

Isle of Man Customs and Excise

Practice Note regarding IOM based yacht leasing and chartering structures

- 1) The aim is to provide a clear framework for the VAT treatment of unacceptable (abusive) yacht leasing and chartering structures. These proposals take into account the following key points;
 - The guidance in Revenue & Customs Brief 56/09.
 - The implications of IOM C&E's former guidance contained in the 'Yacht 2000 letter' and of the withdrawal of that guidance on 14th September 2009.
 - The need for equity of treatment.
 - The need for a transitional period to allow businesses to implement the new VAT treatment.
 - The possible implications of the *Weald Leasing Ltd* case (C-103/09).

The implications of IOM C&E's former guidance contained in the 'Yacht 2000 letter' and its withdrawal

- 2) Following advice given to IOM C&E by IOM's Attorney General, IOM C&E conclude (and HMRC accepts) that no assessment action will be taken by IOM C&E concerning input tax recovered or output tax declared before 14th September 2009¹ in relation to unacceptable yacht leasing and chartering structures, provided the activity pursued met the criteria set out in the 'Yacht 2000 letter'.
- 3) Reference herein to unacceptable structures means structures which meet the following descriptions:

Unacceptable yacht leasing structures

- 4) A yacht is leased to an individual who funded the purchase of that yacht (directly or indirectly²) or is leased to a person (or persons) "connected"³ to that individual.

A leasing structure meets the two-part test for an abusive practice identified by the ECJ in the *Halifax* case (C-255/02) if:-

- it seeks a VAT advantage which is contrary to the purpose of the Directive; and
- the essential aim of the structure is to attain that VAT advantage.

¹ The date when IOM C&E withdrew the guidance contained in the 'Yacht 2000 letter'.

² Indirect funding includes acting as guarantor or providing indemnity in relation to a loan made to another party.

³ "Connected" persons as defined in Schedule 7 of the Value Added Taxes Act 1996, Section 119C of the Income Tax Act 1970 and Section 1122 of the Corporation Tax Act 2010 (formerly Section 839 of the Income and Corporation Taxes Act 1988)

Under the policy of HMRC and IOM C&E, deferment of all or part of the VAT which would otherwise be incurred by a consumer at the consumption stage is a VAT advantage which is contrary to the purpose of the Directive.

Unacceptable yacht chartering structures

5) A yacht is used solely by the individual who funded its purchase (directly or indirectly), and/or by a person or persons "connected"³ to that individual or if it is chartered to third parties as well, the third party chartering activity lacks sufficient continuity and substance to meet the 'business test' derived from the case of *Lord Fisher* (STC 238). The 'business test' is summarised (for information) below:

- Is the activity a serious undertaking earnestly pursued?
- Is it actively pursued with reasonable or recognisable continuity?
- Is there a certain measure of substance in the quarterly or annual value of taxable supplies made?
- Is it conducted in a regular manner and on sound and recognised business principles?
- Is it predominantly concerned with the making of taxable supplies to consumers for a consideration?
- Are the taxable supplies being made of a kind commonly made by those who seek to profit from them?

A structure meets the two-part test for an abusive practice identified by the ECJ in the *Halifax* case (C-255/02) if:-

- it seeks a VAT advantage which is contrary to the purpose of the Directive; and
- the essential aim of the structure is to attain that VAT advantage.

Use of a Yacht within a Charter Structure by the Individual who Funded its Purchase ("the owner")

6) For the avoidance of doubt, unacceptable charter structures may be challenged on the grounds that they meet the two-part test for abuse. Where the features of an unacceptable structure are not present, (i.e. where the vessel is chartered to third parties with sufficient continuity and substance to meet the business test as well as being chartered to the owner) it follows that the structure will not amount to an abusive practice. In these circumstances the VAT treatment of use by the owner will follow the normal VAT rules i.e. the same VAT treatment that applies when the yacht is chartered to third parties.

Transitional Period

7) IOM C&E has determined that there should be a Transitional Period commencing on 14th September 2009 and ending on 31st May 2010 so that businesses involved in yacht chartering or leasing have an opportunity to review their activities in order to identify unacceptable structures and to notify these to IOM C&E. During this Transitional Period no action will be

taken by IOM C&E with regard to unacceptable chartering and leasing structures.

Way forward re unacceptable yacht chartering structures

- 8) Due to the legitimate expectation issues set out at paragraph 2 above, no assessment action will be taken by IOM C&E concerning input tax recovered or output tax declared³ before 14th September 2009 in relation to unacceptable yacht chartering structures (provided that the activity met the 'Yacht 2000 letter' criteria).
- 9) During the Transitional Period (i.e. before 31st May 2010) yacht chartering businesses should review the level of third party chartering to ensure that it has sufficient continuity and substance to meet the 'business test' derived from the case of *Lord Fisher* (as above).
- 10) Where a yacht is used solely by the individual who funded its purchase, or by a person or persons connected³ to that individual, or if any third party chartering activity lacks sufficient continuity and substance to meet the 'business test', then the business should notify IOM C&E of this **by 31st May 2010** and apply to deregister from VAT on the basis that it is no longer carrying out an economic activity for VAT purposes when viewed against the criteria in RCB 56/09.

Deregistration of a Yacht Charter Structure

- 11) When a yacht chartering business is deregistered from VAT, the effective date of deregistration will, in principle, be 14th September 2009 (i.e. the date when the 'Yacht 2000 letter' was withdrawn). However, a later date may be agreed between IOM C&E and the charter business under **Sch.2, para.13(2), VATA 1996**. IOM C&E do not anticipate agreeing to deregistration dates later than 31 May 2010 for cases involving unacceptable charter or lease structures which are notified to IOM C&E within the transitional period.
- 12) IOM C&E will consider the facts of each case where deregistration action is necessary to determine the VAT treatment of the vessel. However, due to the potential complexity of these international transactions (involving the physical movements of yachts), IOM C&E can advise only insofar as the transaction relates to the IOM/UK rules. It is recommended, therefore, that businesses should also seek advice from the relevant tax administration in which the yacht is situated at any time to check the VAT position in that jurisdiction if there is any doubt.
- 13) With that caveat in mind, the VAT treatment is likely to fall in one of the following categories;

³ This reference to output tax covers the possibility that O/T may have been accounted for on the charter of a vessel with less than 10 berths used in UK/IOM territory)

a. Where the vessel was purchased or imported in IOM/UK territory, or where the intra-EU acquisition of the vessel physically took place in IOM or UK territory;

Subject to the specific circumstances the deregistration may mean that the conditions for disregarding the original intra Community transfer of own goods, for the purpose of a supply of services to be made in another Member State, will no longer be fulfilled thus triggering a deemed supply at deregistration irrespective of the location of the vessel. The relevant legislation is contained in Articles 17(1), 17(2)(g) and Art 17(3) of the Principal VAT Directive which are enacted in Manx law under **Sch.5, para.6, VATA 1996** and related provisions⁴.

The value of such a deemed supply would be the open market value of the vessel on the effective date.

b. Where the vessel was not imported in IOM or UK territory, or where the intra-EU acquisition of the vessel physically took place in another Member State (EU 'Fallback' Arrangements);

There may be a deemed supply of goods (the vessel) on the effective date of deregistration (i.e. 14th September 2009 or such later date as may be agreed between IOM C&E and the charter business). The deemed supply would arise under **Sch.5, para.8(1), VATA 1996**. The place of this deemed supply would be the place where the vessel is located on the effective date.

The yacht chartering business should therefore notify IOM C&E of the location of the vessel on the effective date.

- i. Where a vessel is located **within EU territory** on the effective date of deregistration the place of this deemed supply would be the Member State where the vessel was located on the effective date of deregistration.
- ii. Where a vessel is located **outside EU territory** on the effective date of deregistration the place of this deemed supply would be outside the EU. In these circumstances the yacht owning company should;
 - obtain and keep evidence of the vessel's position on the date of deregistration and send a copy to IOM C&E;
 - notify IOM C&E of the date and port at which the vessel is re-imported into the EU.

Way forward re unacceptable yacht leasing structures

⁴ The relevant conditions are contained in [Articles 4(f) and 5 of the Value Added Tax (Removal of Goods) Order 1993 [SD 53/93] and Regulation 42 of the VAT Regulations 1996 (SD194/96)].

- 14) It is apparent that the outcome of the *Weald Leasing Ltd* case (C-103/09) may be relevant to the VAT treatment of unacceptable yacht leasing structures. For this reason the final VAT treatment of such structures will not be determined until the outcome of the *Weald Leasing Ltd* case is known. In the meantime it remains the policy of IOM C&E and HMRC that such structures meet the two-part test for an abusive practice identified by the ECJ in the *Halifax* case.
- 15) During the Transitional Period yacht leasing businesses should review their activities to identify unacceptable leasing structures where the leasing entity incurred VAT on the purchase, acquisition or importation of a yacht after 14th September 2009. Any structures in this category should be notified to IOM C&E **by 31 May 2010**.

Leasing Structures where VAT was incurred on the purchase, acquisition or importation of a yacht after 14th September 2009

- 16) Leasing businesses should notify IOM C&E of any arrangements which appear to comprise an unacceptable leasing structure and where the leasing entity incurred VAT on the purchase, acquisition or importation of a yacht after 14th September 2009. IOM C&E may then make further enquiries and may take appropriate action to protect its position until the outcome of the *Weald Leasing Ltd* case is known.

Leasing Structures where VAT was incurred on the purchase, acquisition or importation of a yacht before 14th September 2009

- 17) Due to the legitimate expectation issues set out at paragraph 2 above, IOM C&E will not take assessment action relating to input tax which was recovered before 14th September 2009 (provided that the activity met the 'Yacht 2000 letter' criteria). Thus, as the principle of abuse cannot be applied to refuse deduction of input tax, it follows that the refund of output tax that would also arise from an abuse redefinition will not be possible. Leasing entities in existing deferment structures (where input tax was recovered prior to 14th September 2009 and so cannot be corrected) should therefore continue rendering VAT returns and accounting for output tax throughout the term of the lease.
- 18) Where, in this category,
- an existing lease is assigned with the original contractual arrangements remaining; or
 - a leasing entity is sold/transferred with the benefit and assignment of the existing lease such that the existing lease remains in place,

then no assessment or deregistration action will be taken in respect of the sale/transfer providing that the leasing entity continues rendering VAT returns and accounting for output tax throughout the term of the lease.

Isle of Man Customs and Excise
26th April 2010