VAT UPDATE
APRIL 2018

Covering material from January – March 2018

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VAT Update April 2018

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1. INTRODUCTION

These notes contain a brief summary of some of the main VAT developments in the last three months – Tribunal and Court decisions, changes in legislation, Customs announcements. They are divided as follows:

- outputs generally;
- land and property;
- international matters;
- inputs generally;
- administration.

The same main headings will be used each quarter. If nothing has happened under a particular heading in a particular quarter, that heading will be omitted – but all headings will still carry the same number. That is why some headings are included with "nothing to report".

1.1 Appeals pending

It is not possible to compile a comprehensive list of cases under appeal, and some of those which are thought to be still "live" may be dropped without a hearing. The following is compiled from several sources, and is just an approximate guide to some of the arguments that do not appear yet to have been finally settled:

The HMRC website section which reports the progress of appeals originally said that it would be updated monthly, but it appears to be less frequent or regular than that. The list says "updated 28 February 2018".

Several of the "decision is final" items are still on the website list, but where they have already been reported in the update they are not reproduced below.

http://www.hmrc.gov.uk/vat/vat-appeal-update.pdf

- *DPAS Ltd*: HMRC appealed points from FTT decision to Upper Tribunal, which decided to refer questions to CJEU after considering the judgments in *Bookit* and *NEC* (Case C-5/17: hearing 24 January 2018, decision awaited).
- *Findmypast Ltd*: HMRC have applied to the Court of Session for leave to appeal to the Supreme Court against the CS ruling that "credits" did not trigger a tax point at the time they were purchased.
- *Gala 1 Ltd v HMRC*: Court of Appeal due to hear taxpayer's appeal against refusal of claims for repayment of output tax on bingo – FTT/UT both ruled that only the representative member of the group could make the repayment claim (not on the HMRC list).
- *Hotels4U.com Ltd*: HMRC have applied for the time limit to appeal to be extended while waiting for FTT to rule on whether to refer questions to the CJEU (time limits extended for this and similar appeals to 5 March 2018).
- *Jigsaw Medical Services Ltd*: HMRC are appealing FTT's decision in favour of taxpayer in case about whether provision of ambulances

qualified for zero-rating as passenger transport (hearing date to be confirmed).

- *KE Entertainments Ltd*: HMRC have appealed to Court of Session against UT decision that change of calculation of bingo takings constituted an "adjustment of consideration" within reg.38, rather than leading to a time-capped repayment claim under s.80 (hearing date to be confirmed).
- *LIFE Services Ltd*: partial win for HMRC in the Upper Tribunal; one point to be jointly decided in the Upper Tribunal with *The Learning Centre (Romford) Ltd* (hearing scheduled for December 2018).
- *Lowcostholidays and Lowcostbeds*: being heard with *Hotels4U.com Ltd* (time limits extended to 5 March 2018).
- *Marriott Rewards LLC and Whitbread Group plc*: both appellants' appeals dismissed by the FTT (TC05634) on place of supply issues. However, the FTT found against HMRC on the fundamental direction of supply point. Marriott and Whitbread have both appealed to the Upper Tribunal and HMRC have cross-appealed.
- *Mercedes-Benz Financial Services Ltd*: CJEU decision in favour of taxpayer reported in the January 2018 update; HMRC list notes only that the matter has been passed back to the referring court.
- *MG Rover Group Ltd*: taxpayer is appealing to CA for permission to appeal against UT's ruling that its *Fleming* claim could not succeed as it should have been made by the representative member of the group (hearing listed for January 2019).
- *Newey t/a Ocean Finance*: HMRC have been granted leave to appeal to the CA against the UT's decision that the FTT was correct to find that the appellant's offshore business arrangements were not an abusive practice (hearing January 2018, decision awaited).
- *Pacific Computers Ltd*: MTIC case remitted by the UT to differently constituted FTT for rehearing.
- *Privin Corporation Ltd*: the FTT found in favour of a MTIC appellant. HMRC were granted leave to appeal to the UT, but it was agreed that the case would be remitted to a differently constituted FTT for rehearing.
- *SAE Education Ltd*: company has been granted leave to appeal against CA's ruling that it did not qualify for exemption as a "college of a university".
- *Stoke by Nayland Golf and Leisure Ltd*: HMRC are appealing to the UT against the FTT's ruling that a members' club did not fall foul of anti-avoidance provisions and qualified for exemption (hearing date June 2018).
- *Summit Electrical Installations Ltd*: HMRC are appealing to the UT against the FTT's ruling that sub-contractor was entitled to zero-rate work on the basis that a building was "dwellings", even after the main contractor had presented a RRP certificate.
- *Taylor Clark Leisure plc*: HMRC have been granted leave to appeal against the Court of Session's ruling that the company was entitled to

a repayment based on a claim made by a former member of its VAT group registration (Supreme Court hearing listed for 11 April 2018).

- *Tesco Freetime Ltd and Tesco plc*: HMRC are appealing to the UT against FTT finding in favour of taxpayer in relation to tax treatment of loyalty points scheme (hearing date to be confirmed).
- *Totel Ltd v HMRC*: Supreme Court granted taxpayer leave to appeal against Court of Appeal's 2016 ruling on requirement to pay VAT before an appeal could be entertained (not on HMRC's list).
- *Volkswagen Financial Services (UK) Ltd*: Supreme Court has referred the main partial exemption issue to the CJEU but found against HMRC on a secondary issue (hearing of Case C-153/17 February 2018, decision awaited).
- *Wakefield College v HMRC*: the college has appealed to the CA against the UT's ruling that it would use its building for a business purpose and therefore did not qualify for zero-rated construction (hearing 7/8 February 2018, decision awaited).
- *Wetheralds Construction Ltd*: HMRC are appealing against the FTT's decision that certain works qualified for the lower rate as relating to insulation for roofs, not "insulated roofs" (hearing listed April 2018).

1.1.1 Decisions in this update

- *Dynamic People Ltd*: HMRC sought leave to appeal the FTT ruling that a special method continued until it was cancelled, even though the company had joined a group; the FTT decided to set aside its decision and rehear the case. Although the method had flaws, the FTT concluded that it produced a fair result and one that was more reasonable than the standard method, and allowed the appeal.
- *Frank A Smart & Son Ltd*: HMRC appealed unsuccessfully to the Court of Session against UT's confirmation of FTT ruling that costs of Single Farm Payment Entitlements were business overheads and deductible. HMRC's list states that HMRC are applying to the Court of Session for leave to appeal to the Supreme Court, and if successful they will apply for a reference to the CJEU.
- *London Borough of Ealing*: FTT referred questions to CJEU about exemption for local authorities providing sporting services: HMRC issued R&C Brief 6/2017 to acknowledge how they will deal with the consequences of the decision in favour of the borough.
- *Synectiv Ltd*: the FTT found in favour of a MTIC appellant. UT set aside the decision on "should have known" and the case was remitted to a differently constituted FTT for rehearing. The FTT considered the evidence in detail again and decided that HMRC had not shown, on the balance of probabilities, that there was no possible explanation for the transactions other than fraud; the appeal was allowed again.
- *The Chancellor, Masters & Scholars of The University of Cambridge*: HMRC appealed against the UT's decision that VAT incurred on investment management was residual input tax of the whole operation; the CA decided to refer questions to the CJEU.

2. OUTPUTS

2.1 Scope of VAT: linking supplies to consideration

2.1.1 Branches and subscriptions

A company limited by guarantee was incorporated in 2009, as a successor to an unincorporated association, to represent the interests of some 83,000 occupational pensioners. It collected subscriptions from its members and distributed some of those subscriptions to branches as a "branch rebate". HMRC ruled that the rebates were in fact consideration for taxable supplies (to be apportioned between zero and standard rated) made by the company to its members.

The company appealed to the FTT, arguing that the branches were autonomous entities, and the rebates were amounts collected on their behalf. They were therefore remitted to the branches as disbursements, and were not part of the company's taxable turnover. The FTT had to determine two issues:

- whether the branches were independent of the company;
- whether the rebates were part of the membership subscription, or could be regarded as a separate amount collected on behalf of the branches.

The disputed ruling was made in 2011, confirmed by letter in 2013 and on review in 2014, and came before the Tribunal in November 2017. The decision opens with the following curious statement:

"*Neither party could assist by giving an indication of the amounts at stake in the appeal. NFOP's understanding is that, whatever the outcome of the appeal, they will be due a refund of VAT from HMRC because of a (separately agreed) change in the method of apportionment between standard and zero rated supplies. As I understand it, the appeal is being brought principally to establish the position for the future and because both parties regard the issues as one of principle that should be resolved. From HMRC's perspective the first issue at least is clearly also potentially relevant to the VAT treatment of other organisations.*"

To add to the complexity, there were differences between branches that made it possible for different decisions to be reached in relation to different parts of the organisation. HMRC wanted the FTT to make decisions about individual branches.

The judge reviewed the history of the organisation, which dated from the 1930s. Members were invited to join a branch when they joined the "head office". There were 270 branches in 1955, 240 in 1971, and 139 in September 2016. Since the company was formed, some branches had closed but no new ones had opened.

Originally, branches had collected the subscriptions and remitted an affiliation fee to the central association. Since the 1970s, a number of different arrangements had subsisted:

- many members paid their subscriptions directly to the company by deduction from their pensions – the pension providers usually

insisted on paying to the central organisation rather than to the branch;

- some members still paid to their branches, which remitted the amount after deducting the rebate;
- some members paid their subscriptions directly to the company by direct debit rather than by deduction;
- a separate category of "friends" were members only of the branches, and no subscription was received by the company, although it maintained records of such people.

The judge went on to examine the constitution of the company and the regulations governing the branches in some detail. She noted that all branches have their own bank accounts to which the rebate was remitted, and they all incur expenditure in their own name. They all prepare accounts to show what they have done with their funds; none has turnover above the VAT registration threshold.

The judge considered the law on taxable persons, and noted that the PVD required them to "independently carry out an economic activity". The VATA recognised the possibility that an unincorporated association could be a taxable person. There was relatively little case law on the issue, but the *Skandia* (Case C-7/13) and *FCE Bank* (Case C-210/04) cases referred to the issue of whether the branch bore the economic risks of its own activities. In *Gmina Wroclaw* (Case C-276/14), the CJEU considered whether a municipality and its budgetary entities (including schools, cultural centres and police services) should be regarded as the same taxable person. The budgetary entities did not have separate legal personality. The court decided that separate legal personality was not an absolute requirement, but again decided that the lack of economic risk meant that the budgetary entities were not independent.

A UK precedent was found in *Old Parkonians Association* (VTD 10,908), which concerned an association and three affiliated sports clubs were a single taxable entity. It was held that the clubs were all independent, because they had their own officers, set their own subscriptions, prepared their own audited accounts, and appeared under the association's constitution to have their own assets.

A number of other UK cases were considered, including the House of Lords decision in *Eastbourne Town Radio Cars Association*. This established the key principle that, to be a "person", an unincorporated association had to be comprised of a number of legal persons (individuals in this case) who have entered into a contract between themselves, under which they have agreed to be associated and have agreed to certain mutual rights and obligations. So as a minimum there must be a contract between the members, who must by definition be an identifiable set of persons. Any assets of the association will be owned on trust for the members and liabilities will be governed by the ordinary law of contract and agency. Beyond this, there were no necessary or sufficient requirements. Lord Hoffmann had listed features that were normally present, but they were not a checklist. Nevertheless, the presence of many of these factors convinced the judge that the branches were "persons".

She then turned to the question of economic independence. She examined the relationship between the branches and the company, and concluded for a number of reasons that they were independent of it. This view was strengthened by the fact that they predated it; there was an existing branch structure before the company was formed. Although the branches operated under the umbrella of the company, they were not controlled by it in the direct manner that HMRC contended for.

Having found for the appellant on the issue of independence, the judge found for HMRC on the agency issue much more briefly. She listed 9 reasons for considering the full subscription to belong to the company. These included:

- the legal terms on which the subscriptions were paid to the company, which were determined by the company's own constitution – that was the relevant contract for determining the VAT position;
- the constitution referred to the company making reasonable charges to members, and did not indicate that a separate amount would be collected and passed on to branches;
- the level of subscriptions and the rebate were set by the company in general meeting, not independently by the branches;
- members who did not join a branch did not enjoy a reduction in their subscriptions;
- friends' branch subscriptions were restricted to twice the equivalent member rebate, which suggested that non-voting friends were charged twice as much as full voting members – that did not support a "commercial and economic reality" that the rebate was actually a separate amount belonging to the branch.

The decision in HMRC's favour was given in principle only, because the amounts involved had not been argued before the judge. She issued case management directions about the further resolution of the dispute. She noted that she had made no decision about the nature or treatment of the rebate itself in the hands of the branch – there had been some discussion in the hearing about whether this was third party consideration for a supply by the branch to its members, or a subsidy that was outside the scope of VAT. If the parties could not agree on this, a further hearing might be required.

First-Tier Tribunal (TC06305): *National Federation of Occupational Pensioners*

2.1.2 Economic activity?

A non-profit company, wholly owned by a municipality, entered into a contract with that municipality in July 2007 to carry out certain public tasks on behalf of the municipality. It received payment and was allowed to use some of the municipality's assets. The tax authorities ruled that it should have charged VAT. It argued that it was carrying out public services and was being paid a grant. Questions were referred to the CJEU.

The Court ruled that the activities of the company were economic activities within art.2 PVD. The company would only be treated as a non-

taxable entity within art.13 PVD if it was a body governed by public law and carried out in the capacity of a public authority. It did not enjoy the rights and powers of public authorities that were enjoyed by the municipality itself. Subject to confirmation of various matters of fact and law by the referring court, the decisions of the tax authorities were correct – the activities were supplies within the scope of VAT.

CJEU (Case C-182/17): *Nagyszénás Településszolgáltatási Nonprofit Kft. v Nemzeti Adó- és Vámhivatal Fellebbviteli Igazgatósága*

2.2 Disbursements

Nothing to report.

2.3 Exemptions

2.3.1 Insurance?

A company offered customers the experience of a track day driving "supercars". If the car was damaged, the driver was liable for the first £2,500 plus VAT of the costs of repair; a collision damage waiver could be purchased for £25 – £30 to negate this possibility. The experience was often purchased in advance in the form of a voucher to be given as a present; the CDW would be purchased separately by the driver on the day.

The company treated the receipts for CDW as exempt. HMRC opened an enquiry in 2015 and pointed out that car hire companies do not treat CDW in this way. It is not underwritten by an insurance company, and no claims are made; it is simply a payment by the driver in return for which the hire company agrees not to make claims. It is commonly treated as VATable.

By 2016, the company had approached its underwriters and had arranged cover for its own liability to pay the policy excess in the event of vehicle damage – in effect, the £2,500 that it would otherwise be entitled to collect from the driver. Judge Poole noted that the premium appeared very high in relation to the risk, and concluded that a major factor in obtaining this insurance was to strengthen the argument with HMRC that it was in fact exempt.

HMRC's counsel argued that a contract of insurance required three elements: it must provide that the assured will become entitled to something on the occurrence of some event; the even must be one which involves some element of uncertainty; and the insured must have an insurable interest in the subject matter of the contract. The company's counsel submitted that "insurance transaction" was a free-standing EU law concept, as referred to in the CJEU judgment in *Card Protection Plan*: "…the essentials of an insurance transaction are, as generally understood, that the insurer undertakes, in return for prior payment of a premium, to provide the insured, in the event of materialisation of the risk covered, with the service agreed when the contract was concluded." She

argued that the arrangement in the present case was similar to the “block policy” in *CPP* that the House of Lords had concluded constituted an exempt supply of insurance.

The judge considered that the appellant’s interpretation was to be preferred. However, the question remained whether the appellant made a supply of that description. For the period before the company insured the risk, the judge was satisfied that it did not do so. The payment of CDW by a hirer was similar in effect to the payment of an insurance premium, but legally it simply varied the liabilities of the parties under the contract for hire. It was part of that contract and not a separate supply of insurance.

After the company purchased its own insurance policy, the contractual position between itself and its customers was unchanged. The policy was not a block policy of the type featured in *CPP*: the company was “the insured”, and the contracts between the company and the hirers remained exactly the same as before. The company was neither acting as an insurer, nor acting as an insurance broker or agent on behalf of its customers.

The appeal was dismissed.

First-Tier Tribunal (TC06311): *Supercar Drive Days Ltd*

2.3.2 Advanced learner loans

HMRC have issued a Brief to clarify their policy on the receipt of student loans by educational establishments that are not “eligible bodies”. Because student loans are provided by the Student Loans Company pursuant to a contract between the student and the Secretary of State for Education, and are repayable by the student, they do not constitute grant funding. They are therefore consideration for a supply of education to the student, and they are taxable at the standard rate unless the provider is an eligible body within VATA 1994 Sch.9 Group 6.

This policy has immediate (and presumably retrospective) effect, because HMRC are only clarifying what they have always believed to be the correct treatment. They have issued the Brief because they are aware that the loans have been treated inconsistently by taxpayers.

R&C Brief 2/2018

2.3.3 Affiliation fees for sports clubs

The extra-statutory concession enabling profit-making sports clubs to treat affiliation fees charged by a governing body as exempt from VAT (paragraph 3.6.2 of VAT Notice 701/45) will be withdrawn with effect from 1 April 2018. HMRC consulted on the withdrawal of this concession between January and March 2017.

The concession aimed to put profit-making commercial clubs in a similar position to non-profit making clubs, so that they didn’t need to account for output tax on the fee charged. It achieved this by allowing profit-making commercial clubs to treat these re-charges to their members as though they were disbursements. However, as such re-charges of affiliation fees are not legally disbursements, the concession goes beyond HMRC’s discretion and is being withdrawn with effect from 1 April 2018.

The Brief publicising the change notes that recharges of affiliation fees by a profit-making club will have to meet the conditions of Notice 700 para.25.1.1 if they are to be treated as exempt disbursements. Charges by a non-profit making sports club will remain exempt, whether or not they constitute disbursements; however, if they do not constitute disbursements, they will have an effect on partial exemption calculations as they will be part of the exempt turnover of the club.

R&C Brief 1/2018

2.3.4 VAT treatment of sports facilities by local councils

HMRC have changed their policy on the VAT treatment of local authorities' supplies of sporting facilities, following the CJEU judgment in *Ealing London Borough Council* (Case C-633/15). Local authorities may now choose to exempt such supplies and make a claim in respect of past accounting periods, provided they continue to exempt supplies for future periods. Alternatively, local authorities can continue to tax supplies of sporting services under current UK law, recovering input tax as appropriate.

Local authorities are entitled to recover any net over-declarations they have made as a result of having treated the supplies as taxable rather than exempt. The net over-declarations are calculated after deducting from the over-declared output tax any input tax wrongly claimed by prescribed accounting period on the assumption that the supplies in question were taxable and not exempt, unless that input tax is treated as insignificant in accordance with paragraph 8.2 of VAT Notice 749 *Local authorities and similar bodies*.

HMRC will now process claims made by local authorities on same basis as the *Ealing* case, subject to satisfactory verification of the amounts. They reserve the right to refuse claims on the grounds of unjust enrichment where they are able to show that the claimant passed the economic burden of the VAT charge on to their customers.

Local authorities with over declarations of output tax within certain monetary limits may wish to correct any errors on their VAT returns under SI 1995/2518 reg.34 rather than submit a formal claim under s.80 VATA 1994 to HMRC. However, in doing so they would not receive any interest. Further information on the monetary limits and which returns may be adjusted is available in Notice 700/45 *How to correct VAT errors and make adjustments and claims*.

HMRC also include a warning that a claim submitted without exercising due care may be subject to a penalty.

R&C Brief 6/2017

Further details on the mechanics of claims and particular types of charges that are and are not covered are given in an Information Sheet. For example:

- charges made to an unincorporated society for participation in sport by its members will be treated as supplied to the members;
- coaching sessions are not treated as sporting services, but may qualify for the education exemption;

- letting of sporting facilities is not covered by the exemption for sport and must be considered in relation to the exemption for land;
- related supplies such as catering, goods and use of sauna facilities must be excluded from claims.

The Information Sheet also gives guidance on the effect on input tax, including the Capital Goods Scheme.

VAT Information Sheet 8/2017

2.3.5 Cost sharing groups

HMRC have published a Brief and an Information Sheet in response to the various decisions of the CJEU about cost sharing groups (CSGs):

- *Commission v Luxembourg* – Case C-274/15
- *Aviva Towarzystwo Ubezpieczen na Zycie S.A. w Warszawie (Aviva)* – Case C-605/15
- *DNB Banka AS (DNB)* – Case C-326/15
- *Commission v Germany* – Case C-616/15

The decisions showed that the CJEU considered the cost-sharing exemption (CSE) to be more restricted than is allowed under UK law. HMRC say that the exemption will now only be permitted for certain exemption groups in VATA 1994; members located in the UK; and instances where no uplift has been charged. HMRC are still considering the impact of the judgments on the test for ‘directly necessary’ services, and on the social housing sector.

The CJEU held that the CSE should only apply to bodies that were exempt within art.132 PVD, not within art.135. It will therefore be restricted to:

- postal services (Group 3)
- education (Group 6)
- health and welfare (Group 7)
- subscriptions to trade unions and professional bodies (Group 9)
- sport (Group 10)
- fund raising by charities (Group 12)
- cultural services (Group 13)

The judgments did not cover non-business activities and therefore CSGs engaged in these activities are unaffected by this change. Housing Associations can continue to apply the CSE for the time being until HMRC issue more guidance.

Revenue and Customs Brief 3/2018

The Information Sheet sets out transitional arrangements until 31 May 2018 for cost sharing groups that have applied the exemption correctly based on earlier guidance. However, in the case of avoidance or abuse, HMRC will apply the court rulings from the date they were issued.

The IS analyses the differences between the judgments and the UK approach in some detail:

- *Luxembourg* – showed that the UK was wrong to allow members of a group to have significant taxable activities (15% in the UK, 30% in Luxembourg);
- *Aviva* and *DNB* – showed that the UK was wrong to allow any exempt entity to join a group, in particular financial and insurance businesses;
- *DNB* – the A-G's opinion was that the exemption could not apply where any uplift was applied, even if this was a transfer pricing adjustment required by the direct tax legislation of the country;
- *Germany* – confirmed that the exemption should apply to the whole of art.132, not to a narrower set of activities.

HMRC concluded that the A-G's opinion in *Aviva* and *DNB*, that the exemption could only apply to group members within the same member state, was consistent with the UK law and approach.

Services that are invoiced or paid for before 31 May 2018 will continue to benefit from the exemption in accordance with previous guidance, but only to the extent that they are actually supplied before that date (to prevent forestalling prepayments). Where an existing CSG has applied the previous guidance correctly, and foresees a significant difficulty in applying these transitional arrangements in the permitted timeframe, they should contact HMRC by 1 May 2018. These CSGs will need to explain the circumstances and provide evidence of any particular difficulties they foresee. HMRC will then consider each case on its own merits. If HMRC are not contacted by 1 May 2018 the revised policy must be applied from 1 June 2018.

HMRC are considering how the judgments impact on CSGs set up by housing associations and will give more guidance at a later date. The previous guidance continues to apply to those CSGs that applied it correctly until HMRC gives more guidance later in the year. Any changes will include similar transitional arrangements to those set out above, but these may be applied if necessary to the period from the date of the IS.

HMRC are also considering the impact of the *Luxembourg* case on the test of "directly necessary services", where there is minor taxable use. In the VAT Cost Sharing Exemption Manual, CSE3740, where a member of a CSG has either exempt or non-business activities (or both) that form 85% or more of their total activities, all the supplies they receive from their CSG are treated as being directly necessary for their exempt or non-business activities. The infringement proceedings by the Commission mean that HMRC must now consider what changes need to be made to the guidance to comply with that judgment. As stated in CSE3720, that consideration will include consideration of transitional arrangements to facilitate an orderly transition. For now, CSGs can continue to apply the 85% test.

HMRC's previous guidance excluded CSGs and members located in countries outside the EU. However it allowed them to be located in other member states subject to the other conditions being met. The CSE will now be restricted to UK based CSGs and members. However, CSGs and

their members located outside the UK but within the EU may be permitted to apply the transitional arrangements where all of the following conditions are met:

- a CSG is located in another member state;
- the CSG has implemented the exemption in accordance with HMRC's previous guidance (where this is different in the member state where it's located);
- the CSG can demonstrate to HMRC's satisfaction that there is no distortion of competition arising, for example because of a mismatch in tax treatment between the UK and the member state in which the CSG is located – any CSG affected that wants to take advantage of the transitional arrangements should write to HMRC by 1 May 2018 setting out their cross-border arrangements.

VAT Information Sheet 2/2018

2.4 Zero-rating

2.4.1 Digital newspapers

The publisher of *The Times*, *The Sunday Times* and *The Sun* claimed zero-rating for the daily digital editions of its newspapers on the grounds that they were "newspapers" and therefore covered by VATA 1994 Sch.8 Group 3 item 2, or else had to be given the same treatment as the paper versions on the grounds of fiscal neutrality. The FTT (Judge Brannan) heard appeals against decisions covering the periods September 2010 to June 2014 and January 2013 to December 2016.

The judge noted the history of the relief for newspapers, which were free of Purchase Tax from 1940 to 1973; this was continued for VAT under the authority of what is now PVD art.110, which allows Member States to retain "exemption with deduction of input tax" for categories of supply that were so treated on 1 January 1991, provided that the rules were adopted for clearly defined social reasons and for the benefit of the final consumer, and were in accordance with Community law. The social policy required by Article 110 which lay behind the UK's decision to zero rate newspapers and books etc was the promotion of literacy, the dissemination of knowledge and democratic accountability by having informed public debate.

The judge reviewed the production of the titles and compared the printed and digital versions. It was suggested that the characteristics of a "newspaper" included that it was an "edition-based" publication, rather than comprising "rolling news" such as might be found on a website. The digital versions of these titles satisfied that definition.

The company's counsel argued that the purpose of the legislation would be served by treating digital publications as zero-rated. He also suggested that the 1973 wording should be updated to apply to present-day technology, rather than being frozen at the time it was written.

HMRC's counsel responded that the wording of Group 3 clearly referred to supplies of goods, not services. There was no doubt that digital newspapers were electronically supplied services (the rules on place of supply in Sch.4A include them in a definition). There was also a clear distinction in the EU legislation; allowing zero-rating would be an impermissible extension of zero-rating.

The judge agreed with HMRC that the implication of the wording of Group 3 was that it related to goods. The idea of legislation being interpreted in accordance with current technology ("always speaking") was set out in a speech by Lord Wilberforce in *Royal College of Nursing v DHSS* (1981), and it excluded the situation in which there was an apparent intention that the law should be restrictive in its operation. As zero-rating was an exception to the general rules of VAT, it was not possible to use a purposive interpretation to extend the scope of the relief beyond the straightforward meaning of the words.

The judge went on to consider the issue of fiscal neutrality. Although he was satisfied that the digital editions satisfied similar needs of customers to the print editions, he did not accept that this was enough to require an extension of the scope of the legislation. In accordance with the *Deutsche Bank* decision of the CJEU, fiscal neutrality could not override the clear words of the law; the 1991 "standstill" in art.110 was such a clear requirement.

HMRC's counsel sought to rely on the recent Commission consultation on the possibility of extending reliefs to digital publications, which implied that they were not currently entitled to the same treatment, and also on art.98, which excluded digital publications from the lower rate. The judge did not consider either argument was particularly relevant in the interpretation of UK law on zero-rating.

Nevertheless, he accepted HMRC's fundamental position and dismissed the appeals.

First-Tier Tribunal (TC06385): *News Corp UK & Ireland Ltd*

2.4.2 Bicarbonate of soda

HMRC ruled that supplies of bicarbonate of soda did not qualify for zero-rating as "food of a kind used for human consumption". This led to assessments for VAT and interest totalling over £300,000. The company appealed to the FTT, arguing that bicarbonate of soda was a food ingredient.

Both parties relied on expert evidence. The company put forward statements from employees of its customers and its suppliers about how the product was sourced and marketed. HMRC argued that the liability depended on the nature of the product, not on how it was marketed.

The company pointed to a number of other products where HMRC's treatment was inconsistent. Salt could be zero-rated in catering packs but standard rated in bulk. Baking powder, of which the principal constituent is bicarbonate of soda, is zero-rated. Other products such as lemon juice and vinegar can be used as food or for other purposes, but are zero-rated.

The judge noted that the decision should be made on the basis of whether the ordinary person in the street would regard the item as "food".

Precedent decisions showed that this was a question of fact, and they should not be elevated into decisions of principle. However, there were principles that could be applied:

- products did not have to be edible without further preparation or on their own to qualify as food;
- items that contribute to the production of food also qualify as food;
- the recipient does not have to be the final consumer of the food.

Although the judge said that this ought to be a short question requiring a short answer, he gave a detailed explanation of his reasons for finding that bicarbonate of soda, sold in small quantities in the baking section of supermarkets, should be zero-rated. The decision also contains discussion of a number of other products and possible points of argument.

First-Tier Tribunal (TC06296): *Phoenix Foods Ltd*

2.4.3 Powders for mixing

A company sold powdered products (Nesquik) to be added to milk. It submitted a repayment claim on the basis that these powders should have been zero-rated as “food for human consumption” (item 1 Sch.8 Group 1). HMRC refused the claim, stating that the powders were covered by excepted item 4 “powders for the preparation of beverages”. The company argued that “beverages” excluded “milk and preparations and extracts thereof” (number 6 in the list of items overriding the exceptions), and that the result of mixing the powder with milk was just flavoured milk, not some other kind of beverage.

The company contended that the purpose of zero-rating milk and milk products was to promote the health benefits of drinking milk. That was part of its own strategy in manufacturing and marketing Nesquik. Also, ready-mixed milk drinks were zero-rated, and fiscal neutrality demanded that its products should be treated in the same way. Nesquik’s chocolate-flavoured powder was covered by item 5 overriding the exceptions: “Cocoa, coffee and chicory and other roasted coffee substitutes, and preparations and extracts thereof.”

The FTT (TC04944) examined the facts in detail, including the history of Nesquik, the comparison with a chocolate version, and ready-made versions of competing products which were produced in evidence.

The first conclusion concerned the interpretation of “beverage” and the interaction between excepted item 4 and overriding item 6: the items were specific, rather than general rules of interpretation, and the exception was not to be interpreted as “beverages other than milk and preparations and extracts thereof”. A powder that is sold separately and has to be mixed with milk is not the same as milk. There was no indication that Parliament must have intended the provision to be extended that far.

Secondly, the FTT concluded that a glass of flavoured milk is a “beverage”, and Nesquik is used to “prepare” it. The appellant’s argument that “no new beverage was created” was rejected.

The FTT considered that the social policy underlying Group 1 was not “to promote the health benefits of milk”, but rather “to remove VAT from

basic foodstuffs such as milk". There was nothing to indicate that a powder sold separately was subject to the same considerations.

The FTT also examined the fiscal neutrality argument in detail, considering in particular the decisions in *Marks & Spencer* and in *Rank*. The company put forward two relevant comparisons: its own chocolate-flavoured Nesquik powders, and competitors' ready-made products. Although the FTT accepted that it was relevant to consider fiscal neutrality, and the principle might require zero-rating to be extended to a competing product, it rejected the argument that these were appropriate comparators. A chocolate-flavoured drink was not similar to a fruit flavoured one – for example, chocolate Nesquik might be drunk hot or cold. A ready-made drink was not the same as a powder that could be kept for a long time and added to fresh milk that had to be purchased separately.

At the conclusion of 210 paragraphs, the FTT rejected the appeal. The company appealed to the Upper Tribunal. The Upper Tribunal noted the history of the legislation, tracing its source to the Purchase Tax Act 1963, which specified 36 groups of items on which purchase tax was levied. Excepted items 1, 2, 4, 5 and 6 are derived from those groups. The wording was little changed when the Finance Act 1972 introduced VAT in place of purchase tax; there were amendments in 1993 to deal with the *Tropicana* decision (so that pure orange juice, which was held not to be "manufactured", became standard rated); and further amendments in 2012 to clarify the liability of sports drinks.

The Tribunal went on to reconsider the company's two main arguments:

- that "beverage" in excepted item 4 did not include milk, so the powder was not for the "preparation of a beverage";
- that, if milk was a beverage, adding flavour and colour to milk did not create a different "beverage", but simply affected the milk, which was zero-rated.

The company's counsel argued that a purposive interpretation of the legislation should be applied. The history of the legislation showed that Parliament had not intended to tax milk or milk-based drinks. The anomalous different treatment of ready-mixed milk drinks and of chocolate Nesquik would be avoided.

The Tribunal rejected these arguments. There was no general principle that milk-based products were intended to be free of tax – ice cream and frozen yoghurt had always been excepted items, and the 2012 changes would certainly tax powders to be mixed with milk to make a protein-rich sports drink. The case law did not reveal any consistent policy underlying the rules on food.

Contrary to the appellant's arguments, the Tribunal favoured a step-by-step reading of Group 1. The natural sense of the words required consideration of:

- whether the "thing" was comprised in the General Items (ZR);
- then whether it was comprised in the Excepted Items (not ZR);
- then whether it was comprised in the Overriding Items (ZR again).

Like the FTT, the UT saw no reason to exclude milk products from "beverage" in Excepted Item 4, nor to exclude powders for preparation of milk drinks from "powders for the preparation of beverages". No wider intention to zero-rate anything made of milk could be sustained.

HMRC's counsel had pointed out a number of other anomalies in Group 1 that countered the appellant's argument that a "sensible result" should follow:

(1) fruit salad is zero rated; smoothies made from fruit are standard rated (*Innocent Ltd*);

(2) oranges are zero rated; fruit juices are standard rated;

(3) turnip crisps are zero rated; potato crisps are standard rated (*Procter & Gamble*);

(4) chocolate cake is zero rated; chocolate biscuits are standard rated;

(5) frozen yoghurt dessert is standard rated; yoghurt which is frozen but is to be eaten above freezing point is zero rated.

In relation to the second argument, the Tribunal noted that Nesquik powder has no other use than to be mixed with milk. It is not like sugar or Worcester sauce, which the appellant's counsel argued could be compared and which did not create new beverages when mixed with tea or with tomato juice. For the same reasons as the FTT, the UT concluded that Nesquik powder was "for the preparation of beverages".

The appeal was dismissed.

Upper Tribunal: *Nestlé UK Ltd v HMRC*

2.4.4 Hot food

A company appealed against an assessment for £114,122 for periods 11/12 to 11/16. This charged VAT on food claimed by HMRC to have been "hot takeaways" and therefore excluded from zero-rating.

The company operated a takeaway food outlet in the Arndale market in Manchester, providing African and Caribbean cuisine such as rice, wraps and curries. This was cooked in the morning and transferred to "gastronorms" which sat in a bain-marie for serving purposes. Food hygiene regulations required that displayed food be maintained at 63 degrees; the company's directors argued that they did not intend to serve hot food, and that the food should not be served hot as it would lose its unique flavour. They claimed that the ambient temperature was 28 – 30 degrees; the food was cooled to 20 degrees after cooking, and "would not have been re-heated to the temperature of the bain-marie" by the time it was sold.

Judge Fairpo considered that it was "basic physics" that food kept in a 56-degree bain-marie for an hour would be heated to above the ambient temperature. She considered that the purpose of the appellant appeared to be that the food would be eaten shortly after sale (napkins and forks were provided), and there was therefore an expectation that it would be consumed at above the ambient temperature. Condition (c) of Note 3B Group 1 Sch.8 was also met, because the food was kept hot after cooking by the bain-marie.

The appeal was therefore dismissed insofar as it related to the definition of "hot food" in the legislation. The judge noted that HMRC agreed to accept that a proportion of the supplies could be attributed to cold foods if the appellants could provide evidence as to the appropriate apportionment. She left it to the parties to agree the amount which the appellant must pay in respect of the VAT on the supplies of cooked food, and directed that a further hearing would determine the matter if agreement could not be reached.

First-Tier Tribunal (TC06382): *Pegasus (Manchester) Ltd*

2.5 Lower rate

2.5.1 Ski lifts

A company operated an indoor snow dome and conference facility ("the Snow Dome"). This has lifts which are used to transport passengers to the top of the two indoor ski slopes. The primary retail shopping centre is in a separate building from the leisure complex. HMRC ruled that lift passes were not eligible for the lower rate of VAT and raised assessments for periods 1/6/2013 to 30/11/2014 (£156,160) and 1/12/2014 to 29/2/2016 (£138,555). The company appealed.

The company had started to account for lower rated VAT from 1 June 2013, shortly afterwards also claiming a repayment backdated to 1 April 2013 (£20,097). Group 13 ("cable-suspended passenger transport systems") had been introduced to Sch.7A with effect from 1 April 2013.

HMRC argued that the lift passes were excluded by Note 1, which provided that the lower rate would not apply to the transport of passengers to, from or within a place of entertainment, recreation or amusement, by the person who supplies a right of admission to, or a right to use facilities at, such a place.

The company argued that sale of a lift pass did not constitute a right to use the facilities. It was not mandatory to buy a lift pass to access the facilities. In correspondence the company had argued that Scotland's other snow sports resorts applied the lower rate to their lift passes, but at the hearing the company did not seek to rely on fiscal neutrality.

Judge Anne Scott examined the way in which the business operated. She noted that the company earned its revenue from the sale of lift passes. Customers were entitled to borrow skis, boots, snowboards, poles and helmets without charge, and those bringing their own equipment did not receive any discount. It would in theory be possible for someone with their own equipment to use the facilities without buying a lift pass and without using the lift, but this was not advertised.

The judge noted that both parties concentrated on the nature of the supply of the lift pass. She concluded that the supply made by the appellant when selling a lift pass was access to the lift for the duration specified on the pass. Anyone could access the slope but someone purchasing a pass, in doing so, acquired an ancillary contractual right to use the slope provided they behaved safely. The wording of Note 1 then clearly

applied: it was the appellant that supplied the right of admission to the place of amusement or recreation. It did not matter whether the price paid for that admission was included in the lift pass, or was not charged at all. The appeal was dismissed.

First-Tier Tribunal (TC06308): *Snow Factor Ltd*

2.6 Computational matters

Nothing to report.

2.7 Discounts, rebates and gifts

2.7.1 Rebates to third parties

A German pharmaceutical company was required by law to give rebates in respect of prescription drugs supplied:

- to persons covered by the statutory public health insurance – medicines were treated as sold to the public health insurance funds, and the rebates were paid to those funds;
- to persons covered by private health insurance – medicines were treated as sold to the individuals, who were reimbursed for their purchases by their insurers, and the rebates were paid to the insurers.

The tax authorities treated the two situations differently. The rebate paid to the public funds reduced the pharmaceutical company's taxable amount, because the public fund was in the supply chain; the rebate paid to the private insurers was not treated as reducing the taxable amount, because there was no chain of supply between the two companies. The company appealed, and questions were referred to the CJEU.

The referring court noted the case of *Ibero Tours* (Case C-300/12), in which a travel agent, acting as an intermediary, granted a rebate to the final consumer at his own expense. This did not reduce the taxable amount for anyone:

- the travel agent's taxable amount related to consideration received from the tour operator, so the rebate paid to the consumer was not a reduction of that consideration;
- the travel agent was not part of a supply chain between the tour operator and the consumer, so it was not possible to regard the repayment as affecting the taxable amount of the tour operator, even if the result was that the consumer appeared to pay less for the holiday.

The referring court considered that the present case was analogous, and as a result there should be no reduction in the pharmaceutical company's taxable amount. However, this appeared to be contrary to the principles of equal treatment and fiscal neutrality.

The court considered that art.90 PVD was engaged: there was a price reduction after the supply took place, in the form of the rebate. It was fundamental to the system of VAT that the taxable amount was the consideration actually received by the taxable person, after adjustment for such price reductions. The *Elida Gibbs* judgment affirmed the principle that similar goods sold within each country should bear the same tax burden whatever the length of the production and distribution chain.

That judgment did note that the law specifically related to the situation in which there was a contract between the parties – a rebate of the price paid by one to the other. However, the court had also commented that it was an expression of the principle of neutrality, and it should be applied in a way that achieved its objective rather than undermining it.

Even if the direct beneficiary of the supply of the medicines was the insured individual rather than the insurance company, that did not break the direct link between the supply of the medicines and the reduction in the consideration received for that supply in the form of the rebate. The fact that the private health insurer paid for the medicines meant that it should be regarded as the final consumer of those medicines, and the amount paid to the tax authority should not exceed the appropriate fraction of the amount paid by the final consumer.

Other analogous authorities included *Le Rayon d'Or* (Case C-151/13) and *International Bingo Technology* (Case C-377/11).

CJEU (Case C-462/16): *Finanzamt Bingen-Alzey v Boehringer Ingelheim Pharma GmbH & Co. KG*

2.8 Compound and multiple

2.8.1 Single supply, single rate

A company operated a sports stadium which incorporated the Ajax football club museum. It offered visits to the arena for an admission charge: the visit comprised a guided tour of the stadium and an unguided visit to the museum. The company took the view that the museum element was a lower-rated cultural supply, and sought to apportion the price for the whole tour between standard rated and lower rated elements. Questions were referred to the CJEU.

The court confirmed that a bundle of supplies that it would be artificial to split, or a compound supply where one element is ancillary to another, can only be charged at a single rate of tax, determined by the principal element of the supply, even if the price of each element could be identified.

CJEU (Case C-463/16): *Stadion Amsterdam CV v Staatssecretaris van Financien*

2.8.2 Books and courses

A college appealed against an assessment for £275,273 (out of a larger amount of £301,131) relating to periods from 10/12 to 10/15. The college had treated its fees as two-thirds standard rated courses and one-third zero-rated books. This apportionment had not been agreed with HMRC, but HMRC did not initially challenge it. Following enquiries, HMRC concluded that the college was making a single supply that should be standard rated.

The college put forward three grounds of appeal at the hearing:

(1) The college made separate supplies of educational services and books. The supplies of educational services should be standard rated. However, the supplies of books should be zero rated under item 1 Group 3 Sch.8 VATA 1994.

(2) If the supplies made by the college constituted a single supply, that supply was a supply of exempt educational services either on the basis that the supplies fell within item 1(a) Group 6 Sch.9 VATA 1994 on the grounds that the College was an "eligible body" within Note (1)(b) to Group 6; or, if not, on the basis that the supplies fell within art.132(1)(i) PVD, which should be given direct effect because of the UK's failure properly to implement that provision in its domestic laws.

(3) The UK had failed in its domestic laws to give effect to its obligations to provide free education under art.26(1) of the Universal Declaration of Human Rights 1948 and art.13(2)(c) of the International Covenant on Economic Social and Cultural Rights 1966. These obligations prevented the UK from imposing additional taxes, such as VAT, on providers of education.

Judge Greenbank noted that the company's first argument appeared simply to be that the supply included books. HMRC responded that there was no evidence that a separate supply was made, or a monetary value could be attached to it; there was a single supply from an economic point of view, and it should not be artificially split. The judge accepted HMRC's argument, because no evidence had been presented about the nature of the supplies or the way the courses were marketed to potential students. It was agreed that students were charged a single fee, and there was no opportunity to receive one part of the supply and not the other. The economic reality appeared to be that there was a single supply; the burden of proof was on the college to show that this was not the case, and it had produced no evidence to discharge that burden.

On the second ground, the college argued that it should be treated as an eligible body because it provided university level education. It was approved for the purpose of student loans and finance. HMRC accepted this, but argued that it did not meet the requirements of Group 6: the term "university" was not related to the level of education. The judge agreed with HMRC. The use of the word was regulated by English law, and the college was not a university according to the general understanding of the term. Although "university education" in art.132 PVD could be taken to extend the exemption to comparable courses, Member States were given some discretion to define the types of institution that could benefit from the exemption.

The judge also did not agree that the UK had failed to correctly implement the PVD. The case of *Minister Finansow v. MDDP sp z oo Akademia Biznesu, sp komandytowa* (Case C-319/12) showed that Member States had the option of excluding profit-making entities from exemption for educational services under art.132(1)(i). Member States should set the conditions for non-public bodies to be eligible for this exemption, and it was for the domestic courts to decide whether those conditions complied with EU law. The Court of Appeal had decided in *Finance & Business Training Ltd* (2016) that the UK's conditions were compatible with the PVD. In order to show that it ought to benefit from exemption, the college would need to show that it was objectively similar to those bodies that were recognised under Group 6, which went beyond simply arguing that it met the basic conditions of art.132(1)(i).

As regards the third ground of appeal, the judge agreed with HMRC that neither the UDHR nor the ICESCR were incorporated in UK law or enforceable in the Tribunal. The UK had signed up to an obligation to provide free education in the UDHR, but that related to primary and fundamental education, and such rights existed elsewhere in UK law. They had no bearing on the supplies of education at issue in this case.

The appeal was dismissed.

First-Tier Tribunal (TC06343): *Essex International College Ltd*

2.9 Agency

Nothing to report.

2.10 Second hand goods

Nothing to report.

2.11 Charities and clubs

Nothing to report.

2.12 Other supply problems

Nothing to report.

3. LAND AND PROPERTY

3.1 Exemption

3.1.1 Timeshares?

A company sold "fractional interests" in a high value property in Mayfair. In return for a substantial upfront price, a purchaser acquired the ability to occupy a residence in the property of a specified category for a maximum number of nights in each year until 31 October 2050, and to access a range of related benefits during that period. These included the option of exchanging stays in other properties and receiving rental income.

The company argued that it simply provided a licence to occupy land. It was not providing accommodation in "a hotel, inn, boarding house or similar establishment" (VATA 1994 Sch.9 Group 1 Item 1(d)), nor was it providing holiday accommodation.

HMRC responded that the appellant did not provide any interest in land capable of falling within the exemption, but rather a taxable service of a right to participate in a bundle of benefits. If it was a supply of land, it was excluded by item 1(d).

The marketing material and website testimonials showed that some customers regarded the property as similar to a luxury hotel, but others treated it as a "second home". The Tribunal did not consider this to be significant one way or the other.

The FTT (TC05318) went on to examine the agreements in detail. The company pointed out a number of significant differences between the rights of a member and the rights of a hotel customer. For example:

(1) Members are required to pay an Annual Residence Fee which covers all running costs of the property and a sinking fund to replace mechanical and other assets. There is no such overt contribution to such costs for hotel guests.

(2) Hotel guests pay a nightly fee only whereas members pay a substantial upfront purchase price plus the Annual Residence Fee.

(3) A hotel guest has no influence over costs whereas the members have some influence through the Members Committee which agrees the Annual Operating Budget and Annual Residence Fee.

(4) A hotel guest has the right to enjoy the residence for the period of the booking only whereas a member has rights to occupy up to 31 October 2050.

(5) A hotel guest cannot leave personal belongings between stays whereas a member can do so.

(6) Unlike a member, a hotel guest cannot rent his room or sell his right to occupy it or use his interest as security.

The appellant argued that the CJEU's decisions in *RCI Europe* (Case C-37/08) and *MacDonald Resorts* (Case C-270/09) showed that its supplies should be regarded as supplies of land. Several other precedents were cited in a comprehensive defence of the company's position.

Both sides agreed that it was necessary to consider the commercial reality and all the surrounding circumstances. The FTT considered that it was clear that the members were paying the substantial upfront price in return for the right to occupy a residence in a desirable location in the heart of Mayfair in London for a maximum period of time each year on an ongoing basis over many years. The use of other programmes offered by the manager was optional and secondary. Unlike *MacDonald Resorts*, there was certainty at the time of supply what property would be involved; that was enough to make it a letting of immovable property. There was nothing in the *Card Protection Plan* principles to change the nature of this principal supply.

The FTT went on to consider the "hotel exclusion". It noted that the CJEU had considered (*Blasi v Finanzamt Mnchen I*, Case C-346/95) "the duration of the stay" relevant in applying the exemption: temporary accommodation would compete with the hotel sector, and should therefore be taxable. A German rule requiring a six-month lease before exemption applied was held not to be incompatible with the Directive. The FTT rejected the appellant's arguments that the length of the agreement was relevant (many years) – it was the length of the stay in each year that suggested it should be treated as temporary accommodation similar to that supplied by hotels.

The FTT considered the differences between the rights of a member and a hotel guest, and between the rights of a member staying in the property and a non-member (who, it was accepted, would be paying for taxable hotel accommodation). Those differences did not seem as significant as the similarities. The hotel exclusion applied, and the appeal was dismissed.

The company appealed to the Upper Tribunal, which summarised the FTT decision as follows:

(1) First, the FTT decided that the supplies of the Fractional Interests fell, in principle, within the exemption from VAT provided for the leasing or letting of immovable property ("the land exemption issue").

(2) Secondly, however, the FTT found that the land exemption was excluded because the grant of the Fractional Interests was the provision of relevant accommodation in a similar establishment to an hotel ("the hotel sector issue").

(3) Finally, the FTT dismissed FPSL's argument that under the principle of fiscal neutrality the supplies of the Fractional Interests should be treated in the same way (in other words as exempt) as more traditional timeshare interests ("the fiscal neutrality issue").

In their response to the company's arguments, HMRC effectively cross-appealed the decision on "licence to occupy". The UT considered extensive arguments that the supply failed to meet the basic conditions for a letting of land, and rejected them. The grant of the Fractional Interest was the grant of a right to occupy a residence and to exclude others from enjoying such a right, and was thus within the concept of the "letting of immovable property" as described in *Temco*.

This was subject to the question whether that grant was a passive activity or whether it was outside the land exemption by reason of the company having added significant value to the supply because of the additional

facilities services and benefits available to members. This was considered by the CJEU in *Stade Luc Varenne* (Case C-55/14). The UT did not wholly agree with the FTT's reasoning in this area. The FTT had concluded that the company had contracted to supply the services of the manager to its customers, and sub-contracted that work to another related company; the UT held that the actual arrangement was more similar to *Telewest*, in that the management services were supplied separately by a related company and were not part of the obligations that fell on the appellant. It might have procured the services, but that was still a relatively passive involvement. The UT agreed with the conclusion of the FTT: subject to the hotel exclusion, the supply by the company was exempt as the leasing or letting of immovable property.

Turning to the hotel exclusion, the UT disagreed with both the reasoning and conclusion of the FTT. It was not correct to concentrate on the individual annual stays as comparable to a succession of lettings similar to hotel accommodation: the actual supply was of an enduring right, which could be sold, sublet or used as security for a loan, and this went substantially beyond anything similar in the hotel sector. The UT set aside the FTT decision and remade it, holding that the hotel exclusion did not apply.

It was therefore not necessary to consider the fiscal neutrality argument. However, the UT would have rejected the company's appeal on this point. The supplies made in the timeshare sector were too varied to be directly comparable; there was no exemption "for the sector". It was necessary to consider the application of the exemption to the particular supplies at issue, as set out in EU and domestic law.

The company's appeal was allowed on the hotel exclusion point, and HMRC's cross-appeal was rejected on the exemption point.

Upper Tribunal: *Fortyseven Park Street Ltd v HMRC*

3.2 Option to tax

3.2.1 TOGC conditions

HMRC ruled that the sale of four properties did not qualify for TOGC treatment and assessed the vendor for VAT and interest totalling £920,128 for its 01/14 period. The company appealed.

At the first hearing in June 2017, its representative advanced an argument (that partial TOGC treatment might be possible) that HMRC said had not been put forward until the last minute. The judge asked for written representations from HMRC and a response from the taxpayer, and a further hearing took place in February 2018 at which HMRC applied to adduce new evidence in the form of documents relating to the option to tax.

The decision starts with a consideration of whether the evidence should be admitted. The judge noted that HMRC accepted that failing to introduce it earlier had been an oversight, and took the following issues into consideration:

(1) The breach was significant. The initial hearing proceeded on certain assumed facts and the new evidence was introduced at a very late stage.

(2) The overriding objective was to deal with the case fairly and justly. That required the judge to take account of all the available evidence in order to be able to come to a just and fair result. The form containing the option to tax was clearly probative of an issue before the Tribunal and to exclude it would risk the Tribunal reaching a decision on incorrect facts.

(3) There might be prejudice to the appellant as a result. That prejudice could be mitigated to an extent by an award of costs in relation to the application.

Judge Greenbank decided to admit the evidence, but to award the costs of the second hearing to the appellant.

The key question was whether the purchasers of the four properties had exercised an option to tax at the appropriate time to secure TOGC treatment. The appellant vendor had opted all the properties.

Property 1 (Byker)

The vendor (V) entered into an underwriting agreement with another company (LSG) whereby LSG would buy the property for £450,000 plus VAT if no higher price was obtained at auction. LSG paid a deposit of £45,000 plus VAT which was held by solicitors as agent for V.

The underwriting agreement was entered into on 4 December 2013. The auction took place on 5 December. LSG notified an option to tax the property on 7 January 2014. Completion took place on 16 January 2014; LSG paid the whole price, on which VAT was charged, and a VAT invoice was issued on 17 January 2014 (but dated 4 December 2013).

Property 2 (Hayes)

The facts were very similar, apart from a higher price (£1.28m plus VAT) and the invoice being dated 5 December.

Property 3 (Havant)

V sold this property at auction on 3 December 2013 for £750,000 exclusive of VAT. The auction contract stated that the purchaser had to pay a deposit that would be held by V's solicitors as agent for V. The purchaser (a pension fund, L) paid the 10% deposit to the auctioneers on 3 December (without adding VAT) but it was not handed on to V's solicitors until 16 December.

L notified HMRC of an option to tax on 4 December, at first stated to take effect on 25 March 2014; on 9 January 2014, L wrote to ask to amend the effective date to 3 December 2013. Completion took place on 14 January 2014, when the balance of the purchase price and VAT was paid. V issued a VAT invoice on 16 January, dated 3 December. HMRC wrote to L on 21 January, confirming that the OTT was effective from 3 December and that notification had taken place on 4 December.

Property 4 (Henley)

An individual (S) notified HMRC of an option to tax this property on 27 November 2013. On 29 November, V entered into a contract to sell the property to S for £2.085m excluding VAT. The deposit was paid by S (without VAT) on 2 December and held by V's solicitors as agent for V.

On 6 January 2014, a new purchaser (M) exercised an option to tax on the property and notified HMRC of this on 7 January. On 9 January, S, M and V entered into a deed of novation by which M took on M's obligations under the original contract. V transferred the property to M on 10 January; M paid the balance of the purchase price, together with VAT; and a VAT invoice was issued on 16 January by V to M, showing the full amount, and dated 29 November 2013.

V did not account for output tax on the sales on the due date for its 01/2014 period. HMRC raised an assessment on 4 June 2014 for £913,000 plus interest. On 16 July 2014, V's solicitors wrote to HMRC to say that they had reviewed the position and decided that the transactions should have been treated as TOGCs, and asking for a review. After correspondence, HMRC confirmed that the assessment would be upheld, and the company appealed to the Tribunal.

The only issue before the Tribunal, as agreed by both parties, was whether the condition in para.2A(a) of art.5 Special Provisions Order 1995 applied:

"[the transferee has, no later than the relevant date] exercised an option in relation to the land which has effect on the relevant date and has given any written notification of the option required by para.20 Sch.10 VATA 1994."

The judge noted that the issue presented itself differently in respect of the different properties, but the dispute between the parties focussed on the definition of "relevant date" in art.5 para.3:

"relevant date" means the date upon which the grant would have been treated as having been made or, if there is more than one such date, the earliest of them.

This led to a consideration of tax points. The easiest point to deal with was the date on which the invoices were issued. HMRC accepted that the date actually shown on the invoice did not determine this; the judge was satisfied that all the invoices had been issued after the completion of the transactions, so they would not determine the tax points. He did not appear to consider the operation of VATA 1994 s.6(5), which would move the tax point to the date on which the invoice was issued if that was within 14 days after the basic tax point set by s.6(2) or (3), if no earlier tax point had been set by a payment made before the basic tax point.

The company argued that:

- either the relevant date should be completion, disregarding a deposit held as agent, in which case the whole transaction should be a TOGC;
- or the transaction could be divided between the deposit, which would not be a TOGC, and the balance, which could, if the conditions were met before completion.

The company contended that the deeming provisions of s.6 could not override the meaning of the word "grant" in the Special Provisions Order. That could only refer to the actual transfer of the property. To the extent that HMRC sought to rely on *Higher Education Statistics Agency*, a 2000 case in which the same point had been considered, that decision had been wrong.

HMRC pointed out that the words "would have been treated as having been made" clearly indicated the relevance of a deeming provision. The High Court decision in *HESA* was binding on the Tribunal.

The judge concluded that the company's arguments were essentially the same as those rejected by Moses J in *HESA*, and he rejected them for the same reasons. The law clearly envisaged a deeming provision and the possibility that several dates might be a tax point for the same transaction; the law required the first of these to be taken.

The judge also rejected the company's argument that the same grant could be divided and treated partly as a TOGC. S.6 would have the effect that a single transaction could have two tax points, but it did not divide a single grant into two. The application of para.2A(a) was then clear: there were two dates, and the relevant date was the earlier of the two – the payment of the deposit.

That decided the appeal against the taxpayer in respect of the Byker and Hayes properties. In relation to Havant, the purchaser notified HMRC of the option after paying the deposit to the auctioneer but before the auctioneer had passed it on to V's solicitors. After a detailed analysis of the general auction conditions and special conditions applying to the particular contract, the judge concluded that the auctioneers held the money as stakeholder, not as agent for V, and the relevant date was therefore only when the solicitors received the money. HMRC did not seek to rely on the later amendment to the option, so this transaction qualified for TOGC treatment.

In respect of the Henley property, the company argued that the deposit paid by S in December was not "in respect of" the supply, because that supply had been cancelled by novation. The actual grant was made by V to M, and the only payment in relation to that took place on 9 January (when the solicitors effectively transferred the credit of S's deposit to M in their records, even though no money moved).

The judge analysed the effect of the novation and considered three possible dates for the payment to be treated as made – the original payment by S, the date of the novation contract, and the date of completion. Each presented problems, but he preferred the date of novation as providing fewer anomalies.

The problem was that the late evidence produced by HMRC – the option form actually submitted by M – showed that the option was exercised by M on 6 January, but was to have effect from 10 January. That was one day after the date of the novation contract. Although the company's representative argued that the seller should be entitled to rely on the date the option was exercised, rather than the date on which it was to have effect, the judge did not agree. The conditions were not met at the relevant date, and this property did not fall to be a TOGC.

The appeal was allowed in respect of the Havant property and rejected in respect of the other three.

First-Tier Tribunal (TC06368): *Clark Hill Ltd*

3.3 Developers and builders

3.3.1 Disputed wall

HMRC assessed a builder to £12,850 in respect of input tax claimed on a development site. At the time of the supposedly zero-rated sale of the site, the only thing that had been constructed was a garden wall. In addition, planning consent was granted retrospectively to allow the development. The project involved the demolition of a semi-detached house, making good the exposed gable end of the other house, the construction of a new boundary wall and then the construction of a new detached house. The property was sold on before the construction of the new house had started; the new purchaser applied for a second planning permission to cover changes to the specification from the original project.

The FTT (TC05356) considered a number of precedents concerning what constituted "in the course of construction", and agreed with the appellant's counsel that this project had gone beyond merely preparatory works. The question was, however, whether the wall constituted a "building", which was less clear. The judge decided that it was right to consider the project as a whole: the wall was a building, and in the context of the project, it was part of a building designed as a dwelling, so the vendor was a "person constructing".

Unfortunately, the planning consent did not allow for the building of the wall in that form at the time of the supply. There were complex issues concerning the changes to the consent and the changes to the design, but the judge concluded that Note 2(d) must be satisfied at the time of the supply, and it was not. Retrospective consent was granted in August 2012, but that could not affect a supply made in May 2012. The appeal was dismissed.

The company appealed to the Upper Tribunal, which noted the complex reasoning in relation to the requirement for planning consent in relation to the wall. It would not be necessary to have planning consent for a wall of up to 2 metres; the intended height of this wall was over 2 metres, so it would have required permission; but it was not 2 metres tall at the time of the sale, so the FTT had based its decision on the intended final height rather than the current height. The company argued that the FTT had erred in interpreting the requirements as applying to the anticipated height of the wall, and also in concluding that the wall was materially higher than 2 metres at the time of supply.

HMRC contended that it was the intention that was relevant, and also that there was evidence before the FTT that meant it was entitled to conclude that the wall exceeded the significant height.

The company sought to bring forward further evidence about the state of completion of the wall. The UT considered the rules and precedents on the submission of new evidence of facts at the UT stage, and concluded that it would not be fair or just to admit any fresh evidence on something that ought to have been settled at the FTT level.

The UT then considered the FTT's finding of fact that the wall had been completed (i.e. was over 2 metres tall) at the time of supply. The appellant had to clear a high hurdle to displace such a finding, and failed to do so. There had been opportunity in the FTT to correct the conclusion

if it was thought at the time to be wrong, but the company's written submissions to the FTT had if anything only reinforced the view that the wall had been completed.

This meant that it was unnecessary to consider the separate point about whether planning permission was required. The UT made no findings on the matter, but commented that it did appear that it had always been understood between the parties that the wall would exceed 2 metres when completed.

The appeal was dismissed again.

Upper Tribunal: *Cavendish Green Ltd v HMRC*

3.3.2 Village hall

HMRC issued a penalty under VATA 1994 s.62 for £53,101 to a not-for-profit sports club on the basis that it had issued a zero-rating certificate when not entitled to. The club appealed on the basis that the building qualified for zero-rating as a "village hall or similar".

The club relied on the *Caithness Rugby Football Club* decision: it was not necessary for a separate community group to control the use of the building, as long as the intended use was always for the local community rather than exclusively for the club. In her submissions, HMRC's representative said that HMRC believed that *Caithness* had been decided wrongly and turned on its own specific facts. Not only should this confirm the penalty, but it also counted against allowing a reasonable excuse defence.

The Tribunal found that the clubhouse was used by many local groups with no preference being given to the club. In 2017 the clubhouse was extensively used for an After Schools Club, karate classes, a Women & Toddlers group, a Ladies Keep Fit and Irish Dancing classes as well as a church on Sundays and several birthday parties. The judge was satisfied that this met the appropriate test as set out in *Caithness* and other cases.

The judge also considered that, if he was wrong on that conclusion, the club had a reasonable excuse. Although the club secretary had not rung HMRC's helpline, which he might have done, he had carried out research by reading the published guidance and had taken professional advice from two people before issuing the zero-rating certificate. That met the standard of "a reasonable thing for a responsible trader conscious of and intending to comply with his obligations" to have done.

The appeal was allowed.

First-Tier Tribunal (TC06321): *Greenisland Football Club*

3.3.3 Separate building

A college paid for the construction of a new block which provided additional teaching space, a café, a staff room and socialisation space for the students. HMRC ruled that the construction was standard rated either as an extension or as an annexe. The college appealed.

HMRC pointed out that there was a link bridge at first floor level between the new building and other buildings on the site. It was therefore not a separate building. In addition, the activities to be carried on were similar

to those carried on elsewhere, which indicated that it was only an "annexe". The judge pointed out to HMRC's representative that she was seeking to rely on *Cantrell*, which supported the proposition that the building had to be considered at the time it was constructed – this was inconsistent with consideration of the subsequent use of the building. The representative conceded the point.

HMRC also made the point that the new building was not compliant with Disability Discrimination legislation on its own. This was the reason for the link bridge: the adjacent building had a lift, which enabled wheelchair users to get to the first floor. Apart from that, the main access to the new building was through its own entrance, not through the bridge. The college argued that the building was totally self-contained, set at a distance of 7.1m from the next nearest building, and having its own plant room, power supply, water supply, heating system, drainage, etc. The building was of a different type to its neighbours, in that its materials, design and function were not the same.

The judge noted that, at least by the end of the hearing, HMRC had accepted that the new building was not an "enlargement or extension". The only question was whether it was an "annexe", and if it was, whether it satisfied the conditions of Sch.8 Group 5 Note 17:

"(a) the annexe is capable of functioning independently from the existing building; and

(b) the only access or where there is more than one means of access, the main access to:

(i) the annexe is not via the existing building; and

(ii) the existing building is not via the annexe."

HMRC had at length accepted that the main access was through the new building's own entrance, not the bridge. Their argument was reduced to "independent functioning", and the only factor they could point to was the lack of access to the first floor for wheelchair users. The judge considered that this went "way beyond any sensible approach". The Disability Discrimination legislation required the college to make reasonable provision, rather than requiring a particular design or arrangement of the building itself. The judge was satisfied that the building was capable of independent functioning, and the access for wheelchair users via the link bridge did not negate this.

The appeal was allowed.

First-Tier Tribunal (TC06384): *St Brendan's Sixth Form College*

3.4 Input tax claims on land

Nothing to report.

3.5 Other land problems

Nothing to report.

4. INTERNATIONAL SUPPLIES

4.1 E-commerce

4.1.1 MOSS guidance

HMRC have updated their guide *Register and use the VAT Mini one-stop-shop for digital supplies*. The main change is the addition of a new "get help" section. The guidance covers both the Union and non-Union schemes.

www.gov.uk/guidance/register-and-use-the-vat-mini-one-stop-shop

4.1.2 Exchange rates

HMRC have published the usual table of exchange rates to be used for VAT MOSS returns for the quarter to December 2017.

VAT Information Sheet 1/2018

4.1.3 Hungary

HMRC have published an Information Sheet to publicise a change to the VAT rate for internet access services within Hungary: from 1 January 2018, it dropped from 18% to 5%. The VAT rate of any other kinds of telecommunication, broadcasting or electronic services is still 27%.

VAT Information Sheet 9/2017

4.2 Where is a supply of services?

4.2.1 Establishments and fixed establishments

The FTT (Judge Harriet Morgan) has come to an important decision on place of supply, establishment and fixed establishment. The dispute was about where a supplier and a customer "belonged" for the purposes of VAT, and involved application of case law and the Implementing Regulation. However, the basis of the dispute was input tax: whether a UK insurance services company (H) could recover input tax under the Specified Supplies Order (SI 1999/3121) on the basis that it was making supplies of insurance-related services to a person belonging outside the EU, a Gibraltar insurance company (A).

The decision starts with the basic principle of "belonging" in the UK law. A business "belongs":

(1) where it has a business establishment ("BE"); or

(2) if different, where it has a fixed establishment ("FE"); or

(3) if it has both a BE and a FE (or several such establishments), where the establishment is located which is most directly concerned with the supply.

It was not disputed that A had a BE in Gibraltar. The question was whether it also had a FE in the UK and, if so, whether the supplies of services were made to that FE rather than to its BE in Gibraltar. The

place where A's supplies of insurance were made was also relevant to the analysis and was also to be determined by reference to where A "belonged". This similarly depended on whether A made the supplies of insurance from its BE in Gibraltar or from a UK FE.

The judge noted that the rules on place of supply had changed during the period in dispute (1 February 2009 to 31 December 2013), but the changes did not affect the principles involved. The Implementing Regulation (IR) also came into force during that period, but it effectively legislated for the pre-existing case law. The IR provided that a BE was "the place where the functions of the business's central administration are carried out" and a FE was "an establishment other than a BE, characterised by a sufficient degree of permanence and a suitable structure in terms of human and technical resources", where looking at the location of the recipient of the supply, "to enable it to receive and use the services supplied to it for its own needs" or, where looking at the location of the supplier, "to enable it to provide the services which it supplies".

The appellant contended that it supplied services to A at its BE in Gibraltar, which enabled it to make supplies of insurance from that BE.

HMRC's view was that A made its supplies of insurance in the UK through H acting as a FE. H provided the human and technical resources that enabled A to make supplies. Therefore H's supplies were made to the UK FE, and therefore fell outside the Specified Supplies Order.

The company's response was that A did not have a FE in the UK. In its view, for H's resources to comprise a FE of A:

(1) A would need to have control over the resources comparable to that of an owner. In its view, A plainly did not have that level of control.

(2) The resources would need to provide in the UK all that was necessary for A to make the insurance supplies or receive the services from H for its own needs and use (as relevant). H noted that in fact many of the functions needed for A to make insurance supplies were carried out through its own staff and resources in Gibraltar, such as making the underwriting decisions (in particular, deciding what to insure for what risk price) and decisions on large loss claims and dealing with reinsurance, investment and regulation.

The Tribunal heard evidence from a number of witnesses of fact who worked for A and for H, as well as expert evidence produced by each side. H applied to exclude HMRC's expert's report, and the judge agreed to exclude most of it, because it was either legal opinion, which ought to be argued by submissions to the Tribunal, or else it sought to prejudge the issues that the Tribunal had to determine. Some sections of his report were admitted as casting some light on the regulatory background to the UK insurance industry.

The facts

The judge set out the way in which both businesses operated, as well as a review of their history:

- H sold insurance for a panel of about 20 insurers, of which A was one. It had business agreements with A dating from 2005, updated in 2010 and 2012. H's main office was not dedicated to selling A's products.

- A had always been established in Gibraltar. There were regulatory reasons for setting the business up there: at the time it was incorporated, the capital requirements and corporation tax rates were lower than in the UK. A was licensed and regulated by the Gibraltar Financial Services Commission throughout the period on the basis that its "mind and management" was situated in Gibraltar.
- From September 2006 until February 2009, both A and H were in the same corporate group. In February 2009, some of the managers of A acquired the company in a buy-out. H's employees also owned an 18.1% shareholding in their own company. The companies were "related parties" but not in common ownership. In April 2012, H acquired A, and the companies were therefore again part of the same group.
- Throughout the period, the two companies had separate management structures and no directors in common.

The judge went on to examine the nature of the insurance business and the services provided by H in detail, as well as the interaction between the two. H sold insurance policies in the UK on behalf of A and other insurance panel members. H had binding authority to conclude insurance contracts and renewals of contracts on behalf of A, within the underwriting guidelines and limits set. A, however, had control of what risks or business could be underwritten/insured.

During the period, H's staff grew from 700 to over 1,500. It had 962 customer-facing staff in 2012 and 1,138 in 2013, including some hundreds dealing with claims. H owned the website, it had the relationship with price comparison websites, it owned the call centres, the computer system which was used to provide quotes, the software system used for selling policies and for claims, the rating tables, anti-fraud software, customer database and the electronic and paper records of the insurance transactions and claims, which were physically kept in Bexhill. A had read-only access, during normal business hours, to the claims and policy software systems, which contained records of the customers and their claims. It also had access to H's management information system which contained the extensive monthly reports prepared by H.

After lengthy consideration of the way in which premiums and commissions were set, claims and complaints were handled, and other details of the operation of the businesses in both the UK and Gibraltar, the judge summarised the issues for determination:

- first, whether A had a FE in the UK both as regards (a) supplies of insurance it made and (b) as the recipient of the supplies of services made by H;
- second, if A did have a FE in the UK, the further question is whether A's BE or FE is to be preferred as the place of supply/belonging.

The cases that predated the IR were still relevant, according to the CJEU in *Welmory* (Case C-605/12). The judge reviewed *Berkholz* (Case C-168/84), *Faaborg-Gelting Linien* (Case C-231/94) *ARO Lease* (Case C-190/95) and *DFDS* (Case C-260/95) as well as *Welmory*. In *Welmory*, after reviewing the precedents, the CJEU had emphasised the importance

of the presumption that the BE is the place of belonging to ensure legal certainty:

"the place where the taxable person has established his business as primary point of reference appears to be a criterion that is objective, simple and practical and offers great legal certainty, being easier to verify than, for example, the existence of a [FE]. Moreover, the presumption that the services are supplied at the place where the taxable person receiving them has established his business makes it possible both for the competent authorities of the Member States and for suppliers of services to avoid having to undertake complex investigations in order to determine the point of reference for tax purposes."

The wording of art.44 PVD suggests that the use of a FE is an exception to the general rule. The situation in *Welmory* involved a Polish company (P) and a Cypriot company (C), and similar arguments to the present case: the Polish authorities considered that P was a FE of C in Poland and was making supplies to consumers. The CJEU commented:

"the fact that the economic activities of the two companies, which are linked by a cooperation agreement, form an economic whole and that their results are of benefit essentially to consumers in Poland is not material for determining whether [C] possesses a [FE] in Poland.. …the services supplied by [P] to [C] must be distinguished from those supplied by [C] to consumers in Poland. They are distinct supplies of services which are subject to different schemes of VAT."

The judge summarised the FE test as follows:

(1) The establishment must be of a minimum size with both the human and technical resources "necessary", "adequate" or "suitable":

(a) for the provision of the supplies on an "independent basis", when looking at the location of the supplier, or

(b) to enable the establishment to receive and use the relevant supplies for its own needs, when looking at the location of the recipient of the supplies.

(2) As stated in *Berkholz*, those resources must be permanently present or, as phrased in *ARO Lease*, the establishment must have "a minimum degree of stability derived from the permanent presence of both the human and technical resources" necessary for the provision of the supplies or to enable the establishment to receive and use the relevant supplies for its own needs.

After further detailed consideration of the precedents, including *Daimler* (a case about 8th Directive refunds), the judge summarised her conclusion as follows:

"we have concluded that, on the facts of this case, [H]'s resources were not available to [A] with a sufficient degree of permanence for them to constitute its FE on any view of the applicable case law. Whatever view of the FE test is taken, it is clearly not envisaged that the resources of an entity comprise a FE of another legal (albeit related) entity as a result of the provision of services under commercially agreed contractual arrangements where, in fact, each entity operates a separate business with its own commercial imperatives and financial risk taking."

The judge said that the functions of an insurance business had been split between A and H. It was clear that A managed its own business and was the decision-maker on all of its functions, although it used H's support in dealing with underwriting and claims handling. H dealt with the customer-facing side of the business, selling policies and handling claims on behalf of A, and was remunerated through commission. Although the companies were related for part of the period, the evidence was that the service agreements were negotiated on an arm's length basis. There were sound business reasons for this.

The fact that the two related entities operated essentially as different parts of what could be described as a single economic whole did not of itself, without more, lead to the conclusion that the human and technical resources of H, as the service provider, formed a FE of A. Under both the approach in *Welmory* and that in *DFDS*, a closer analysis was required according to the contractual arrangements between the parties and how they operated in practice. The essence of A's supplies was insurance, and what was essential for that was the ability to decide what or who to cover for what risk price. That was not something that H provided from the UK. There was therefore a successful separation of the two functions into independent entities.

HMRC argued that the FE test was the appropriate one because otherwise there would be an "irrational result", as set out in the *Berkholz* decision. The judge did not agree. Both sides appeared to agree that there was a composite supply of services by H to A, and they were not "predominantly" related to the marketing and sale of insurance activities carried out in the UK. The services were used to carry out its underwriting function in Gibraltar. There was therefore no reason to depart from the basic presumption that B2B supplies of services were received where the customer belongs at its BE.

The appeal was allowed, in 613 paragraphs.

First-Tier Tribunal (TC06306): *Hastings Insurance Services Ltd*

4.2.2 Updated Notices

HMRC have updated their Notice *Freight transport and associated services* to take account of several changes in law and policy since the December 2010 edition. A new paragraph 1.3 has been added to reflect revised policy on the treatment of hiring means of transport and supplies of transport services. Paragraph 3.1 has been updated to reflect the amendment to the law regarding the supply to a business customer of the transport of goods and related services which takes place wholly outside the EU. Section 8 has been updated to reflect HMRC's revised policy on goods handling services for aircraft provided at places that are not customs and excise airports.

Notice 744B

HMRC have updated their Notice *Ships, aircraft and associated services* to take account of several changes in law and policy since the July 2011 edition. Section 2 has been updated to reflect industry concerns about the calculation of a ship's gross tonnage. Section 4 has been amended to reflect revised policy on the treatment of hiring means of transport and

supplies of transport services. Section 8 has the same update as Notice 744B above in relation to non-customs and excise airports.

Notice 744C

4.2.3 Article

In an article in *Taxation*, Neil Warren discusses the place of supply rules for business-to-business services, and suggests that some UK advisers tell clients to charge UK VAT when it is not appropriate.

Taxation, 26 January 2018

4.3 International supplies of goods

4.3.1 Which despatch?

A German company (BPM) sold petroleum products to an Austrian company (BIDI). BIDI undertook to transport the goods from Germany to Austria. Without informing BPM, BIDI resold the goods to another Austrian company, K. K then collected the goods from BPM and transported them to Austria. BPM treated its sales to BIDI as exempt despatches, and BIDI added Austrian VAT to its sales to K. Commercial disputes between the parties followed, during which it became apparent that BIDI had not accounted for the Austrian output tax. Meanwhile, the German tax authorities demanded payment of German VAT from BPM. BIDI was by now insolvent, so the refusal of a deduction of input tax to K by the Austrian authorities would leave it out of pocket. It appealed against that decision, and questions were referred to the CJEU.

The court considered the application of art.32 PVD. The first paragraph provided that, where goods were dispatched or transported by the supplier, or by the customer, or by a third person, the place of supply was to be deemed to be the place where the goods were located at the time when dispatch or transport of the goods to the customer began. In order to determine which of the two supplies the intra-Community transport should be ascribed to, it was necessary to undertake an overall assessment of all the specific circumstances of the case.

It was clear that K had been the owner of the goods before the intra-Community transport had taken place. It was therefore clear that the supply between BIDI and K was exempt; presumably BPM was therefore liable to German output tax.

The principle of the protection of legitimate expectations did not give K a right to claim the overpaid amount as input tax. That principle would only apply when an administrative authority had caused the person to entertain the expectation, which was not the case here. The only right was to demand repayment from the person who had incorrectly charged the VAT, which would be no solution for K.

CJEU (Case C-628/16): *Kreuzmayr GmbH v Finanzamt Linz*

4.3.2 Evidence of export

HMRC assessed a company to output tax of £30,016 on the basis that it should not have zero-rated certain exports because it did not have the required evidence. HMRC also assessed a penalty, but suspended it.

The exports had been sold to customers in Nigeria, and described on air waybills as "personal effects". The director of the company explained that the airline gave them a better rate for this description, and he considered it less likely that the goods would be stolen than if they were accurately described.

The company argued that the totality of the following documentation ought to be enough to satisfy para.6.5 of Notice 703:

(1) Transpase's purchase orders.

(2) Air waybills.

(3) Invoices from the International Air Transport Association ("IATA").

(4) Sales invoices issued by Transpase to its customers (although these are headed "receipts" they do not show any payments and so appear more properly to be invoices).

(5) MNCL bank statements.

(6) Transpase's accounts for 2013/2014.

The Notice has the force of law and requires:

The evidence you obtain as proof of export, whether official or commercial, or supporting must clearly identify:

- *the supplier*
- *the consignor (where different from the supplier)*
- *the customer*
- *the goods*
- *an accurate value*
- *the export destination, and*
- *the mode of transport and route of the export movement.*

The judge noted that the parties agreed that the FTT had a full appellate jurisdiction in relation to the matter, in spite of references in s.30(6) VATA 1994 to HMRC being "satisfied" (and therefore, by implication, taking a decision which might only be challenged on grounds of reasonableness).

HMRC argued that the last two conditions were not met: there was no indication in the documentation of the destination or the mode of transport or route. The judge agreed. As there was no clear description of the goods on the waybills, it was not possible to relate most of the documentation to the particular movements of goods; there was no documentation from the customer; and nothing showed the destination within Nigeria, or the route. The appeal was dismissed.

First-Tier Tribunal (TC06328): *Transpase Ltd*

4.3.3 Fulfilment businesses

The Fulfilment Businesses Regulations (Approval Scheme) 2018 set out the detailed framework of the fulfilment house due diligence scheme for fulfilment houses operating in the UK that handle imported goods on behalf of third parties located outside the EU. The Regulations will come into force on 1 April 2018 and 1 April 2019, except in relation to dealing with contraventions mentioned. The new regulation revokes and replaces a previous version (SI 2018/299).

Part 3 of the Regulations impose obligations on approved persons to:

- not start a new third country goods fulfilment business with a person, or continue an existing third country goods fulfilment business with a customer, that the approved person knows or has reasonable grounds to suspect is not meeting a VAT or customs duty obligation. The approved person must also notify the Commissioners when they first become aware or suspect that a customer is not meeting those obligations;
- give notice to all third country customers;
- conduct due diligence checks on third country customers and maintain records of those checks;
- verify a third country customer's VAT registration number or VAT exemption reference number and notify the Commissioners of discrepancies;
- notify the Commissioners of changes in registered details;
- tell the Commissioners when they cease to carry on a third country goods fulfilment business.

SI 2018/326

A Tax Information and Impact Note has been issued in relation to the regulations. It states that the expected revenue from the measure will be approximately £250m a year once the scheme is up and running.

www.gov.uk/government/publications/the-fulfilment-businesses-regulations-2018

The CIOT has raised concerns about the fulfilment house due diligence scheme, in particular that where a non-EU supplier is declaring UK VAT and duty correctly to HMRC, the 'approved' person or business under FHDDS could still face harsh penalties, such as of £500 for each occasion it records an incorrect import entry number of the goods stored, even if they have otherwise been fully tax compliant and have not been involved in any fraudulent supply chain to date.

www.tax.org.uk/media-centre/press-releases/press-release-concern-over-harsh-penalties-minor-breaches-new-vat-rules

The Finance (No 2) Act 2017, Part 3 (Appointed Days) Regulations 2018 confirmed that HMRC would begin registering businesses for the scheme from 1 April 2018. Existing fulfilment businesses must register by 30 June; new businesses by 30 September. The full record-keeping, due diligence and penalty obligations begin in April 2019.

SI 2018/298

4.3.4 Online marketplaces

HMRC updated their guide *VAT joint and several liability for online marketplaces* in March 2018 to reflect the extended rules on joint and several liability introduced by Finance Act 2018. This sets out the relative responsibilities of UK traders and overseas traders selling to UK customers through an online marketplace, and also responsibilities of the marketplace itself.

www.gov.uk/guidance/vat-overseas-businesses-using-an-online-marketplace-to-sell-goods-in-the-uk

HMRC have also published guidance on the VAT checks online marketplace operators must carry out on their sellers under the extended joint and several liability rules introduced by Finance Act 2018. From 15 March 2018 new legislation allows HMRC to hold the operator of an online marketplace jointly and severally liable for the unpaid VAT of overseas sellers operating on the marketplace where:

- an overseas seller operating on the marketplace has not registered for UK VAT;
- the operator of the online marketplace, knew or should have known that the seller should be registered for UK VAT.

The new rules also extend existing rules, so the operator can also be held jointly and severally liable if HMRC tells them that a UK or overseas seller operating on the marketplace is not meeting its VAT obligations.

The guidance sets out checks that online marketplace operators need to make:

1. Check the seller's VRN

You should request a VRN when you think a seller offering goods for sale on your marketplace should be registered for UK VAT.

It's up to you to validate the VRN of a seller operating on your marketplace within 10 days of receiving it.

You can check the VRN on the EUROPA website. UK VAT registrations are updated every day.

2. VRN display and verification requirements

You must display a verified VRN on your website within 10 days of the seller giving you it - unless the seller has given it to you before they offer goods for sale on your online marketplace, when the deadline is extended to the end of the day when the seller first offers goods for sale on your marketplace.

You should also take reasonable steps to remove any VRNs that are displayed on your online marketplace within 10 days of you becoming aware that that they're wrong.

If you don't you could be liable to a penalty.

If an overseas seller hasn't registered for VAT you could also be jointly and severally liable for their unpaid VAT if HMRC decide you knew or should have known.

3. VRN mismatch or discrepancy

If there are any differences in the name of the online seller on your database and the EUROPA website you should treat it as a discrepancy.

If you identify a minor difference between the 2 databases, carry out further checks to confirm that the seller isn't using another business's VRN.

If the only difference is in a prefix or a suffix in the business name (for example, 'Ltd' rather than 'Limited'), then it's reasonable for you to decide that the VRN and the name shown on the EUROPA website accurately match with the business name on your database, if there aren't other indicators that they aren't meeting their VAT responsibilities.

If you identify a significant difference between the 2 databases (for example, if the name of the seller on your database is clearly different from the name of the VAT registered business on the EUROPA website) it's reasonable for you to decide that the seller isn't registered for VAT, and is using another business's VRN.

HMRC will consider a range of factors before deciding if you've correctly validated a VRN.

These will include if there was any information you held or you should have reasonably requested that would help you decide the seller should have registered for VAT.

4. Seller has registered for VAT but hasn't received a VRN yet

Don't allow an overseas seller to continue to trade on your marketplace if they don't have a VRN and they're either:

- *advertising or offering goods for sale*
- *trading on your marketplace and haven't provided you with a valid VRN after 60 days of trading*

You should suspend the seller's account or remove it from your marketplace and tell them to contact the HMRC VAT Helpline if this will cause them any problems.

There is also guidance on how to determine the location of goods at the time of sale.

www.gov.uk/guidance/vat-online-marketplace-seller-checks

4.3.5 Commodity derivatives

The European Commission has announced infraction proceedings to be directed against the UK concerning VAT treatment of certain commodity derivatives trading under the Terminal Markets Order (TMO – SI 1973/173). The TMO is a Statutory Instrument that allows a specific VAT zero rate for derivative transactions in spots, futures (and options on) commodity contracts, when traded on an exchange.

The Commission has sent the UK government a formal letter, requiring a response within two months.

www.gov.uk/government/news/statement-on-infraction-proceedings-on-vat-treatment-of-certain-commodity-derivatives-trading

4.3.6 Taxation (Cross-border Trade) Bill

The Taxation (Cross-Border Trade) Bill was introduced to Parliament in January to impose and regulate customs duties on imports after Brexit.

services.parliament.uk/bills/2017-19/taxationcrossbordertrade.html

The government also published a guide to the Bill (and the earlier Trade Bill) to explain its terms. It included the following summary:

The Taxation (Cross-border Trade) Bill will allow the government to create a standalone customs regime. It provides for a range of negotiated outcomes, as well as legislating for a contingency scenario where the UK leaves the EU without a negotiated outcome. Among other things, it ensures that the UK can:

- *establish a new UK tariff, charge customs duty on goods (including on goods imported from the EU), set and vary rates of customs duty, and suspend or relieve duty at import in certain circumstances*
- *define how goods will be classified to establish the amount of customs duty due*
- *request, collect, store, and share tax-related information*
- *accommodate the transition to a new customs regime*

It also provides for measures to replace existing powers and schemes in EU law that relate directly to the rate of customs duty chargeable. These include:

- *a new UK trade remedies framework that can be used to impose additional customs duty in certain circumstances*
- *the creation of a unilateral trade preference scheme to enable the UK to continue to reduce or remove the tariffs paid on imports from developing countries*
- *the ability to vary the rate of duty in the event of a dispute between the UK government and the government of another territory or country, where authorised to do so by international law.*

www.gov.uk/government/publications/preparing-for-a-uk-trade-policy-a-guide-to-trade-legislation

The Lords Delegated Powers and Regulatory Reform committee, whose remit is to examine current Bills and report on any shortcomings they find in the granting of law-making powers or levels of parliamentary scrutiny, has highlighted areas of concern with powers contained in the Bill. The Bill provides for the secretary of state or HMRC to effectively be able to make law by issuing public notices. The committee considered that it would be more appropriate to require the positive affirmation of statutory instruments, to avoid "a massive transfer of power from the House of Commons to Ministers of the Crown".

publications.parliament.uk/pa/ld201719/ldselect/lddelreg/65/6503.htm

At second reading of the Bill, there was discussion of the potential cash flow disadvantage of moving from acquisition VAT to import VAT. The Financial Secretary to the Treasury, Mel Stride, said that it was not

intended that there should be such a disadvantage, and that the matter was being closely reviewed.

The Bill completed its committee stages on 1 February.

4.3.7 Article

In an article in *Taxation* mainly aimed at ATT students, Karen Bullen explains in simple terms the different treatments of imports, exports, acquisitions and despatches.

Taxation, 1 March 2018

4.3.8 Updated Notices

HMRC have issued an updated version of their Notice *Customs special procedures for the Union Customs Code*, which covers:

- storage comprising of Customs Warehousing (CW) and Free Zones
- specific use comprising of Temporary Admission (TA) and end-use (EnU)
- processing comprising Inward and Outward Processing

Transit is a special procedure, but is not covered in this guidance.

Notice 3001

HMRC have updated their Notice *Guide for international post users* from the March 2017 version with additional information on the requirements for waiver of customs duty and import VAT relief on multi-gift packages. It also reflects the increase in the level at which a formal declaration is required, from £750 to £873, because of a fall in the value of the pound against the €1,000 EU limit.

Notice 143

4.4 European rules

4.4.1 Rates, and Simplification for SMEs

The Commission has published two proposals for reform of VAT. One provides for more flexibility for Member States to apply more lower rates:

In addition to a standard VAT rate of minimum 15%, Member States would now be able to put in place:

- two separate reduced rates of between 5% and the standard rate chosen by the Member State;
- one exemption from VAT (or ‘zero rate’);
- one reduced rate set at between 0% and the reduced rates.

The current, complex list of goods and services to which reduced rates can be applied would be abolished and replaced by a new list of products (such as weapons, alcoholic beverages, gambling and tobacco) to which the standard rate of 15% or above would always be applied.

To safeguard public revenues, Member States will also have to ensure that the weighted average VAT rate is at least 12%.

The new regime also means that all goods currently enjoying rates different from the standard rate can continue to do so.

The package for SMEs is only supposed to take effect when “the definitive regime” is in place, which may be some time coming. It is intended to deal with the “cliff edge” faced by a business that exceeds the turnover threshold, and also the problem that small business exemptions only apply in the country in which the business is established:

While the current exemption thresholds would remain, the proposals would introduce:

- A €2 million revenue threshold across the EU, under which small businesses would benefit from simplification measures, whether or not they have already been exempted from VAT;
- The possibility for Member States to free all small businesses that qualify for a VAT exemption from obligations relating to identification, invoicing, accounting or returns;
- A turnover threshold of €100,000 which would allow companies operating in more than one Member State to benefit from the VAT exemption.

europa.eu/rapid/press-release_IP-18-185_en.htm; IP/18/185

4.4.2 Fraud losses

The Commission issued a press release on 8 March, announcing that a formal letter had been sent to the UK government concerning €2.7bn of customs duties lost to the EU budget because imports into the UK were undervalued between November 2011 and December 2017. The Commission say that the UK failed to take appropriate action to limit the losses, mainly arising on imports of textiles and footwear from China, in spite of warnings. The Commission states that the UK will be liable for the loss to the EU budget.

http://europa.eu/rapid/press-release_MEMO-18-1444_en.htm

4.4.3 Abusive practices

Some property developers owned a development site in Ireland. They constructed some holiday homes, and in 2002 (before the *Halifax* decision of the CJEU) entered into transactions with an associated company whereby long leases were granted followed by short leases back, which were subsequently cancelled by mutual surrender. This enabled the properties to be sold as "second hand" and therefore not subject to VAT under Irish law.

The Irish Revenue Commissioners assessed for additional tax on the basis that the "first supplies" were artificial transactions that had been entered into to avoid tax and should therefore be disregarded. The Irish courts upheld the assessments on the basis that the leases lacked commercial reality and were therefore an abusive practice. The taxpayers appealed to the Supreme Court, arguing that they should be protected by the principles of legal certainty and legitimate expectations, and that in the absence of any allegation of fraud, their transactions should not be regarded as abusive.

The CJEU affirmed that the principle of abusive practice did not require a domestic implementing provision in order to be applied directly, and that direct application even before the *Halifax* judgment did not infringe the principle of legal certainty. After all, the *Halifax* judgment concerned transactions that took place before the *Halifax* judgment.

The CJEU was also asked to rule on how the transactions should be recharacterised. It noted that the precedents clearly stated that they should be redefined to re-establish the situation that would have prevailed without the abusive practices, but not going further than was necessary to ensure the correct charge to VAT and the prevention of tax evasion. This would involve disregarding the abusive transactions, and charging tax on the basis of the remaining non-abusive ones.

The taxpayers argued that the leases had been acceptable tax planning rather than an abusive practice, but the CJEU did not accept that distinction. There was no aim other than the obtaining of a tax advantage. This appeared to be contrary to the purpose of the Directive, in that the Directive intended to tax the first sale of such buildings, and the leases artificially created "first sales" to avoid the charge.

CJEU (Case C-251/16): *Cussens and others v Brosnan*

4.4.4 Reduction of liability to pay

A Slovenian company agreed a compromise with its creditors under which it would only pay 44% of its debts over a period of 9 years. The tax authority ruled that it should adjust its input tax deductions as a result. The company appealed, and questions were referred to the CJEU.

The court ruled that art.185(1) PVD should be interpreted as requiring such an adjustment, because the reduction in the liability to pay creditors was a change in the factors used to determine the amount to be deducted. This accorded with the principle of the neutrality of the tax, because presumably the supplier would reduce the output tax under art.90.

The court also confirmed that the situation did not fall within art.185(2), which provided that no adjustment would be required in certain situations – "no adjustment shall be made in the case of transactions remaining totally or partially unpaid or in the case of destruction, loss or theft of property duly proved or confirmed, or in the case of goods reserved for the purpose of making gifts of small value or of giving samples, as referred to in Article 16. However, in the case of transactions remaining totally or partially unpaid or in the case of theft, Member States may require adjustment to be made."

It was not necessary for the Slovenian law to spell out the effect of a compromise with creditors more clearly than it did.

CJEU (Case C-396/16): *T-2, družba za ustvarjanje, razvoj in trženje elektronskih komunikacij in opreme, d.o.o., (in insolvency) v Slovenia*

4.5 Foreign refund reclaims

4.5.1 Limitation on claims

Between 2004 and 2010, a German company and two Slovakian companies (H) supplied VW in Germany with moulds for the manufacture of vehicle lights. No VAT was charged on the basis that the payments were "financial compensation" rather than consideration for a supply. The H companies realised in 2010 that they had made a mistake and filed corrective returns in Slovakia. They raised invoices for unpaid tax for all the years from 2004 to 2010, which VW paid; VW then in July 2011 submitted a claim to the Slovakian authorities for repayment of that tax.

The tax office accepted the claims for the periods from 2007 to 2010, but ruled that the older periods were outside the 5-year limitation period provided for by Slovak law. It applied the time limit by considering the date of delivery of the goods, which in respect of this tax had taken place between 2004 and 2006, over 5 years before the claim was submitted.

VW appealed and questions were referred to the CJEU. The company argued that the right to refund of VAT only arose when goods and services had been supplied and the VAT had been applied by the supplier through the issuing of an invoice. The limitation period could not therefore begin to run if those two conditions had not been met.

The court observed that a time limit of some sort had been approved in earlier decisions as supporting the principle of legal certainty. Member States had the power under art.273 to impose further conditions on the right of deduction to prevent avoidance, evasion and abuse. However, such conditions should not go further than was necessary to meet those objectives, and should not systematically undermine the right to deduct VAT and therefore compromise the neutrality of the tax.

In this case, it was clear that the tax had not been accounted for by the H companies until 2010, and that there was no risk of avoidance, evasion or abuse. VW could not have exercised its right to deduct the VAT any earlier than the making of the adjustment. VW had not shown any lack of diligence or any fraudulent collusion with the H companies. In those circumstances, a limitation period could not be applied that had expired before it was even possible for VW to make a claim.

CJEU (Case C-533/16): *Volkswagen AG v Financné riaditelstvo Slovenskej republiky*

5. INPUTS

5.1 Economic activity

5.1.1 Single Farm Payment Entitlements

A company ran a farming business in Aberdeenshire. It was allocated an initial entitlement to Single Farm Payments when the scheme started in 2005, then purchased more SFPEs for £7m plus VAT of just over £1m. To be entitled to the payments, the holder had to have "at its disposal" one hectare of land in "Good Agricultural and Environmental Condition" (GAEC) for each unit of entitlement. The company entered into agricultural leases with other farmers to secure this extra land, but under leaseback agreements the other farmers continued to carry on the farming activity on the land.

HMRC regarded the purchase of the SFPEs was a non-business activity on which no input tax could be claimed. The director of the company responded that the purchase (and occasional sale) of SFPE units was an essential part of the financial management of the farm. All the money generated by the payments had been retained in the business and was used for expanding and diversifying it, for example by considering the establishment of a windfarm. None of the SFPs had been withdrawn from the business for personal purposes. The purchase of the units was an overhead of the business similar to the sale of a going concern in *Abbey National* and the share issue costs in *Kretztechnik*: there was no exempt supply or private use that would interfere with the right of deduction.

In the FTT (TC04179), HMRC's representative pointed out that the payments themselves were outside the scope of VAT (in line with the CJEU decision in *Mohr*). The activity of buying SFPEs was therefore not "predominantly concerned with making taxable supplies". The costs were not components of any outputs. The trader had leased 35,000 hectares of land to support the extra entitlements, but carried on no farming activities on them. The farm itself was only 200 hectares.

The Tribunal agreed with the taxpayer that the purchasing of SFPEs was not a separate activity, but an integral part of the farming business. Given that the purchase was carried out in the context of a fully taxable business, there was no reason to deny the deduction of input tax. It was a fully recoverable overhead cost.

HMRC appealed to the Upper Tribunal, which confirmed the decision below. The judge considered the precedents of *Midland Bank*, *Abbey National*, and *Kretztechnik*, and derived the principle that overheads were sufficiently connected with the taxable outputs of a business to justify recovery – it was not necessary for a cost to relate to particular taxable outputs, as long as it related to outputs in general. It was established that transactions outside the scope of VAT, such as the receipt of SFP payments, were to be ignored in considering input tax recovery – only exempt income led to a restriction.

HMRC considered the purchase of the SFPE units to be "artificial" because it was so out of proportion to the actual farming activities. However, their counsel confirmed to the judge that HMRC regarded any level of SFPE purchases as falling foul of their view that they were linked

to activities outside the scope of VAT – it was not just the quantity that created the problem. The judge concluded that HMRC's view was simply wrong. The FTT had come to a justifiable decision of fact on the basis of evidence that the purchases were connected to the taxable business, and that led inevitably to the conclusion that the VAT was deductible as input tax.

HMRC appealed again to the Court of Session. Their argument was slightly refined to the contention that the company was carrying on an extensive separate activity of trading in SFPE units. This was a non-business activity, and the VAT on the purchase of units was incurred in relation to that non-business activity. It was therefore not deductible. Alternatively, input tax could only be deducted on overheads to the extent that they related to the taxable outputs of the business.

The CS set out the relevant provisions of the PVD and the VATA, and recited the same CJEU precedents as the Upper Tribunal, as well as *AB SKF, Sveda* and *Iberdrola*. In respect of the second, the presentations at the hearing were based on the A-G's opinion (which favoured HMRC's case), and the CS asked both sides for further written submissions after the full court judgment differed significantly from that opinion.

The CS summed up the principles derived from the authorities as follows:

First, at a general level, the deduction of input tax is intended to relieve a trading entity entirely of the VAT that is payable in the course of all of its economic activities; this ensures overall neutrality of taxation in respect of all activities that are subject to VAT.

Secondly, if VAT paid on an input transaction is to be deductible, there must be a direct and immediate link between that input transaction and the output transactions that give rise to a right of deduction. This is necessary because, if deduction of the input tax is to be permitted, the expenditure on the relevant inputs must be a component in the cost of the output transactions that are charged with the output VAT from which the input VAT is to be deducted.

Thirdly, such a link will be broken if the goods or services obtained through the input transaction are used by the taxpayer for the purposes of an exempt transaction or a transaction that does not fall within the scope of VAT, including activities that are not economic activities in the sense in which that expression is used in dealing with VAT.

Fourthly, the direct and immediate link will not be broken if the goods or services in question form part of the general overheads on the taxpayer's business, in such a way that they form component parts of the price of the taxpayer's product. This represents common sense. When goods or services are supplied to a customer, the costs incurred by the supplier in providing the relevant goods or services will include not only the cost of purchasing or manufacturing the goods or providing the services but also general overheads. To take a simple example, if the supplier manufactures goods, the cost of providing the goods will include not merely the cost of raw materials but also the cost of plant and equipment. This is a general proposition that has been recognized throughout the case law of the Court of Justice.

Fifthly, if the goods or services in question are used partly as general overheads of the taxpayer's business and partly for the purposes of

exempt or zero-rated transactions, the input tax must be apportioned between those two uses. The reasons for this are obvious and straightforward.

The judges noted the findings of the FTT that the SFPEs were acquired for the purposes of financing the farming business and possible diversification, and could see no reason to overturn that. Accordingly, the SFPEs were properly considered an input of the business, and the lower Tribunals had reached the correct conclusion.

The judges went on to explain the logical error in HMRC's argument. The receipt of the SFP payments (outside the scope) was merely a consequence of the acquisition of the SFPEs. It should not be considered a separate business activity distinct from the taxpayer's general business. The SFPEs were rather a form of investment, made by the taxpayer for the purposes of its business, and from which income was derived.

The judges found it difficult to understand HMRC's further contention that the intention of the directors as to how the SFPs would be used was irrelevant. The intention of the directors of a company is an objective fact, and it appeared to the CS to be a factor that may properly be taken into account. There was evidence in the documents in this case that established the intention; the statutory expression "used or to be used for the purposes of the business" clearly pointed to the importance of intentions.

The judges also considered it central that the SFPs were paid into the company's bank account, and the directors then had fiduciary duties to apply the funds for the benefit of the company. The primary findings of fact by the FTT contradicted HMRC's argument, which therefore had to be rejected.

The judges commented on a further HMRC argument that SI 1993/1507 would apply if any of the SFPs was used for a non-business purpose. Counsel for the taxpayer had accepted this proposition, and the judges agreed that it was correct to do so.

The judgment concludes with a discussion of other cases that were cited by the parties, which the judges did not think added significantly to the cases already mentioned. Some were consistent in the principles applied, and some related to significantly different facts (e.g. *Securenta* and *VNLTO*).

The judges also referred to the decision of the Upper Tribunal in *Vehicle Control Services Ltd*, where overhead input tax was disallowed because the company had a significant proportion of outside-the-scope income (relating to parking penalty notices). This would be applicable to the present case if, and only if, the SFPs were not in fact used for the purposes of the taxable business (e.g. by developing a wind farm or in farming).

HMRC's appeal was refused.

Court of Session: *HMRC v Frank A Smart & Son Ltd*

5.2 Who receives the supply?

Nothing to report.

5.3 Partial exemption

5.3.1 Investment management costs

The University of Cambridge has an endowment fund in which it invests donations. It pays professional fees to managers to look after this money, and the income and capital growth on the investments are used to support the various activities of the university, amounting to some 6% of its operational expenditure. As a charity, the university has activities that are business and non-business, and the business activities are taxable (mainly commercial research, sales of publications, consultancy and hire of facilities) and exempt (education).

The university generally claimed input tax in accordance with the 'CVCP guidelines' agreed between HMRC and higher education institutions. These enabled it to avoid preparation of detailed partial exemption calculations. For some years it did not include the investment management costs as residual input tax in the CVCP workings. It made a claim in 2002 which was refused and not pursued, but then claimed again in March 2009 following *Fleming*. The amount claimed was £182,500.

HMRC argued that the investment activity should be regarded as a 'free-standing activity' and therefore 'a supply made not by a taxable person acting as such', in line with the decisions in *NSPCC* and *Wellcome Trust*. Overheads relating to a non-economic activity undertaken for the purpose of an economic activity should not be regarded as recoverable.

The FTT (TC02836) did not agree. In line with the decision in *Kretztechnik*, something that did not involve the taxable person making a supply – whether the issue of shares, or in this case the receipt of dividends – should be related to the activities of the entity as a whole. As the endowment fund financed all the activities of the university, the management fees were residual, and the input tax was partly recoverable.

The FTT decision reviewed each of the major precedents in turn and comments on the reasons for following or not following them. In particular, HMRC's reliance on *BLP Group* was rejected: in that case, the sale of shares was held to constitute an economic activity, whereas the university was not engaged in such activity in relation to its investments.

HMRC appealed to the Upper Tribunal (Mr Justice Simon and Judge Sinfield, 2015). Their counsel's argument was summarised as follows in the decision:

In order to be regarded as overheads, the costs incurred in acquiring the input transactions must be cost components (in the sense of being incorporated in the price) of all the taxable person's economic activities. Putting it another way, the input transactions must 'burden' the cost of the taxable person's economic activity as a whole. Mr Singh contended that the costs of F&CM's investment management services do not burden the cost of all of the University's economic activities. He submitted that

F&CM generates investment income from the Fund and that income subsidises the University's economic activities, thereby reducing the cost to the University of making supplies of education, research, catering, bar sales and conferencing services. He submitted that, in principle, the costs of generating investment income from the Fund do not have a direct and immediate link with and cannot be cost components of the price (or burden the cost) of the University's economic activity as a whole. Mr Singh submitted that the correct analysis was that the costs of the investment management services are cost components of the price of the University's disposals of its investments for consideration and are thus directly and immediately linked with those disposals. He further contended that it is not permissible to 'look through' the disposals of investments for consideration in order to attempt to attribute the costs of the investment management services to the University's economic activity as a whole.

By contrast, the taxpayer's counsel put forward a simple question based on *Kretztechnik*: for what purpose is the outside the scope activity carried out? He submitted that, in the present case, the answer was straightforward: the investment activity is not carried on for its own sake, but for the benefit of all the University's activities.

The Upper Tribunal reviewed *BLP Group*, *Abbey National* and *Kretztechnik* for authority on the treatment of overheads. The principle of *BLP Group* was that an exempt supply to which costs were directly attributable "broke the chain" between overheads and taxable activities of the business as a whole. Here, there was no such chain-breaking event, because the sale of investments was outside the scope investment activity rather than exempt economic activity.

The judges also considered *Securenta* and *AB SKF* for VAT on costs relating to investment activities and the sale of shares. The costs of the investment activity did not "burden the investment activity in the sense that fees were incorporated into the price of investments that were sold". According to *AB SKF*, then, they could be overheads of the business as a whole. HMRC's counsel tried to find a distinction between the raising of capital and the generation of income, but the judges considered that this only arose in the CJEU cases because of their facts, not as a principle of law.

The FTT had found that the investment activity was not carried out for its own sake but for the benefit of the University's economic activity in general. It followed that the costs associated with that investment activity were part of the University's overheads. HMRC's appeal was dismissed.

HMRC appealed again to the Court of Appeal. Patten LJ set out the leading judgment. He reviewed the facts, the law and the precedents. He summarised the issue as the need to choose between two different ways of looking at the attribution of inputs to taxable outputs: one, favoured by HMRC, that required a direct transactional link to a particular taxable output, and ruled out deduction for something that was directly linked to a non-taxable investment "activity"; and the other, which took a more general view of inputs that were associated with the business activity as a whole, and did not regard the investment transactions as an end in themselves.

He discussed the different lines of reasoning as set out in a number of CJEU cases, including *BLP*, *Midland Bank* and *Abbey National*. In the last, the CJEU had not ruled out deduction of VAT incurred in relation to the transfer of a business as a going concern, even though the law regarded it as a "non-supply". That implied, even though it did not spell out, a distinction between something that was directly attributable to making exempt supplies (as in *BLP*) and something that was attributable to activities outside the scope of VAT. The Court's decision in *AB SKF* also supported a distinction between the "magnetism and chain-breaking effect" of exempt outputs on the one hand and non-taxable activities on the other.

The judge accepted HMRC's submission that a finding of a direct link to such a supply will render the input tax irrecoverable just as in the case of an exempt output supply. However, he considered that the appropriate question was whether one can link the expenditure to the ultimate economic activity by treating it as a cost component of a specific taxable supply or as an overhead of the business, i.e. are the costs incorporated in the cost of the taxpayer's economic activities.

Finally, he noted the *Iberdrola* decision, and the fact that the CJEU had overruled the A-G's view that the input tax incurred on a benefit provided to someone else without charge should be irrecoverable. He described the decision as the application of a "but-for test of causation to the works themselves".

The university's counsel sought to rely on the CA judgment in *Associated Newspapers*, which he contended related to a similar question. However, the judge said that in that case it was difficult to treat the purchase of an incentive to buy the newspapers as anything but part of the promotion of the taxpayer's business. In this case he considered that the link in transactional terms was more remote and that the decisions in cases like *Kretztechnik* may have depended on a difference in tax treatment between exempt and non-taxable supplies which later CJEU decisions appear no longer to follow. There was some force in HMRC's comparison with the *Wellcome Trust* case, in which the VAT on the costs of selling a large investment holding was held to be wholly consumed in the selling operation, rather than being capable of attribution to wider economic purposes of the charity concerned.

Overall, the law was not *acte clair*, and the Court of Appeal decided it was appropriate to make a reference to the CJEU. The parties were asked for assistance in drafting the questions.

Court of Appeal: *HMRC v Chancellor, Master and Scholars of the University of Cambridge*

5.3.2 Special method

HMRC refused to agree a proposed special method, and the company appealed to the FTT. The appellant provided domiciliary care to patients in their own home. It also provided training in the same activity, to its own staff and to outsiders. Until January 2017, this was treated as a taxable activity because the company was not an eligible body; since then, it has received government funding for the training and it has therefore been treated as exempt.

In 2011 the company incurred input tax on two buildings (Unit 1 and Unit 3) that were used for training purposes. It suggested a method which sectorised costs relating to the buildings. The apportionment would be based on physical use as represented by floor area. After a visit to the premises, HMRC agreed to the method in 2012.

In 2014 the company formed a VAT group with two non-trading subsidiaries, and asked for confirmation that the PESM could continue. HMRC did not accept this, and asked the company to make a formal request for a new PESM incorporating the activities of the new group members.

By now the company was providing exempt care, taxable cleaning and taxable training. It proposed a similar method to that agreed in 2011: property costs were to be allocated on an area basis, and general costs on an income basis. As under the 2012 agreed method the appellant had asserted that a basement office and breakout area in Unit 1 were used exclusively for the purposes of taxable training and that the whole of Unit 3 was similarly used.

HMRC rejected the proposal, stating that "Floor space can be used as a measure of the use of input tax, but only where the facilities are designed for a specific function – an example might be the apportionment of a building which comprises residential and commercial spaces could be apportioned by the floor area because each area has a unique purpose and supply. However, the information obtained so far gives no indication that these spaces are only intended to be exclusively taxable, they could serve any purpose, so this makes the method very difficult to audit. The method also assumes that an empty room is used and can only be used, for taxable supplies. It is our opinion that if no taxable training is taking place, the rooms could and should be treated as residual because there is nothing in the design of the room that limits its used to taxable supplies. The method proposed should reflect actual use, which this PESM proposal does not do. Whilst the main business activity may use the building costs in a different way to the training services, you need to demonstrate that the choice of the floor space provides a more accurate measure of the use of the building costs than outputs."

In 2016, the appeal first came before Judge Bishopp (TC05003). He pointed out that HMRC had decided that the agreed special method was automatically cancelled by the creation of a VAT group. He questioned whether this was the case, and confirmed that HMRC had never issued a special method override notice. In the end, the FTT decided to set this decision aside and reconsider the matter, once HMRC had reconsidered the legal basis of the dispute.

The new Tribunal (Judge Amanda Brown) made a number of findings of fact, noting in particular that no part of Unit 1 was exclusively used for training. However, that was balanced by the fact that parts of the building that had mixed use were allocated exclusively to exempt supplies.

The judge also noted that the taxpayer's representative had abandoned all but one of his arguments during the course of the hearing. The only remaining issue was whether the proposed method gave rise to a fair and reasonable attribution of input tax as between taxable supplies and, if so, whether that result was more fair and reasonable than the standard method.

HMRC asserted, without authority, that an approved method must be auditable by HMRC which required the appellant to be able to evidence precisely what use was made of the various spaces. They argued that the outcome and the operation of the method were both relevant in determining its fairness and reasonableness.

The Tribunal agreed that the operation and auditability of a method were relevant to its fairness and reasonableness. However, the Tribunal considered that the proposed method was materially identical in terms of operation and audit to that proposed in 2012 when HMRC accepted it was fair and reasonable. They submitted that they were not in error in doing so in 2012. To now conclude that a completely different result arose from VAT grouping with non-trading entities that in no way influenced how the property inputs were used was perverse. There might be weaknesses in the operation of and auditability of the method but they were precisely the same weaknesses as were present in 2012 when HMRC accepted it as a fair and reasonable method. The Tribunal saw no reason to now conclude that the method was not one within the relatively broad group of possible methods which could be considered to be fair and reasonable.

The standard method would only give rise to recovery of a little more than 1% of the input tax on Unit 3. The PESM would give 20.9%. The building had unused for long periods, but had been subject to an option to tax, so disposal or unrelated lettings would have been taxable. The Tribunal did not consider a method that produced 1% recovery was more fair and reasonable in the attribution of a relatively small amount of input tax.

The judge directed that the proposed method should be applied between 2014 and 2017. Because of the change in the liability of the training in 2017, a new method would have to be agreed from that date.

The appeal was allowed.

First-Tier Tribunal (TC06345): *Dynamic People Ltd*

5.3.3 Empty properties

A Portuguese property management company had opted to tax some buildings and recovered input tax accordingly. The tax authorities carried out an audit and found that some parts of two buildings had been empty for more than two years, and directed that input tax adjustments were required as a result. The company appealed, and questions were referred to the CJEU.

The court noted that the right to deduction was based on the intention of use at the time the input tax was incurred. That right was not lost if, due to circumstances beyond the taxpayer’s control, the inputs could not subsequently be used for taxed transactions. This did not fall within the art.185 subsequent changes that required amendment of the deduction. The Portuguese law, which effectively made the right to deduct dependent on the outcome of the economic activity rather than the intention, was contrary to the PVD.

The CJEU refused to limit the temporal effect of this ruling.

CJEU (Case C-672/16): *Imofloresmira – Investimentos Imobiliários SA v Autoridade Tributária e Aduaneira*

5.3.4 Updated Notice

HMRC have updated their Notice *Capital goods scheme*. The preamble states that the only change from the November 2017 version is a minor stylistic alteration to paragraph 4.12, which relates to "refurbishment in phases":

If you do this you'll need to decide whether the work should be treated as a whole for CGS purposes or whether there's more than one refurbishment. If you think that each phase is really a separate refurbishment then they should be treated separately for CGS purposes.

Normally there's more than one refurbishment when there are separate contracts for each phase of the work, or where each phase in a contract has separate options. Each phase would need to be completed before the next phase starts.

A refurbishment which is only undertaken in phases because the building is occupied and where the contractors work on one floor at a time is normally considered to be only one refurbishment.

This may relate to the case of *Water Property Ltd* (TC05450), in which part of the question was whether costs of separate phases of work should be added together.

Notice 706/2

5.4 Cars

Nothing to report.

5.5 Business entertainment

Nothing to report.

5.6 Non-business use of supplies

Nothing to report.

5.7 Bad debt relief

Nothing to report.

5.8 Other input tax problems

5.8.1 MTIC argument rejected

A company appealed against a refusal of input tax amounting to £1.4m in relation to April and June 2006. The company had in 2001 been involved in a criminal prosecution for conspiracy to cheat the revenue which was struck out in 2005 because HMRC had withheld vital evidence from the defendants, so there had been an abuse of process. The FTT (TC03059)

concluded in late 2013 that, at the very least, its directors would therefore have a detailed knowledge and understanding of the risks of MTIC fraud. There were a number of features that confirmed the usual decision, that the directors knew or ought to have known that their later transactions were connected with fraud.

The company appealed to the Upper Tribunal on the basis that the FTT did not properly set out its reasoning. The UT agreed: although the FTT had listed 12 factors that HMRC said indicated that the company's trading was "too good to be true", it did not explain why it had considered that those factors were satisfied, and had not explained the inference (if any) it had drawn from the absence from the hearing of one of the directors.

The UT considered whether it could remit the case to the same FTT to set out its reasoning more clearly, but decided that the length of time since the original hearing made this impractical. Instead, it would remit the case to a differently constituted FTT for rehearing, with specific directions on case management to make sure that a proper decision was reached this time.

The new appeal came before Judge Sarah Falk over two days (the original hearing had taken nine). She started by expressing regret that the parties had effectively agreed the approach to take in the new appeal, rather than asking for a case directions hearing at which a judge could consider the Upper Tribunal decision. Nevertheless, in the interests of dealing with cases fairly and justly and avoiding cost and delay, she decided to proceed to a conclusion based on the material before her.

The judge then went through the various factors which HMRC alleged should have alerted the trader to the fact that the transactions were connected with fraud. The judge decided that, although there were points that were "surprising", and they should certainly have alerted a prudent trader to the significant risk of fraud, HMRC had not discharged the burden of showing that there was no other reasonable explanation. She was satisfied that the trader had a reasonable response to all of HMRC's arguments.

The company's appeal was allowed. It is clear that the judge was concerned, at the very least, to set out the reasons for doing so very clearly, in case of a further appeal to the Upper Tribunal (this time by HMRC).

First-Tier Tribunal (TC06350): *Synectiv Ltd*

5.8.2 Addition to s.33 bodies

The *VAT (Refund of Tax to the Essex Police, Fire and Crime Commissioner Fire and Rescue Authority) Order 2018* specifies a new government body entitled to recover input tax under VATA 1994 s.33 on non-business supplies with effect from 1 February 2018.

SI 2018/16

6. ADMINISTRATION AND PENALTIES

6.1 Group registration

Nothing to report.

6.2 Other registration rules

6.2.1 Consultation

Following recommendations by the OTS in its report on VAT simplification, the Chancellor announced in the Autumn Budget 2017 that the government was not considering a reduction in the threshold. Instead, it would be frozen for two years from April 2018.

However, in the Spring statement in March, he announced that HM Treasury will consult until 5 June 2018 on the effects of the current VAT threshold on business growth, and ways to smooth the cliff-edge effect for businesses of reaching the threshold. Policy options considered in this consultation include:

- the EU proposal for SMEs, which would allow businesses to exceed the threshold by 50% for up to a year without registering, and introduce separate thresholds for absolute exemption and simplified administration;
- two options for 'administrative smoothing', suggested by the OTS:
  - extending the first period for which a business has to account for and pay VAT to 6 months; and
  - applying the threshold test over two years rather than over a single year;
- financial smoothing, including examination of practices in other countries, the OTS suggestion of early years' reductions, and a progressive structure along income tax lines.

There is also a proposal to extend the small business exemption to businesses established in other Member States, which currently do not benefit from any registration threshold. However, it is considering a lower level for this threshold (€85,000, currently about £75,000) and an EU-wide threshold above which a business would not benefit from any national thresholds (proposed at €100,000). This seems to be in line with the Commission's proposals set out at 4.4.2.

In outlining its argument, the government says, among other things:

- the UK threshold of £85,000 is the highest in the EU and among OECD nations, more than double the average in the EU and the OECD which is around £29,000 for both;
- only around 1.2 million businesses – out of about 5.7 million total businesses – are above the VAT threshold;

- the VAT threshold exempts businesses from VAT, and therefore costs the Exchequer money each year – in 2017/18 it is forecast to cost £2.1bn.

www.gov.uk/government/consultations/vat-registration-threshold-call-for-evidence

6.2.2 Article

In an article in *Taxation*, Julie Butler examines the CJEU decision in *Shields & Sons* and the implications for farmers wishing to use the Agricultural Flat Rate Scheme.

Taxation, 15 March 2018

6.3 Payments and returns

Nothing to report.

6.4 Repayment claims

6.4.1 Builders' block

The Upper Tribunal has released a further decision in relation to Taylor Wimpey's claim for historic input tax blocked under the various versions of the "builders' block". The previous decision was covered in the April 2017 update, and set out various issues of principle for the parties to attempt to apply in order to reach an agreement.

Four matters remained to be decided:

- whether claim items which were not fixtures were "fittings" and "incorporated" for the purposes of the block;
- whether such "incorporated fixture" items were excluded from the block before amendments made in 1984;
- whether "non-incorporated" items were a separate standard rated supply or part of a composite zero-rated supply of a house;
- if they were separate supplies, whether the unpaid output tax should be offset against the unclaimed input tax.

The case is very specialised and fact-specific, so only a very brief summary of the conclusions is included here.

The UT decided that all the claim items were either fixtures or installed fittings, and so were incorporated in the buildings for the purposes of the block.

From 1982 "Low Specification Appliances", including extractor hoods, were "ordinarily installed". The claim therefore succeeded in respect of these items between 1982 and 1984, when amendments excluded most electrical goods.

Because the UT had concluded that all the items were "incorporated" in the building, there was no possibility of separate supplies. They were all part of a composite zero-rated supply. The UT did not consider the issue further, as it would be purely theoretical.

By contrast, the UT decided that it would consider the question of offset as a matter of law, in case an appeal found that it was wrong on the earlier point. After a lengthy consideration of statute and precedent, the judge concluded that it would be appropriate to offset the output tax due against any input tax claimed. As the output tax would in all cases be higher, that would rule out any repayment to the company (but the excess output tax would not be collectable).

Upper Tribunal: *Taylor Wimpey plc v HMRC*

6.5 Timing issues

6.5.1 Crowdfunding

A company raised £672,447 using a crowdfunding platform, "Kickstarter". It received this amount, net of fees, on 6 January 2015. HMRC ruled that this triggered the "forward look" registration test on 16 December 2014. Initially the company argued that it did not have an intention to make taxable supplies, but by the time of the hearing it had accepted that it did. The question before the FTT was whether the receipt of the crowdfunding money created a tax point. The FTT had to consider whether the receipts were consideration for a supply of services, or consideration for a supply of vouchers; and if they were consideration for a supply of vouchers, whether they were "single purpose vouchers".

The aim of the company was to send an unmanned robotic landing module to the South Pole of the moon and drill for moonrock. The company would also place a 21st century time capsule in the borehole, including information about the subscribers to the mission. This was eventually accepted as capable of being a taxable supply. Those who pledged at least £60 received a certificate that referred to itself as a "voucher for your digital memory box in the time capsule".

The FTT considered the precedent from the Court of Session in *Findmypast Ltd* in deciding what constituted a voucher. The judge set out the issues for determination in the present case as:

(1) To what services is a backer contractually entitled in return for a payment of £60?

(2) Does the £60 amount to a prepayment for the supply of those services?

(3) Does the backer receive a face value voucher?

(4) If so, is that face value voucher a single purpose voucher?

The company's representative submitted as follows:

(1) The principal benefits to a backer pledging at least £60 were as follows:

(a) The right to upload digital information to a digital memory box, and/or

(b) The right to include a strand of hair in the time capsule.

(2) Payment of the £60 is not a prepayment for a future supply of services. In particular it was not known at the time of payment what the backer would receive, either in terms of digital or physical space or in terms of the quantity of such space. Further, it was uncertain whether any supply at all would take place because of uncertainties inherent in the mission.

(3) The backer receives a face value voucher satisfying the requirements of paragraph 1(1) Schedule 10A.

(4) The face value voucher is not a single purpose voucher because it represents a right to receive more than one type of service, namely digital space and physical space.

HMRC responded in turn:

(1) Backers were contractually entitled to £60 worth of digital space in a digital memory box. There was no contractual entitlement to physical space.

(2) The payment of £60 was a prepayment for a future supply of services.

(3) Backers do not receive a face value voucher because the conditions in paragraph 1(1) Schedule 10A are not satisfied.

(4) If there is a face value voucher, then it is a single purpose voucher. This is because the contractual entitlement is limited to digital space, or because digital space and physical space are properly to be regarded as one type of supply.

The judge considered each question in turn. In relation to the first, he was satisfied that the appellant was contractually obliged to provide digital space and/or physical space in the event that the project was completed. However, it was uncertain how much space of either kind would be provided for a pledge of £60.

The judge also accepted that there was significant uncertainty at the time the payment was made, including uncertainty about whether the project would ever go ahead so whether anything would be supplied. The payments therefore did not amount to prepayments for a supply.

The judge concluded that the rights acquired by the subscribers did satisfy the various conditions for a face value voucher. The company argued that this could not be a single purpose voucher because the subscriber could receive “physical space” (to send a strand of hair) or “digital space” (to send information). The judge did not consider this to be a relevant distinction, in accordance with the purpose of the legislation as explained in the *Lebara* decision. The question was whether the VAT chargeable could be determined with certainty at the time of the payment; as both types of supply would be standard rated, the voucher counted as “single purpose”.

The appeal was therefore dismissed.

First-Tier Tribunal (TC06286): *Lunar Missions Ltd*

6.6 Records

Nothing to report.

6.7 Assessments

6.7.1 Not best judgement

A trader appealed against an assessment for £29,539 for VAT periods from 06/11 to 09/14. HMRC had enquired into the affairs of a second-hand car dealer and had concluded that his business was making unsustainable losses. They decided that he had to be understating sales, and effectively raised the assessment based on the figures for deficits in the accounts.

Judge Fairpo acknowledged that the trader's paperwork was terrible, but found him a credible witness. She held that HMRC's assessment was a pure guess, allowing no other explanation for the losses and deficits. It was not made to best judgement, but it was impossible for her to determine the proper tax due with any degree of accuracy. She directed that the assessments should be reviewed by HMRC to take into account the appellant's evidence about the funds that he had introduced from his mortgage and other debts in order to finance the deficits, and to discuss the figures with the trader's accountant. If revised figures could not be agreed, a further hearing would be necessary.

The appeal was allowed.

First-Tier Tribunal (TC06335): *Thomas O'Rouke t/a Southgates UK*

6.7.2 Assessment

An individual was assessed to a total of £14,605 to reflect disallowance of some input tax items and to charge output tax on underdeclared sales. On two occasions, in July 2016 and July 2017, the trader's representative contacted the Tribunal to say that the trader had been admitted to hospital and neither he nor the representative would attend the hearing. On the second occasion, the judge issued a direction requiring production of medical evidence, with which the trader did not comply.

The hearing subsequently went ahead without the trader being represented. The essence of his appeal was that he had started a business in connection with a former colleague, and the sales that HMRC were assessing on him had in fact been made by the colleague. The judge reviewed the evidence presented by HMRC and concluded that the trader fell far short of the required burden of proof – it appeared that he had carried out a deliberate deception. HMRC had fairly put to him that the input tax claimed on a truck was based on a forged invoice, and he had come up with no convincing explanation to show that the document was genuine.

The appeal was dismissed.

First-Tier Tribunal (TC06388): *Paul Shore*

6.8 Penalties and appeals

6.8.1 Default surcharge

A company appealed against a 5% surcharge of £1,192 for its 11/15 quarter. Its grounds of appeal, submitted only on paper, were that the company was waiting for a disputed CIS repayment for the tax year 2014/15. This was also the reason for the default in the 08/15 period, after a first default in 05/15. The company had only registered for VAT on 22 September 2014.

The Tribunal reviewed the history of the defaults and the correspondence based only on HMRC's files. Judge Gammie noted that the company had in fact paid the outstanding VAT before the CIS repayment was received, which suggested that it was not the only factor leading to the delay. There was no record of an attempt to negotiate Time To Pay. From the limited information available in the absence of an appearance by the taxpayer, the judge had to conclude that there was no reasonable excuse. The appeal was dismissed.

First-Tier Tribunal (TC06288): *NSF Utilities Ltd*

An individual appealed against a 15% surcharge of £5,922 for the period 03/17. He was represented at the hearing by his accountant. The grounds of appeal related to a late receipt from a customer, which the taxpayer thought – based on unevidenced assurances from his bank – would clear in two days and give him enough money to pay the unusually large VAT liability for the quarter.

Judge Poon noted that the cheque had been presented on Friday 5 May, and it was not reasonable in any circumstances to expect it to clear by the due date of Sunday 7 May. There was some dispute about whether an instruction to pay had been made on 6 May or on 9 May, but the judge concluded that, on the balance of probabilities, an instruction had been made in time but had been refused because of a shortage of funds.

She then turned to that shortage as a possible reasonable excuse. The business had suffered a substantial default, and the proprietor had brought forward another contract and had his workforce on overtime trying to complete it in order to be able to bill it in time to pay the VAT. All of this appeared to be the actions of a conscientious and diligent businessman who was doing all he could to meet his obligations. The judge considered that, in all the circumstances, the shortage of funds was a reasonable excuse, and allowed the appeal.

First-Tier Tribunal (TC06282): *Jonathan Skuce*

A company appealed against a 5% surcharge of £9,573 for its 05/17 period. The VAT of £191,471 was paid on Monday 10 July, 3 days late. The grounds of appeal amounted to no more than "difficult cash flow and unfairness"; Judge McNall could find no reasonable excuse. He considered that the company had done too little, too late to make sure that the money was available. Its appeal was dismissed.

First-Tier Tribunal (TC06310): *Norman Emerson Group Ltd*

A company appealed against surcharges for four successive periods from 12/13 to 09/14. It was common ground that the company's major customer had wrongly deducted CIS tax during this period (applying the

20% deduction to an invoice that included a considerable amount of materials, which ought to be paid gross), and that money was sitting with HMRC. The company put forward two different defences based on this: either the excessive tax deposited with HMRC meant that it had no net liability, or the resulting cash flow difficulties constituted a reasonable excuse.

HMRC were prepared to allow the overdeduction for the 09/13 period, as it occurred shortly before the due date for that period. However, the company had been in the surcharge regime since 03/12, and should have been well aware of its responsibilities; by the due date for 12/13, it ought to have taken steps to rectify the situation, or else to find alternative sources of finance or apply for Time to Pay.

Judge Popplewell did not accept that the director genuinely believed that an excessive CIS deduction could be set against a VAT liability. On the balance of probabilities, he knew that it could only be set against PAYE or recovered in the following year. He considered the application of *Steptoe* to the circumstances at length, and concluded that the director had taken conscious decisions to pay other creditors; the cash flow history of the company did not support the assertion that the CIS deduction was the main or only cause of the late payment of VAT. The effect of the deduction was foreseeable, and the result could have been avoided by the company putting alternative plans into action or asking for Time to Pay. The appeal was dismissed.

First-Tier Tribunal (TC06333): *SDL Interiors Ltd*

A company appealed against a £448 surcharge for its 06/17 period. Its grounds were that HMRC was holding CIS tax; its profits for the year ended 30/11/2016 was only £97 on turnover of £22,753. Judge Fairpo did not accept that there was a reasonable excuse. The CIS deduction was foreseeable; the credit for the 2016/17 tax year had been set against VAT liabilities for earlier periods, and the trader could not reasonably believe that the 2017/18 deductions could be utilised as early as 06/17. The appeal was dismissed.

First-Tier Tribunal (TC06342): *Skytone Events Ltd*

A sole trader appealed against a surcharge of £1,726 levied at 15% for period 11/16. The trader had entered the surcharge regime in 02/15, and had not had to pay the 2% and 5% charges because they were below £400. The 10% surcharge of £928 for period 05/16 had been paid and not appealed.

The grounds of appeal were only that the trader thought "Monday would be acceptable when the due date fell on a weekend"; the amount was unfair; and it would impact heavily on the business. None of this could constitute a reasonable excuse; HMRC's notices made it clear that payment had to arrive no later than the due date, even when that fell on a weekend. The appeal was dismissed.

First-Tier Tribunal (TC06353): *Stephen Richard Hall t/a Deli-Licious*

A partnership appealed against a surcharge of £1,292 for its 03/17 period. It had been registered since 1986 and had been in the surcharge regime since 09/11, having appeals against some earlier surcharges dismissed in January 2014. The liability for 03/17 was paid one day late. The

correspondence showed that a partner had claimed not to be aware that payment had to be made before the weekend when the due date fell on a weekend. He also claimed that HMRC had misallocated his payment to an older debt, but there was no doubt that it had been paid after the due date.

Judge Thomas accepted that there was plenty of warning about weekends published by HMRC. Although the firm appeared to be paying regular weekly sums, there was no evidence that it had agreed Time to Pay with HMRC. The appeal was dismissed.

First-Tier Tribunal (TC06369): *Romano's (a partnership)*

A company appealed against a surcharge of £1,020 for its 04/17 period. The Tribunal also considered a further surcharge of £2,292 for the following period, although it was not formally covered by the appeal. The company argued that there was a direct debit in place but HMRC failed to process it; it had been cancelled earlier, but the company believed it had been reinstated in time for HMRC to call for the money due for these periods, for which the returns had been submitted on time.

Judge Fairpo agreed with HMRC that its letters to the taxpayer clearly explained that a direct debit was not in place and it would need to make direct transfers to settle the liability. A prudent trader would have asked questions earlier. The appeal was dismissed.

First-Tier Tribunal (TC06377): *Crown Blinds Ltd*

A sole trader appealed against 37 surcharges from 12/05 to 12/14, totalling £5,436. HMRC had accepted two reasonable excuses on review (for 06/08 and 09/08), which reduced the amount under appeal to £5,304 by the hearing.

Judge Gillett noted that the trader had had significant particular problems that amounted to a reasonable excuse – a computer breakdown in 2008 that HMRC had accepted, and the death of a relative that he allowed for a further three periods in 2010/11, reducing the charges by a further £512. However, the rest of the periods were simply a result of difficult trading; the trader accepted that he had in most cases charged VAT to his customers and had received it, and had therefore chosen to use that money to pay other bills. The appeal was dismissed, apart from the cancellation of a further 3 periods.

First-Tier Tribunal (TC06399): *Philip Ashley Legg*

In an article "A Perfect Storm" in Taxation, Mike Thexton sets out the circumstances of the *Global Switch* case (TC06252). It appears likely that the company will appeal to the Upper Tribunal against the £297,000 surcharge.

Taxation, 1 February 2018

6.8.2 Problems with review

A company registered in Jersey was told by HMRC that it should be registered for VAT on the basis that it was supplying services from a fixed establishment in the UK. A penalty was raised under s.67 VATA 1994. The company argued the unusual ground that there was no appealable decision, so the First-Tier Tribunal (TC05375) would not have

jurisdiction to consider the matter. This was on the basis that the "decisions" were in the form of letters that did not appear to contain a final conclusion. The letter stated that the company had been trading above the threshold and should be registered, and asked for a schedule of income from UK clients; the judge concluded that this was not hypothetical but a clear decision about registration, and s.83 was therefore engaged.

The taxpayer's counsel argued that the registration certificate was invalid because it had been sent to the wrong address. The judge agreed with HMRC's counsel that a registration does not have to be "notified" to be effective. The backdated registration to April 2008 was therefore also an appealable decision.

There is a requirement for a penalty to be notified to the taxpayer. The judge relied on the precedent of *Grunwick Processing Laboratories Ltd v Customs & Excise* (1986) in arriving at the conclusion that failure to notify does not wholly invalidate the penalty – it simply makes it unenforceable until it is notified. Later notification therefore rectified the failure. However, the letter accompanying the penalty notification stated that the company could "ask for" a review, rather than explaining that it had a statutory right to a review. The judge considered that this was a significant failure and it invalidated the decision. As a result, there was no appealable matter in respect of the penalty.

HMRC issued a revised penalty assessment, correcting what they said was a calculation error, which rendered the FTT decision effectively irrelevant. Nevertheless, they appealed to the UT, because they considered the point to be an important one of wider application. Judge Berner and Judge Falk decided that they did have jurisdiction to consider the matter, even though it appeared to be purely theoretical, because it related to a point of law arising from the FTT decision.

It was common ground between the parties that VATA 1994 s.83A imposes an obligation on HMRC to offer a review. This is in contrast to the position in relation to direct taxes under the Taxes Management Act 1970, where HMRC has a discretion to offer a review. The real dispute between the parties was over whether HMRC did in fact comply with the obligation under s.83A, and the consequences of any failure to comply.

HMRC argued that the letter offering the review complied with the law. Although it appeared to offer a choice rather than a right, it was clear to any reasonable reader that the recipient was given the opportunity to have the decision reviewed, and this was under their control. They also argued that the legislation did not detail the consequences of a failure to offer a review; in the absence of a specific provision, the failure should not be taken to invalidate the notice.

The UT noted that there were a number of precedents dealing with failures to comply with requirements of the law, and these sometimes invalidated the underlying action by the authorities. After detailed analysis, the judges concluded that a failure to offer a review did not invalidate the assessment; the two things were separate, and it was still (contrary to the FTT's decision) possible for the taxpayer to appeal a decision, even if no review had been offered.

The judges also agreed with HMRC on the reading of the letter. "The clear implication is that any review asked for will indeed be carried out." They therefore concluded that HMRC had complied with s.83A.

The appeal was therefore allowed as the FTT decision had contained an error of law, but the UT did not exercise its discretion to set aside the decision or to remake it, because the assessment had been withdrawn. There was therefore no purpose in reconsidering the effect of the decision.

Both parties had applied for costs. The judges commented, "Whilst we will of course consider any application for costs, we should point out that the circumstances of this case are unusual. There was no need for HMRC to pursue the appeal for the purposes of the substantive dispute between the parties, because the original penalty assessment has been withdrawn and replaced. HMRC's sole reason for pursuing the appeal was to establish a point of principle. NT ADA has chosen to defend the appeal, but presumably again not for reasons directly related to the ongoing substantive dispute. In those circumstances we would anticipate that the appropriate result is for the parties each to bear their own costs."

Upper Tribunal: *HMRC v NT ADA Ltd (formerly NT Jersey Ltd)*

6.8.3 Costs

A company appealed against a 2013 notice requiring security. It withdrew one appeal at the hearing in November 2016, and HMRC applied for costs. The company made a further appeal and also applied for costs, while HMRC applied to have the second appeal struck out. The Tribunal (Judge Jonathan Richards) awarded costs to HMRC and struck out the company's appeal.

The judge reviewed the history of the dispute, which included a chain of litigation between the owner of the company and HMRC, but also other disputes including prosecutions relating to the operation of a pub. There were disputes about basic facts such as who was actually running the business.

He concluded that the company had acted unreasonably in some parts of its conduct of the proceedings, but not in bringing them, and not in withdrawing when it did. The award of costs reflected these conclusions.

The second appeal was effectively an attempt to relitigate the first decision. It was phrased in terms of an appeal against a refusal to consider new material in relation to the requirement to deposit security, but that was not itself an appealable decision – HMRC had not considered new material and come to a separate new decision about security that could be appealed, but had simply refused to amend their original decision that had been confirmed by the taxpayer withdrawing from the appeal process.

First-Tier Tribunal (TC06309): *The Moreton Bell Ltd*

6.8.4 Strike out

A company applied to reinstate an appeal against a 2013 Post Clearance Demand Note in the amount of £97,382. The appeal was struck out in April 2014 for failure to comply with an Unless Order. The appellant was informed by post and e-mail, but received no reply until a request on 1

June 2017, over three years later, from the same e-mail address, to have the appeal reinstated. The appellant did not attend the strike-out hearing in February 2018.

Judge Fairpo applied the standard criteria for reinstating appeals and missing time limits, and agreed with HMRC that the delay was substantial and there appeared to be no reasonable excuse. Further, the trader's failure to engage with the Tribunal throughout constituted unreasonable conduct, and she awarded costs of the hearing to HMRC.

First-Tier Tribunal (TC06397): *N M Consultants (Logistics) Ltd*

A company appealed against assessments totalling £672,710 in respect of periods between 2012 and 2015. The most significant of the various errors being assessed was a failure to account for output tax on the sale of motorhomes. The appellant contended that they had been adapted and supplied to handicapped persons and therefore were eligible for zero-rating.

The appeal was initially made in a timely fashion. It appeared to be based on a complaint that HMRC were imposing unclear and unreasonable record-keeping requirements. HMRC's statement of case in June 2016 pointed out that this did not appear to be an appealable matter, but the Tribunal did not take this at the time to be an application for strike-out. Further case management directions were issued calling for witness statements. In early 2017 the appellant company went into liquidation; the liquidators continued to ask for extensions of time to comply with the directions, confirming that they intended to maintain the appeal, but there was a "clear and persistent failure to comply with the direction of the Tribunal that witness statements be produced".

Further, it appeared that the grounds of appeal were based on the assertion that HMRC had effectively approved what the trader was doing at earlier visits, and it was then unreasonable for HMRC to raise a retrospective assessment. This was not a matter that was within the jurisdiction of the FTT. The judge granted HMRC's application to strike the appeal out.

First-Tier Tribunal (TC06398): *Scream Wholesale Ltd*

An appellant applied for a summons requiring two HMRC officers to attend the hearing of his appeal and an order requiring HMRC to produce certain files and records. Judge Richard Thomas heard the application and declined to make these orders, and informed the appellant that he was minded to strike the appeal out as having no reasonable prospect of success. He invited the appellant to make submissions, which he did, but the judge struck the appeal out anyway.

The appeal was against an assessment for extra VAT because the trader had applied the FRS percentage to his net turnover rather than the gross amounts. His appeal was based on a number of complaints about the way the FRS was presented to him and other taxpayers, and how he had been dealt with by HMRC.

The judge expressed the problem as follows: "I remind myself that the bar is low when it comes to relevance. But the appellant has not got off the ground, let alone reached the bar or cleared it." The Tribunal could not consider anything other than the correctness of the assessment in accordance with the law, which the taxpayer did not appear to dispute.

The judge commented further "Mr Smith had shown the tenacity and investigative skills one would expect of a good journalist. I do not have sufficient material in my bundle to tell whether his complaints are well grounded, but if what he says is right then he would seem to have some legitimate ground for complaint about his treatment by HMRC. But such complaints are about maladministration. The avenue of redress for that is through HMRC's complaints procedures and from there to the Revenue Adjudicator or the Parliamentary Commissioner for Administration (Ombudsman). I am afraid that his researches, and possibly advice he has received, have led him to be under a major misapprehension about the role of this Tribunal."

The appeal was struck out, as it had no reasonable prospect of success.

First-Tier Tribunal (TC06285): *David James Smith*

6.8.5 Late appeals

On 23 September 2014, HMRC issued a decision that certain building works did not qualify for zero-rating when carried out in 2009 and 2010. The customer, a college, appealed against the ruling on 6 February 2017, more than two years late. It argued that the pending Court of Appeal hearing of Wakefield College's appeal would be critical: if the CA upheld the UT's decision that education of part-funded students was a business activity, its appeal would fail, but if the CA reversed the decision, it would have an arguable case. It therefore applied for leave to appeal late, and for that appeal to be stood over behind *Wakefield*.

The dispute dated from 2013, when the college applied for a retrospective zero-rating certificate in relation to a large amount of the building work. HMRC refused in October 2013; the college appealed to the Tribunal in December 2013, stating that the amount in dispute was £1,375,113. HMRC then decided that their decision should be reissued, which meant that the Tribunal proceedings were stayed. Further correspondence followed, with regular chasing by the Tribunal for progress, and apparently significant delays mainly from the college's side. HMRC continued to correspond with the college and its agent; the agent was adamant that "HMRC indicated that they would not object to a late appeal", and therefore there was no need formally to appeal against the new decision.

When the appeal was finally lodged, on the Tribunal's insistence that the matter be put on a proper footing, HMRC did object. At the hearing to consider whether the appeal should be entertained, HMRC said that they had not received anything of substance from the taxpayer or the agent since July 2015. They had responded to this on 20 July 2015, setting out the issues between the parties, but had received no further information in reply.

The judge (Dr Christopher Staker) decided that it was reasonable to take into account the belief of the taxpayer that it was able to challenge the later HMRC decision in the earlier Tribunal proceedings, without having to commence a new Tribunal appeal. Whether or not this was correct in law, the belief was understandable for a number of reasons, including the apparent implication of various statements by HMRC in correspondence. The Tribunal only insisted on a new appeal form on 24 January 2017, and the appellant filed a new form within 14 days.

The judge noted that an extension should only be granted as an exception to the general rule. He stated clearly that he had taken into account the arguable dilatoriness of the appellant, but he did not consider there to have been bad faith. If HMRC had wanted to force the matter, they could have applied to the Tribunal for directions, but they had not done so. The amount of money at stake was considerable; it appeared that the case was not prima facie hopeless; and, although HMRC argued that they would be prejudiced because the officers who were involved the case had moved on, that would have been the situation at least up until July 2016 when HMRC were clearly still willing to carry on deferring the matter.

The judge emphasised that he was not applying a more relaxed attitude than would be applied by a court under the Civil Procedure Rules, but in the interests of dealing justly with the case, he granted the application to bring the appeal late.

First-Tier Tribunal (TC06356): *Newcastle Under Lyme College*

A company applied for leave to appeal out of time against an assessment dated 7 April 2015. The director argued that he had believed that his former accountants were dealing with the matter, and they had failed to provide him with crucial information. He had received a penalty assessment and signed a document agreeing to suspension conditions, but he thought that was part of the appeal process.

HMRC argued that there was no good explanation for the delay. The company had changed advisers twice since the decision, and could have enquired into the progress of a supposed appeal on either occasion. This had not happened. Similarly, correspondence relating to the penalty should have prompted an enquiry. The latest adviser wrote in June 2017 asking for permission to make a late appeal without any reference to an earlier appeal having been made (either in fact or in belief), and after HMRC responded that an application would have to be made to the Tribunal for permission, this was not done for another two months.

Judge Fairpo applied the *Data Select* criteria, carried out the appropriate balancing exercise, and decided in favour of HMRC. She did not consider the merits of the underlying case at all, and did not explicitly say that the amount of VAT at stake (only £4,990) was not particularly great; however, a prudent taxpayer would have done more within a two year period to investigate progress in an appeal, if there was a genuine belief that one had been made.

First-Tier Tribunal (TC06370): *Homechoice Flooring (Skegness) Ltd*

6.9 Other administration issues

6.9.1 Brexit update

On 30 January 2018, the EU Commission set out a brief statement of the likely consequences of the UK leaving the EU for customs duty and for VAT. While arguments continue about whether there will be a "hard Brexit" (leaving the customs union and Single Market without any special arrangements) or something softer, this is at least a fairly concrete idea of some of the changes that we will see, so businesses that are affected can consider what action to take.

https://tinyurl.com/y8bb2svs

6.9.1.1 Registration liabilities

If a UK business makes taxable supplies in another Member State that require local VAT to be accounted for, the rules on freedom of establishment mean that it can register for VAT in that state and deal directly with the tax authorities. Following Brexit, a UK business may be required to appoint a local VAT representative to guarantee compliance.

UK businesses making digital supplies to consumers in other Member States have been required since 1 January 2015 to register for foreign output tax, most likely through the Mini One Stop Shop (MOSS) operated by HMRC. A single MOSS return is submitted to the home tax authority, and the VAT is shared out between the various other countries. Following Brexit, a UK business will have to register using the non-Union MOSS system in one of the remaining 27 countries.

6.9.1.2 Reclaiming foreign VAT

A UK business that incurs VAT elsewhere in the EU can at present claim it back using the electronic refund procedure established by Directive 2008/9 (the replacement for the 8th Directive). This is based on claims made through an electronic portal to the home tax authority, for a calendar year, submitted within 9 months of the year end.

Following Brexit, UK businesses will become "third country traders", and will have to claim using the 13th Directive system. This involves submitting separate claims (in the local language, on paper) to the authorities in each country.

6.9.1.3 Movement of goods

Goods crossing the UK border will all become imports or exports, rather than acquisitions and despatches where they move from or to the EU. The practical aspects of that are still a crucial aspect of the negotiations (paperwork, the potential for delays or simplifications), but there are important cash flow implications for input tax:

- on an import, VAT is paid either on arrival of the goods, or later through a duty deferment account (effectively on about a month's credit), and then reclaimed on the next VAT return;
- on an acquisition, generally the acquisition tax and input tax claim cancel out on the same VAT return.

- This means that the cash flow advantage of acquisitions will disappear. Imports are treated in much the same way as domestic purchases, on which the input tax will generally be paid to the supplier based on the delivery date and then recovered later.
- The VAT difference between exports and despatches is less significant, and clearly all the other aspects of exporting rather than trading within the single market are more important than the VAT change. The main differences are:
- exports are ZR based on various legal conditions that are mainly related to proving that the goods left the UK (at present, the EU);
- despatches have the additional requirement to show the VAT number of the customer and to make further reports on Sales Lists and Intrastats.

6.9.1.4 Supply of services

The supply of services across the UK boundary is much less affected than the supply of goods, but there will be differences of detail, some of which remain to be agreed.

First, the rules on international supplies are mainly related to "place of supply", rather than qualifying for zero-rating on particular conditions. This will generally remain the same after Brexit:

- a UK business making business-to-business supplies (B2B) to a non-UK business will still normally not charge any VAT, and the customer (if in the EU) will still account for a reverse charge as now;
- a UK business buying B2B services does not at present distinguish between suppliers inside or outside the EU, and will not do so in future – in general, a reverse charge will be required.

Some of the differences of detail include:

- the special rules that apply to some B2C supplies where the recipient belongs outside the EU (accountancy, legal services etc.) – these could become "outside the scope" where the customer is simply "non-UK";
- the requirement mentioned above for digital businesses to register elsewhere using the non-Union MOSS;
- the possibility that "specified supplies" of insurance and financial services will generate input tax recovery where the counterparty is outside the UK, rather than outside the EU as at present.

6.9.1.5 Legal rights and wrongs

The "Great Repeal Bill" appears to contain the intention that "everything stays the same until it is specifically changed", for most practical purposes, that is probably all general practitioners need to know. The mechanics of achieving this are controversial and appear to give the government very wide powers to create legislation without a great deal of scrutiny. The history of VAT is littered with botched attempts to introduce new laws which have later been held by the Court of Justice to

be unlawful. In the future, there will be no such external check on the UK's laws.

VAT specialists will be concerned about the authority of EU legislation and case law precedent:

- for disputes that arise after Brexit, in relation to facts arising after Brexit;
- for disputes that arise after Brexit, in relation to facts arising before Brexit;
- for disputes that arose before Brexit but are unresolved by the time we leave the EU.

6.9.1.6 Briefing paper draft withdrawal agreement

The draft legal text of the withdrawal agreement was published in February 2018, then updated non 15 March and revised again on 19 March. The House of Commons Library published a briefing paper on the agreement on 22 March. In relation to VAT, it states that current EU VAT arrangements will apply to goods dispatched or transported from the UK's territory to Member State territory, or vice versa, where dispatch or transport started before the end of the transition period and ended afterwards; however, there seems to be very little substantive commentary on these provisions.

https://researchbriefings.parliament.uk/ResearchBriefing/Summary/CBP-8269

6.9.2 Making Tax Digital for VAT

The Value Added Tax (Amendment) Regulations 2018 have been laid before Parliament and therefore enacted, even though HMRC accept that there are still matters that need to be resolved. They say that the Notice (still being worked on) will have the power to amend the law; it is not ideal for there to be regulations in place that will be disapplied by the Notice, but that is where we are. Important information will follow from:

- the Notice, when it is finalised;
- information from software providers, when more of them become involved;
- information from professional bodies and HMRC when the pilot is up and running (starting in April 2018).

This update will emphasise only two points:

First, that the rules are supposed to apply to the first return period commencing on or after 1 April 2019. That means that someone on a calendar quarter stagger is affected on 1 April, but someone on a different stagger will be affected on a different date. If the accounting year end does not match the VAT year, it may be necessary to change accounting system part way through the year. A trader on annual accounting will only be affected when the next annual return period starts.

Second, to reproduce an extract of the regulation that will come into effect, setting out what has to be recorded in digital form. Note that the current requirement appears to be that the following details have to be so

recorded "as soon as possible" – we await guidance on what this means for such things as petty cash expenses, which presumably will have to exist in non-digital form in some businesses for some period of time.

The following has been inserted in SI 1995/2518. The underlinings are my own emphasis.

32A Recording and keeping of information in electronic form

(1) Subject to regulation 32B a taxable person shall keep and maintain the information specified in paragraphs (2) and (3) in an electronic form ("the electronic account").

(2) The information specified for the purposes of paragraph (1) is—

(a) the name of the taxable person;

(b) the address of the taxable person's principal place of business;

(c) the taxable person's VAT registration number; and

(d) any VAT accounting schemes used by the taxable person.

(3) Subject to paragraph (4) the information specified for the purposes of paragraph (1) for each accounting period is—

(a) subject to sub-paragraph (c) for each supply made within the period—

(i) the time of supply,

(ii) the value of the supply, and

(iii) the rate of VAT charged;

(b) subject to sub-paragraph (c) for each supply received within the period—

(i) the time of supply,

(ii) the value of the supply, and

(iii) the total amount of input tax for which credit is allowable under section 26 of the Act;

(c) where more than one supply is recorded on a tax invoice and those supplies are either—

(i) supplies made which are required to be accounted for in respect of the same prescribed accounting period and are subject to the same rate of VAT, or

(ii) supplies received for which credit is allowable in the same prescribed accounting period,

they may be treated as a single supply for the purposes of either sub-paragraph (a) or (b), whichever is relevant;

(d) the information specified in each sub-paragraph of paragraphs (3) and (4) of regulation 32;

(e) where adjustment or correction is made to the VAT account which is required or allowed by any provision of the Act or any regulations made under the Act, the total amount adjusted or corrected for the period pursuant to that provision or those regulations;

(f) the proportions of the total of the VAT exclusive value of all outputs for the period which are attributable in each case to standard rated, reduced rated, zero-rated, exempt or outside the scope outputs.

(4) The information specified in paragraph (3) may be varied by direction of the Commissioners to make provision about—

(a) supplies of investment gold which are subject to the provisions of regulation 31A;

(b) the operation of the flat-rate scheme under Part 7A of these Regulations (flat-rate scheme for small businesses);

(c) the operation of retail schemes under Part 9 of these Regulations (supplies by retailers);

(d) cases where the Commissioners are satisfied that keeping and maintaining information as specified in this regulation is likely to be impossible, impractical or unduly onerous.

(5) The electronic account must be kept and maintained using functional compatible software.

(6) The functional compatible software must take a form approved by the Commissioners in a specific or general direction.

(7) A direction under paragraph (6) may also specify the circumstances in which functional compatible software may be used or not used.

(8) The information specified in paragraph (3) must be entered in the electronic account for the relevant prescribed accounting period no later than the earlier of the date by which the taxable person is required to make the return or the date the return is made for that prescribed accounting period.

(9) Changes to the information specified in paragraph (2) must be made no later than the end of the prescribed accounting period in which those changes occur.

(10) Where a taxable person discovers an error or omission in the electronic account that person must correct the electronic account as soon as possible but in any event no later than the end of the prescribed accounting period in which the error is discovered.

Regulation 32B is an exemption for those who are currently exempt from online filing by reason of religious belief, disability, age, remoteness of location or other reason. It is unlikely to apply widely. Recent appeals against the requirement to file online have generally been unsuccessful.

SI 2018/261

6.9.3 Compliance checks

HMRC have updated two of their factsheets from the November 2017 versions, adding details of open-source information they may collect and use when dealing with compliance checks:

“HMRC may observe, monitor, record and retain internet data which is available to anyone. This is known as ‘open source’ material and includes news reports, internet sites, Companies House and Land registry records,

blogs and social networking sites where no privacy settings have been applied."

CC/FS1a: General information about compliance checks

CC/FS1b: General information about checks by campaigns and projects

6.9.4 Disclosure of tax avoidance schemes

HMRC have updated their guide Disclosure of tax avoidance schemes – overview to include the new disclosure rules for VAT and other indirect taxes (DASVOIT) which came into effect on 1 January 2018. It explains that there are 3 different disclosure regimes:

- VAT disclosure regime (VADR);
- Disclosure of Tax Avoidance Schemes: VAT and other indirect taxes (DASVOIT);
- Direct taxes (including Apprenticeship Levy) and National Insurance contributions (DOTAS).

The disclosure regime for VADR applies to arrangements entered into before 1 January 2018. VADR does not apply to arrangements that are notifiable under DASVOIT, which came into force for arrangements promoted or entered into on or after 1 January 2018.

VADR has 2 categories:

- listed schemes;
- hallmarked schemes.

Listed schemes are specific schemes (there are 10) that are defined in the disclosure legislation. A trader registered or are liable to be registered for VAT in the UK which is involved in a listed scheme must notify HMRC unless annual turnover (or if part of a group, the turnover of the group) is below £600,000.

Hallmarked schemes are schemes that include or are associated with a 'hallmark' of avoidance defined in the legislation.

The trader does not have to disclose if either:

- a third party, such as the scheme promoter, has voluntarily disclosed the scheme to HMRC and provided the trader with the Voluntary Registration Scheme (VRS) reference number;
- the trader or the trader's group has an annual turnover below £10m.

The Voluntary Registration Scheme cannot be used from 1 January 2018.

More information about VADR is available in VAT Notice 700/8: disclosure of VAT avoidance schemes.

The *Disclosure of Tax Avoidance Schemes: VAT and other indirect taxes*, 'DASVOIT', came into force on 1 January 2018. It applies to VAT and a list of other indirect taxes.

DASVOIT applies to arrangements which are used on or after 1 January 2018. However, there is an exclusion from this for arrangements which were marketed or made available by a promoter, or where a promoter knew about arrangements being implemented, before 1 January 2018.

The main duty to disclose under DASVOIT falls on the promoter of the arrangements. However there are circumstances where the person using the arrangements must disclose. They are:

- if there is a non-UK promoter who has not disclosed;
- if a lawyer is unable to disclose due to legal professional privilege;
- if there is no promoter – for example, it is an in-house scheme.

The rules apply whether they are proposed arrangements yet to be implemented or if they have been implemented.

Arrangements or proposed arrangements are notifiable if:

- they enable, or might be expected to enable, a person to obtain a tax advantage;
- the main benefit, or one of the main benefits, of the arrangements is a tax advantage;
- the arrangements fall within one or more descriptions known as 'hallmarks'.

There are 8 hallmarks. If any of these are met, in addition to the tax advantage and main benefit tests noted in the first 2 bullets above, then the arrangements should be notified.

When a scheme is notified to HMRC a scheme reference number (SRN) may be issued to the person who disclosed the scheme. The promoter must pass this number, as well as information provided by HMRC, to his client. The client must in turn provide this to any other parties to the scheme.

Promoters must regularly provide HMRC with a list of clients to whom they promoted the arrangements. Scheme users also have a duty to notify HMRC of their use of the scheme.

Penalties apply if anyone fails to meet a DASVOIT obligation, i.e. if:

- there is a failure to disclose arrangements to HMRC;
- if a disclosure is not made in the required form and manner;
- if a disclosure is not made within the time limits.

If a promoter fails to make a disclosure and the First-Tier Tribunal deems the maximum penalty amount stated in the legislation insufficient, they can increase the penalty to an amount of up to £1 million.

www.gov.uk/guidance/disclosure-of-tax-avoidance-schemes-overview

HMRC have issued a new Notice *Disclosure of tax avoidance schemes for VAT and other indirect taxes* to explain the new regime. Some of it has the force of law, e.g. the prescription of forms for making disclosures.

Notice 799

HMRC have also updated the old Notice *Disclosure of VAT avoidance schemes* to reflect the fact that it no longer applies to schemes disclosable under the DASVOIT regime. The old rules will continue to apply to arrangements entered into before 1 January 2018.

Notice 700/8

HMRC have published detailed technical guidance on the serial tax avoidance legislation ("STAR"), which introduces a range of new sanctions, including penalties, for taxpayers who entered into tax avoidance schemes on or after 15 September 2016, where HMRC has defeated these schemes after 5 April 2017.

The main aspects of the regime are:

- the legislation doesn't just apply to persistent avoiders, it can apply to taxpayers who have used only one avoidance arrangement that has been defeated – it will affect all new avoidance arrangements entered into on or after 15 September 2016 and defeated after that date and may affect existing avoidance arrangements entered into before 15 September 2016 but defeated after 5 April 2017;
- STAR applies to relevant defeats of arrangements which are covered by the legislative regimes for the general anti abuse rule ('GAAR'), follower notices, disclosure of tax avoidance schemes ('DOTAS') or Disclosure of tax Avoidance Schemes: VAT and Other Indirect Taxes ('DASVOIT'), or its predecessor VAT Avoidance Disclosure Regime ('VADR') – such arrangements are referred to in this guidance as 'avoidance arrangements' – for VAT and other indirect taxes this guidance refers primarily to the DASVOIT regime in Schedule 17 Finance (No. 2) Act 2017, which applies with effect from 1 January 2018;
- following a relevant defeat of avoidance arrangements, HMRC must issue a warning notice to the taxpayer (within 90 days) requiring them to provide to HMRC annual returns of information on their use of arrangements which are DOTAS arrangements or disclosable VAT or other indirect tax arrangements during a warning period which must last for 5 years, but which will sometimes be longer;
- tax-geared penalties apply to new avoidance arrangements used (as defined in STAR) in a warning period and defeated within or after the end of the warning period – 20% for the first defeat, 40% for the second defeat and 60% for the third and successive defeats;
- taxpayers with 3 or more defeats of avoidance arrangements used (as defined in STAR) during the same warning period can be named;
- a taxpayer with 3 defeats of avoidance arrangements that attempt to exploit direct tax reliefs where such arrangements were used (as defined in STAR) in the same warning period, will be subject to a 3 year restriction on access to direct tax reliefs;
- special rules apply to taxpayers who are associated with, or in the same group of companies as, a person who uses avoidance arrangements, or if they are in a partnership which uses avoidance arrangements, and the arrangements are defeated. They will be put on warning as well as the person they are associated with or in the same group as, or in partnership with;
- where a taxpayer enters into arrangements which are, or turn out to be, DOTAS arrangements or disclosable VAT or other indirect tax arrangements , the legislation applies if that taxpayer 'relied on' the arrangements, by submitting a return, claim or election, or failing to discharge an obligation, on the basis that the arrangements work;

- before 6 April 2017, if in relation to a taxpayer's existing avoidance arrangements any of the following apply:
    - the taxpayer's tax affairs in relation to such existing avoidance arrangements are settled with HMRC;
    - the taxpayer provides HMRC with full information about such existing avoidance arrangements;
    - the taxpayer agrees to provide HMRC with full information about such existing avoidance arrangements and thereafter does so within the time limit set by HMRC they will not receive a warning notice;
- at any time, a taxpayer whose tax affairs are not already under enquiry and who has no reason to believe that enquiries are about to start, can prevent a warning notice letter being issued regarding their DOTAS or DASVOIT arrangements – they can do this by fully disclosing to HMRC details of such avoidance arrangements and the amount of tax understated, with a view to settling with HMRC.

www.gov.uk/government/publications/serial-tax-avoidance-regime-guidance

HMRC's introductory guide to the serial tax avoidance rules was updated in January 2018 to reflect new technical guidance on the serial tax avoidance regime (STAR) and disclosure of tax avoidance schemes for VAT and other indirect taxes (DASVOIT).

CC/FS38

Mel Stride, the Financial Secretary to the Treasury, announced on 15 March that he expects Finance Act 2018 (which had just received Royal Assent) to curb avoidance, evasion and non-compliance totalling £1.2bn. The press release highlighted a number of measures, of which the only one relating to VAT was the new regime for online marketplaces.

https://tinyurl.com/y9pmkvox

6.9.5 Consultations

Following the Spring Statement, HMRC are running a consultation until 8 June 2018 on what online platforms could do to make users aware of their tax obligations, similar to the role employers play in the PAYE system. Measures introduced by other countries are described:

- In France, platforms must provide users with a description of their obligations in relation to each transaction;
- Estonia has enabled voluntary reporting from some online platforms, allowing users to opt-in to having data sent to the tax authorities to allow pre-population of returns; and
- Belgium has introduced a new tax rate for those providing services who make less than €5,000, with platforms able to withhold 10% of gross payments.

www.gov.uk/government/consultations/online-platforms-role-in-ensuring-tax-compliance-by-their-users

HMRC are also consulting until 29 June 2018 on VAT "split payment" for online sales as a means of preventing online VAT fraud, whereby a supplier would receive the net amount, with VAT remitted directly to HMRC. The government examined the feasibility of introducing a split payment method in a call for evidence during 2017.

The Commission also received a report from Deloitte on the idea in late 2017. Deloitte's conclusion was that the revenue raised by the government would be less than the costs to business of implementing the system. However, the government may not see that as a fundamental disadvantage, as the costs would be incurred outside the government's budget.

www.gov.uk/government/consultations/alternative-method-of-vat-collection-split-payment

Following the Spring Statement 2018, the government is also assessing the ways VAT and air passenger duty (APD) impact the tourism industry in Northern Ireland, and how the industry can be supported. The consultation closes on 5 June 2018.

www.gov.uk/government/consultations/vat-air-passenger-duty-and-tourism-in-northern-ireland

6.9.6 Treasury committee inquiries

The House of Commons Treasury committee has announced that it will carry out three tax inquiries:

- a wide-ranging VAT inquiry covering four areas:
  - the tax gap, which amounted to £12.6bn of VAT in 2015/16;
  - Brexit opportunities and challenges;
  - burdens on business; and
  - good tax policy, and how VAT measures up against these principles.
- a sub-committee inquiry into avoidance and evasion, and steps that HMRC have taken to address public concerns about tax lost through the actions of individuals and businesses.
- a second sub-committee inquiry into the conduct of tax enquiries and the resolution of tax disputes. This will look at HMRC's governance processes, including such matters as 'sweetheart deals' and whether HMRC gives preferential treatment to big business.

www.parliament.uk/business/committees/committees-a-z/commons-select/treasury-committee/news-parliament-2017/vat-launch-17-19/

6.9.7 Articles

In an article in *Taxation*, Alex Byrne explains how the Criminal Finance Act 2017 could affect tax practitioners. Although it is already a crime to evade tax or to deliberately help another person to do so, the government believes that accountancy practices should be criminally liable for failing to prevent their employees and agents criminally facilitating tax evasion, whether the firm knew about the offence or not. Only proper policies and

procedures, together with records demonstrating regular compliance, will give the practice a defence.

Taxation, 11 January 2018

In an article in *Taxation*, Rupert Moyle and Nadav Shayovitz discuss the Office of Tax Simplification's key recommendations for reforming VAT. There will be both opportunities offered by Brexit (possible greater flexibility) and problems (changes to the economy). Improvements to HMRC's VAT guidance could be made immediately to minimise administrative burdens on taxpayers. Structural changes such as reform of the registration threshold, zero and lower rates and exemptions could take longer to implement.

Taxation, 11 January 2018

6.9.8 Security

A company appealed against notices to deposit security for VAT (£31,500, later reduced to £28,100) and PAYE (£14,457) and NIC (£21,343). The Tribunal reviewed the reasons for HMRC's decision that there was a risk to the revenue and concluded that there was nothing unreasonable in its decision. The appeal was dismissed.

First-Tier Tribunal (TC06283): *School Estates Consultancy Ltd*

6.9.9 Updated Notice

HMRC have updated their Notice *Insolvency* with new contact details for the VAT 426 processing team.

Notice 700/56

6.9.10 Litigation privilege

A company issued proceedings against RBS in relation to an alleged MTIC fraud in the emissions allowances market in 2009. The claimant applied for production of various documents that had been produced by RBS in connection with an investigation by HMRC, including transcripts of interviews with key RBS employees and ex-employees.

The High Court accepted RBS's argument that these documents had effectively been produced in connection with anticipated litigation (defending the company against an assessment of some £90m in disallowed input tax) and were therefore privileged. The fact that RBS was cooperating with HMRC's investigation did not change the nature of the documents nor the reason for their production.

The application for disclosure of the documents was refused.

High Court: *Bilta (UK) Ltd (in liquidation) and others v Royal Bank of Scotland plc and another company*