

FTT affirms HMRC's refusal of VAT refund under Thirteenth VAT Directive (1/24/17)

On 20 April 2017 the First-tier Tribunal (FTT) issued a ruling in JDI International Leasing Ltd vs HM Revenue and Customs. This case involves a claim by JDI International Leasing Ltd for VAT incurred in the UK when it acquired specialised tools for use on oilfields in the UK. JDI International Leasing Ltd ("JDI") is a company established in the Cayman Islands and has no fixed establishment in the UK. JDI wanted to recover the VAT under the Thirteenth VAT Directive (Council Directive 86/560/EEC) and made a claim under the VAT Act. HMRC refused the claim on the grounds that JDI made no use of the tools for an economic activity.

Background

JDI is a trader established outside the EU and a member of the Baker Hughes group of companies. JDI leased and then bought tools from a UK VAT-registered trader and was charged VAT on those transactions. JDI then leased the tools to Baker Hughes Nederland BV, a trader established in the Netherlands, for no consideration. JDI also sells spare parts for the tools, for which it makes a charge. JDI wanted to recover the VAT under the Thirteenth VAT Directive and made a claim. HMRC refused the claim and JDI appealed HMRC's decision to the FTT.

The question the FTT had to consider was whether the VAT charged on the supply of the tools to JDI would have been JDI's input tax had JDI been a taxable person in the UK. The burden of proof lay with JDI, and so it had to show the tools were used for an economic activity.

The FTT considered recent cases concerned with determining when a direct and immediate link could be considered to exist with either the company's particular transactions or business activities in general. To this end the FTT looked at CJEU Sveda (case C-126/14) and Royal Courts of Justice Associated Newspapers Ltd (case [2017] EWCA Civ 54).

The Sveda case focused on a link between the costs of installing a path on Sveda's premises that was free for anyone to use and the supplies Sveda made on those premises, such as sales of gifts and refreshments.

The Associated Newspapers Ltd case focused on a link between retail vouchers Associated Newspapers Ltd bought to give to participants in a business promotion scheme and the company's business activities in general.

In both cases a sufficient link was found to allow the company to recover input VAT.

It was accepted that JDI has an economic activity in selling spare parts for the tools and at the same time no economic activity in leasing the tools for no consideration. The FTT found there was no obvious link between JDI's acquisition of the tools and sale of spare parts. There would need to be a link for the input VAT to be recoverable. Although there is no obvious link, the FTT considered that there is perhaps a link and went on to examine whether this was the case. While it is possible to find an objective link between the acquisition of the tools and the sale of spare parts because JDI is the only source of the spare parts,

there is a weakness. This weakness arises from JDI's failure to require that the tools be used frequently, to help increase sales of spare parts, in the lease with Baker Hughes Nederland BV. The link is further weakened by allowing the tools to be used on a call-off basis. There being no charge for the lease, Baker Hughes Nederland BV was under no pressure to use the tools, as there was no need to generate enough income to at least pay the rental charge. The FTT thus concluded that JDI had failed to show that the goods had been used for making taxable supplies.

The ruling

Having examined the economic activity, the FTT found that there was no evidence that JDI was acting as a taxable person when it acquired the tools. Accordingly, the FTT found that JDI had no right to recover the VAT.

In summary, we would point out that under CJEU case law, a taxable person must satisfy two tests to qualify for recovery of input VAT incurred on supplies of goods or services. Firstly, the taxable person must be acting as such at the time of receiving those supplies. Secondly, the taxable person must use the goods or services for making taxable supplies. Both tests are objective in the sense that they must be confirmed by objective evidence and do not depend on the subjective intentions of the taxpayers.