VPG submission on consultation on OECD Consolidated Guidelines

The VAT Practitioners Group (VPG) is grateful for the opportunity to contribute to the consultation on OECD Consolidated Guidelines. The VPG is representative of the majority of VAT practitioners in the UK. The response is based on the input from the members that have contributed to the consultation response. Where there is a divergence of interest this has been made clear in the text.

The VPG membership is drawn from over 400 members covering professions such as:

- Accountants;
- Barristers;
- Solicitors;
- Certain members of International firms;
- Chartered Tax Advisers;
- Industry;
- Insurance;
- Members of law firms;
- Queens Counsel;
- Sole traders; and
- Trade and finance.

The VPG's comments

The comments in this response to the consultation are restricted in the main to paragraphs 3.1 to 3.107.

Whilst the VPG welcomes the aim of these guidelines it considers that as they are currently drafted they are unlikely to be fully adopted by tax authorities. There are some areas where the guidelines appear ambiguous which make it more unlikely that tax authorities will implement them.

One of the main objectives of the guidelines appears to be the avoidance of double or non taxation of transactions, yet the guidelines seem to be too simplistic. This is likely to result in the failure to meet this aim.

In some cases the guidelines appear to create confusion by using different phrases to mean the same thing. In particular we refer to Annex 2, page 62, in the fourth paragraph reference is made to a "decision tree" and four paragraphs later the phrase "allocation key table" is used. It is unclear whether these are meant to refer to the same thing which would appear to be the best interpretation rather than different items.

Supplies within legal entities

Guideline 3.5

In those cases where the services are used by one or more establishments other than the establishment that entered into the business agreement, the taxing rights are allocated in two steps. In the first step, taxing rights are allocated to the jurisdiction where the customer establishment that enters into the business agreement is located. In the second step, taxing rights are allocated to the jurisdiction where the customer establishment that uses the service or intangible under a recharge arrangement is located.

There is a concern that if international transfers within legal entities are treated as supplies for VAT purposes, there will be additional administrative burdens, costs and anomalies created.

For example, if a business has an overseas branch that employs staff who are paid by the head office in another country, the wages of the staff employed in the overseas branch would become subject of VAT in the country of the head office. The overseas branch would be supplying services to the head office equivalent to the value of the overseas wages being paid (plus any other costs incurred by the overseas branch), which would become subject to the reverse charge in the country of the head office. If the business concerned was partially exempt, it would add a real cost to the business.

In effect, the head office would be paying VAT on the wages of its overseas employees, but not on the employees in its own country. This would discourage businesses from setting up overseas branches. The same principle can also apply to overseas subsidiaries. This is illustrated by the example in Annex 2.

Holding companies

It is a consistently stated principle of VAT that it is not designed or intended to be a burden on business and should only represent a cost at the final stage of consumption. We are of the view that the current approach within the EU to VAT incurred by holding companies can often result in a VAT cost burden which is not consistent with this stated principle of neutrality.

The particular problem arises where a holding company, often a special purpose company, is created to acquire the share capital of a trading company or group of companies. The reasons for doing this are commercial rather than tax-related and are generally concerned with risk management. The costs of the acquisition will be borne by the holding company and most if not all of these costs will incur VAT.

Holding companies which are non-trading entities thus suffer VAT as a cost of the resulting business in a way which does not represent the final stage of consumption. Holding companies which have trading activities, e.g. management services, routinely face resistance from domestic tax authorities when they seek to reclaim VAT on acquisition costs. This is clearly evidenced by the amount of litigation which has been pursued by taxpayers and defended by tax authorities as far as the Court of Justice of the EU.

We believe it would assist business generally for this aspect of VAT legislation to be reviewed and revised in order to provide a clear route by which the VAT cost burden on holding companies can be removed. The general options for consideration to revise the law could include the following:

- specific VAT reliefs for services provided to holding companies in connection with acquisitions of trading companies; or
- legislating to establish as a principle the nexus between such costs and the activities of the business being acquired such that the VAT can be reclaimed in accordance with the normal provisions of the law as they apply to the trading entity/group
- extending, where adopted, VAT grouping provisions to allow VAT incurred by holding companies on acquisition costs to be treated as recoverable by a VAT group which includes as its members the holding company and the trading company/group which it has acquired.
- create a scheme to allow remission of VAT incurred by holding companies on specified acquisition costs

Adopting such measures would uphold the principle of a nil burden of VAT on business and would also serve to reduce the level of litigation by establishing clearer VAT laws.

Conclusion

The guidelines need to be more specific in the guidance given to help tax authorities to implement them in a consistent manner. If tax authorities have too much leeway in implementing the

guidelines there are likely to be different applications of them leading to anomalies in tax treatment.

VAT Practitioners Group

May 2013