

# THE INTERNATIONAL ASPECTS OF VAT ON LEGAL ADVISORY FEES

Etienne Wong\*

The question is simple enough: where legal advice is provided by a UK advisor to a non-UK client, is UK VAT payable on the advisor's fees? Many would say 'no' without a second's hesitation. And in the majority of cases, that would be right. But it is not right in every case.

To be right in every case, the process would take a little longer and would involve consideration of the following:

- whether the advisory services fall within the default rules or the exceptional rules;
- whether the client is a relevant business person; and
- where the advisor or the client (or both) belong(s).

### The Rules

The provision of advice is a supply of services. UK VAT is payable on a supply of services where the supply is treated as made in the UK.

I say where the supply is treated as made as opposed to where the supply is made because the rules that determine the place of a supply of services are in the main deeming provisions. The underlying idea, as one would expect of a tax on consumption, is that goods and services should be taxed so far as possible in the country of consumption; in most cases, however, the rules are less concerned with finding the actual place of consumption than with avoiding double or non-taxation (see *Srf konsulterna* (C-647/17)).

The default rules are set out in the Value Added Tax Act 1994 (**VATA 1994**), section 7A(2), which provides that a "supply of services is to be treated as made –

---

\* Barrister of Old Square Tax Chambers; email: taxchambers @15oldsquare.co.uk

- (a) in a case in which the person to whom the services are supplied is a relevant business person, in the country in which the recipient belongs, and
- (b) otherwise, in the country in which the supplier belongs”.

Exceptions to the default rules are set out in VATA 1994, Schedule 4A.

There are:

- general exceptions;
- exceptions specific to supplies made to relevant business persons; and
- exceptions specific to supplies made to persons who are not relevant business persons.

General exceptions include rules specific to (broadly):

- services relating to land;
- passenger transport;
- the hiring of means of transport;
- restaurant and catering services;
- the hiring of goods; and
- broadcasting services

(VATA 1994, Schedule 4A, Part 1).

In addition to the general exceptions, there are further exceptions framed by reference to whether the person receiving the supply is a relevant business persons or not.

Where the person receiving the supply is a relevant business person, the further exceptions include rules specific to (broadly):

- electronically-supplied services;
- admission to cultural, educational and entertainment activities;
- the transport of goods;
- ancillary transport services;
- repair services supplied under certain circumstances; and
- telecommunication services

(VATA 1994, Schedule 4A, Part 2).

Where the person receiving the supply is not a relevant business person, the further exceptions include rules specific to (broadly):

- intermediaries;
- the transport of goods;
- ancillary transport services;
- the long-term hiring of means of transport;
- valuation services;
- cultural, educational and entertainment activities;
- electronically-supplied, telecommunication and broadcasting services; and
- (until a date to be appointed – probably the day immediately following the end of the Brexit transitional period) certain services (**Schedule 5 services**) supplied to persons belonging outside the EU (or, after the appointed day, outside the UK (which, for VAT purposes, includes the Isle of Man))

(VATA 1994, Schedule 4A, Part 3).

In determining where the supply of services constituted by the provision of legal advice is made, the first question is whether the services relate to land. If they do, the exception specific to services relating to land would apply, in which case the supply would be treated as “made in the country in which the land in connection with which the supply is made is situated” (see VATA 1994, Schedule 4A, paragraph 1(1)).

Where the services do not relate to land, and:

- (i) the person receiving the supply is a relevant business person, the supply is subject to the default rules; and
- (ii) where the person receiving the supply is not a relevant business person, the supply may be subject to either the default rules or the exception specific to Schedule 5 services, depending on where the person belongs (and whether the current rules or the post-Brexit rules are engaged).

By way of illustration (using the current rules): if the person receiving the supply is not a relevant business person and they belong in France (i.e. another EU country), the supply is subject to the default rules (and is treated as made in the UK); if, instead, they belong in Japan, the supply is subject to the exception specific to Schedule 5 services (and is treated as made in Japan).

In case there is any question regarding whether advice given via email constitutes an electronically-supplied service (and thus falls within the exception specific to electronically-supplied services), VATA 1994, Schedule 4A, paragraph 9(4) provides

that "... where the supplier of a service and the supplier's customer communicate via electronic mail, this does not of itself mean that the service provided is an electronically supplied service ...".

## Services Relating to Land

The exception specific to services relating to land enacts in the UK the provisions of Article 47 of the Principal VAT Directive (**PVD**) i.e. Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax.

PVD, Article 47 refers to "services connected with immovable property". Article 31a(1) of the Implementing Regulation (Council Implementing Regulation (EU) 282/2011 of 15 March 2011 laying down implementing measures for Directive 2006/112/EC on the common system of value added tax) provides that such services "include only those services that have a sufficiently direct connection with [immovable] property", such as "where they are ... directed towards, an immovable property, having as their object the legal ... alteration of that property". The Implementing Regulation, Article 2(q) provides expressly that services connected with immovable property extend to:

"legal services relating to the transfer of a title to immovable property, to the establishment or transfer of certain interests in immovable property or rights *in rem* over immovable property (whether or not treated as tangible property), such as notary work, or to the drawing up of a contract to sell or acquire immovable property, even if the underlying transaction resulting in the legal alteration of the property is not carried through",

and Article 3(h) provides that such services do not include:

"legal services other than those covered by [*the Implementing Regulation, Article 2(q)*], connected to contracts, including advice given on the terms of a contract to transfer immovable property, or to enforce such a contract, or to prove the existence of such a contract, where such services are not specific to a transfer of a title on an immovable property".

## The Client

As can be seen from the above, one of the key questions in determining where a supply of services constituted by the provision of legal advice is treated as made is whether the person receiving the supply is a relevant business person.

However, even before we get to that question, there is a more fundamental one which is often overlooked – namely, whether the advisor's client is the person receiving the supply.

While, in 99% of cases, the contractual position between the advisor and the client would be determinative – and the client would be the person receiving the supply – the reason for that is not because the contractual position is definitive, but because in 99% of cases, the contractual position aligns with economic reality – or, in layman’s terms, in 99% of cases, the contractual position fully reflects the substance of what is actually happening.

That still leaves the 1% where the position is not so straightforward.

The area is complicated, and I do not propose to discuss it in detail here. The relevant legal principles are helpfully summarised by Gloster LJ in *Airtours* [2014] EWCA Civ 1033 (when that case was in the Court of Appeal):

- “i) “Consideration of economic realities is a fundamental criterion for the application of the common system of VAT” as regards the identification of the person to whom services are supplied: see e.g. per Lord Reed in [*Aimia* [2013] UKSC 15 (**Aimia**)] at [56] and [66]; [*Loyalty Management UK & Baxi (Cases C-53/09 & C-55/09)*] at [39]; and [*Newey (Case C-653/11) (Newey)*] at [42] (“*Newey*”).
- ii) Decisions about the application of the VAT system are highly dependent upon the factual situations involved. Thus a small modification of the facts can render the legal solution in one case inapplicable to another: see e.g. per Lord Reed in [*Aimia*] at [68] and in [*WHA* [2013] UKSC 24 (**WHA**)] at [26].
- iii) The case law of the CJEU indicates that, when determining the relevant supply in which a taxable person engages, regard must be had to all the circumstances in which the transaction or combination of transactions takes place: see per Lord Reed in [*Aimia*] at [38] and in [*WHA*] at [26]. In cases where a scheme operates through a construct of contractual relationships, it is necessary to look at the matter as a whole in order to determine its economic reality: see per Lord Walker in [*Aimia*] at [114]-[115] and per Lord Reed in [*WHA*] at [26]. Thus the relevant contracts have to be understood in the wider context of the totality of the arrangements between the various participants.
- iv) The terms of any contract between the parties, whilst an important factor to be taken into account in deciding whether a supply of services has been made, are not necessarily determinative of whether as a matter of “economic reality” taxable supplies are being made as between any particular participants in the arrangements. However, the contractual position is generally the most useful starting point for the VAT analysis: see per Lord Reed in [*WHA*] at [27]. That may be particularly so where certain contractual terms do not wholly reflect

the economic and commercial reality of the transactions: see per the CJEU in [Newey] at [43]-[44].

- v) There may, as a matter of analysis, be two or more distinct supplies within the same transaction ...”

In their guidance on when VAT is recoverable by holding companies (set out in VIT50600 of their internal manual), HMRC state that they:

“... consider that a holding company is the recipient of [a] supply where it has contracted for the supply, including by novation and it has made use of the supply, been invoiced and paid for the supply.”

Although the guidance is framed by reference to holding companies, it is nevertheless of interest as there is no reason why a different approach should apply in relation to any other types of persons.

### **Relevant Business Person**

Once the advisor’s client has been established as the person receiving the supply constituted by the provision of the advice, the question arises as to whether the client is a relevant business person.

As mentioned above, VATA 1994, section 7A sets out the default rules for determining the place where a supply of services is treated as made, and section 7A(2)(a) enacts in the UK the provisions of PVD, Article 44, which sets out the default rules in relation to a supply of services made to a “taxable person acting as such”. The “relevant business person” concept is the UK’s iteration of a “taxable person acting as such”. It is defined in VATA 1994, section 7A(4). In anticipation of Brexit (or, rather, the end of the Brexit transitional period), the Taxation (Cross-Border Trade) Act 2018, section 43 and Schedule 8, Part 1, paragraph 1.8 introduced a new definition, which reads as follows:

“For the purposes of this Act a person is a relevant business person in relation to a supply of services if –

- (a) the person carries on a business, and
- (b) the services are not received by the person wholly for private purposes,

whether or not the services are received in the course of business.”

Apart from the tailpiece, the post-Brexit definition of a “relevant business person” is in substance the same as the current definition.

Both refer to the “taxable person” concept set out in PVD, Article 9. The post-Brexit definition takes a simpler approach, and has the appearance at least of being more user-friendly – a “person [*who*] carries on a business” is certainly easier to conceptualise than a “taxable person”. The word “business”, however, is a term of art for VAT purposes and it does not always align with the natural and ordinary meaning of the word. In eschewing use of the technical term “taxable person”, the post-Brexit definition no longer contains any “health warning” that a person who is regarded as carrying on a business in the real world may not be regarded as carrying on a business in the VAT world (and *vice versa*). The post-Brexit definition may, therefore, appear more user-friendly, but to a user who is less familiar with VAT, it may be less than friendly in fact.

As mentioned above, the “relevant business person” concept is the UK’s iteration of a “taxable person acting as such” (as used in PVD, Article 44). There are three points to note in this respect:

- (a) PVD, Article 43(2) provides that, for the purposes of applying the rules concerning the place of supply of services:

“a non-taxable legal person who is identified for VAT purposes shall be regarded as a taxable person.”

In other words, a person who does not carry on a business for VAT purposes who is nevertheless registered for VAT is deemed for these purposes to be a person who does carry on a business for VAT purposes.

This is captured in the current definition of “relevant business person” but, it would appear, not in the post-Brexit definition;

- (b) Recital (19) of the Implementing Regulation states that:

“It should be clarified that when services supplied to a taxable person are intended for private use ... that taxable person cannot be deemed to be acting in his capacity as a taxable person ...”

This is captured in both the Post-Brexit and current definitions of “relevant business person” via the condition that the services in question must not be received “wholly for private purposes”; and

- (c) turning to the tailpiece, there is a live debate over whether in order to be a “taxable person acting as such”, the person in question must not only be registered for VAT, but also be using the services they receive for business purposes, the argument being (very broadly) that if they must be both, then where they are receiving services for a non-business purpose, the place where those services are treated as supplied is the country where the person making the supply belongs

(which may be a jurisdiction that does not charge VAT) and not the country where the person receiving the supply belongs.

This is the subject of a referral currently before the CJEU (*Wellcome Trust*, Case C-459/19).

The tailpiece to the post-Brexit definition of “relevant business person” represents HMRC’s preferred outcome in the case, and enacts it into law (and, of course, even if the case goes against HMRC, it matters little after Brexit, as by then the UK will no longer be bound to follow what the position ought to be under PVD).

## Belonging

So, going back to the beginning, the question is still simple: where legal advice is provided by a UK advisor to a non-UK client, is UK VAT payable on the advisor’s fees?

Say we have established that the client is the person receiving the supply constituted by the provision of the advice. The question now is where they belong.

A relevant business person belongs:

- “(a) if [*they have*] a business establishment, or some other fixed establishment, in a country (and none in any other country), that country,
- (b) if [*they have*] a business establishment, or some other fixed establishment or establishments, in more than one country, the country in which the relevant establishment is, and
- (c) otherwise, the country in which [*their*] usual place of residence or permanent address is”

(see VATA 1994, section 9(3)).

For these purposes, the “relevant establishment” is “whichever of the person’s business establishment, or other fixed establishments, is most directly concerned with the supply” (see VATA 1994, section 9(4)).

The Implementing Regulation, Article 10 provides that a person’s “business establishment” is “the place where the functions of the business’s central administration are carried out”, and in determining the location of such a place, “account shall be taken of the place where essential decisions concerning the general management of the business are taken, the place where the registered office of the business is located and the place where management meets”, and where “these criteria do not allow the place of establishment of a business to be determined with certainty,



the place where essential decisions concerning the general management of the business are taken shall take precedence”.

The Implementing Regulation, Article 10(3) provides that the “mere presence of a postal address may not be taken to be” a business establishment.

For the purposes of determining where a relevant business person receiving a supply of services belongs, the Implementing Regulation, Article 11 provides that a “fixed establishment” shall be any establishment, other than a business establishment (as defined for these purposes – see above), “characterised by a sufficient degree of permanence and a suitable structure in terms of human and technical resources to enable [*the relevant business person*] to receive and use the services supplied to it for its own needs.”

The Implementing Regulation, Article 11(3) provides that “having a VAT identification number [*such as a VAT registration number*] shall not in itself be sufficient to [*constitute*] a fixed establishment.”

A person who is not a relevant business person belongs:

- “(a) in the country in which the person's usual place of residence or permanent address is (except in the case of a body corporate or other legal person);
- (b) in the case of a body corporate or other legal person, in the country in which the place where it is established is.”

The Implementing Regulation, Article 12 provides that:

“... the ‘permanent address’ of a natural person ... shall be the address entered in the population or similar register, or the address indicated by that person to the relevant tax authorities, unless there is evidence that this address does not reflect reality”,

and Article 13 provides that:

“The place where a natural person ‘usually resides’ ... shall be the place where that natural person usually lives as a result of personal and occupational ties. Where the occupational ties are in a country different from that of the personal ties, or where no occupational ties exist, the place of usual residence shall be determined by personal ties which show close links between the natural person and a place where he is living.”

In the case of a body corporate or other legal person who is not a relevant business person, the place where such a person is established is:

- “(a) the place where the functions of its central administration are carried out; or

- (b) the place of any other establishment characterised by a sufficient degree of permanence and a suitable structure in terms of human and technical resources to enable it to receive and use the services supplied to it for its own needs”

(see VATA 1994, section 9(6) and the Implementing Regulation, Article 13a).

### **The Complication with Counsel**

So, back again to the question: where legal advice is provided by a UK advisor to a non-UK client, is UK VAT payable on the advisor’s fees?

Say the client is, on proper analysis, the person receiving the supply constituted by the provision of the advice, and they belong in France.

If the advice is in substance a service relating to land and the land is situated in the UK, then the answer is ‘yes’, UK VAT is payable on the advisor’s fees.

Or if the client is not a relevant business person, then the answer is (under current rules) also ‘yes’, even if the advice does not constitute a service relating to land situated in the UK.

The answer is not, therefore, always ‘no’.

Where the legal advice in question is provided by Counsel, instructed by a UK firm with a non-UK lay client, the answer can be even more convoluted. To simplify discussions, let’s assume the advice in question is not a service relating to land.

The first question then is whether the person receiving the supply made by Counsel is the firm or the lay client. In the vast majority of cases, Counsel would contract with the firm and the firm would be the person receiving the supply. However, as discussed above, the contractual position is not always definitive, but (again) to simplify discussions, let’s say the firm is the person receiving the supply. Because, in our example, the firm is a UK firm – shorthand for a firm belonging in the UK – UK VAT would be payable on Counsel’s fees.

The VAT would be input tax for the firm. Even if Counsel’s fees (and the VAT on the fees) are borne by the lay client, the VAT element of Counsel’s fees is input tax for the firm and not the lay client.

The firm itself would be making a supply of services – to the lay client. If we assume that the lay client is a relevant business person who belongs in Germany, no UK VAT would be payable on the firm’s fees.

So what one would expect if Counsel charges 1,000 (plus VAT at 20%) and the firm's own fees are 2,000 is that:

- (1) Counsel would invoice the firm for 1,200;
- (2) the firm would invoice the lay client for 3,000; and
- (3) the firm would recover 200 from HMRC.

This represents the legal position. Which, from the firm's perspective, may be seen as less than ideal.

A concessionary procedure was agreed between HMRC, the Law Society and the Bar Council back when VAT was first introduced in the UK. Under this procedure, UK VAT may be avoided on Counsel's fees even where the person receiving Counsel's supply is the firm and the firm belongs in the UK provided the lay client either:

- is a relevant business person and belongs outside the UK; or
- (under the current rules) where it is not a relevant business person, belongs outside the EU.

The procedure was published in the 4 April 1973 edition of the Law Society Gazette. The relevant parts read as follows:

“ ...

**B Counsel's Fees**

...

B 2 Solicitors may treat counsels' fees for VAT purposes either as their own input, and later as an output by the solicitor to his own client, or as an input to the client direct through the agency of the solicitor ...

...

B 4 The Bar Council and The Law Society have agreed that solicitors can amend a counsel's fee note prior to payment in the following ways:

- (a) by inserting the name of the client in the fee note and the word 'per' immediately preceding the solicitor's own name and address; Customs [*now HMRC*] have accepted that if this is done the input may be taken by the client;
- (b) by amending or inserting the rate of VAT and the appropriate amount of VAT payable as at the date of payment; this is of importance if the rate of VAT should change after delivery of the fee note but before payment;
- (c) in cases where the solicitor considers that the supply should be zero-rated [*or, in more contemporary parlance, free of UK VAT by virtue of the supply being treated as made outside the*

UK], by certifying the fee note accordingly and accounting to counsel for the amount of his fee only ...

- B 5 If the client's name is inserted in the fee note it will enable the client to obtain an immediate input credit ...

..."

The concessionary procedure is referenced (but not reproduced) in the ninth edition of the Bar Council's Taxation and Retirement Benefits Guidance (the **Bar Council Guidance**) (dated May 2016):

"...

- 279 Under this procedure it is possible for the instructing solicitor to treat the supply of counsel's services as having been made directly to the ultimate client. This entails the solicitor re-addressing counsel's fee note by adding the client's name and address and the word "per" before the solicitor's. Once receipted, the fee note should be passed by the solicitor to their client thus enabling them to treat the VAT as input tax, if they are a taxable person and the supply of counsel's services was obtained for the purposes of their business.
- 280 If, because of the nature of counsel's services and the identity and location of the solicitor's client, the supply of those services is not subject to UK VAT, for example legal advice to a business abroad, the solicitor is entitled to certify the fee note accordingly and ask their client to pay the VAT exclusive amount only. Alternatively they may ask counsel's clerk to cancel the original fee note and submit a new one; this will have no adverse VAT implications in that counsel's fee note only becomes a tax invoice when receipted. In either case, the fee note will have to be addressed to the ultimate client.
- 281 It is important to note that it is the UK solicitor who decides whether to adopt the concessionary treatment. It is not the barrister; if the solicitor does not elect for the concessionary treatment, VAT remains chargeable under the general rule."

The next paragraph of the Bar Council Guidance cites a passage from the Customs and Excise Manual which has now been archived and is not reproduced anywhere, but which, it is believed, still represents current practice:

*"Barristers and advocates*

*Invoices from barristers and advocates (known as Counsel) are usually addressed to the firm which instructed them, rather than the ultimate client. Most practices will recover the VAT on Counsel's fees and account for output tax when they are charged on to the client. However, under an agreement between the Department and the Law Society, they may opt to treat Counsel*

*fees as disbursements, in which case the firm will manually write the client's name and 'per' above their own name on the Counsel fee note. The original Counsel fee note must be forwarded to the client."*

Finding a copy of the concessionary procedure as it was originally published is extremely difficult, and curiously, it would appear never to have been updated. Although originally framed by reference only to solicitors, it is believed that in practice, HMRC is happy for accountants also to avail of the procedure. Use of the procedure nowadays is more likely based on anecdotal understanding of the concession than actual knowledge of the text.

It is important to note that the procedure is concessionary – it does not represent the legal position and cannot, for example, be forced on Counsel if Counsel were not prepared to go along with the procedure. Even where all parties are happy to use the procedure, there are steps that must be followed (see above), and one must take care to follow the procedure properly and not fall outside both the legal position and the scope of the concession (if only because in that scenario what is done then would just be plain wrong).

### **A Quick Word on Input Tax**

Irrespective of where it is treated as made – in the UK or in another country – a supply of services constituted by the provision of legal advice is a taxable supply, and any VAT incurred by the person making the supply is input tax attributable to a taxable supply, and thus deductible (see VATA 1994, sections 26(1) and (2)).