VAT Cases & VAT News

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VAT Cases

01 Concept of Taxable Person

The decision in ***XT v Valstybinė mokesčių inspekcija prie Lietuvos Respublikos finansų ministerijos and Vilniaus apskrities valstybinė mokesčių inspekcija prie Lietuvos Respublikos finansų ministerijos (Contrat d'activité commune)*** C-312/19 was delivered by the CJEU on 16 September 2020. The court had to determine who the taxable person was in the context of a partnership and therefore who would be liable for accounting for VAT on supplies made. In this case, two natural persons planned and implemented a construction project for several buildings; however, only one of them – XT – actively carried on the business, whereas his business partner, who funded 70% of the acquisition costs, was involved only in project decisions and received a corresponding share from XT on completion of the joint project and the sale of the new buildings. Proceedings arose between XT and the Lithuanian Tax Inspectorate concerning an order issued to XT by the Vilnius tax authority requiring payment of VAT and interest. The VAT provisions under review were Articles 9 and 28 of the EU VAT Directive, which set out the meaning of taxable person and the provisions on undisclosed intermediaries, respectively.

In the period from February 2010 to February 2013 a number of steps were taken by XT and his partner to construct and sell five buildings. The partnership agreed to carry out a building project, and XT's partner had passed his financial contribution of 70% to XT. The plot of land on which the buildings were to be constructed was purchased by XT in his own name. XT applied for the construction permit, and obtained it, in his own name. XT in his own name concluded the property development

agreement with a related company. The partners decided that it would be XT who would be entered in the land register as sole owner of the land. XT concluded in his own name the contracts of sale relating to all of the buildings and to the plots of land attached to them both before and after the decision to terminate the partnership.

XT and his partner did not consider that the sales of the buildings to third parties were an economic activity and therefore did not account for VAT on the sales and did not reclaim any VAT. The Vilnius tax authority considered XT to be a "taxable person" and responsible for accounting for VAT on the sales but allowing for input deduction on the costs incurred. Lithuanian law does not apply a legal personality to a partnership, and therefore it was unclear whether the taxable person was XT alone or the partnership.

The question referred was whether a natural person must be considered to be the taxable person and liable for VAT where that person has entered into a partnership agreement (without legal personality) with another natural person whereby the first person is empowered to act in the name of the partners as a whole but acts alone and in his own name in relations with third parties when carrying on the economic activity of the partnership and carries out that activity independently. Article 9(1) provides that "'taxable person' shall mean any person who, independently, carries out in any place any economic activity, whatever the purpose or results of that activity". The concept is broadly defined and is focused on independence in pursuing an economic activity. In assessing who the taxable person is, you need to establish who has independently carried out the economic activity. Independence means allocating the transaction concerned to a particular person or entity but at the same time guaranteeing that the customer can exercise any right of deduction with legal certainty (by having the full name and address of the taxable person in question). Consideration is also to be given to assessing whether the person concerned carries on an economic activity in their own name, on their own behalf and under their own responsibility, and whether they bear the economic risk associated with the carrying on of those activities.

Even though the partnership agreement provided that XT was the person who acted in the name of both parties when dealing with third parties, the referring court found that only XT participated in those relations, that he did not mention the partner's identity or the partnership, and that it was highly likely that the third parties were unaware that a partner existed. Based on the facts, the court found that XT acted in his own name and on his own behalf and that he assumed the economic risk associated with the taxable transactions. It stated that the economic activity could not be allocated to the activity of the partnership, as XT and his partner did not act together when dealing with third parties. XT, as the person permitted to act on behalf of the partnership, did not act in accordance with the representation rules of the agreement, so the partnership cannot be regarded as having carried out the taxable transactions.

As the partner has not carried out any transaction himself, then based on the facts, XT is to be regarded as having acted independently and therefore as being a taxable person. The presence of the following facts did not alter this conclusion: that the partner provided significant finance for the purchase of the land; that the liabilities and

the assets were divided; or that the decisions relating to the economic activity were taken by the partners together. As XT held himself out to third parties and did not mention the partnership or the identity of his partner, the acts resulting from those decisions were carried out by XT on his own behalf and not by the partnership.

02 Origin and Scope of the Right to Deduct Input VAT

The CJEU handed down its decision in the case of ***Mitteldeutsche Hartstein-Industrie AG v Finanzamt Y*** C-528/19 on 16 September 2020. The dispute arose from a refusal by the German Tax Office Y to deduct input VAT paid by Mitteldeutsche Hartstein-Industrie AG (MHI) for carrying out works for the extension of a road belonging to a local municipality. MHI is a managing holding company with subsidiaries, A GmbH and B GmbH.

The Regional Council approved the redevelopment and operation of a limestone quarry. A GmbH was authorised to operate the quarry, and this was subject to the development of access to the quarry by way of a public road belonging to the municipality. The extension to the road was necessary for extracting the limestone. The authorisation would expire if the road was not completed by a certain date. A GmbH and the municipality agreed that the municipality would plan and implement the extension and that, if the road remained open to the public, A GmbH would have unrestricted access. A GmbH would fund the road extension. B GmbH was engaged to carry out that extension. Once completed, the road was used by A GmbH's heavy goods vehicles and other vehicles. MHI reclaimed input VAT only in relation to the services supplied by B GmbH. Tax Office Y took the view that MHI had provided the municipality with free-of-charge work liable to VAT by constructing the road extension.

A number of questions were referred to the CJEU, the first of which was whether a taxable person is entitled to deduct input VAT paid for road extension works that were carried out for the benefit of the municipality. The court reiterated the principles that apply in relation to input VAT recovery – to include acting as a taxable person when the goods or services are acquired; using those goods or services for making taxable supplies; establishing a link between the input and output transactions or, in the absence of a link, assessing whether the costs are part of the general costs linked to the taxable person's overall economic activity and whether the input costs are included in the output transactions.

In this case, there is a direct and immediate link between the extension works and a taxed output transaction carried out by MHI or its economic activity. The court stated that, in applying the direct link test, all of the circumstances surrounding the transactions should be assessed and account of the objective content of the transactions should be taken. It would not have been possible, practically and legally, to operate the quarry without the road extension. In the absence of the works, MHI's economic activity could not have been pursued. The input VAT incurred on the services were linked to the works that formed part of the cost of the output transactions (the operation of the quarry). This link was not broken by the fact that the road was open to the public free of charge. The court held that MHI is entitled to deduct input VAT paid for works on the municipal road extension carried out for the benefit of a municipality where that road is used both by MHI for its quarrying operation and by the public.

The second question raised was whether the authorisation to operate the quarry granted unilaterally constituted consideration received by MHI. resulting in the works comprising a transaction carried out for consideration, as MHI carried out the road extension works without monetary consideration.

A transaction would be classified in this way if there is a direct link between the supply and the consideration received (not necessarily monetary consideration). In this case there was a legal relationship between the parties due to the agreement between MHI and the municipality to carry out the works. As noted above, the parties agreed that MHI would fund the works and the municipality would plan and implement the road extension and provide unrestricted access. However, the court noted that it could not be argued that there was a reciprocal arrangement in relation to the works and the grant of the authorisation to operate the quarry, as the authorisation was granted by the Regional Council, not by the municipality. The court has previously held that a unilateral act by a public authority cannot, in principle, impose a legal relationship entailing reciprocal performance. The works were a requirement of the authorisation to operate the quarry and, as such, were not consideration in money or in kind. The court held that there was no direct link between the road extension works and the authorisation, as the authorisation did not constitute consideration for a supply.

The third question posed was whether the works carried out for the municipality comprised a supply of goods for consideration. A supply of goods includes self-supplies, disposals free of charge and the application of goods for non-business purposes (Article 5(6) refers). In this case, as noted above, an entitlement to input VAT could arise and the works may constitute a transfer free of charge, so that elements of Article 5(6) are present. The works on the road extension were carried out to meet the needs of MHI, and the outcome of the works enabled MHI to operate the quarry. The court noted that even though the works were carried out free of charge for the municipality:

> "[the supply] is not liable to give rise to a situation of untaxed final consumption or to a breach of the principle of equal treatment, since such works do not constitute a transaction which must be treated as a supply of goods made for consideration, within the meaning of Article 5(6)".

Subject to confirmation by the referring court, the works carried out benefitted MHI and have a direct and immediate link with its taxable economic activity and the input costs can be linked to MHI's output transactions.

03 Exemption for Insurance Transactions

The CJEU published its decision in the case of ***United Biscuits (Pension Trustees) Ltd, United Biscuits Pension Investment Ltd v HMRC*** C-235/19 on 8 October 2020. The case dealt with the exemption for insurance and reinsurance transactions under Article 135(1)(a) of the VAT Directive in the context of the provision of pension fund management services by investment fund managers. The case arose as HMRC imposed VAT on pension fund management services – different VAT rules applied according to whether the services were provided by insurers or by non-insurers. The benefit of the exemption for insurance transactions was confined to suppliers who were authorised in their capacity as insurers. United Biscuits Pension (UBP) is the trustee of a defined-benefit occupational pension scheme for employees of United Biscuits (UK) Ltd. It and a former trustee, United Biscuits Pension Investment Ltd (UBPIL), received management services, which were supplied by both insurers (exempt) and non-insurers (VATable). VAT refunds were sought in respect of the VAT charged on the services supplied by non-insurers.

The question referred was whether investment fund management services supplied for an occupational pension scheme, which do

not provide any indemnity from risk, can be classified as "insurance transactions" under the exemption in Article 135(1)(a). The court reiterated the essentials of an insurance transaction – the insurer undertakes, in return for prior payment of a premium, to provide the insured, in the event of materialisation of the risk covered, with the service agreed when the contract was concluded. The services contractually provided to UB comprised fund management solely for its account, to the exclusion of any indemnity from risk. The court commented that the supplies of services do not meet the criteria for an insurance transaction as the exemption is justified by the difficulty of determining the correct amount of VAT for insurance premiums relating to the coverage of risk.

The term insurance is to attract the same interpretation in the VAT Directive as it does in the Insurance Directives. The court indicated that the case law quoted by UB (e.g. *CPP* C-349/96) refers to the detailed arrangements for providing insurance or where an intermediary exists between the insurer and the insured. However, the court in earlier case law:

> "which referred to the term 'insurance' in general and not to the concept of 'insurance transactions', within the meaning of the common system of VAT, did not intend to establish the necessary and intrinsic link between the latter and possible legal categories which appear in the directives on insurance. Thus, both the judgments referred to by the applicants in the main proceedings take and apply the criteria referred to in paragraphs 29 and 30 of this judgment without calling those criteria into question or adding to them in the light of EU law on insurance matters."

The court indicated that a detailed analysis of the relevant provisions of the Directives does not support the idea that supplies of pension fund management services fall within the scope of Article 135(1)(a). The court reviewed the wording used in the First Life Assurance Directive and noted that the life insurance activity is either "insurance" or "operations". Management of group pension funds is included under "operations" in that Directive. The court distinguished between insurance activities and operations that are related activities closely linked to insurance activities, which are therefore ancillary activities and do not constitute insurance as referred to in the Insurance Directives. Consequently, the EU legislators did not intend pension fund management services to be regarded as "insurance".

The court also considered the different language versions of the Insurance Directive, where in some it is referred to as classes of insurance and others as classes of activity. Where there is a difference between the various language versions, the legislative provision is to be interpreted according to the purpose and general scheme of the rules of which it forms part:

> "Therefore, in the light of the general scheme of the directives in the matter of insurance, it is consistent for the classification of activities laid down by those directives in their annexes to include insurance and pension fund management activities, without it being possible to interpret that classification as treating those operations as insurance."

The court held that:

> "Article 135(1)(a) of Directive 2006/112 must be interpreted as meaning that investment fund management services supplied for an occupational pension scheme, which do not provide any indemnity from risk, cannot be classified as 'insurance transactions', within the meaning of that provision, and thus do not fall within the VAT exemption laid down in that provision in favour of such transactions."

04 Legislative Interpretation and VAT Rate on Certain Food Items

The Supreme Court in Ireland delivered a decision on 29 September 2020 in the case of ***Bookfinders Ltd v The Revenue Commissioners*** [2020] IESC 60, rejecting arguments by an Irish Subway franchisee that it is not liable for VAT on certain of its takeaway products, including teas, coffees and heated filled sandwiches. It had sought VAT refunds on the grounds that the rate of VAT applicable to some of its products should be 0%. The appeal by Bookfinders Ltd included consideration of whether the bread used in Subway sandwiches fell outside the statutory definition of bread intended under the VAT Act 1972, as amended, to attract a zero VAT rate. The five-judge court ruled that the bread falls outside that statutory definition because it has a sugar content of 10% of the weight of the flour included in the dough (under the bread definition that applied at the time). A significant portion of the judgment dealt with statutory interpretation, namely, whether the general principles of interpretation applied or the principles of conforming interpretation, and a detailed review of related case law and the Interpretation Act 2005 is included. It is planned to include an article considering the impact of this decision in *Irish Tax Review* Issue 1, 2021.

05 Liability to VAT on Residential Property Sales

Tax Appeals Commission determination **149TACD2020** concerned whether the appellant was liable to account for VAT on the sale of residential properties to third parties by the bank with which he had an outstanding loan. The appellant and another person jointly owned a property since 1 July 2005. The property was developed, by their construction company, into residential units between 2007 and 2010. The construction business ceased on 23 April 2010. The residential properties were disposed of on 1 February 2013. Revenue, as a result of an audit of the appellant's taxes for 2013–2016, raised an assessment for VAT in respect of the appellant's share (50%) of the 2013 disposals. The appellant argued that even though the partnership was registered for VAT, it did not recover any VAT on the purchase of the property. The appellant submitted that it was a forced sale as the partnership could not repay the loan and therefore the bank is obliged to pay the VAT on the sales proceeds. It was evident that a receiver had not been appointed and the properties were not taken over by a mortgagee in possession. The TAC found that the appellant, as the owner of the properties, had developed the properties in the course of business and was entitled to recover the VAT on the development of the properties and was therefore liable to account for VAT on the sales in 2013.

It is not known if the Tax Appeals Commission has been requested to state and sign a case for the opinion of the High Court.

VAT News

Ireland

VAT registration

Revenue has published eBrief 183/2020, containing details on the Tax and Duty Manual "Guidelines for VAT Registration". The manual has been updated to reflect system changes and to improve readability. According to the eBrief, some sections have been moved as a result, and material previously published separately in the manual "Mandatory e-Filing Notification for New VAT Registrations" and in the appendix to the "Guidelines for Registration of Taxpayers" (TDM 38-01-03e) has been consolidated in this manual. There are no substantive changes to the registration process for taxpayers or agents. Revenue also issued eBrief 184/2020, dealing with cancellation of registrations.

UK

Reverse charge: construction

HMRC is introducing a domestic reverse charge for construction services, but Revenue and Customs Brief 7 (2020) outlines that the implementation date has been delayed to 1 March 2021 (from 1 October 2020) due to the Covid-19 pandemic. HMRC also provided technical guidance on how the new domestic reverse charge affects businesses and how it should be used and accounted for.

Import VAT for non-owners

Revenue and Customs Brief 15 (2020), explaining the outcome of a policy review, provides information for non-owners who have reclaimed import VAT on goods imported to the UK, and for advisers or agents dealing with businesses importing goods to the UK. In particular, it covers reclaiming the correct input VAT for agents, customs warehousing, goods temporarily imported for repairs, goods imported for onward leasing, customs special procedures and postponed VAT accounting, which UK VAT-registered businesses will be able to use from 1 January 2021.

Trading with the EU after 1 January

On 14 September 2020 HMRC published the text of a guidance letter sent to VAT-registered businesses in the United Kingdom that are trading with the European Union or the rest of the world, which highlights the things that they should pay attention to in order to be able to continue trading with the EU from 1 January 2021.

EU

e-Commerce

The EU provided detailed guidance on the new VAT e-commerce rules on 2 October 2020. The main changes consist of extending the simplified VAT registration and reporting regime (one-stop shop, or OSS) to all cross-border business-to-consumer supplies of goods and services and implementing a VAT reporting and payment liability for businesses operating online marketplaces. These changes are due to come into effect on 1 July 2021. The implementation date was moved from 1 January 2021 due to Covid-19. (See also article by Dermot Donegan, "Q&A: VAT and the eCommerce Package", in this issue.)