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SIMPLIFYING THE VAT LAND EXEMPTION

Response by Association of Taxation Technicians

1 Introduction

- 1.1 The Association of Taxation Technicians (ATT) is pleased to have the opportunity to respond to the HMRC call for evidence *Simplifying the VAT Land Exemption* ('the call for evidence') issued on 12 May 2021¹.
- 1.2 The primary charitable objective of the ATT is to promote education and the study of tax administration and practice. We place a strong emphasis on the practicalities of the tax system. Our work in this area draws heavily on the experience of our members who assist thousands of businesses and individuals to comply with their taxation obligations. This response is written with that background.
- 1.3 Overall, we do not believe that a radical overhaul of the VAT rules on land and property is required at this time. Whilst the rules are indeed complex, it is difficult to see how significant simplification can be made achieved once the requirement for specific exceptions (such as for residential property) is factored in. We therefore believe that effort should instead be focused on making the rules easier to apply in practice, for example by offering a publically accessible register of properties where an option to tax has been made (see 3.23 to 3.24 below).
- 1.4 We have set out our response to the specific questions posed by the call for evidence in Sections 2 and 3 below.
- 1.5 We would be pleased to discuss any aspect of this response further. Relevant contact details can be found in Section 4.

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

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

- 2.1 We agree that the land and property rules have increased in complexity over the years.
- 2.2 In our experience, it is usually the boundaries between tax rates or taxable and exempt transactions which create difficulties. Generally, the more boundaries, the more issues there are to resolve.

¹ <https://www.gov.uk/government/consultations/call-for-evidence-simplifying-the-vat-land-exemption>

2.3 This presents a challenge when it comes to simplification of the land and property rules, as whichever approach is taken it is unlikely that these boundary issues can be removed entirely. Many of the options set out in the call for evidence include reference to the need for exceptions to ensure certain interests remain taxable or exempt. Whilst such exceptions may well be necessary (for example to ensure VAT is not charged on residential accommodation), they will act to introduce new boundary issues and create complexity.

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

- 2.4 Areas of the land and property rules where our members have experienced particular difficulties include:
- Establishing the correct liability with zero rated construction work and land transactions.
 - Application of the 5% rate to renovations and alterations – in particular identifying whether or not the premises have not been lived in for at least two years where there is a change in ownership.
 - When a supply ceases to be a supply of land due to the provision of other services alongside it (for example room hire).
 - The boundary between supplying an exempt letting of land and the supply of accommodation in a hotel or similar - the decisions in cases on the subject have led to a distinction that relies in part on impression and how the property is presented.
- 2.5 One other common area of difficulty is in establishing liability when the land interest is only one of the elements that is being supplied. In these cases, the question arises as to whether the importance of those other elements is such that the supply becomes one of a ‘package’ of services rather than simply a supply of land. Members have observed that HMRC seem to regard the addition of anything at all (even a seemingly only minor element) as being sufficient to alter the nature of the supply from being one of purely an interest in land into something else. Clearly this is an issue that would remain, notwithstanding any simplification of the land-related legislation. However, further guidance on this area would be welcome.
- 2.6 A specific example of the difficulties posed in establishing liability is whether provision of five-a-side football pitches by a business that organises leagues can qualify for exemption. Here there appears to be a tension between EU legislation (which refers to leasing and letting of immovable property and would appear to restrict exemption) and UK legislation (which instead refers to interests in and rights over land etc.).

Question 3. Do you think that the land and property VAT rules require simplification? Please explain why.

- 2.7 We believe that the main benefit lies in making the land and property VAT rules more straightforward and easier to apply in practice, rather than an overhaul of the current regime.
- 2.8 Attempts to radically redesign the rules with the aim of simplification could actually result in further complexity. As set out at 2.3 above, it is difficult to change the rules without creating new boundary issues which taxpayers and their agents would be required to navigate.

3 Chapter 3: Ideas for simplification

Question 4: What are your views on the options presented in the OTS report outlined above? Do you agree with their assessment?

- 3.1 We discuss each of the three options proposed by the OTS in the following paragraphs 3.2 to 3.4. Overall, we feel that these options are not worth pursuing due to the extra costs and/or administrative burdens that would

be associated with them. We also believe that they are unlikely to deliver significant simplification once necessary exceptions (such as carving out residential property) are taken into account.

3.2 Option 1 - removing the ability to opt and making all relevant transactions exempt.

We agree that this would potentially be a simplification. However, it would lead to much higher costs for businesses due to the inability to recover input VAT. This could, in turn, reduce economic activity, particularly in the property construction and letting sectors.

3.3 Option 2 - Removing the option to tax and making all land and property taxable at a reduced rate.

Again, whilst we agree this option could be a simplification, it would introduce practical problems and additional costs for businesses and the public. For example, it may lead to increased numbers of businesses and individuals having to register for VAT. There are also concerns over how this would apply to the residential housing market. Whilst many smaller individual landlords may be below the VAT registration threshold, this would not be the case for larger landlords and social housing (for example).

3.4 Option 3 - Making all commercial land and property taxable at the standard rate with an option to exempt.

Whilst again this could be a simplification, we believe the idea of an 'option to exempt' it is not consistent with the basis of the VAT system being that transactions are taxable unless they are exempt. This option would also not remove the complexity of the current option to tax rules, but rather invert them in the form of a new 'option to exempt'. Finally, as noted in paragraph 3.1.2 of the call for evidence, there would also be significant practical issues for both HMRC and taxpayers of changing over from the existing system to any new system. .

Question 5: What are the advantages and disadvantages of making all minor and short-term interests in land and property subject to VAT?

3.5 Overall we believe there are potential advantages to exploring this approach.

3.6 As noted in the call for evidence, there are fifteen exceptions to the land exemption which are standard rated. Of these, seven relate to what we now commonly refer to as the hospitality and leisure industries. Briefly these are as follows:

- The right to take game or fish
- Accommodation in hotels etc.
- Holiday accommodation
- Pitches for caravans
- Pitches for tents
- Occupation of boxes etc. at sports, theatres etc.
- Facilities for playing sport

Whilst there may be some longer term lettings (e.g. fishing rights running for several months or years) amongst this group, most of the lettings by the hospitality and leisure industries are relatively short-term, or form a series of short-term lettings.

3.7 Another three exceptions which we would group together are as follows:

- Parking vehicles
- Storage, mooring or housing of aircraft, ships etc.
- Self-storage of goods.

This group is more of a mixed bag. More often than not parking is short-term, but may run to months or even years. On the other hand, the opposite can apply to moorings etc. and self-storage of goods, which are often medium to long term (though short-term is not uncommon).

- 3.8 Overall, our point is that of the fifteen exceptions to the land exemption there may be as many as ten which are always or often short-term. It appears feasible that, with careful drafting, these ten exceptions could be replaced by one exception which made short-term lettings standard rated. This would maintain the current position but streamline the legislation.
- 3.9 However, whilst we believe the legislation could be made more straightforward by making all short-term lettings taxable, there is a potential problem with residential lettings. These should remain exempt, and not be within the scope of any legislation which makes all short-term lettings taxable.
- 3.10 In summary, if the majority of short-term lettings were standard rated this should encompass all or most of the current exceptions applying to the hospitality and leisure industry (and perhaps some other sectors too). It would have the advantage of not identifying these exceptions by type, but instead by length of the letting or lease. This should be more easily understood and maintain the current range of standard rated land transactions. However, there would have to be an exception to ensure that residential lettings remain exempt.

Question 6: How should a minor and short-term interest be defined?

- 3.11 The practicality and relative advantages and disadvantages of making all short-term or minor interests in land taxable will depend heavily on how these terms are defined.
- 3.12 Our view is that any definition should be based on the length of the lease / letting agreement. This is something which is already familiar to taxpayers and advisers (for example, the status of the granting of a lease changes at 21 years from a service to goods).
- 3.13 We believe that more research should be undertaken to determine the optimum period of a short-term interest for these purposes.

Question 7: What are your views on the option to make supplies of land and property subject to VAT apart from certain specified exceptions?

- 3.14 Whilst making all supplies subject to VAT could deliver some measure of simplification, this is likely to be heavily diluted by the need for specific exceptions.
- 3.15 Each time a government creates a new exception from VAT or a category to which a different rate applies, it creates issues. There are always products or services which do not clearly fit into one category or another. Businesses are then expected to decide into which category the product or service falls and consider how this may affect the VAT to be charged and how much VAT may be reclaimed.
- 3.16 Introducing specific exceptions is therefore likely to create new boundary issues. Depending on the number needed, this could severely reduce the simplicity of such a proposal. At the extreme, we could end up with a system which is as complicated as that which we currently have.

- 3.17 There are also practical issues associated with such a change, in particular it could require increased numbers of businesses and individuals to register for VAT. Our concerns noted above at 3.3 above regarding how the second OTS option would apply to the residential housing market would also apply equally here.

Question 8: Which particular supplies of land and property should continue to be exempt from VAT if this option were to be considered further?

- 3.18 As noted elsewhere in this response, we believe residential property in particular would need to continue to be exempt from VAT.

Question 9: Are there any supplies that should be subject to VAT that are currently exempt or vice versa?

- 3.19 One suggestion from our members is that supplies of dwellings created by a conversion of a mixed use building should always be zero-rated, rather than the current situation where dwellings created may be supplied zero-rated or exempt depending on how the conversion has been carried out. The Upper Tribunal's decision in the *Languard* case² was a fairly recent example of the consequences of the current unsatisfactory situation. If the public policy is to encourage the creation of new housing then the current exemption in some cases is illogical, as it discourages developments or causes developments to be carried out in a way to achieve the best VAT outcome, which may not be the best use of the building. This is becoming more of an issue as more pubs and part-commercial buildings are being converted to dwellings.

- 3.20 One of our members has also highlighted a potential idiosyncrasy in Schedule 9 which causes hotels to be treated differently from other suppliers. The exception to the exemption in Group 1 item 1(d) includes:

“(d) the provision in an hotel, inn, boarding house or similar establishment of sleeping accommodation or of accommodation in rooms which are provided in conjunction with sleeping accommodation or for the purpose of a supply of catering.”

We understand the reference to hotels and similar in respect of sleeping accommodation (to distinguish these from residential lettings, we assume), but why are hotels singled out when it comes to rooms for catering? We are not aware that any of the other exceptions focus on the nature of the supplier rather than the nature of the supply in this way. Given that HMRC would often argue that a room supplied (by anyone) for the purpose of catering is likely to amount to a package of services anyway, it would arguably be fairer to all if the exception for a room supplied for the purpose of catering was listed as taxable irrespective of the identity of the supplier. That would be consistent with practice and would resolve a potential breach of fiscal neutrality.

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?

- 3.21 This may represent a simplification. However, as acknowledged at paragraph 3.4.5 in the call for evidence, any such approach is likely to need exceptions, which would detract from its inherent simplicity.

Question 11: What are the potential advantages and disadvantages of such an approach?

- 3.22 We agree that one advantage of this approach would be to provide greater certainty of the VAT liability of land transactions, by virtue of these being based on a publically accessible record.

² [HMRC v Languard Homes Ltd and DD & DM Macpherson v HMRC \[2017\] UKUT 307](#)

- 3.23 However, as noted above, the simplification introduced by this option may be limited by the number of exceptions needed.

Question 12: Do you have any other suggestions on how the land and property VAT rules could be simplified?

- 3.24 Paragraph 2.2.5 of the call for evidence highlights the uncertainty that can arise where businesses are unaware of whether a property has been opted to tax and has no facility to check.
- 3.25 As HMRC must be notified of every option to tax, they must already have records of all opted to tax properties. Subject to data protection issues, there seem no good reason for not allowing more open access to these records. We consider this should be achievable by better resourcing of the option to tax office and ridding the system of the delays which are a significant problem for all involved with buying and selling commercial property. Another idea may be to make it mandatory to register any option to tax with the Land Registry Office in the same way as it is necessary to notify Land Registry of any charge against the property.
- 3.26 Another possibility for practical simplification of the option to tax rules is to follow the approach in some countries (such as Germany) of an automatic disapplication of an option to tax if the tenant is itself operating a business that is largely exempt from VAT. If desired, this could be narrowed such that, for example, automatic disapplication was only available to businesses operating in the social exemption sphere which would enable exemption to apply to school property, doctor's surgeries etc.
- 3.27 Further simplification could also be introduced by making greater use of the zero rating provisions, which the UK may now have more freedom to do post-Brexit. The option to tax was originally introduced because the UK used to zero rate certain land transactions, but was forced to drop this on joining the EU in favour of exemption. As this would have created issues with VAT recovery for property developers, the option to tax was introduced. It may therefore be worth looking back at the old pre-option to tax legislation to see if that might work better in certain circumstances. Indeed, the UK could go further and look at using zero rating for the social exemption sector (for example). This would enable one of the boundary issues to be removed by dropping the 5% rate for renovations etc.
- 3.28 As a separate matter, the anti-avoidance measure in Regulation 12 of Schedule 10 of VATA 1994 continue to cause many problems. Whilst we understand the reasons why such rules are required, this may be a good time to attempt to make them more straightforward.

Question 13: Would you prefer to keep the VAT rules on land and property as they are? If so, please explain

- 3.29 Overall we believe it would be better to leave the main basis of the VAT rules on land and property as they are.
- 3.30 Effort would instead be better directed at fixing practical problems with the existing rules, rather than attempting an overly ambitious overhaul.
- 3.31 As set out above, such an overhaul would cause disruption to taxpayers, and could result in businesses incurring extra costs for no real simplification benefit. In particular, whichever proposal is adopted, it appears unlikely that this would address the underlying boundary issues in determining the VAT treatment of land and property supplies which, as noted above, constitute the main problems in applying them in practice.

4 Contact details

- 4.1 We would be pleased to join in any discussion relating to this consultation. Should you wish to discuss any aspect of this response, please contact our relevant Technical Officer, Emma Rawson on 07392 824718 or erawson@att.org.uk

The Association of Taxation Technicians

5 Note

- 5.1 The Association is a charity and the leading professional body for those providing UK tax compliance services. Our primary charitable objective is to promote education and the study of tax administration and practice. One of our key aims is to provide an appropriate qualification for individuals who undertake tax compliance work. Drawing on our members' practical experience and knowledge, we contribute to consultations on the development of the UK tax system and seek to ensure that, for the general public, it is workable and as fair as possible.

Our members are qualified by examination and practical experience. They commit to the highest standards of professional conduct and ensure that their tax knowledge is constantly kept up to date. Members may be found in private practice, commerce and industry, government and academia.

The Association has more than 9,000 members and Fellows together with over 6,000 students. Members and Fellows use the practising title of 'Taxation Technician' or 'Taxation Technician (Fellow)' and the designatory letters 'ATT' and 'ATT (Fellow)' respectively.