



## FLA RESPONSE TO HMCE CUSTOMS & EXCISE CONSULTATION ON THE OPTION TO TAX

FLA is the main representative organisation for the UK consumer credit, motor finance and asset finance sectors, and the largest organisation of its type in Europe. Our members comprise banks, subsidiaries of banks and building societies, the finance arms of leading retailers and manufacturing companies, and a range of independent firms. The facilities they provide include finance leasing, operating leasing, hire purchase, conditional sale, personal contract purchase plans, personal lease plans, secured and unsecured personal loans, credit cards and store card facilities.

FLA members achieved £93.3 billion of new business in 2004. Of this FLA members provided asset finance to business of over £25.0 billion, representing over a quarter of all fixed capital investment in plant, machinery, vehicles, ships and aircraft in the UK in 2003. The remaining £68.3 billion was provided to the consumer sector and FLA members represented 29.3% of all unsecured lending in the UK. Included in the above total is £18.3 billion of finance provided to the motor sector. FLA members financed at least 50% of all new car registrations in the UK in 2004

FLA welcomes the opportunity to respond to the consultation paper. The paper is of interest to FLA members who act as landlords, tenants or both. Furthermore, a significant level of business conducted by FLA members is purchase of receivables of underlying lease contracts.

### SPECIFIC COMMENTS

Q.1	<i>Given that the revocation of an option to tax will restrict the right to input tax recovery, would you expect to revoke your option to tax after 20 years?</i>
Answer	<b>Businesses like flexibility. Revocation is a possibility but this will depend on market conditions, whether input tax incurred on the building remains within the capital items adjustment regulations; whether or not the tenant is or is not able to recover VAT; and whether large amounts of taxable expenditure on the property are contemplated in the foreseeable future.</b>
Q.2	Would you agree that the level of demand for revocation is likely to be low; if not, why not?
	<b>Yes, it is agreed that the level of demand is likely to be low. After 20 years of use it is possible that the landlord of a property will be</b>



	<p>contemplating refurbishment. Hence he will wish to continue the option in order to be able to recover the VAT on the costs of refurbishment.</p> <p>It is also recognised that revocation of an option may be used as a bargaining tool when negotiating rent reviews.</p>
Q.3	<p>Would you be disadvantaged if the facility for revoking the option to tax after 20 years, were withdrawn? If yes please give examples.</p>
	<p>It is considered that some taxpayers would be disadvantaged but only to a small extent. As businesses like flexibility the withdrawal of the revocation will be a loss. It would also represent the loss of a potential bargaining tool when fixing rents. The following is an example of where a trader would be disadvantaged:</p> <p>A building was purchased 20 years ago and let to a partially exempt subsidiary. It has been well maintained since and therefore no major capital expenditure is envisaged by the landlord in the immediate future. The landlord has negotiated a rent review and future VAT inclusive rents beyond 2009 have been fixed and agreed assuming that the revocation of the option will be made either because the landlord considers no works are necessary for the foreseeable future or because the lease requires the tenant to attend to and pay for these.</p>
Q.4	<p><i>Do you have any views about the proposed information requirements.</i></p>
	<p>Yes, they are too onerous.</p> <p>It is already becoming apparent that evidence of some of the original options of more than 10 years ago is difficult to trace. Customs do not require information on why a taxpayer wishes to opt to tax so why do they need to know why he wishes to revoke an option? If it is to be a requirement to give details of "Capital Goods Scheme items created in the last 5 years in respect of the property" it is difficult to understand why Customs also need details of output tax declared and input tax reclaimed in respect of the property over the last 5 years. This suggests that Customs wish to use the information to check whether capital items adjustments have been done accurately. This should be part of normal control visits and not part of the notification procedure for revocations.</p> <p>It is noted and accepted that when notifying revocations taxpayers will need to state a future date from which the revocation is to become effective. Are Customs considering putting a limit on how far into the future revocations can be made?</p>
Q.5	<p><i>Are there other circumstances where you consider it important for Customs to allow automatic permission? Please give examples.</i></p>
	<p>Yes:</p> <p>If a taxpayer opts to tax a property which he incurs and recovers input tax on development costs at the outset and then collects taxable rents for 20 years with no significant input tax recovered since the initial expenditure. There would appear to be no reason</p>

	<p>why the revocation cannot be automatically permitted.</p> <p>Where a taxpayer disposes of his entire interest in an opted property to an unconnected third party then the option should be revoked automatically. If the property is subsequently re-acquired then the option will have to be made and notified again if desired.</p> <p>In order to prevent avoidance it may be necessary to disapply this if the property is reacquired within a period of 10 years.</p> <p>It is considered that automatic permission should be made available to the greatest extent possible. This will make administration simpler for both the taxpayer and Customs. If automatic revocation is only permitted in a very limited range of circumstances as indicated in para 3.5 then why bother with automatic permissions at all.</p>
Q.6	<i>Do you consider that there is a need for a cooling off period for revocations?</i>
	<b>Yes, but it is considered that it would be rarely used. For this reason we wonder if such applications could be dealt with under Customs overall care and management of the tax?</b>
Q.7	<i>Do you consider that there are other circumstances where an option should be reinstated during the cooling off period?</i>
	<b>Yes e.g. if there has been no tax difference/advantage then it could be reinstated, similarly if no exempt supplies have been made it could be reinstated.</b>
Q.8	<i>Do you agree that the 20 year period should restart when the re-option is made outside the cooling off period, and if not, in what circumstances would that rule create an unfair result?</i>
	<b>No. However the rule would be acceptable generally but the exception would be that where no exempt supplies or TOGC's have been made since the revocation was made it would be unfair to insist that the 20 year period should restart.</b>
Q.9	<i>Do you think that Landlords should have a legal obligation to inform their tenants that they have revoked an option to tax?</i>
	<b>No: One would hope that this is done by common courtesy. However if it is not done the revocation should be evident by the lack of VAT on the next rent invoice. It is becoming much more common for leases to state whether the rent is inclusive or exclusive of VAT. It is therefore considered that the concern expressed in paragraph 3.10 is in respect of a diminishing problem.</b>
Q.10	<i>Do you think that the effective date of the revocation should create a tax point for rents accrued to date?</i>
	<b>Yes; but only if the option to tax creates a similar tax point. At the moment it is considered that Customs unfairly benefit where tax is demanded from a taxpayer who receives a rental after an option to tax has been made but which relates to settlement of an invoice issued before the option was made. The taxpayer in most cases has to pay the VAT demanded out of the exempt rent collected, having</b>

	<b>little or no chance of obtaining the VAT from what is already a slow payer.</b>
Q.11	<i>Are the proposals in relation to avoidance reasonable? If not can you provide examples to illustrate where the proposals would create an unfair result?</i>
	<p><b>Any evidence of intention is very difficult to prove either way and the “strong evidence” referred to in paragraph 4.3 would be even more difficult to provide. We therefore consider it unreasonable to impose this requirement on the taxpayer. It will be observed that it will also be difficult for Customs to provide evidence that the intention of the taxpayer is other than he or she states. It is considered that introduction of this requirement will inevitably lead to much litigation and contention. It is considered that the proposals in 4.4 would be acceptable if permissions are given within a reasonable timescale i.e within 3 weeks which Customs published answering for letters.</b></p> <p><b>If such a deadline cannot be met it will represent an unreasonable barrier to doing business.</b></p> <p><b>In paragraph 4.5 It gives an example of where a taxpayer “will not be allowed to revoke”. It would seem unreasonable if this prohibition was permanent.</b></p>
Q.12	<i>Are there any other situations where early revocation would be desirable?</i>
	<b>No comments.</b>
Q.13	<i>If revocation of the option to tax were allowed between 3 months and twenty years after it was made, would this be of assistance to businesses and, if so, in what circumstances?</i>
	<b>Yes. We can identify with the examples quoted in paragraph 5.2</b>
Q.14	<i>What is your view of the option outlined at para 5.4</i>
	<b>For let properties it fails to take account of the output tax Customs will have received on Rentals. Having to account for output tax on market value could be extremely expensive especially if the taxpayer is revoking with the intention of making exempt supplies. The recent increase in market values of properties at a rate far exceeding the average rate of inflation should not be overlooked.</b>
Q.15	<b>Do you have any alternative options:</b>
	<b>No.</b>
Q.16	<i>Is there still a business need for global options? If so, can you give examples of the reason for that business need</i>
	<b>No.</b>
Q.17	<i>Have you concerns about the proposal to cap existing global options? If so, can you give examples where you would envisage difficulties?</i>
	<b>No.</b>
Q.18	<i>Is it reasonable for Customs to require details of properties included in existing global options?</i>

	<b>In respect of properties currently owned, yes. It may be onerous to require details in respect of opted properties disposed of over the period from 1989 to date. Much of this information may no longer be available especially in respect of properties disposed of more than 10 years ago for which there is no requirement to keep records.</b>
Q.19	<i>Do you have examples of the current "relevant associate" rules that cause problems for group members?</i>
	<b>Where an option was made in 1989 and it is not clear which company in the VAT registration group made the option and that VAT group has been absorbed into other VAT registration groups it is difficult to determine whether or not the option carries through to the current VAT registration group.</b>
Q.20	<i>Is the proposed solution an improvement on the existing situation?</i>
	<b>Yes, it could be but for example what if A's option is currently subject to the disapplication, if B did not opt to tax would A be required to charge VAT even though its option is disapplied?</b>
Q.21	<i>What are the advantages to business of continuing to allow the separate treatment of land and buildings?</i>
	<b>It is not considered there are many. Some taxpayers may welcome the flexibility.</b>
Q.22	<i>Are there any disadvantages of the current system?</i>
	<b>Yes as outlined in para 8.3. The current treatment does not follow English and Welsh land law and therefore creates confusion.</b>
Q.23	<i>Should demolition of a building be treated as revoking the option on the underlying land?</i>
	<b>No, it may be better to allow revocation on demolition only if requested by the land owner.</b>
Q.24	<i>Should a building constructed on opted land be covered by the option or should a developer be allowed to revoke prior to development taking place?</i>
	<b>Yes and yes, it is considered that both could be accommodated.</b>
Q.25	<i>Do you agree that when an option spreads to an extension or linked building the 20 year period should run from the day of the original option?</i>
	<b>Yes.</b>
Q.26	<i>Do you think there are strong arguments for changing any of the linked building rules and if so, what do you see as the problems and solutions?</i>
	<b>It is considered that there is no particular need to change the linked building rules at present. The only area where there may be a need for change would be where the owner of adjacent non-linked buildings, one of which is opted and the other not, may wish to "knock through" to create a larger building. There maybe scope to allow the option position of the new larger building to be revisited whether or not the previous opted area is greater than 50% of the total area of the linked buildings. It could give a developer more flexibility in the VAT status of the building and give a wider potential market for the</b>

	<b>larger premises. Clearly the capital items adjustment regulations would also have to be considered in such circumstances.</b>
Qs.27-42	<b>FLA will not respond to these questions as they are particular to the individual taxpayers' circumstances.</b>

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