Scope of VAT grouping: HMRC consultation

Indirect Tax

01 February 2017

HMRC published a consultation document on the subject of VAT groups on 5 December 2016. The deadline for responses is 27 February 2017. We would like to hear your views.

What is a VAT group?

The idea behind a VAT group (or single taxable entity as it is known in EU law) is that two or more persons can be treated as a single entity for VAT purposes. There are two objectives behind this; the first being administrative simplicity, and the second to counter avoidance from artificial splitting of businesses.

In the UK we think of VAT groups only in terms of groups of companies, and in fact the UK rules currently only allow incorporated entities to form a VAT group. However, the UK has made use of the wider EU single taxable person principle in other areas such as to prevent avoidance through business splitting (VATA 1994, Sch1, para 1A and 2), to treat partners in a partnership as a single taxable entity (VATA 1994, s45), and also to treat associations as a taxable body (VATA 1994, s46(3)).

To be treated as a single taxable entity, the EU legislation says that the persons must be closely bound by financial, economic and organisational links (Principal VAT Directive, Article 11). In the UK we use the rules found in the Companies Act to determine the eligibility of companies to join a group. What the UK has historically done is to treat control as a proxy for the three EU requirements, except that it has recognised that control is not always a valid test. For instance, to counter certain abuses, it requires other tests to be applied (see the Value Added Tax (Groups: Eligibility) Order SI 2004/1931 as an example).

Thus, the current rule may be summarised as if there is control there is a presumption of the three criteria being met unless the contrary rules provide otherwise.

The consultation

HMRC accept that, following the cases of *Larentia* (C-108/14) and *Minerva and Marenave* (C-109/14), a Member State may not restrict VAT grouping to those entities which have legal personality (for example incorporated companies), unless it is justified by the prevention of abusive practices, tax evasion or avoidance. Therefore, VAT grouping could be extended to natural and other non-legal persons.

This would mean, for example, that a sole trader could also VAT group with a company which he owns, or that an unincorporated charity could VAT group with its trading subsidiary. The possibilities are considerable.

The difficulty lies, therefore, in how to decide how the three criteria (financial, economic and organisational links) are met. HMRC are consulting upon the eligibility criteria, and we would like to hear from members about this. For example, could the criteria be based on the factors that create a partnership? A partnership comprises persons carrying on business together by agreement.

The consultation is also seeking views on the impact of the changes introduced by the UK following the *Skandia* (C-7/13) judgment, and whether there are any other CJEU decisions that have had a financial or operational impact on UK VAT groups.

Finally, the consultation seeks views on the interaction of the VAT cost sharing exemption (VATA 1994 Sch 9, Group 16) with VAT group treatment, particularly in the light of widening the eligibility for VAT grouping. Cost sharing is a particularly important issue because of the increasing moves towards the pooling of resources in the economy, yet the exemption is very tightly drawn, based on EU legislation over 40 years old. We would like to hear what thoughts you have about any business model designed to share resources.

The consultation document can be found at on the GOV.UK website. Please send any comments to us by 13 February 2017, or direct to HMRC by 27 February 2017.