

## Simplifying the VAT Land Exemption - call for evidence

### Response by the Chartered Institute of Taxation

#### 1 Executive Summary

- 1.1 The Chartered Institute of Taxation (CIOT) is the leading professional body in the UK for advisers dealing with all aspects of taxation. We are a charity and our primary purpose is to promote education in taxation with a key aim of achieving a more efficient and less complex tax system for all. We draw on the experience of our 19,000 members, and extensive volunteer network, in providing our response.
- 1.2 We are pleased to summarise our main comments below, before moving on to address each of the questions in turn.
- 1.3 The CIOT would be happy to meet with HMRC to discuss points raised in this submission or to discuss other examples of simplifying of the VAT land exemption or simplifications for the land and property sector outside the VAT exemption.
- 1.4 The CIOT would like any changes to the VAT rules for land and property to be considered from a wider social policy and green taxation policy perspective (see paragraphs 3.3 and 3.4).
- 1.5 The feedback we received from members contributing to this submission indicated that for the majority of land and property transactions, the VAT position is clear and/or administratively straightforward, and that a major overhaul of the VAT rules for land and property would create additional complexity for taxpayers and hence is not supported at this time.
- 1.6 Discreet areas of complexity for the VAT rules for land and property supplies were identified and would benefit from further focus. The two main areas are legislative definitions and the option to tax.
- 1.7 A major area for focus is to identify where there are areas of complexity arising from definitions in English land law, Schedule 9 to the VAT Act 1994 and the inherited definitions from the EU's Article 135(1)(l) of the Principal VAT Directive. The definitions for the UK's 'right over land' and the EU's 'leasing or letting of immovable property' cause complexity.

- 1.8 Ideas for simplification of the administration and operation of the option to tax system have already been made in the Office for Tax Simplification's VAT report. These points are supported by the CIOT and should continue to be focus for HMRC. The option to tax position also impacts the transfer of a going concern provisions and the capital goods scheme, which are both highlighted in this submission.

## **2 About us**

- 2.1 The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. Our comments and recommendations on tax issues are made solely in order to achieve this aim; we are a non-party-political organisation.
- 2.2 The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.
- 2.3 The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries.
- 2.4 Our members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.

## **3 Introduction**

- 3.1 We are pleased to set out our comments in relation to HM Revenue and Customs' Call for Evidence: Simplifying the Land Exemption.
- 3.2 Our stated objectives for the tax system include:
- A legislative process that translates policy intentions into statute accurately and effectively, without unintended consequences.
  - Greater simplicity and clarity, so people can understand how much tax they should be paying and why.
  - Greater certainty, so businesses and individuals can plan ahead with confidence.
  - A fair balance between the powers of tax collectors and the rights of taxpayers (both represented and unrepresented).
  - Responsive and competent tax administration, with a minimum of bureaucracy.
- 3.3 The CIOT would like the starting point for any potential simplifications to the land exemption, or indeed any zero/reduced rated taxable supplies in the property sector that subsequently come within the scope of this consultation process, to be considered within the bigger picture of the government's social policy for taxation.

For example, the current social policy allows the zero-rating for the first sale of a newly constructed dwelling, which provides a clear VAT liability position for very high value dwellings, yet the VAT liability position can be complex for certain small properties, such as newly constructed artist live/work studios.

- 3.4 The CIOT would also like to see any potential simplifications or changes to the VAT rules for land and property to be considered from a green taxation policy perspective, ensuring that where applicable, potential changes are considered in the light of the strategic policy laid out at Point 7 'Greener Buildings' (or other policy points where applicable) of the government's '[Ten Point Plan for a Green Industrial Revolution](#)'.<sup>1</sup>

## 4 Chapter 2: VAT rules for land and property and drivers for simplification

### 4.1 **Question 1: What is your experience of the VAT rules on land and property?**

- 4.2 The feedback received for this call for evidence was drawn mainly from a number of CIOT members who are highly experienced in VAT and/or tax specialists in the property sector, and who are members of the CIOT's Indirect Tax and/or Property Committees ('the feedback group') so they have extensive experience in dealing with VAT for land and property transactions.

- 4.3 It was their view that for the majority of land and property transactions (well over 90% was suggested), the VAT position is either clear or is fairly straightforward to administer for taxpayers and their advisers, which is positive. This indicated that although there are areas where simplification is desirable and areas where the VAT guidance could be improved, there was not an appetite for any major overhauls to the current position, with a view that existing complexity could end up being replaced with new complexity.

- 4.4 However, for land and property transactions where the VAT liability position is not as clear, where the supply does not fall neatly within the current definitions in legislation or guidance, the position can become complex and result in disputes with HMRC, potentially escalating to the tribunal resulting in administrative and financial burdens for the taxpayer. The feedback group considered various circumstances where simplification could be achieved as set out in this submission.

### 4.5 **Question 2: Are there any supplies that are particularly difficult to establish the correct liability for, leading to financial and administrative burdens?**

- 4.6 Examples discussed included:

- a. The most common 'difficult' issue discussed in the feedback group was establishing the correct VAT liability where it wasn't clear whether the supply was a right over land (VAT exempt), the supply of facilities (taxable standard rated supply) or the supply of something else (VAT liability to be identified). An example of this is sports lettings – for taxpayers such as local authorities, universities, schools and colleges, there can be overlapping exemptions to consider: property, sport, and if applicable, education so the position can be complex. There was feedback that HMRC had tried to apply the rules for sports lettings to other types of supply e.g. use of theatrical facilities. For a licence to occupy a taxpayer would still receive lighting and heating services in the room hire.

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[https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/936567/10\\_POINT\\_PLAN\\_BOOKLET.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/936567/10_POINT_PLAN_BOOKLET.pdf)

- b. Issues arising from principles established in the *Sinclair Collis* case (C-275/01), that is, where the VAT position is not clear from the interpretation of Group 1, Schedule 9 to the VAT Act 1994, the European legislation definition of 'leasing or letting of immovable property' (Article 135(1)(l) of the Principal VAT Directive) including the 'passive provision of space' must be considered. It was noted that the right over land was considered in HMRC's 'landlord books' up until the 1980s. It was further noted that the UK interpretation of 'right over land' was much narrower than in some EU countries, e.g. Italy and Spain.
- c. Examples of difficulties with the *Sinclair Collis* position and UK land law include: The grant of a right to a third party to site equipment on the grantor's land, eg an electric vehicle charging point or a seaside telescope or a bus shelter, each of which have caused dispute between HMRC and local authorities. As we note in (b) above, '*Sinclair Collis*' is cited to argue that such grants are VATable, not being a right to occupy land; but '*Sinclair Collis*' was decided on the basis that no exclusive right to occupy a specific site for a defined period was granted to the vending machine operator, not that the right to site a vending machine cannot be a licence to occupy land. Under UK land law, if an object - such as a charging point or telescope or bus shelter - is affixed to the land it becomes the property of the landowner so a licence must be granted to the object's 'owner' in order to facilitate the continued use of it, which would be a licence to occupy the land on which the object is sited. A review of this area of the VAT and property rules and improved guidance appears to be a priority area.
- d. In addition to (b) and (c), where somebody trades from a vehicle, there can be difficulty identifying whether they are being supplied with parking, a right over land or the grant of facilities.
- e. There can be a misunderstanding by certain taxpayers who have not taken VAT advice, that when purchasing an opted property, the seller's option to tax ('OTT') is also binding on any subsequent supplies of the land or property that they make. This issue was raised in the Office of Tax Simplification's 2017 VAT report ('OTS report') at paragraph 6.3.
- f. Disapplication of the option to tax ('OTT') – In the OTS report at paragraph 6.4, it highlights that '*the anti-avoidance legislation is complex, circular in places, catches businesses not seeking to avoid VAT, results in creative planning*'; the feedback group concurred that the legislation remains complex though comments were made that HMRC's guidance in gov.uk and VAT manuals was easier to follow and was clearer. Whilst this is positive feedback about guidance, this should not distract from the legislation itself being difficult to use to arrive at conclusions, as it is the legislation that should be clear.
- g. The rules where permission is required for the option to tax is also complicated. It was noted that in some EU countries there is no requirement for taxpayers to notify the tax authorities about the option to tax at all; it is all dealt with by the taxpayer.
- h. Transfer of a going concern issues ('TOGC') where a property is included in the transfer. Complexity and/or errors can arise in scenarios such as the taxpayer and HMRC being in dispute over the change of business being of the same kind or not. Errors also occur with the option to tax administration requirements for the transfer, so process simplifications would assist.
- i. Exclusions from exceptions can cause complexity.
- j. The publication for Revenue & Customs Brief 12/20 has created complexity for the VAT liability of dilapidations; although HMRC allow the treatment to be outside of the scope as compensation currently, taxpayers are entering into leases that will end long after the current HMRC review has published its conclusions, so the eventual VAT liability remains uncertain, though we appreciate that this scenario should be clarified by HMRC fairly soon.

- k. Call options, rights to light – although these are supplies related to land and property, should they be treated as supplies of land or property themselves? It was noted that these are long standing questions under discussion at the Land & Property Liaison Group.
- 4.7 Often in the examples presented, the matter of the VAT liability may not in itself be an issue, but the need for certainty for the taxpayer is.
- 4.8 **Question 3 - Do you think that the land and property VAT rules require simplification?**
- 4.9 The CIOT's opinion is that changing the land and property VAT rules en masse would be too complex for taxpayers, potentially replacing complexity with more complexity. Any radical solutions are likely to still have borderline issues but these would then have to be dealt with without the benefit of decades of case law to assist. However, the simplification of VAT rules for land and property in discreet problem areas would be sensible.
- 4.10 The current definition in Schedule 9 to the VATA94 relies on English land law which provides a key reference point for VAT analysis. The EU legislation's definition on of letting and leasing produces complexity interacting with, or taking direct effect over, the VATA94. The CIOT would like the position reviewed and simplified where possible to increase clarity and certainty for taxpayers and advisers.
- 4.11 There appears to be scope for simplification around the administration of, and the anti-avoidance rules for, the option to tax. We support the recommendations already submitted by the Office of Tax Simplification's (OTS) VAT report.

## 5 Chapter 3: Ideas for simplification

- 5.1 **Question 4 - What are your views on the options presented in the OTS report outlined above? Do you agree with their assessment?**
- 5.2 The OTS considered and rejected the following suggestions:
- a. All transactions become exempt (includes new residential)
  - b. All transactions become reduced rate (includes new residential)
  - c. All commercial transactions become standard rated (with ability to opt to exempt).
- 5.3 The CIOT agrees with the OTS VAT report's views and the reasons for the rejection of the hypothetical changes to the VAT rules for land and property transactions.
- 5.4 **Question 5 - What are the advantages and disadvantages of making all minor and short-term interests in land and property subject to VAT?**
- 5.5 It is difficult to encompass all property scenarios into one fixed rule; a short-term let of domestic accommodation using an unoccupied holiday home in the off-peak season could be measurable in days or months (though exceeding the time period deemed as holiday accommodation), whereas a minor interest of a lease of a newly constructed residential property during a slump in the property market prior to the grant of a major interest may be measured in months or years.
- 5.6 Whilst in principle this could provide clarity and simplification of the VAT liability, there would still be a requirement for exceptions where the short-term let falls within the government's social policy for taxation.

We would anticipate that minor and short-term supplies of property that have a residential or social policy (non-hospitality sector domestic accommodation, relevant residential purposes, relevant charitable purposes) purpose would still need to be excepted, increasing complexity and the question would need to be asked whether the position was simplified compared to pre-changes.

- 5.7 It should be noted that due to the COVID pandemic, taxpayers have experienced circumstances where short-term land and property arrangements have had to be made, either by granting or obtaining a lease, and under the current rules there has been flexibility around whether short term interests are taxable or exempt. We are still currently in a continued period of uncertainty with the pandemic and the CIOT would not like to see major changes to these rules, at least in the short term.
- 5.8 ***Question 6 - How should a minor and short-term interest be defined?***
- 5.9 The definition of a minor and short-term interest should be based on clearly identifiable factors that are easily understood by persons that are not tax experts. As stated in paragraph 5.5 above, different minor and short-term interests may be different for each type of supply of land or property (which could increase complexity and scope for errors) so it is not yet certain whether this would result in simplification or not. However, a basis for the definition could be based on one/both of the following factors:
- a) Time: number of days, months, or years – this would appear to be the clearest indicator of ‘short-term’
  - b) Floorspace: a maximum percentage rate of the overall floorspace – this may be required on occasion to define ‘minor interest’.
- 5.10 It should be noted that there could still be complexity arising for taxpayers who go on to extend the time period or increase the floorspace during the initial minor interest agreement term.
- 5.11 ***Question 7 - What are your views on the option to make supplies of land and property subject to VAT apart from certain specified exceptions?***
- 5.12 The feedback group discussed the position in Cyprus, which in c.2017, made all property transactions subject to VAT, unless the taxpayer proactively chooses ‘not to tax’. It was understood that this had significantly reduced VAT enquiries on land and property matters. It was noted however that the VAT registration threshold of €15,600 in a 12-month period is significantly lower than the UK, so the position may be simplified for very small businesses whereas in the UK these businesses benefit from VAT simplification by means of the high VAT registration threshold. HMRC may wish to engage with its counterparts in Cyprus to develop further understanding of the effects of the changes. It should be noted that there could be other differences in the tax systems not considered that could impact the UK position, such as Stamp Duty Land Tax.
- 5.13 Questions were also raised on the position for supplies such as renewals, break clauses; HMRC would have to undertake significant work in considering the impact of the hypothetical change for many types of land and property supply.
- 5.14 Any change would require a transition period, which was described as ‘from complex to complex’. Questions were raised on the impact on all of the existing leases that could be over 900 years? Planning for a transition period could also give rise to unintended consequences and loopholes.
- 5.15 In conclusion, the consensus in the feedback group was that a wholesale change is likely to create more problems than it solves.

- 5.16 **Question 8 - Which particular supplies of land and property should continue to be exempt from VAT if this option were to be considered further?**
- 5.17 Supplies subject to the government's social policies should continue to be exempt, including residential accommodation and properties with a relevant residential or relevant charitable purpose.
- 5.18 **Question 9 - Are there any supplies that should be subject to VAT that are currently exempt or vice versa?**
- 5.19 No suggestions were made.
- 5.20 **Question 10 - What are your views of linking the VAT liability of interests in land to those recorded in Land Registers in England, Scotland, Wales and Northern Ireland? and Question 11 - What are the potential advantages and disadvantages of such an approach?**
- 5.21 The feedback group discussed examples of Land Registry complications for large and historic portfolios:
- a. Land Registry records are more accurate, though not for all transactions types. There are exceptions which would create uncertainty.
  - b. Land Registry freeholds and leases may have different land registry numbers, potentially causing uncertainty.
  - c. The VAT rules for leases are different even within the UK which could cause complications with Land Registry records
  - d. The OTS VAT report at paragraph 6.13 raises the issue with confidentiality between HMRC and the Land Registry, and the limited ability to share information and that this is prescribed in legislation, so this issue would still need to be overcome.
- 5.22 **Question 12 - Do you have any other suggestions on how the land and property VAT rules could be simplified?**
- 5.23 We have received various suggestions from the feedback group as follows:
- 5.24 Following the Grenfell tragedy, there is a new property tax in development, the Residential Property Developer Tax, that will recover the costs of safe replacement cladding from the largest residential property developers over a ten-year period. The new tax is due to come into force in 2022. The CIOT would like HMRC to review the interaction of RPDT and VAT, and if any unintended consequences arise and the complications for taxpayers. VAT guidance needs to be available to provide clarity for taxpayers and their advisers, and it must be available with a lead in time that allows taxpayers to make appropriate arrangements prior to the RPDT's launch. The CIOT would be happy to contribute to a VAT working group with an RPDT focus, should this be considered.
- 5.25 Consider reducing the period for the disapplication of the option to tax from 20 to 10 years, to align with Capital Goods Scheme 10-year rule. Currently if a fully taxable business purchases an opted property and it uses that property for its own fully taxable use for ten years, and no adjustments are required under the CGS, it then has the choice whether to sell or lease the property as VAT exempt or it has the choice to opt to tax. It isn't clear why taxpayers who have opted to tax don't have the same choice open to them after a ten-year period.
- 5.26 Rebasing Stamp Duty Land Tax (SDLT) to exclude VAT as part of the calculation would remove the post-transaction difficulties where a disposal of a property has been included in the transfer of a going concern (and hence treated as VAT free), which HMRC subsequently reject resulting in VAT becoming due which in

turn means further administration and costs for the increased SDLT position. It is noted that this would come with a cost to the exchequer in decreased SDLT revenues.

- 5.27 We would like to see further consultation on the simplification of VAT for land and property outside of just the land exemption. For example, for supplies of, or connected to, residential properties, depending on the supply the VAT liability can be exempt, zero-rated, reduced rated or standard rated.
- 5.28 We received a suggestion that there should be an increase in the number of characters allowed for business names in HMRC's option to tax registration system, as the current limitation on the number of characters causes confusion and issues for corporate groups that have companies with similar names, but where the first few words are identical.
- 5.29 ***Question 13 - Would you prefer to keep the VAT rules on land and property as they are?***
- 5.30 The CIOT would broadly keep the current VAT rules on land and property with specific areas and exceptions highlighted from the responses to other questions. In the examples provided of areas of uncertainty, this highlights the need for HMRC to improve the clarity of the legislation and provide clearer guidance so that taxpayers and advisers have greater certainty that the VAT liability position they apply to the supply is correct.
- 5.31 We have in the past suggested to the non-statutory clearances team that where HMRC have been able to provide rulings to taxpayers as the guidance did not extend to the circumstances under question, that on each occasion, the guidance should be subsequently updated to incorporate the principles of the non-statutory ruling so that the question would not need to be asked again by a different taxpayer. If not already done so, we suggest that this is always carried out where the question is for land and property issues. We would also like to see a similar responsibility to communicate with the guidance team (whether that be via GDS for gov.uk guidance or via HMRC policy for the VAT manuals content) rolled out to other HMRC departments that experience related land and property VAT queries, such as the option to tax team or the written enquiries team.

## **6 Acknowledgement of submission**

- 6.1 We would be grateful if you could acknowledge safe receipt of this submission, and ensure that the Chartered Institute of Taxation is included in the List of Respondents when any outcome of the consultation is published.

The Chartered Institute of Taxation

5 August 2021