

### **VAT recovery & Change of intention Community Housing Association Ltd**

*4 Eyes Ltd recently represented a registered social landlord(RSL) at the VAT tribunal in relation to an appeal for a repayment, under regulation 109 of the General VAT Regulations. The contested repayment was based upon the change of use provisions.*

The RSL in question is actively engaged in the construction of new social housing. The dispute related to input VAT recovery on costs incurred on a number of a buildings which were ultimately to be used for exempt purposes. (Ordinarily there would be no input VAT recovery possible).

In February 2006, CHA set up a wholly-owned subsidiary, CHA Ventures, to commission the design and development of housing and to appoint construction contractors. From this point, all collateral warranties (i.e. separate contracts, designed to establish unequivocal ownership in the event of taking a suit) were in CHA Venture's name. All future invoices were to be addressed to CHA Ventures and any invoices for works underway but not complete, were to be reissued to CHA Ventures.

Where supplies had previously been made to CHA but the remainder of the development was transferred to CHA Ventures, prior to completion, CHA onwards billed the value of all supplies that it had received to-date to CHA Ventures. (It should be noted that with effect from the inception of CHA Ventures, CHA ceased to have its own development function. Henceforth, this was transferred in its entirety to CHA Ventures). In onwards billing supplies already received, CHA was seeking to transfer all responsibility for the development to CHA Ventures. CHA subsequently argued that this recharge effectively changed the use of the costs where previously the intention had been to generate exempt income from rental houses and now it had used the supplies to make a taxable recharge to CHA Ventures. HMRC rejected the ensuing VAT reclaim and the question for the Tribunal was whether CHA was making an onward taxable supply of the professional services which had previously been supplied to it and therefore whether it could now attribute the input tax to a taxable supply on which it could seek to recover VAT?

In their arguments, HMRC said that for costs incurred prior to February 2006 (prior to CHA Venture's establishment), there was no new supply and CHA's intention was always to use the costs for an exempt supply. It was in their view irrelevant that CHA had made an onwards supply of the services on which it had charged and accounted for VAT. Having made the initial decision to use the supplies for exempt business purposes, it could not change this by simply onwards billing.

Once CHA Ventures was set-up, it became liable for the cost of the services and thus there was no 'onward supply' by CHA. Even if there was, the purpose of the supply was not altered, regardless of how the costs were shifted about. Effectively, because CHA continued to have substantive interest in each site, it was the main buyer and user of the services. HMRC relied on the earlier case of Pierhead Housing Associations Ltd which dealt with a similar scenario, asserting that the idea that there was a transfer of a supply was contrary to the reality of what happened (i.e. ultimately, CHA would use the buildings for the original exempt use).

The Tribunal found in favour of HMRC.

This decision is subject to further appeal by CHA.

#### **Implications**

This is an example of HMRC disregarding a recharge for the purposes of a supply. It is also an interesting indication of how contracts and invoices influence HMRC's view on the true recipient of a supply.

It is important to note that HMRC expressly agreed the operation of CHA Ventures going forward and the fact that this would save all future irrecoverable VAT on the construction of social housing. 4 Eyes Ltd developed this VAT efficient arrangement in response to the needs of RSLs and strongly advises any developing RSL which has not yet implemented a similar arrangement to give it very serious consideration.

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