the VAT Directive did not apply. The Court concluded that the exemption laid down in that provision is not applicable to supplies of services made by an independent cost sharing group to a VAT group that is regarded as a single taxable person, where not all the members of the VAT group are members of the cost sharing group.

Comment

Generally, VAT is payable in the UK by a UK entity in relation to the receipt of services from a supplier established outside the UK. This procedure is known as the 'reverse charge' mechanism and it ensures that exempt businesses do not gain a tax advantage by purchasing services on a VAT free basis from suppliers established overseas.

The issue of VAT on overseas recruitment agent's fees has been a thorny issue for many years for many UK universities. Here Kaplan sought to combine the exemption for services supplied by a cost sharing group with the special provisions in UK law for VAT groups. Unfortunately, the CJEU considers that the cost sharing exemption does not apply where the members of the CSG and the VAT group are not one and the same.

HMRC Policy

Supplies of goods between the EU and GB via Northern Ireland (and vice versa)

On Friday 20 November 2020, HMRC revised its policy document entitled "Accounting for VAT on goods moving between Great Britain and Northern Ireland from 1 January 2021". The document now includes two further paragraphs which cover the VAT treatment of supplies of goods from GB to the EU via Northern Ireland and vice versa.

The guidance now states (in relation to GB to EU via NI) *"This refers to goods transported via Northern Ireland to an EU Member State, for example the Republic of Ireland. Similar to accounting for a direct movement from Great Britain to Northern Ireland, the seller will be liable to account for the import VAT and zero-rating the goods on export to the EU. The VAT charged will be accounted for as output VAT on the UK VAT return by the seller. The seller will not be able to claim this back as input VAT. There will be an exception to this rule where goods are declared into a special customs procedure or Onward Supply procedure when they enter Northern Ireland or before arriving at the first EU member state."*

In relation to EU to GB via NI – the guidance now states *"This refers to goods transported via Northern Ireland from an EU member state, for example the Republic of Ireland. Where goods are sold and moved via Northern Ireland to Great Britain from a VAT-registered business in an EU member state, including the Republic of Ireland, the seller will be liable to account for the import VAT to HMRC. The EU business will have to register with HMRC and account for the VAT on a UK VAT return. The UK customer will be able to reclaim the VAT as input VAT, subject to the normal rules."*

The first paragraph seems to imply that supplying goods to the EU via Northern Ireland will lead to an additional 20% VAT charge that will not be reclaimable. In other words, the cost will increase by 20% in comparison to goods that are supplied directly from GB to the EU. HMRC has yet to provide any further clarification in relation to these two new paragraphs.

Comment

It seems to make no economic sense to impose an additional VAT charge of 20% for supplies of goods between GB and the EU (including the Republic of Ireland) where the goods transit through Northern Ireland and HMRC has yet to offer any explanation for this change of policy.

It is possible that the effect of the new policy (ie the imposition of an additional 20% cost) was not intended and we shall be seeking further clarification on this point from HMRC. It is possible that the wording of the policy paper is drafted such to appease the European Commission as part of the Brexit negotiations. The Commission is concerned that the lack of a hard border between NI and the Republic could lead to VAT free goods circulating within the EU. Look out for further developments in future ITUs.

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