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Indirect tax update

Week ending 18 October 2019

Summary

Welcome to this week's Indirect Tax Update.

This week we look at a couple of judgments from the Court of Justice. In the first case, (Case C-573/18 C GmbH & Co KG) the issue to be resolved by the Court related to the correct value of a supply of goods made by a fruit and veg co-operative to its members.

The co-operative was a 'producer organisation' and it purchased goods on behalf of its members. It received part payment from the member organisation as consideration for the supply but it also received a contribution from an operational fund derived partly from a turnover based levy imposed on the members and partly from EU subsidies. The co-operative only accounted for VAT on the contribution received from the members and the German tax authority argued that the amount received from the fund should be regarded as a subsidy which should be included in the value of the supply.

The second case (Case C-653/18 – Unitel) - relates to the exemption for exports from the Community and whether a Member States is entitled to deny the exemption where the substantive conditions laid down in the Directive for exemption to apply have been met.

The company in this case was denied exemption for an export of goods because the tax authority could not identify the recipient of the supply. The Court considered that if the substantive conditions of the VAT Directive have been complied with, then the VAT exemption cannot be denied by the Member State as such refusal would offend the EU principle of proportionality. However, exemption can be refused if the tax authority is satisfied that either no supply of goods has actually taken place or that the supplier knew or ought to have known that his transaction was connected with VAT fraud.

Finally, we look at a First-tier Tax Tribunal decision in the case of In Tandem Resources Ltd. In this case the company set up an arrangement designed to lower the cost of providing employee benefits. For the arrangement to work it was required to TUPE in the employees of its clients. HMRC considered that it then supplied these employees back to its clients – a supply of staff upon which VAT was due.

Court of Justice – Judgment – C GmbH & Co KG

VAT – Value of supply

VAT law provides a set of rules for determining the value of a supply of either goods or services for VAT purposes. These rules are set out in the VAT Directive and Member States are required to implement the rules into domestic law. This requirement is intended to ensure that there is a common system for valuing supplies for VAT purposes throughout the whole European Community.

Article 73 of the VAT Directive states that "*in respect of a supply of goods or services, the taxable amount (*ie the 'value' of the supply*) shall include everything which constitutes consideration obtained or to be obtained by the supplier in return for the supply from the customer or a third party including subsidies linked to the price of the supply*'.

In this referral to the Court of Justice by the German courts, the taxpayer was a 'Producer Organisation' as defined by EC Regulations concerning the common organisation of the market in fruit and vegetables. It was a 'members' organisation which procured the supply of certain capital goods on behalf of members. It received part payment for these supplies directly from the member to whom the goods had been supplied but it also received a contribution from an 'operational fund'. This fund received money partly from EU grants and partly from a turnover based levy paid by the members.

The company had only accounted for VAT in relation to the consideration it had received from the member. It did not account for VAT on the contribution received from the fund. Considering that the contribution from the fund constituted "a subsidy linked to the price of the supply", the tax authority in Germany considered that the value of the supply made by the taxpayer should have included not only the consideration received from the member but also the contribution from the fund.

The Court of Justice has issued its judgment in this case and has agreed with the German tax authority. The contribution made by the fund was a subsidy and the value of the supply of goods by the co-operative to its members should have included the value of the subsidy in the taxable amount.

By including the subsidy in the taxable amount, it ensures that VAT is charged and collected in relation to the full value of the consideration received by the supplier from his customer or a third party. The Court ruled that the Producer Organisation reduced the price of the supply of capital goods to its members by the precise amount of the sums received from the operation fund and that there was, thus, a direct link between the supply of the goods and the consideration actually received. The payments received from the operational fund were made exclusively for the purpose of supplying the goods in question and, therefore, constitute subsidies directly linked to the price of those goods.

Comment – Determination of the 'taxable amount' for a supply of goods or services is a crucial part of the VAT rules. If the taxable amount determined is too high, suppliers will calculate and account for too much VAT. Conversely, if the taxable amount determined is too low because, as in this case, the value of subsidies directly linked to the price of the goods is left out of account, then the supplier will not charge enough VAT and the tax authority may well assess the supplier for the difference. In such circumstances, the supplier may not be able to pass on the additional VAT cost to his customers and, in many cases, this could leave the supplier in a position where he actually makes a loss.

Court of Justice – Judgment – Unitel

Whether a Member State can refuse exemptions for the export of goods from the EU

This was a referral to the Court of Justice by the Polish Supreme Administrative Court.

To encourage exports from the EU and to ensure that VAT is collected in relation to the place of consumption of goods, the VAT Directive provides an exemption for the export of goods outside the European Community. The law stipulates that certain conditions need to be met for the exemption to apply (the substantive conditions) but Member States may impose there own conditions to ensure the straightforward application of the exemption and to prevent avoidance or abuse.

In this case, the Member State was unable to identify the end customer for a supply of goods and, for this reason, refused to allow the exemption for the export even though there was unequivocal evidence that the goods had been supplied and that they had left the EU.

The Court of Justice has, once again, ruled that if the substantive conditions set out in the Directive have been met, a Member State is not entitled to refuse the exemption as such refusal would offend the principle of proportionality (ie refusal to allow exemption goes beyond the measures necessary to achieve the objective)

According to the CJEU, there are two exceptions to that rule however. Firstly, the exemption can be refused by a Member State if the lack of identity of the customer is a barrier to proving that a supply has actually occurred. Secondly, exemption will be refused if the Member State considers that the taxpayer knew or should have known that the transactions in question were connected with VAT fraud.

Comment

The Court of Justice has ruled on many occasions that Member States are not allowed to defeat the objectives of the Directive by insisting on compliance with local formal conditions.

Here, the Polish tax authority took the view that, as the ultimate customer for the supply of goods could not be sufficiently identified, the supply could not benefit from the exemption for exports from the community. The Court confirmed that unless the lack of identification of the customer meant that there was no proof that the supply had occurred or that the supplier knew or should have known that his transactions was connected to VAT fraud, refusal to allow exemption would offend the principle of proportionality

First-tier Tax Tribunal – In Tandem Resources Ltd

In this case, the taxpayer company identified an opportunity to reduce the cost of providing employee benefits. The arrangements put in place were to transfer (under TUPE arrangements) the employees of the company's customers to itself and to then re-supply the employees back to the original employer. By doing so, the company was able to obtain greater discounts on employee benefits and it would pass on those savings to its customers.

The taxpayer considered that the wages and NI payments made by the customers were not consideration for any supply made by the company and that, as a consequence, there was no VAT due. Unfortunately, HMRC took the view that the company was supplying staff to its customers and that, as a result, VAT was due on the full consideration for that supply including the element relating to the employees wages and NI contributions.

HMRC also took the view that the failure to account for the correct amount of output VAT was a deliberate inaccuracy for which a penalty assessment was issued and HMRC had stated that it was their intention to make the Director of the taxpayer personally liable for those penalties.

The Tribunal agreed with HMRC in respect of the VAT liability. It was clear from the contracts between the company and its customers that the employees would be transferred and then re-supplied. Accordingly, VAT was due on the full consideration for that supply received from the customer. On the penalty point, the Tribunal took the view that, on the evidence, the inaccuracies in the VAT returns were not deliberate but were, nevertheless, careless. As a result the penalty assessments were reduced to reflect this.

Comment

This case demonstrates that failure to consider the VAT implications of a transaction can lead to unforeseen costs and, in some cases to personal liability for any associated penalties.

The tax, interest and penalties at stake in this case was in excess of £20 million.

There have been a number of cases over the last few years (Reed and Adecco) that have found that VAT is due on the full consideration received for a supply of staff.

Unfortunately, in this case, it seems that the taxpayer was not aware of the previous case law and implemented an arrangement that was not efficient from a VAT perspective. It is not known at this stage whether the taxpayer company will seek leave to appeal.

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