ICAS comments on the
Value Added Tax (Amendment) (No) Regulations 2015 –
deductible VAT relating to foreign branches

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About ICAS

The Institute of Chartered Accountants of Scotland ("ICAS") is the oldest professional body of accountants. We represent around 19,000 members who advise and lead businesses. Around half our members are based in Scotland, the other half work in the rest of the UK and in almost 100 countries around the world. Nearly two thirds of our members work in business, whilst a third work in accountancy practices. ICAS members play leading roles in around 80% of FTSE 100 companies. ICAS is also a public interest body.

We wish to comment on the draft regulations issued by HMRC. We have concerns that the scope of the changes proposed go further than the judgement in the Credit Lyonnais case at the Court of Justice of the European Union. The changes are due to be introduced in the UK from 1 August 2015.

The draft regulations note that these are intended to:

- Simplify the tax system and make it fairer by mitigating the risk that some partly exempt businesses could artificially increase the amount of input tax that they deduct; and
- Implement the 2013 decision of the Court of Justice of the European Union

It is our understanding that the changes will require affected businesses to adjust the calculation for partial exemption they prepare under Regulations 101, 102(2) and 103 of VAT Regulations 1995 (2518). The tax information and impact note makes clear that the measures are intended to mean that deduction of input tax used to support activities of the foreign establishments of a business can only be calculated by reference to supplies made by the UK establishments of that business. We believe that this goes beyond the principles established by the Credit Lyonnais case and is not supported by EU law.

The Credit Lyonnais case itself supports the position that branch turnover should not be included in the partial exemption calculation, but it does not support the view that input VAT used to support the activities of the foreign establishments should be restricted in line with the activities of the UK establishment – as outlined in the adjustments to regulation 103. The case has no concrete suggestions on how to deal with input tax allocated to a foreign establishment pot.

The amendments to regulation 103 have the effect that a business is unable to deduct VAT on overheads incurred in the UK where these are attributable to supplies made by non-UK branches. In our view this change would conflict with the principle of neutrality which ensures the right to VAT deduction – article 169A of the Principal VAT Directive. It would have the effect that the head office of an overseas firm that manages its European branches from the UK would not be able to deduct any of the VAT it incurs on managing those foreign branches in the UK.

We are aware that the Chartered Institute of Tax have also raised issues on the draft regulations and suggested that there should be a consultation and meeting with professional bodies and affected businesses before the legislation is finalised. We would endorse this approach.