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The co-ownership **VAT conundrum** (part I)

Introduction

How does one ride half a horse? Well, one does not, obviously. Together with the other owner(s) of a horse, you create a rota who gets to ride the horse at any given time. Jointly grooming a horse might be doable, feeding it perhaps, but riding? No, that 'ain't gonna fly'. Okay, the smarty-pants amongst us must be saluted for their creative approach in stating that one can actually ride a quarter-horse, but let's discard of that notion for the sake of this contribution. Selling your share in a horse usually is also not possible until after your co-owners have waived their right to 'first refusal'. The essence here is that if one owns a share in a horse, one simply is not capable to dispose of (that share in) the horse as an owner: you will always need to agree on stuff with your co-owners. And herein lies the VAT-challenge that I put before you today.

VAT on a whole horse

Firstly, explaining the VAT conundrum requires a good understanding of the more or less 'normal' situation that one person owns an entire horse. Having full ownership of a horse makes VAT life easy: first and foremost there is the fact that an intracommunity delivery of a physical good (a horse) between VAT-taxable persons benefits from the reversed charge mechanism. In the situation of an intracommunity delivery, not the delivery is the taxable fact, but the acquisition by the buyer, thus making the buyer responsible for payment of the VAT on the transaction. Because this VAT is considered both output-VAT and input-VAT at the same time, the VAT tax-return of the buyer is nil. An intracommunity delivery of a horse exists if the horse is sold by a VAT-entrepreneur in one EU-memberstate to another VAT-entrepreneur in a different EU-memberstate AND the horse is physically delivered from the former EU-memberstate to the latter. Both parties must have a valid EU VAT identification number and the seller must keep proof of delivery of the horse to that other memberstate. A detail often overlooked is that the EU VAT identification numbers must be of said former, respectively latter memberstates. This is because in the EU VAT-system, the goods are 'followed' from memberstate to memberstate, thus allowing the levy of VAT to take place in the country where the ultimate end-user 'consumes' the horse.

Consumption of a horse?

Now, please do not take this literally: the word 'consumption' must be read according to its meaning in the EU VAT Directive, which in that context means the ultimate consumer using the good. More or less comparable to an end-consumer buying a car or bicycle. Assuming the VAT-entrepreneur who has bought the horse in the example above sells the horse to an end-consumer in that EU Memberstate, he will charge the VAT-rate applicable in that country and pay the VAT as 'output VAT' to the local tax-authorities.

Moving horses between EU-memberstates

The moving of goods from one memberstate to another by a VAT-taxable person, especially in the equine industry, happens all the time. Taking a horse to competition, having the horse trained or treated in a different EU-memberstate? It is every day practice to most of our clients these days. Now beware, what follows might come as a bit of a shock for some of you: bringing a horse into another EU memberstate as a VAT-taxable person is also a taxable fact.

No sale of a horse, yet a VAT taxable fact? How is this possible? Has the EU legislater taken leave of her marbles? No, dear reader, she has not because the VAT-system is aimed to be a taxation of consumption of goods and services by the end-user/consumer and this VAT-burden is to be levied at the place of consumption. If a VAT-taxable person therefore brings a good (a horse) into another memberstate, the VAT-system is so organized that a subsequent sale of this horse in that memberstate will be taxable according to the local VAT-regime and rate. The VAT-taxable person who brings his good into a different memberstate shall have to register with the local tax-authorities in that other memberstate for VAT-purposes and declare the bringing of a horse from one memberstate to the other as an intracommunity delivery, and in that other memberstate as an intracommunity acquisition. In every day life, to many VAT-entrepreneurs this does not really represent a problem because there are a few exemptions to this rule, that are well cut to the equine business. The most important exemptions are

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goods that are brought into another memberstate to be worked on (maintenance/ training) by third parties, after which the horse returns to the memberstate where it came from. Also, if the horse is used for services to other parties (competing?) for a short while and afterwards returning to the memberstate where it came from is exempt. But, if the horse is stabled elsewhere, not temporarily, the bringing of a horse into a different memberstate is considered a taxable fact.

The VAT conundrum

Equipped with the knowledge described above, I now would like to introduce the VAT-conundrum when buying or selling a share in a horse. Selling a share in horse requires a transfer of (part-)ownership to be sure. This can be arranged in accordance with (civil) law and is ideally written down in an agreement that simultaneously stipulates the arrangements with regards to the sharing of costs and revenues, decision-making on training, stabling and caring for the horse and what not. It is clear that one can legally become part-owner in a horse but that does not automatically imply that the transfer of ownership-rights qualify as a 'supply of goods' in the meaning of the EU VAT directive. As explained above, for a supply to be recognized for VAT-purposes the acquiring party must obtain 'the right to dispose of tangible property as owner', which is not the case when a co-owner cannot freely dispose of his or her share in the horse. A practical solution often applied between VAT-entrepreneurs is to still charge VAT on the transaction. Because VAT-taxable persons do not experience VAT as a burden (thanks to the system of deduction of input-VAT from the output-VAT), this does not present a problem for either party and also tax-authorities do not really have a problem here, as there is no 'leakage' of VAT: as long as the horse is in the value-adding chain, there is always the latent VAT-claim on the horse in case the horse reaches an end-consumer.

Negative TAX-gap

If this practical solution is applied on an intracommunity delivery (and acquisition), however, the problem is that, as explained above, the transfer of co-ownership is not a 'supply of goods' according to the VAT Directive and can for this reason also not be deemed an intracommunity delivery (or supply). The seller retains (in this example) a 50% share in the horse. If the retained share in the horse is brought into that other memberstate, does that then also qualify as a taxable fact? This particular taxable fact is based on the words in the EU VAT Directive that state that transfer of goods, forming part of his business assets, to another state 'shall be treated as' a supply of goods. In other words: the transfer of a share in a horse may be a taxable fact due to a fiction ('shall be treated as'), but the corresponding internal acquisition of the share in the horse in the other memberstate would not qualify as an intracommunity acquisition, thus leaving a negative TAX-gap for this VAT-entrepreneur.

Is co-ownership a contractual cooperation?

Over the past few years, equestrian entrepreneurs have been subject of many cross-border audits from tax authorities and in our experience, tax authorities in different countries take different approaches to this situation. In one case, the solution for this situation was found in qualifying the co-ownership in a horse as a contractual partnership, rather than supply of goods. That 'fixed' incidental VAT charges on individual delivery of shares in horses, but left a void in the sense that in future situations it is unclear what a taxable fact would be upon leaving the contractual partnership in a horse, and what the basis (value) for taxation would be. This matter is not yet resolved and is subject of discussion between VAT-taxable persons and tax authorities. In a follow-up on this article, I shall elaborate on the co-ownership as a contractual partnership and the VAT implications of that, but for now this subject is hopefully brought to your attention. It may be prudent to discuss this with your tax adviser.

Summary

The transfer of a share in the ownership of a horse can legally be done in accordance with civil law, but that does not automatically imply that the transfer of said part-ownership qualifies as an 'supply of goods' for VAT purposes. As long as transactions are done between VAT entrepreneurs, practical solutions are usually found, but in essence there remains a difficult question how to correctly deal with a transfer of a share in a horse: no case-law exists yet where it concerns co-ownership in horses and tax authorities in various memberstates take different views on how to qualify delivery of a share in a horse. In a follow-up article, I shall elaborate on the contractual cooperation that is the co-ownership of a horse and the consequenses thereof for VAT purposes.

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If you have any questions and/or comments after reading this article, we would be happy to hear from you. You can also contact us for all equine-law related questions or matters. Please contact us via info@europeanequinelawyers.com or by telephone +31-(0)135114420.

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