

VAT alert

HMRC announces VAT changes for Cost Sharing Groups

March 2018

Summary

HMRC has announced important changes to the UK's VAT rules relating to the operation of cost sharing groups. The changes follow a number of recent judgments from the Court of Justice that have clarified how the VAT exemption for such groups is to be applied by Member States.

Revenue & Customs Brief 03/2018 sets out the details of the changes and VAT Information Sheet 02/2018 sets out HMRC's view on the impact of its change of policy.

It took the UK almost 35 years to enact the mandatory VAT exemption for cost sharing groups. The law came into force in July 2012 and, in essence, it entitles entities that make VAT exempt supplies to form a cost sharing group which, in turn, can exempt supplies of services to its constituent members.

A cost sharing group can provide a substantial VAT saving for member entities as, in most cases, the members are not entitled to reclaim VAT incurred on costs due to the exempt nature of their own particular activities.

Revenue & Customs Brief 03/2018 and Information Sheet 02/2018

Recent judgments issued by the Court of Justice of the European Union (CJEU), HMRC have clarified the circumstances in which the VAT exemption for cost sharing groups (CSG) can be applied.

The exemption introduced in 2012, allows businesses with VAT exempt activities to reduce VAT costs when they decide to work together to for example gain efficiencies. When the exemption was introduced, HMRC made it clear that there was uncertainty as to its scope and that their original approach could be modified based on future litigation. Following the judgment of the CJEU in the cases of DNB Banka AS (Case C-616/15) and Aviva S.A. (Case C-605/16), their policy is to be revised. The CJEU judgments surprisingly made it clear that the exemption is restricted to those entities whose supplies are exempt from VAT under the provisions of Article 132 of the VAT Directive. This Article exempts supplies of goods and services that are, or are deemed to be, activities in the public interest.. Unfortunately, banking and insurance activities are not included in this list and, as a result these entities are now precluded from forming CSG's.

With immediate effect, the UK's CSG exemption will, as a consequence, apply only to entities that operate in the postal services, education, health and welfare, trade union / professional bodies, sport, fund raising (by charities) and cultural services sectors. Housing associations although not in this list have been allowed to continue to use CSG's at least for the time being. In addition, HMRC will restrict membership to entities located in the UK and will strictly enforce the condition that recharges to members by the CSG must only be at cost.

Although the policy changes have immediate effect, HMRC has stated that, where entities have applied the existing published guidance correctly, they will be entitled to continue operating under that regime until the end of May 2018. HMRC have further warned that they may introduce further changes to restrict the types of services that can be exempted by the CSG.

Comment – HMRC' will welcome the judgments of the CJEU as it enables them to greatly restrict the scope of the exemption. The announcement of a change of policy was expected albeit, perhaps, not as speedily as has happened. All members of an existing CSG will need to review its operation and consider whether they are affected by the changes.

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