HMRC - VATSC46400 - ECJ Judgment In The Mirror Group Case

A number of tribunal decisions in the 1980s found that reverse premiums were consideration for taxable supplies by the recipient tenants. This included the agreement by the tenant to take a lease. These decisions had the effect of bringing virtually all such payments within the scope of VAT.

The 2001 judgment of the European Court of Justice (ECJ) in the case of Mirror Group plc (C-409/98) has altered this position. In this case, the ECJ found that a tenant, in being paid an inducement to take a lease, does not make a supply within the exemption for the letting or leasing of immoveable property in Article 13B(b) of the EC Sixth Council Directive (now Article 135 of the Principal VAT Directive 2006/112). However, the ECJ also considered whether such a payment was consideration for a supply of services for the purposes of Article 2(1) of the Directive (now Article 2(1) of the Principal VAT Directive).

Paragraph 26

In paragraph 26 of its judgment the ECJ held that there is no supply if the recipient of the inducement does nothing more for it than become a tenant and pay the rent. The ECJ goes on to say that a tenant does make a taxable supply when acting as an “anchor tenant” - this supply being one of advertising services in transferring its business to the property to attract other tenants to it

Clearly paragraph 26 changes the scope of earlier policy, based on Tribunal precedent, that VAT is due even where a tenant does nothing more than enter a lease. Since the Court’s judgment the question has been just how widely the comments in paragraph 26 apply.

In 2003 the High Court gave final judgment in the Mirror case (following its referral back from the ECJ) and, in doing so, advised that paragraph 26 of the ECJ’s judgment should be read narrowly. It held that a tenant receiving an inducement would supply taxable services to a landlord by way of obligations incurred under the lease agreement.

As a result, Customs and Excise’s (Business Brief 04/2003) took a robust line on this issue. It advised that a prospective tenant receiving an inducement would make a taxable supply, by affording the landlord the advantages of being bound by the lease obligations he has to fulfil. This meant any lease obligation other than to pay rent (for example to redecorate the demised area every five years) could therefore be seen as a taxable supply by a tenant.

However, subsequent representations to us have led to reconsideration of the policy set out in the Business Brief. It is now accepted that normal lease obligations to which tenants are bound do not constitute supplies for which a reverse premium is consideration.

It is therefore likely that the majority of reverse premium payments will not constitute consideration for supplies as they are no more than inducements to tenants to take leases and to observe the obligations in them. Only where such a payment is directly linked to benefits a tenant provides outside normal lease terms will there be a taxable supply. However, merely putting such a distinct benefit into the lease terms would not mean it becomes outside the scope of VAT.

In effect, reverse premium payments will now follow the position of rent-free periods - see VATSC48000 - in being mainly outside the scope of VAT and only taxable consideration when directly linked to a specific benefit supplied by a tenant to a landlord.

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