VAT UPDATE
JANUARY 2016

Covering material from October – December 2015

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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 says that it will be updated "on a monthly basis", but it appears to be less frequent or regular than that. The latest update appeared on 17 November 2015.

Several of the "appeal will be dropped" 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

1.1.1 UK appeals awaiting hearing or decision

- *Associated Newspapers Ltd*: HMRC are appealing to the UT against the FTT's interpretation of SI 1993/1507 on gifts of business services, and also the recent decision that the company was entitled to input tax deduction even on the issue of retailer vouchers which UK law regards as outside the scope of VAT (hearing listed for 5 – 7 October 2015).
- *Bridport & West Dorset Golf Club*: the HMRC list notes that three follower cases were heard by the FTT on the question of unjust enrichment, hearings June 2015, decisions awaited.
- *British Film Institute*: HMRC have been granted leave to appeal to the Court of Appeal against the UT's confirmation of the FTT's decision that the Institute was entitled to rely on the cultural services exemption in the period 1990 – 1996 in support of a *Fleming* claim; the appeals list says that the matter will be referred to the CJEU.
- *The Chancellor, Masters & Scholars of the The University of Cambridge*: HMRC are seeking leave to appeal against the UT's

decision that VAT incurred on investment management was residual input tax of the whole operation.

- *Colaingrove Ltd*: HMRC's list used to contain four separate appeals, but this has been reduced to just TC02534 (fuel – UT decision in favour of HMRC in last update; in April the CA started to hear the company's appeal against the UT's decision that it was not entitled to apply the lower rate to electricity supplied as part of a compound supply of "caravan with electricity"). This therefore appears to be the only remaining "live" issue, but the CA hearing is not mentioned in the HMRC list. The cases about removable contents/definition, removable contents/apportionment and verandas are now resolved.
- *Copthorn Holdings Ltd*: HMRC are seeking leave to appeal against the FTT's decision that they should reconsider their refusal to allow retrospective grouping.
- *Davis & Dann Ltd and Precis (1080) Ltd*: HMRC have received leave to appeal to the Court of Appeal against the Upper Tribunal's decision that the companies did not have the means of knowing that their transactions were connected with fraud (hearing listed for 24 November 2015).
- *Finance and Business Training Ltd v HMRC*: taxpayer is applying for leave to Court of Appeal against UT's upholding of FTT's decision that it was not an "eligible body" by being so closely connected with the University of Wales that it became a "college of the university" – oddly, the list says that "HMRC is appealing", even though the decisions below went against the taxpayer (hearing 7/8 October 2015, decision awaited).
- *Finmeccanica Group Services SpA*: taxpayer has been given leave to appeal to the Court of Appeal against the UT's ruling that it was making supplies in the UK and was therefore not entitled to a refund under the 8th Directive.
- *GMAC UK plc v HMRC*: the UT reaffirmed its own decision in favour of the taxpayer on the basis of the CJEU decision (Case C-589/12). HMRC have been granted permission to appeal to the CA.
- *Investment Trust Companies (in Liquidation) v HMRC*: after the CA effectively reversed the High Court's decision in relation to the companies' direct claims for overpaid VAT, both parties have been given leave to appeal to the Supreme Court (hearing listed for May 2016).
- *Iveco Ltd*: HMRC have been granted leave to appeal to the Upper Tribunal against the FTT's ruling that a claim for repayment was not subject to the cap (hearing listed for 24 – 25 November 2015).
- *Kati Zombory-Moldovan t/a Craft Carnival*: HMRC have been granted leave to appeal to the Upper Tribunal against the FTT's ruling that the trader was making exempt supplies of land.
- *Littlewoods Retail Ltd*: HMRC are seeking leave to appeal against the CA's decision in favour of the company on the question of compound interest on long-term repayments.

- *Longridge on the Thames*: HMRC have been granted leave to appeal against the UT's dismissal of their HMRC appeal against the FTT's ruling that a charity was not in business and could receive building services zero-rated (appeal scheduled to start in the Court of Appeal 19/20 April 2016).

- *Mercedes-Benz Financial Services UK Ltd v HMRC*: HMRC have been granted leave to appeal to the Court of Appeal against the decision that the Agility product involved a supply of services rather than goods (hearing 22 October 2015, decision awaited).

- *MG Rover Group Ltd*: HMRC have been granted leave to appeal against the FTT's decision about who is entitled to claim a refund where an overpayment was made on a group VAT return – case management decisions on this case and *Standard Chartered/Lloyds Banking Group* were issued in March 2015, hearing listed for July 2016.

- *Newey t/a Ocean Finance*: HMRC have been granted leave to appeal to the Court of Appeal 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 listed for July 2016.

- *National Exhibition Centre*: Upper Tribunal has referred questions to the CJEU.

- *Open University*: HMRC have been granted leave to appeal to the Court of Appeal against the UT's decision that the FTT was correct to find that supplies by the BBC to the OU qualified for exemption on the basis that the BBC was "another organisation defined by the UK as having similar objects", hearing listed for February 2016.

- *Pacific Computers Ltd*: the FTT found in favour of a MTIC appellant. HMRC have been given leave to appeal to the UT.

- *Privin Corporation Ltd*: the FTT found in favour of a MTIC appellant. HMRC are seeking leave to appeal to the UT.

- *The "Spotting the Ball" Partnership & Others*: the taxpayers have been granted leave to appeal to the CA against the UT's overruling of the FTT decision in their favour in relation to the exemption of "spot the ball" competitions (hearing listed for November 2015 has been postponed – new date awaited).

- *University of Huddersfield Higher Education Corporation*: the company has been granted leave to appeal to the CA against the UT's decision that its scheme was abusive.

- *Vodafone Group Services Ltd*: HMRC have been granted leave to appeal against the FTT's decision that the trader could replace the reasons for an in-time but disputed claim with the grounds for an accepted but out-of-time claim (UT hearing listed for December 2015).

- *Wakefield College*: HMRC have been granted leave to appeal against the FTT's decision (itself a finding on remittal from the UT) that the college's buildings were used for non-business purposes (hearing 27 – 28 July 2015, decision awaited).

- *Whistl UK Ltd*: the Court of Appeal will hear a further application for judicial review after the High Court held that the UK's amendments to the VAT exemption for postal services were compatible with EU law (hearing April 2016).

1.1.2 Unresolved cases not on the list

The following cases have disappeared from the HMRC website list, but do not appear to be resolved yet:

- *HMRC v Atlantic Electronics Ltd*: the Court of Appeal has reserved judgment in a dispute about the admissibility of evidence in a MTIC fraud case.
- *John Wilkins Ltd and others*: Supreme Court refused HMRC permission to appeal one aspect of the case, in which the Court of Appeal decided that motor dealers were entitled in principle to claim compound interest on VAT repayments. Substantive issue stayed pending the *Littlewoods* decision in the Court of Appeal (High Court applied the CJEU's judgment in Case C-591/10 in favour of the taxpayer, but HMRC have appealed).
- *R (on the application of Rouse) v HMRC*: HMRC appealing against Upper Tribunal's decision that they were not entitled to set off a credit against money owing from the taxpayer under s.130 FA 2008.
- *Shop Direct Group Ltd*: the company is continuing to appeal against the ruling that VAT repayments and interest are subject to corporation tax (Supreme Court hearing concluded 10 December 2015 with judgment reserved, but the case is no longer on HMRC's list).
- *Wilton Park Ltd*: company will appeal to CA against FTT and UT decisions that its charges to dancers for redeeming "Secrets Money" were standard rated (hearing listed for 5/6 October 2016).

1.1.3 Cases in the current update

The current update includes the latest developments in the following cases from HMRC's list:

- *Brockenhurst College*: the Court of Appeal has decided to refer questions to the CJEU. HMRC are appealing against the UT's confirmation of the FTT's decision that supplies of meals to outsiders were an essential part of the education of the students who prepared and served the meals.
- *CCA Distribution Ltd*: HMRC's appeal in relation to 4 of 8 stated grounds against FTT's finding that fraud was not the only explanation of transactions in a MTIC case was successful: case to be remitted to the FTT.
- *DPAS Ltd*: Upper Tribunal allowed in part HMRC's appeal against the FTT's acceptance that a VAT planning arrangement to circumvent the *AXA* judgment was effective – it failed where customers did not explicitly enter into a new contract to receive payment processing services. The final resolution of the case will be stayed pending the CJEU judgments in *Bookit* and *NEC*.

- *Leeds City Council v HMRC*: taxpayer council's appeal to the Court of Appeal against the UT's decision that the three-year cap validly blocked a number of claims for repayment was unanimously dismissed.

2. OUTPUTS

2.1 Scope of VAT: linking supplies to consideration

2.1.1 Public/private divide

A Portuguese company provided services in respect of the planning and management of the regional health service for the Autonomous Region of the Azores. Its customer was a public authority, and it provided services in respect of which the authority would have been regarded as acting in its public capacity; it did not charge VAT, and was assessed to over €5m in back tax and interest by the tax authorities. Questions were referred to the CJEU to determine whether the company could rely on art.9(1) and art.13(1) PVD to put its activities outside the scope of VAT.

The Court went through the PVD provisions and the precedent case law and confirmed that the general application of VAT to all services supplied for consideration must be followed: the company was engaged in economic activity. Further, its services did not fall within the healthcare exemption in art.132, because it was involved in planning and management rather than diagnosis and treatment.

The Portuguese authorities had ruled that art.13(1) did not protect the company because of the risk of distortion of competition; however, the CJEU appears to have regarded the problem as more basic. To fall outside the scope under that provision, supplies have to be made by a body governed by public law, acting in the capacity of a public authority. These were EU law concepts rather than dependent on the laws of any particular Member State. As an exception to the general rules, art.13(1) had to be interpreted strictly. A suggested cross reference to a definition of "body governed by public law" in art.1(9) Directive 2004/18 was dismissed.

The judgment states that it is for the national court to determine whether the company can be regarded as a body governed by public law, but it seems unlikely that it can. Even if it is, its activities would still only be outside the scope to the extent that the referring court considered that such a treatment would not lead to significant distortions of competition.

CJEU (C-174/14): *Saudacor – Sociedade Gestora de Recursos e Equipamentos da Saúde dos Açores SA v Fazenda Publica*

2.1.2 "Overpayments"

NCP reclaimed VAT on alleged "voluntary payments" made by customers in its car parks between June 2009 and December 2012. The total amount claimed was £488,000. The basis of the claim was the fact that customers without the correct change would pay more than the amount required to obtain a "pay and display" ticket for a given period. As the machines did not give change, the company made an extra profit. It argued that this was not subject to VAT, as the displayed prices set the consideration for parking and the balance was "ex gratia". This argument had succeeded in *Borough Council of King's Lynn and West Norfolk* (TC02342).

The company's representative cited cases such as the "Dutch potato case" (*Staatssecretaris van Financien v Cooperatieve Aardappelenbewaarplaats GA* Case C-154/80), *Apple & Pear*

Development Council, Tolsma, *Commission v Finland* and *Societe Thermale d'Eugenie-les-Bains* on what constitutes consideration and the requirement for a direct and immediate link to the supply. She argued that the customer did not enjoy any additional consumption for the additional payment. Customers were not obliged to pay an extra amount: they could park elsewhere, go and find change, or pay by an alternative method. The payment of an additional amount was similar to giving a tip in a restaurant – it was not part of the consideration for the main supply.

HMRC's counsel responded that the correct starting point was the contract made between the parties. The obligation on the customer was to pay not less than the amount displayed on the tariff board: paying an extra amount was a contractual offer which was accepted by the company through the medium of its machine, or an offer by the company of parking at a minimum price which was accepted by the customer paying a greater amount.

HMRC did not appeal the *King's Lynn* decision. It was specific to its facts, because the local authority had statutory restrictions on the amount it could charge for parking. HMRC did not claim that the decision had been wrong, but that it was not applicable to a commercial company.

The Tribunal noted that the approaches of the taxpayer and HMRC were quite different: the taxpayer started with EU concepts of consideration, while HMRC relied on domestic concepts of contract law. As EU law had to be paramount, it was regrettable that there was no EU legal definition of consideration.

The Tribunal did not agree that the extra payments were arbitrary, uncertain or voluntary. A customer was faced with a "binary choice": pay the available change for the right to park, or park somewhere else. Unlike in the *Finland* case, the payment arose from a commercial decision by the customer, and not from "the ability to pay" in the sense of an external judgement about the person's income.

The Tribunal was not convinced that the *King's Lynn* decision was justified on the basis of the statutory order. In any case, that decision was not binding on the Tribunal, and the circumstances were certainly different; many of the arguments about contracts had not been put to the earlier Tribunal.

The company had also argued that the earlier decision created the potential for a fiscal distortion if local authorities were able to keep the "VAT" in their overcharges but commercial companies were not. The present Tribunal did not agree. While two customers might be receiving similar supplies, and the statutory regime might be an "artificial distinction based on insignificant differences", the Tribunal was not persuaded that it should follow a decision that it was not bound by and was not convinced by.

The Tribunal concluded that the full amount paid by the customer was all consideration for the supply of parking, and the appeal was dismissed.

First-Tier Tribunal (TC04784): *National Car Parks Ltd*

2.1.3 Off street parking supplied by local authorities

The Court of Appeal has dismissed an appeal by the Isle of Wight Council and three other appellants against the FTT's decision that treating off-street parking as a non-taxable activity of local authorities would create a significant distortion of competition.

The Lord Chancellor (Sir Terence Etherton) noted that the dispute has a long history – the first decision (in favour of the councils) was given by the VAT Tribunal in 2006; it was referred back to the Tribunal by the High Court, then referred to the CJEU after the Tribunal found for the councils again. In Case C-288/07, the court gave the following guidance to the UK High Court on how the matter was to be determined:

1. ... the significant distortions of competition... must be evaluated by reference to the activity in question, as such, without such evaluation relating to any local market in particular.

2. The expression 'would lead to' is, for the purposes of the second paragraph of art 4(5) of the Sixth Directive, to be interpreted as encompassing not only actual competition, but also potential competition, provided that the possibility of a private operator entering the relevant market is real, and not purely hypothetical.

3. The word 'significant' is... to be understood as meaning that the actual or potential distortions of competition must be more than negligible.

The case was then referred back to the FTT for further findings of fact to apply these principles to the case. After a directions hearing and a substantive hearing, Sir Steven Oliver (with two other panel members) finally found for HMRC, releasing the decision in October 2012.

The councils appealed, arguing that the FTT had incorrectly accepted that the incidence of taxation was an important factor in the pricing of local authority off-street parking – they claimed that pricing policies are wholly driven by other considerations. This, they said, had led the FTT to a conclusion that amounted to an error of law.

The UT examined the FTT decision in detail, noting the reasoning that had been applied. It was agreed that the FTT had identified the issues correctly; it appeared to have taken into account all the relevant factors, and the UT was not persuaded it had wholly misunderstood the relevant law on the pricing of off-street parking services. The decision appeared to be one of fact rather than one of law, and the appellants' attempts to undermine it on legal grounds did not change that. The UT was satisfied that the decision – that non-taxation would lead to potentially significant distortions of competition in pricing and in outsourcing of off-street parking provision – was a reasonable one justified by the findings of the FTT. The appeals were dismissed, and the councils appealed again.

The Chancellor reviewed the basis of the decisions below and the criticisms made of them by the councils' representative. He noted that the correct approach was to consider a hypothetical market-place in which VAT had never been imposed on local authorities' off-street parking charges, and no one had ever suggested that they should be. In that situation, it was plainly reasonable for the FTT to have concluded that the authorities would have charged lower prices, and that this would create a

downward pressure on other providers. There was no basis in the regulations affecting local authority pricing (which were examined in some detail) to undermine that conclusion: "*It is plain that if one supplier in the market for OSCP is able to have lower prices over time because of its special tax status that is likely significantly to distort competition.*"

The UT had been incorrect to suggest that the FTT had concluded that there would be a significant distortion of the outsourcing market, because the FTT had not reached such a decision. However, the FTT had clearly considered that there would have been a distortion; it only failed to express a view on whether that would be significant. In view of the CA's support for the general conclusions of the UT, the appeal was unanimously dismissed.

Court of Appeal: *Isle of Wight Council and others v HMRC*

2.2 Disbursements

Nothing to report.

2.3 Exemptions

2.3.1 Insurance intermediary

A company supplied an "assist service" and a "support service" in relation to insurance contracts. HMRC ruled that these were standard rated. The company appealed, arguing that they were covered by item 4 Group 2 Sch.9 VATA 1994.

At the first hearing, it became apparent that the company's witness did not have personal knowledge of the way the business was carried on. "Out of an abundance of fairness" to the company, the Tribunal decided to adjourn the hearing to allow the appellant to adduce further evidence. At the second hearing, two further witnesses with the appropriate level of personal knowledge were able to provide more detailed answers.

The company assisted insurance companies which had carried out a risk survey before issuing a policy and stipulated "risk improvement requirements" to the policyholder. The "support service" involved providing questionnaire surveys to the insurers, and the "assist service" involved helping the insured to satisfy the risk improvement requirements. In the event of a claim, the company's files could be called in evidence to show whether the insured had complied with the contract and therefore had a valid claim.

HMRC had confirmed in 2003 and 2005 that both services were exempt. This view was changed by a decision in 2013 that was upheld after internal review. The company argued that it was an insurance agent acting in an intermediary capacity; the support service was work preparatory to the conclusion of contracts of insurance, and the assist service was assistance in the performance of contracts of insurance. None

of the exclusions in the Group 2 notes applied: the services were not market research, product design etc., nor were they valuation or inspection, nor were they loss adjusting etc.

The company referred to an EC Directive on insurance mediation, to the HMRC VAT insurance manual, and to Public Notice 701/36, in support of its assertion that its activities fell within the scope of "insurance agent" and "intermediary capacity". The following criticisms were made of the disputed decision:

(1) The statement that an agent's "supply will be to the person requiring the insurance" was incorrect, as recognised in the Manual at VATINS5205.

(2) Although HMRC had stated that "the services must be closely related to insurance and not just incidental to it", no justification of that had been provided; it was disputed by the appellant on the facts. Similarly, the statement that "the supply of risk management lies outside of the insurance transaction chain" was simply incorrect; the services were at the core of the transaction chain, being a crucial element leading to the decision to supply insurance or not.

(3) The statement that the services "have more in common with an actuary than with a broker or agent" was incorrect and unjustified.

The company drew further support from a number of appeals on related, but slightly different, matters, including *Insurancewide.com/Trader Media Group Ltd* (CA 2010), *Morganash Ltd* (VTD 19,777) and *Westinsure Ltd* (UT 2015). It was well-known that HMRC intended to rewrite the Group 2 exemption following the *Arthur Andersen* decision of the CJEU in 2005, but until they did so, the company was entitled to rely on the existing wording of the UK law.

HMRC responded that there had been no change of policy. The business had been transferred from one company to another; when the second company asked for confirmation of a ruling that had been given to the predecessor, a new and more detailed examination of the facts led to the ruling being changed. The services were sub-contracted by the insurer and were not undertaken in the capacity of an intermediary between the insurer and the insured. The company was only acting for one party.

The Tribunal agreed with the company that, to the extent that the UK law provided a wider scope of the exemption than that envisaged by the CJEU in *Arthur Andersen*, the company was entitled to rely on the UK law. The judge summarised the requirements as follows, noting that they were "cumulative":

(1) Riskstop must be an "insurance agent" for the purposes of Item 4. (Riskstop accepts that it is not an "insurance broker" for those purposes).

(2) Riskstop's services must be those of an "insurance intermediary" (as clarified by Note 1).

(3) The services must be related to an insurance transaction (including an abortive transaction).

(4) The services must be provided in the course of Riskstop acting in an intermediary capacity (as clarified by Note 2).

(5) None of the exclusions in Notes 7 to 9 must apply. HMRC accept that Note 7 is irrelevant, leaving just Notes 8 & 9.

The judge considered that the recent UT decision in *Westinsure* was relevant and binding, even though it was mainly concerned with insurance brokers rather than agents and was also subject to appeal to the CA. The UT's analysis of the various precedents on "insurance broker and agent" was quoted; the judge concluded that this appellant did not qualify. "*There is no element of finding prospects or introducing them to the Insurer, nor of putting the Insurers in touch with potential Insureds for the purpose of concluding insurance contracts, or bringing insurance products to the attention of the potential Insureds. Instead, the policy opportunities come to the Insurer either from the Insureds themselves (perhaps through the advertising or reputation of the Insurer) or via a broker; Riskstop plays no part in that process. That means, we conclude, that Riskstop does not satisfy the test to be an "insurance agent" within art 135.*"

This meant that the company failed the first of the five criteria listed. The judge decided not to give an opinion on the other four, beyond making some findings of fact that would be relevant to a higher court's considerations if the case is appealed further. The company's appeal was dismissed.

First-Tier Tribunal (TC04636): *Riskstop Consulting Ltd*

2.3.2 Claims handling

A similar argument is being considered by the CJEU, based on the Directive rather than the UK law. The Advocate-General (Kokott) has given an opinion, but it is not available in English.

A Polish company provides claims handling services in the name of and on behalf of an insurance company, although it has no legal relationship with the insured person. The company receives and processes claims, and enquires into the circumstances in order to agree the amount to be paid under the policy.

The A-G was clear that this was not covered by the exemption for "insurance and reinsurance transactions". "Related services" was a broad enough expression to cover the activities of the company, but they still had to be "performed by insurance brokers and insurance agents". To fall within that definition, the company had to act as an intermediary – it had to have a relationship both with the insurer and with the insured. This company's activities did not extend to concluding insurance contracts or finding new customers and introducing them to the insurer, so it was not an "insurance agent" in line with the CJEU's ruling in the *Arthur Andersen* case. In the A-G's opinion, exemption did not apply.

CJEU (A-G) (Case C-40/15): *Minister Finansów v BRE Ubezpieczenia Sp. z o.o.*

2.3.3 Postal services

A dispute arose about whether "postal money orders" fell within various EU rules about postal services. A Bulgarian company had been given exclusive rights to organise the payment of retirement pensions by money

order, and another company argued that this was contrary to rules on competition.

Although the case is not about VAT, it could be relevant to a dispute about the scope of the VAT exemption. The CJEU ruled that the money order service was not within the scope of "postal services", even if supplied by the Universal Service Provider.

CJEU (C-185/14): *EasyPay AD, Finance Engineering AD v Ministerski savet na Republika Balgaria, Natsionalen osiguritelen institut*

2.3.4 Payment services

A company operated a service whereby dental patients could spread the cost of dental treatment by making regular payments throughout the year. It collected money from patients and paid it over to the dentists, after deducting its own charges. HMRC regarded these as wholly taxable, relating either to "administration" or to "debt collection", in line with the *AXA (UK) plc* case. The company argued that it made separate supplies to the dentists (which would have to be taxable) and to the patients. The supply to the patients was exempt under the heading "payment services". HMRC further argued that, if the contracts were effective in creating a separate exempt supply to the patient, they constituted an abuse of rights.

The company had been registered for VAT from the commencement of its business in 1996. The proprietor realised in 2003 that its services were similar to those of *Sparekassernes Datacenter*, and he successfully applied to HMRC for deregistration at that time. Following the *AXA* judgment, HMRC ruled that the company should again be registered; however, as this was effectively a change of an agreed position, they would not pursue output tax arising before 1 January 2012 (a concession which was extended generally to businesses affected by *AXA*).

The company decided, following *AXA*, that it would change its contractual arrangements so that it made supplies to patients as well as supplies to dentists. It did so because it was clear that its own supplies, as reflected in its contracts at that time, would be covered by the *AXA* judgment. The new arrangements were put into effect from 1 January 2012.

The documentation sent to dentists about the new arrangements explained that they arose from the consequences of the *AXA* judgment, and that they would make "no practical difference". It is therefore not surprising that HMRC argued that they constituted an abuse of rights. However, the covering letter also claimed that the changes "reflect the nature of the reality of our services" – that, in fact, the company had always made payment service supplies to the patients, but these had not previously been recognised in the contracts.

The dentists were invited to ask their existing patients to agree to the new arrangements, and some 30% did so. The company claimed that continuing to pay the direct debits, after being notified of the change, was acceptance of the contractual variation by conduct. After considering Chitty, the authority on contract law, the FTT (TC03058) agreed with this proposition. The new contractual arrangements therefore applied to all existing customers as well as all customers signing agreements for the first time from 1 January 2012.

The Tribunal then had to consider whether, as a matter of economic and commercial reality, the contracts reflected supplies made by the company to the patients, and if so, whether that supply was exempt. The judge concluded that the patient was indeed paying for something more than dental services, and that "something extra" was provided to the patient by the company. That "something extra" included elements of administration, but the judge was satisfied that the predominant supply was related to processing payments. It was therefore a compound exempt supply. It would not be excluded as "debt collection" because that would have to be a supply made to the creditor, not to the customer.

On abuse of rights, HMRC contended that it was clear from the correspondence that the sole reason for the company's change of arrangements was to avoid the consequences of the *AXA* decision. It was therefore intended to obtain a VAT advantage. However, the judge did not regard the contracts as in any way artificial, or contrary to the purpose of the legislation. Precedent cases showed that similar transactions could have different VAT treatments; there were numerous examples of taxpayers learning from the unfortunate experiences of others, and setting up their transactions to be treated in a more favourable way. This was a choice that the law permitted.

The FTT allowed the company's appeal, finding that:

(1) DPAS makes a supply of services to the patient for consideration;

(2) the supply is exempt as a transaction concerning payments;

(3) the services are not debt collection, which would be standard rated, because they are supplied to the debtors, i.e. the patients, not to the creditors, i.e. the dentists;

(4) the £10 registration fee is consideration for a service ancillary to the principal supply which is thus also exempt; and

(5) the contractual arrangements from 1 January 2012 did not amount to an abusive practice.

HMRC appealed to the Upper Tribunal, challenging all five of the FTT's conclusions. First, HMRC's counsel argued that the FTT had been wrong to consider only the contractual arrangements after 1 January 2012. He relied on the *Debenhams* decision as authority for the proposition that the previous contractual arrangements were relevant and significant in interpreting the new contracts. The UT did not agree with this criticism. The FTT had ruled that the old arrangements do not *necessarily* determine the new; the FTT had correctly taken the old arrangements into account as part of the context. The FTT judge had recognised that the purpose of the changes was to circumvent the CJEU ruling in *AXA*.

HMRC's counsel next argued that the FTT had been wrong to regard the paperwork as creating a contract for supply between DPAS and the patient. Again, the UT agreed with the FTT's analysis: the DPAS authorisation form was a tripartite agreement, and it created legal relations between the patient and the company. The various criticisms of the FTT decision raised by HMRC were rejected.

As regards those 30% of existing patients who signed the acceptance form, acknowledging the change of arrangements, the UT again agreed with the FTT that a new contract had been brought into existence. The

position was less clear in respect of the other 70%, who were assumed to have consented by silence. The UT considered the competing arguments and concluded that it was not possible to infer a contract from the lack of a response. For those existing patients who did not sign a form, therefore, there was no supply between DPAS and the patient.

The UT went on to consider the "social and economic reality" of the arrangement. HMRC argued that there was no supply by DPAS to the patient, because it was entirely bound up in a single supply that was in reality made by DPAS to the dentists. The UT did not agree: the fact that DPAS made supplies only to the dentists before 1 January 2012 did not mean that it was impossible for the company to make supplies to the patients after that date. There was a service of ensuring that money was taken by direct debit from the patients' accounts and passed, after deduction of fees, to the dentists. That was a supply that could be made to either the dentists or the patients, depending on the contract. Where the contract was properly entered into by the patient, there was nothing wrong with the FTT's conclusion that the supply was made to the patient.

The UT went on to consider whether the services were exempt within art.135 PVD. HMRC wanted a reference to the CJEU on this point, arguing that the facts were materially different from the *Bookit* and *NEC* cases already awaiting considering by the court. The UT decided that those cases would be relevant in deciding this issue. Given that the UT had concluded that there were some supplies that were made by the company to the patients, and which might fall within art.135 or might constitute "debt collection", the final resolution of the appeal was stayed until after the CJEU has issued its rulings.

One minor issue was determined by the UT in HMRC's favour: a £10 registration fee was consideration for a taxable supply by DPAS to the clients, because it was for something quite separate from the payment processing services that could qualify for exemption.

As regards the question of abuse of law, the UT commented that an ineffective scheme cannot be abusive: if the CJEU decides that the services in *NEC* constitute debt collection, DPAS will not have succeeded in obtaining any rights, so it cannot have done so abusively. By contrast, if such services are not debt collection, the UT considered that the company should be free to structure its contracts to achieve a more favourable result.

HMRC's counsel put forward three arguments in support of the argument that the arrangement was abusive. He contended that the result of the arrangement contravened:

(1) the purpose of Article 135(1)(d) which is "to alleviate the difficulties connected with determining the tax base and the amount of VAT deductible and to avoid an increase in the cost of consumer credit" (see Case C-455/05 *Velvet & Steel Immobilien* at [24]);

(2) the purpose of the Directive generally which is that single supplies should not be artificially split into multiple supplies with a view to reducing the overall level of VAT which may be paid (see Case C-94/09 *Commission v France* at [32]); and

(3) the principle of fiscal neutrality which precludes treating similar goods and supplies of services, which are thus in competition with one another,

differently for VAT purposes (see Joined Cases C-259/10 and C-260/10 *Rank Group plc v HMRC* at [32] – [36]).

The UT did not agree that (1) was the only clear purpose of the exemption in art.135(1)(d). It was not easy to discern an overriding purpose beyond the plain words of the provision. If the CJEU decides that the services in *Bookit* and *NEC* are exempt within that provision, the UT could not see how DPAS's arrangements would be contrary to its purpose.

The UT rejected (2) on the grounds that it had found that the company made genuine supplies to the patients. It would only be an artificial split if that was not the case.

As regards (3), the UT agreed that considering the previous contractual arrangements was relevant to the question of abuse. However, the UT rejected the suggestion that any change in contractual arrangements would necessarily be an abuse just because it improved the VAT position of the taxpayer. Fiscal neutrality is engaged where two situations are effectively identical and are given different tax treatments under the law; the UT had already decided that the situations before and after 1 January 2012 were not identical.

The decision concludes by:

- allowing HMRC's appeal in relation to those existing patients who did not sign the acceptance form, and in relation to the £10 registration fees;
- staying the resolution of the rest of the appeal until the CJEU decides *Bookit* and *NEC*.

Upper Tribunal: *DPAS Ltd v HMRC*

2.3.5 Bitcoin exchanges

The full court has confirmed the opinion of Advocate-General Kokott that the service of exchanging Bitcoins for "traditional" currency:

- is a service supplied for consideration, applying the principles of the *First National Bank of Chicago* case;
- is exempt within art.135(1)(e) PVD as "transactions, including negotiation, concerning currency, bank notes and coins used as legal tender";
- is not within art.135(1)(d) or (f) ("transactions, including negotiation, concerning deposit and current accounts, payments, transfers, debts, cheques and other negotiable instruments, but excluding debt collection" and "transactions, including negotiation but not management or safekeeping, in shares, interests in companies or associations, debentures and other securities, but excluding documents establishing title to goods, and the rights or securities referred to in Article 15(2)").

Although Bitcoins are not legal tender and are not legally regulated in the same way as traditional currencies, they are used for the same purposes by those who deal in them; to treat them differently would deprive the exemption of its natural effect.

This is consistent with the UK's position on Bitcoins (*R&C Brief 09/2014*), and is important because it should now lead to a consistent treatment in other EU countries that have not applied the exemption. Germany and Spain have adopted the same position as the UK; Belgium has applied exemption under art.135(1)(d); Estonia and Poland had treated Bitcoins as outside the scope of any of the art.135 provisions.

CJEU (Case C-264/14): *Skatteverket v David Hedqvist*

2.3.6 Education

A trader supplied instruction in motocross riding, motorcycle repair and maintenance to children. He claimed exemption for private tuition in a subject ordinarily taught in schools and universities; HMRC accepted that his supplies were educational, but ruled that they were not within the exemption.

The Tribunal heard evidence that motocross riding is included as a possible option in the GCSE PE syllabus, and four schools have applied to offer it as part of their PE courses. However, that is only a small number; a Department of Education survey from June 2013 set out the "most common sports to participate in" and analysed school sports provision, and did not mention motocross (even though Kabaddi made it onto the list with 2% participation).

There is also a GCSE in Motor Vehicle and Road User Studies. This was offered by between 70 and 90 schools in Northern Ireland between 2011 and 2014, but fewer than 20 schools in England and Wales (information obtained by a Freedom of Information Act request by the appellant). There are over 3,000 secondary schools in England.

The Tribunal referred to the CJEU judgment in *Haderer* for the principles to be applied in deciding what is educational. The Court emphasised that the exemption should be capable of consistent application throughout the EU, and should therefore not depend on the particular way in which education is organised in one Member State. The judgment included the comment: "*While it is unnecessary to produce a precise definition in this judgment of the Community concept of 'school or university education' for the purposes of the VAT system, it is sufficient, in this case, to observe that that concept is not limited only to education which leads to examinations for the purpose of obtaining qualifications or which provides training for the purpose of carrying out a professional or trade activity, but includes other activities which are taught in schools or universities in order to develop pupils' or students' knowledge and skills, provided that those activities are not purely recreational.*"

Because HMRC had accepted that the courses were educational, the issue was not whether they fell the wrong side of the "recreational" borderline (as in the cases of belly-dancing and yoga classes heard over the last two years). As in the case on Pilates (*Christine Joy Hocking*), the issue was simply whether it was a subject ordinarily taught in schools and universities. This is to be read in view of the slightly different wording in the PVD: "*tuition …covering school or university education*". The FTT in *Hocking* had noted that the Advocate-General in *Haderer* had used the expression "instruction is commonly given" as a way of interpreting that term.

The same FTT also considered *T K Philips t/a Bristol Motorcycle Training Centre* (VTD 7,444), in which courses in motorcycle road safety were held to be educational. There had been evidence that many schools in the Bristol area sent pupils to the appellant, and the Tribunal decided that they fell within the exemption.

The FTT in the present case did not agree with HMRC's submission that it was relevant to consider whether the appellant's courses were taught in a comparable way to how the subject was dealt with in schools. That was an unwarranted gloss on the legislation. The judge also discounted the relevance of the low level of take-up in the schools in which the courses were offered – a subject that might only be of interest to a minority could nevertheless be "ordinarily taught".

HMRC had also argued that the judge should consider only information that was available to them when they made their ruling in 2013. This was incorrect, because the appeal was not concerned with the reasonableness of the decision but its correctness. The information gathered by the appellant later was relevant. However, it was important to consider whether the courses were commonly taught during the period under appeal; some of the appellant's information related to the intentions of schools to offer such courses later, and this would not assist him.

The judge considered different ways of measuring "ordinarily" or "commonly" taught. There were obvious difficulties in considering the question across the whole of the EU; in the UK, it appeared that motorcycle studies could be regarded as "commonly taught" in Northern Ireland, but not across the UK as a whole, based on the percentage of schools involved. On balance, he concluded that it was not possible to regard the subject as sufficiently widespread to fall within the exemption.

The appellant had also included grounds for a legitimate expectation that exemption would apply, based on HMRC guidance that had been withdrawn and changed without adequate notice. The judge said that he understood why the appellant regarded this as unfair, but agreed with HMRC that the FTT had no jurisdiction to consider such an argument. He would have to take it up by way of judicial review or a complaint to the Adjudicator. The judge specifically stated that he made no findings in relation to the alleged unfairness.

The appeal was dismissed.

First-Tier Tribunal (TC04689): *Simon Newell t/a Chiltern Young Riders*

2.3.7 More education (perhaps)

The Court of Appeal has decided to refer questions to the CJEU in the *Brockenhurst College* case.

Background

A college of further education ran courses in catering and hospitality. To provide experience to its students it ran a restaurant at which members of the public could buy meals, on the understanding that they were prepared and served by trainees. The college subsidised the meals, charging a price which represented 80% of the cost of the food. Similar arrangements existed in relation to concerts and performances which were put on as part of relevant courses and charged to members of the public.

The college accounted for output tax on these supplies as catering, but in 2009 claimed repayment of £79,900 of output tax and £103,750 of overpaid input tax on the grounds that the supplies should properly have been regarded as exempt. The FTT decision did not make it clear how incorrectly treating exempt supplies as taxable could lead to a repayment of input tax.

The appellants argued that the meals were supplied as an essential part of the students' education. They were therefore within Art.132(1)(i) Principal VAT Directive, which exempts: "*Children's or young people's education, school or university education, vocational training or retraining, including the supply of services and of goods closely related thereto, by bodies governed by public law having such as their aim or by other organisations recognised by the Member State concerned as having similar objects.*" It was common ground that the college was an "eligible body" within Group 6 Sch.9 VATA 1994.

Art.134 restricts the exemptions under art.132 where:

(a) the supply is not essential to the transactions exempted; or

(b) the basic purpose of the supply is to obtain additional income of the body in question through transactions which are in direct competition with those of commercial enterprises subject to VAT.

The UK law requires that "services and goods closely related" to education, the goods or services must be for the direct use of the pupil, student or trainee (as the case may be) receiving the principal supply. HMRC ruled that this condition was reasonable and was not met; the college argued that it was too restrictive and not in accordance with the Directive.

First-Tier Tribunal

The FTT examined the facts and the underlying law in detail, and came to a surprising conclusion. First, it did not agree with the appellant's argument about the compliance of the "direct use of the pupil" condition with the Directive. However, it also concluded that it was not proper to consider only the money transaction, nor to view the supply in the abstract: in its context, it was an essential part of the education of the students, and clearly did not generate extra income for the college because it was supplied at a loss.

The points made by the FTT in reaching its decision were:

- the VAT Act must be construed in a manner which is consistent with the purpose of the VAT Directive;
- the closely related activity has to be essential to the main supply of education;
- the related supplies were integral to the main supply of education – they were not an end in themselves, but a means of providing the students with a better education, as part of the course;
- if there was an intention to generate extra income, the operation would have been organised on more commercial lines.

The students directly benefited from the activity, even though the paying customers "received a supply" in the common understanding of the terms

for VAT. The FTT concluded that the supplies to the customers were an essential and integral part of a supply of education, and were therefore within the exemption at art.132(1)(i).

Upper Tribunal

HMRC appealed to the Upper Tribunal. Judge Berner examined a number of relevant precedents and set out the following principles that he derived from them:

(1) As a general principle, the exemption must be construed so as to be consistent with its objective and so as to ensure its intended effect (see, for example, PFC Clinic AB, para 23).

(2) An especially narrow interpretation of the exception for activities closely related to a principal exempt supply of education is not appropriate, since the exemption is designed to ensure that the benefits of the principal supply are not hindered by the increased costs of providing it that would follow if the principal supply, or the closely related activities, were subject to VAT (EC Commission v Federal Republic of Germany, para 47).

(3) To be closely related to a principal exempt supply, the service in question must be an ancillary supply, that is one that does not constitute an end in itself, but is a means for better enjoying the principal service supplied (Horizon College, paras 28 and 29).

(4) The closely related supply must be essential to attain the objective of the principal supply (Article 134(a)). In order to satisfy that requirement, the ancillary supply should be of a nature and quality such that, without it, there could be no assurance that the education from which the students benefit would have an equivalent value (Horizon College, para 39).

(5) There is no requirement that the closely related supply be made to the same recipients as the principal supply. To be services closely related to education it is not necessary for those services to be supplied directly to those students (Horizon College, para 32).

The Tribunal rejected HMRC's argument that the students would have to benefit from the subject matter of the supply (the meals and entertainment), rather than benefiting from taking part in the provision of the supply. Rather, the question was whether the supply – regardless of its subject matter or its direct recipient – was ancillary to the supply of education to the students, in that it was a means of better enjoying the principal service.

The FTT had found that the catering and entertainment services were essential to the education of the students, were not an aim in themselves but were a means of providing a better education, and were for the direct benefit of the students even though the supplies were made to third parties. They were therefore exempt as supplies of services and goods closely related to the provision of education by the college. HMRC's appeal was dismissed.

It was not necessary for the UT to rule on whether the UK's provision on 'direct use' complied with the Directive. It could be interpreted in a manner consistent with the Directive, in that the direct benefit to the student's education was 'direct use'. If that was not a correct

construction, it would still have been necessary to interpret the law in that way in order to comply with the Directive (the *Marleasing* principle).

Court of Appeal

Both parties wrote to the Court suggesting a reference to the CJEU. The following draft questions were submitted:

1. With regard to article 132(i) of the Principal VAT Directive (2006/11 2/EC), are supplies of restaurant services and entertainment services made by an educational establishment to paying members of the public (who are not recipients of the principal supply of education) "closely related" to the provision of education in circumstances where the making of those supplies is facilitated by the students (who are the recipients of the principal supply of education) in the course of their education and as an essential part of their education?

2. In determining whether the supplies of restaurant services and entertainment services are within the exemption in article 132(i) as services "closely related" to the provision of education:

a. is it relevant that the students benefit from being involved in the making of the supplies in question rather than from the subject matter of those supplies;

b. is it relevant that those supplies are not received or consumed either directly or indirectly by the students but are received and consumed by those members of the public who pay for them and who are not recipients of the principal supply of education;

c. is it relevant that, from the point of view of the typical recipients of the services in question (that is to say, the members of the public who pay for them), the supplies do not represent a means of better enjoying any other supply but are an end in themselves;

d. is it relevant that, from the point of view of the students, the supplies in question are not an end in themselves but participating in the making of the supplies represents a means of better enjoying the principal supply of education services;

e. to what extent should the principle of fiscal neutrality to be taken into account?

The Court heard oral representations from HMRC's representations, and summarised HMRC's 8 propositions on which the department's case relied. The judges agreed that, in the absence of a directly relevant precedent, the principles were not *acte clair*. The situation was not uncommon and could therefore have widespread application. It was therefore appropriate to make a reference. The detailed questions would be agreed.

Court of Appeal: *HMRC v Brockenhurst College*

2.3.8 Sports affiliation fees

Two proprietary golf clubs and one members' club appealed against decisions by HMRC concerning affiliation fees collected by the clubs and paid on their behalf to the national golf body. The clubs argued that the fees represented standard rated supplies by the clubs, and could not be regarded as disbursements when recharged by the clubs to their members.

The judge noted that this seemed the opposite of what he would expect a taxpayer to argue. The background was a campaign by a number of clubs, and a representative body that was originally involved in the appeal, to oppose the 1999 Sports Order, which they argued had a disastrous effect on the golf industry, distorting competition between members' clubs and proprietary clubs. They wanted a reference to the CJEU to consider the legality of that legislation.

The Tribunal reviewed the nature of the affiliation fees. Clubs do not have to join their county unions or England Golf, the national body, but they do so to attract members. The main benefits received by members are access to the CONGU handicapping system, being able to play in competitions and a discount card that entitles them to play for lower fees at other participating courses. The affiliation fees are payable by the club, based on the previous year's headcount. They are payable in advance, and the club then tries to recover them from the members, frequently suffering a shortfall.

The Tribunal also noted that the Sports Order had prevented arrangements whereby proprietary clubs could licence their facilities to members' clubs and so enable their members to pay exempt subscriptions. The lead appellant in the present case had won a VAT Tribunal case in 1997 which upheld the legitimacy of such arrangements under previous legislation.

The issues which were put before the Tribunal in relation to whether the supply in relation to affiliation fees was standard rated or exempt were as follows:

1) Were golfers the true beneficiaries of the supply?

2) Even if they were true beneficiaries were CONGU handicaps essential to participating in sport?

3) Even if golfers were true beneficiaries and the CONGU handicaps were essential could the supply be exempt in so far as it was the case that golfers did not regard the CONGU handicap as a benefit or had not for that reason or another paid the fees?

The judge considered that it was necessary to come to an objective view of the nature of the transaction, independently of what might be the intention of individual golfers. It would not be possible to base the VAT liability on whether a particular golfer was or was not interested in having a CONGU handicap.

He considered that the true beneficiaries of the supply were indeed the golfers. The clubs argued that they paid the fees for their own reasons (because not being affiliated would lead to a loss of members), but that was incidental. In *Canterbury Hockey Club*, the CJEU held that it was common for sport to be organised by structures such as clubs for administrative reasons, and a supply to a club could be for the benefit of the people actually playing the sport. The judge saw no reason why this principle should not be extended to a sport played socially and individually, as well as the more competitive team sports such as hockey.

Although a handicap is not essential to playing golf, it is essential to taking part in competitions. It is therefore closely linked with playing sport. The judge was satisfied that it potentially qualified for exemption as a sporting service.

However, it was clear that it did not meet the conditions for a disbursement when charged on to the members. If the fee paid to the national or county bodies was exempt (because they could be eligible bodies), when a proprietary club charged it on to a member, that would constitute consideration for a taxable supply. HMRC had operated an ESC since 2000 to allow proprietary clubs to treat such recharges as disbursements; the appellants argued that this was contrary to the legal position, in order to advance their argument against the whole legal basis of the regime in the UK. The judge noted that both parties agreed that the legal conditions for a disbursement were not met, and the question of whether HMRC were right to operate a concessionary treatment was a matter for judicial review.

Turning to the question of distortion of competition and the appellants' request for a reference to the CJEU to consider the legality of the Sports Order, the judge noted that none of the appellants actually operated the kind of arrangements that the Order made ineffective. The question was therefore purely hypothetical in the context of the affairs of these appellants. He could not make a reference in relation to hypothetical questions – only if there was a genuine legal issue between the parties on the facts of the case. He therefore refused to do so.

The overall conclusion was that the fees would be standard rated when recharged by the proprietary clubs to their members, and that could not be prevented by the principle of fiscal neutrality; the CJEU had in *Bridport and West Dorset Golf Club* confirmed that fiscal distortion was inherent in the law in this area, and the clear words of the Directive had to be followed.

First-Tier Tribunal (TC04781): *Abbotsley Ltd and others*

2.3.9 Civic objects

The chief lodge of freemasons claimed exemption for its membership subscriptions under art.132(1)(l) PVD on the basis that it was a body with aims of a philosophical, philanthropic, religious or civic nature. It was common ground that it was a non-profit making institution whose supplies were in its members' common interest in return for subscriptions fixed in accordance with its rules, and no argument was advanced that the exemption of its membership services would distort competition.

The FTT (TC03302) considered the precedents of *Expert Witness Institute* and *British Association for Shooting and Conservation*. He derived the principle that the aims of an organisation are at least prima facie to be found its constitutional documents "tested against the reality of what it does".

The judge examined the history and practice of freemasonry in some detail in order to assess what the aims of the body were. He derived a list of these aims, which he tested in turn against the statutory words that conferred exemption. He concluded that several of the body's aims would qualify for exemption, but some would not – in particular, the aims of fellowship and self-improvement were not within art.132(1)(l). These non-qualifying aims were too significant to be ignored, with the result that the subscriptions could not qualify for exemption.

The organisation appealed to the Upper Tribunal. It argued that the FTT had erred in finding that the practice of freemasonry had changed since 2000; it also argued that the "other aims" that had led to the FTT's decision were insignificant and ancillary to the qualifying aims, and should therefore not have disqualified the organisation from exemption.

The UT examined the criticisms of the decision below in detail, and rejected them. The FTT had approached the statutory question in a sensible and practical way, and was entitled to come to the conclusions it had drawn. The body's own brochure referred to Masonry as consisting of "a body of men brought together for the sake of mutual intellectual social and moral improvement", and this was a significant aim which did not fall within the exemption. The appeal was dismissed.

Upper Tribunal: *United Grand Lodge of England v HMRC*

2.4 Zero-rating

2.4.1 Sanitary products

A coalition of MPs – Labour, SNP and some Eurosceptic Conservatives – put forward a Finance Bill amendment to cut the rate of VAT on sanitary products to zero. The debate was full of inaccuracies, including incorrect use of the term "exempt from VAT"; the assertion that sanitary protection is subject to 5% VAT "because HMRC regard it as a non-essential, luxury item", a claim that it is difficult to track down to a source; and the suggestion that razor blades, being an "essential", are zero-rated.

The vote was defeated by 305 votes to 287; the names of those who voted against were published on social media so they could be attacked for recognising the restrictions on the power of the UK Parliament to reduce VAT rates. Ireland zero-rates sanitary protection, but it did so before joining the EU, so its rules are protected under transitional provisions.

Following this controversy, the Autumn Statement contained an announcement that an equivalent amount of money to that raised from this tax – £15m a year – would be allocated by the government to women's charities. The statement indicates that the government will try to make the case to the Commission that such supplies should be zero-rated, but there seems to be little prospect of that succeeding.

https://www.gov.uk/government/publications/spending-review-and-autumn-statement-2015-documents/spending-review-and-autumn-statement-2015#policy-decisions – para.6.5 and 12.2

2.4.2 Caravans

The Value Added Tax (Caravans) Order 2015 took effect on 2 December 2015 to ensure that the VAT zero-rate continues to apply to supplies of static residential caravans, following publication of a revised 2015 version of the British Standard to which such caravans must conform. The BS was updated to make sure that caravans intended for year-round occupation met health and safety standards.

SI 2015/1949

2.5 Lower rate

2.5.1 Article

In an article in *Taxation*, Steve McIntyre and James Llewellyn explain the rules on the application of the lower rate to residential property projects. The authors suggest that building contractors may be persuaded to charge the right rate by directing them to the relevant parts of HMRC's public notice.

Taxation, 12 November 2015

2.5.2 Changes to the reduced rate

The Autumn Statement included details of the legislation to be included in the Finance Bill 2016 to give effect to the CJEU decision in Case C-161/14 that the UK was not entitled to apply the lower rate to installation of energy-saving materials in residential property. The changes will take effect from 1 August 2016, subject to transitional arrangements.

Reduced rating will in future be restricted to:

1. Services of installing energy-saving materials in residential accommodation where the materials are not supplied by the installer;

2. Services of installing energy saving materials, including the supply of the materials themselves, where:

a) the supply is made to a person over 60 years old or on certain benefits;

b) the supply is made to a relevant housing association; or

c) the building in question is used for a relevant residential purpose;

3. Services of installing energy-saving materials, including the supply of the materials themselves (other than services and materials falling within 2 above) in residential accommodation, provided the cost of the materials does not exceed the cost of the installation services. If the cost of the materials is greater, only the installation element will be subject to the reduced rate and the materials will be standard-rated.

The legislation also withdraws, from the same date, the application of the reduced rate to solar panels, wind turbines and water turbines.

The details of the legislation are subject to a current consultation.

www.gov.uk/government/publications/vat-changes-to-the-reduced-rate-for-energy-saving-materials

2.6 Computational matters

Nothing to report.

2.7 Discounts, rebates and gifts

Nothing to report.

2.8 Compound and multiple

2.8.1 Distance learning courses

A commercial provider supplied distance learning courses in various trade subjects such as electrical and plumbing work, and animation and "games" courses, enabling people to become proficient in designing and animating computer and iPhone-type games. A dispute arose with HMRC over the liability of the supplies. Both sides argued that the courses were a single supply: the appellant claimed it was a zero-rated supply of manuals, while HMRC argued that it was a single supply of education by a non-eligible body, and therefore did not qualify for any relief.

The judge (Howard Nowlan) started by commenting that "*we have found it difficult to rationalise all of the relevant authorities and to arrive, with confidence, at the correct tests to apply in identifying the nature of the single supply. While we regret this observation, we consider that this case may well be one where there will be appeals to a higher court, and quite possibly a referral to the ECJ for guidance.*"

There were subsidiary questions, including a secondary argument by the company that if it was supplying education, there should be a large zero-rated element for the manuals. HMRC accepted that the manuals were not an "ancillary supply", but considered that this did not change the fundamental nature of the company's offering.

Other issues arose from the history of the dispute and the way in which HMRC had changed their views over time. Up to 2009, it had been agreed that there were two separate supplies, and the taxpayer and HMRC reviewed from time to time the methodology underlying the accepted split of the consideration received into zero-rated and standard rated portions. Generally the result was 75% zero-rated. HMRC had formally agreed a method in 2000; this was withdrawn with retrospective effect in 2009 in relation to the refusal of an additional repayment claim for 2006. Shortly before judicial review proceedings were due to commence, HMRC decided not to pursue the past assessments, but nevertheless to sustain their view of the correct position going forward.

When HMRC dropped the retrospective assessments, they agreed to pay the repayment claim. However, they refused to add interest, arguing that this was not properly "VAT" but a payment to reflect the trader's legitimate expectations. The trader maintained a claim to interest.

A particular point outstanding from the judicial review dispute was the treatment of VAT payable under "continuous supply" provisions. The company had always fixed its VAT liability on 3-year courses when the customer signed a contract. However, VAT was only collected on courses paid for through a finance company when each instalment fell due. This meant that changing the liability from 25% to 100% standard rated during the 36-month period of a course would have an unfair effect on the company – it would have to account for output tax when it had no means of adjusting the charge to the customer. HMRC argued that the FTT had no jurisdiction to consider this point.

The judge concluded that the jurisdictional issues would fall away if the principal point in dispute were to be decided in favour of the taxpayer – the repayment in 2006 would become VAT, and there would be no need

for any adjustment in the middle of a course. He therefore proceeded to deal with that first; adopting the following approach:

- *first to give a general description of the Appellant's trade;*
- *then to amplify the description of the two types of example course that were considered extensively during the hearing, and to indicate the elements of non-book supplies that were offered in relation to each;*
- *then to summarise the marketing of the courses, and the way in which specialist "interviewers" were involved in selling the courses;*
- *and then to describe the relevant features in relation to exams and qualifications that customers might wish to pass and to obtain.*

In describing the business, the judge commented that it appeared the "tutorial support" element of the courses might have been over-emphasised in the marketing material. The essence of what was offered was a great deal of self-taught reading material. The appellant claimed that tests were marked by a computer system, and "tutors" who could be contacted by telephone would only refer the caller to the appropriate part of the manual. There was no intention to add anything to the manuals themselves.

The judge noted that at any time the company might have between 40,000 and 60,000 customers engaged on courses. It only had 14 employees, of whom only 8 dealt with "tutor support". Although there was some dispute about the importance of the tutor support, the judge concluded that it was clear enough that only a tiny minority of customers sought tutorial support on only a trivial number of occasions. The appellant suggested that a customer needed to spend 500 to 750 hours working on the material; in comparison, any "service" element was immaterial.

The judge distinguished the *College of Estate Management* case, which had 100 staff including academics who undertook assessment of students through written assignments, and where there was considerable classroom contact to which the printed materials were ancillary. In this case, the judge concluded:

"*...we consider that the manuals are the Appellant's principal provision and all other items are ancillary. This results not only from the fact that the manuals in isolation are intended to be, and we consider them to be, sufficient to achieve the customers' desired end in itself, and the "add on" items are irrelevant in this context, but the majority of customers continued with the courses and continued to receive and, presumably, to study the manuals, yet many (indeed we were told a considerable majority) made no use of the "add-on" functions whatsoever. This is not to say that they were not available and part of the contracted supply. Of course they were. But if the end could be, and often presumably was, attained without resort to any of the "add on" functions, this demonstrates that the add-on functions must have ranked as ancillary.*"

The judge went on to analyse the law, commenting that it is not entirely clear. He considered that in a dispute between "two separate supplies" and "one supply with two elements", the tests are "relatively straightforward" – it is necessary to consider all the circumstances from an economic point of view, and from the perspective of a typical

consumer. If one element is the principal supply and the others are ancillary and for its better enjoyment, it would be artificial to split the supply into different elements. If each is an aim in itself for the customer, it will be necessary to apportion the consideration.

There is more difficulty in deciding the nature of a single supply, if it is concluded that there should be no apportionment. In some cases, it will take its nature from the principal supply to which the other elements are ancillary (described as "test 1"). However, this will not always be the case, as illustrated by the restaurant meals in *Faaborg-Gelting Linien* and the vaccination of patients in *Dr Beynon & Partners*. Where a customer wants a particular service which encompasses the principal element (e.g. "a meal in a restaurant" encompassing "the food"), that will be a different single supply from the principal element (described as "test 2").

"Test 3" was derived from *Deutsche Bank*, where the CJEU held that both the supply of investment research (standard rated) and transactions in investments (potentially exempt) were of equal importance; neither was subsidiary to the other. However, the composite supply could not be said to fall within the exemption.

"Test 4" applies where there is an apt description of the overall supply which differs from the component elements. This includes the cases referred to under test 2, and also *College of Estate Management*, where the overarching supply was "education". The judge examined the reasoning of these cases in detail, and also *Byrom t/a Salon 24* and *Finnamore t/a Hanbridge Storage Services*.

In summary, HMRC argued that test 4 was the appropriate one to apply, and the appellant's supply should be regarded as "education". The appellant contended that the European precedents applied tests 1 to 3, and the UK precedents in which test 4 had been developed were of less binding force. The judge noted that he could not derive the correct legal principle with confidence, and it might become necessary to refer questions to the CJEU for guidance. However, he was satisfied that test 1 was the appropriate principle in this case. He applied it in some detail to the various arguments raised by HMRC, but concluded that the case was very different from *College of Estate Management*. There was a supply of books, to which all the added-on elements were ancillary and incidental.

Turning to the other issues, the judge gave opinions that would become relevant if the decision on the principal issue is overturned on appeal. In his view, HMRC's refusal to add interest or repayment supplement to the "concessionary" repayment of the 2006 claim would be correct: there would be no "VAT credit" that would carry a statutory right to such additions. The protection of legitimate expectations was outside the VAT Act provisions.

As regards the judicial review point in relation to the change of liability of contracts in progress, the judge considered three separate arguments advanced by the appellant in support of the FTT having jurisdiction to hear such a matter, and rejected all of them. However, he also went on to express the decision he would have given if he had jurisdiction: if HMRC had been correct in 2009 to change the treatment agreed in 2000, they should have allowed the company to continue that agreed treatment for contracts in progress, because that reflected a legitimate expectation. To require the company to change the treatment when it had no means of

changing its charges to its customers was effectively retrospective taxation.

The company's appeal was allowed, but there may be a further appeal by HMRC.

First-Tier Tribunal (TC04675): *Metropolitan International Schools*

2.8.2 Pens and bingo

A bingo club made a *Fleming* claim for output tax accounted for on "dabber pens" supplied to bingo players for marking their cards. The club claimed that these pens should have been regarded as part of a single exempt supply of bingo.

The FTT rejected most of the club's assertions of fact as being unsupported by evidence. On the argument of principle, it appeared that the pens were offered for sale separately and were never presented to the customers as part of a package. The game and the pen could always be purchased without the other. The FTT agreed with HMRC's submission that treating the two supplies as part of a single whole would be an artificial interpretation of the situation. The tests in the various precedents showed that the result should be based at least partly on the impression given by the supplies. In this case, it appeared that there were two separate supplies.

The club also argued that fiscal neutrality required the pens to be exempt, because felt-tipped implements for operating mechanised bingo machine keys were offered as part of a package. These had a similar function to the pens used to mark paper bingo cards. The judge dismissed this very briefly, simply stating that he was satisfied that the two supplies should not have the same VAT treatment. Presumably he regarded mechanised bingo (played on machines) as a different product from main stage bingo (played on paper with pens), at least to the extent that the paper version required a separate pen to be used to mark the card.

First-Tier Tribunal (TC04690): *Cavenbridge Ltd*

2.9 Agency

2.9.1 Unfortunate result

A company was involved in the supply of top-up vouchers to users of mobile phones. The company had accounted for VAT on the full amount received on “supply” of vouchers to wholesalers (and it appeared that they would have recovered that amount as input tax); however, it appeared to the Tribunal that the company never received or made a supply of the vouchers. It could therefore not deduct any input tax, because it had not received a supply. If it recovered output tax on the supply it had not made, it would have to pay it back to the customers who had claimed it from HMRC. This position was described as “unfortunate”.

The company had been running a shop selling phones and SIM cards since 2001. It began to develop a line of business in relation to topping up Pay-As-You-Go phones. If a customer wanted to add £10 of airtime to his phone, he would pay the appellant £10, often presumably in cash. A distinct company, ePay, had then installed a machine (and eventually several machines) in the appellant’s shop which printed out a receipt with a code on it. The customer keyed this in and added £10 of airtime to his phone. The machine also enabled ePay to debit the appellant for £10; the aggregate of such debits was collected from time to time by direct debit. ePay also paid the £10 to 02, Vodafone or other mobile network provider. The network provider then paid ePay a commission, and in its turn ePay paid the appellant an agreed proportion of this as sub-commission.

As it expanded its trade, the company started to sell the top-up vouchers to other traders. It consistently treated its commission receipts as VATable, but also accounted for output tax on the basis that the £10 received from the customer (whether an individual or another business) was a VAT-inclusive amount. This was in spite of not being issued with VAT invoices in respect of the “supply of vouchers” by the mobile phone companies.

The providers asserted that they only supplied airtime directly to customers, and would provide VAT invoices to those customers if requested. In their view, ePay and the appellant were only acting as agents, facilitating a supply that was made directly between the mobile company and the user. The Tribunal considered that this analysis was consistent with the limited documentation and the terminology used between the various parties: the appellant and ePay earned “commission”, which was consistent with their status as agents, not principals.

As the company had issued VAT invoices to its business customers, it was required under VATA 1994 Sch.11 para.5 to account for the VAT shown. During the course of the dispute between the parties, the company had argued that HMRC should accept alternative evidence for an input tax deduction on the purchase of the vouchers to produce a fair result; the judge ruled that this was a red herring, because there was no supply and there therefore could be no input tax deduction. He speculated that it might be possible for HMRC to decide that it would obtain a double recovery of VAT and should therefore forgive some of it as a matter of fairness, but as a matter of law the appeal had to be dismissed.

First-Tier Tribunal (TC04740): *Phone Nation Ltd*

2.9.2 Tripartite arrangements

A recruitment company (AUK) made a voluntary disclosure to claim back VAT charged on receipts from clients who employed temporary staff. The company argued that the decision in *Reed Employment* meant that it should only have accounted for output tax on its margins. A number of other claims were made by companies that were now in the same VAT group registration, but had not been at the time that the claimed overpayments had been made. There was therefore a separate issue about the identity of the appropriate claimant, but the judge was not asked to rule on that.

The judge (Barbara Mosedale) described three business models of AUK:

- employed temps, actually subject to contracts of employment with the company;
- non-employed temps, who were the subject of the appeal – treated as employees for various regulatory and tax purposes;
- contract workers, who would enter into an agreement directly with the client – the client would typically pay a one-off fee to the company, and the company did not employ or pay these individuals in any sense.

The second class of people were the subject of the appeal. AUK had paid VAT in full on the amounts received from clients in respect of such people. On 24 March 2011, Judge Berner released the FTT's decision in *Reed Employment*, holding that on the facts of that case, that employment agency was acting as an intermediary and only needed to account for output tax on its commission. AUK subsequently made various claims for overpaid VAT totalling over £11m. HMRC rejected the claims, and the company appealed.

The judge summarised the issues as follows:

The question for the Tribunal was simple in essence. What did Adecco supply to its clients? However, that question was logcially indistinguishable from the question of to whom did the temps supply their work? If Adecco merely supplied introductory services to its clients, then it follows logically that the temps supplied their services direct to the clients and not via Adecco: if, however, the temps supplied their services to Adecco, then it follows that Adecco must have on-supplied these services to its clients. So the question of what services Adecco provided to its clients is really indistinguishable from the question of to whom did the temps supply their services.

The parties agreed that the Tribunal should examine four representative contracts to cover all supplies during the relevant period (with two exceptions). The Tribunal examined the terms of the contracts between the temps and the company, and between the company and its clients, as well as considering the differences between those arrangements and the situation of employed temps.

The judge concluded that the company was liable to pay the temp the agreed payment for its services in undertaking the assignment for the client. The client had no contractual obligation with either the temp or AUK to pay the temp for its work in undertaking the assignment. The

client's only obligation to pay for the work was an obligation to pay AUK the agreed fee. The appellant's interpretation of the contract was inconsistent with the company's standard temp contract and inconsistent with the lack of legal obligation between the temp and the client. Looking at the contract in its context, HMRC's interpretation was clearly to be preferred.

Two client companies used their own standard contracts rather than those normally put forward by AUK. The judge had to consider whether the different wording of those contracts led to a different conclusion. The first certainly included clauses that suggested AUK was making payments to the temps on behalf of the client. It was clear that it had been drawn up with VAT in mind: it appeared to be an attempt to invoke the "staff hire concession under BB 10/04. However:

"*The problem for the appellant is that this contract clearly anticipated that VAT would only be charged on the commission element: if in fact VAT was only charged on the commission element then Adecco has no claim in respect of it because, even on the appellant's case, no VAT was actually overpaid. On the other hand, if VAT was charged on the full fee, then the only conclusion can be that the parties did not in practice fully operate the terms of the contract.*"

There was nothing in either of the clients' contracts to change the legal relationships. In each case, AUK was contracting with the temp and with the client as principal, not as an intermediary or agent.

After coming to that conclusion, the judge went on to cite the *Newey* decision of the CJEU: the contracts were not absolutely determinative of the VAT position. In *Aimia*, the Supreme Court had commented that a tripartite arrangement had to be considered "having regard to all the circumstances in which the transaction or combination of transactions takes place".

The company argued that this supported its case: the "reality" was that it introduced the temps to the clients, and the temps did their work for the clients. This was the decision of the FTT in *Reed Employment*: although HMRC had appealed that case, they had not done so in respect of this particular aspect of the decision. The company suggested that this "almost" created an issue estoppels, preventing HMRC arguing the point in the current case. The judge rejected this, stating that issue estoppel only exists between the same parties. It was "undesirable" that HMRC would abandon a particular argument in one case and then take the same view in a dispute with another taxpayer just three years later, but there was nothing to stop them doing so.

The judge therefore had to consider the decision in *Reed* and whether she agreed with it. She identified three key paragraphs in the *Reed* decision (at 84, 85 and 88) in which Judge Berner appeared to base his conclusion on the fact that Reed had no control over the temps. Because it could not exercise any control, it was not really capable of "supplying their services". It must therefore be making a more limited supply, one involving introductory services.

Judge Mosedale did not agree with this conclusion. It was perfectly possible for a supply to involve the following: "*If A agrees with B, in return for money, to do what C tells it to do, that is doing something in*

return for consideration and there is no reason in logic why that cannot be a VAT supply by A to B, even though at no time does A agree to work under B's direction. Yet the conclusion in Reed Employment seems to have been that A can't supply its work to B if what A agrees to do for B is to work at C's direction. I simply can't agree."

Nevertheless, that was not the end of the matter. It was possible that *Reed* could be distinguished on the facts, in which case the current decision might be different (i.e. AUK might win, even though Reed should have lost, in Judge Mosedale's opinion). The judge therefore examined a number of precedents about supplies of staff: the 1995 *Reed Personnel Services* case; *Hays Personnel Services*; and the more recent case of *Wendy Lane* from 2013. She did not regard any of them as comparable. She then turned to precedents about tripartite arrangements in general, reviewing *Redrow*, *Tolsma*, *Loyalty Management/Aimia* and *Baxi*. She paraphrased the *Redrow* principle as "follow the liability to pay", which favoured HMRC in the present case.

There is an interesting section in which Judge Mosedale considers the difference between the CJEU and Supreme Court decisions in *Aimia*. She comments that the majority of the Supreme Court concluded that the CJEU had been asked the wrong question and had therefore given an answer that did not apply to the facts. She also reconciles the different decisions in *Baxi* (which sold boilers and gave "points" away free) and *Aimia* (which bought and sold "points", and was therefore more involved in the supply chain involving the redemption of those points).

It was more difficult to reconcile the decision in *Redrow* with that in *WHA*, where the Supreme Court had come to the opposite conclusion – the person who paid for the supply (the insurance company) did not receive it, but rather the garage made its supply to the owner of the car. It was difficult for a Tribunal judge to know which Supreme Court precedent to apply. She summed up the principle she derived from these cases as follows:

"*My analysis of the situation is therefore that the Tolsma/Redrow/Aimia 'follow the liability to pay' rule is the default rule under which the VAT supply will follow the contracts and that rule applies in tripartite situations unless the economic reality is inconsistent with the contractual position. And the economic reality is inconsistent with the contracts where final consumption takes place without a contract (or other legal relationship) supplying the thing to be consumed to the final consumer.*"

Lastly, she considered the *Airtours* decision, commenting that the majority decision of the CA was "*difficult to understand as they appeared to find that there was no contract [between Airtours and PwC]: this is because they said PwC owed no liability to the company to provide the report to the bank, yet nevertheless the company was liable to pay for the report.*" Nevertheless, that case could be distinguished on the facts, and had no effect on the present appeal.

Finally, she concluded "*I take from consideration of all these cases that a VAT supply, ordinarily at least, requires a legal relationship between the supplier and recipient under which the supplier is obliged to make the supply and the recipient is liable to pay for it, whether or not that liability arises under an enforceable contract (Tolsma, Redrow, Town & County Factors). Nevertheless, where the economic reality of the legal*

relationship is such that it results in final consumption of goods or services by a consumer in circumstances where in effect there is no VAT charge on that consumption then this normal rule is overridden because the ultimate purpose of the Principal VAT Directive is to tax final consumption...

"*In conclusion, in a situation where B agrees to pay A to provide goods and/or services to C, and C agrees with B to pay for the goods and/or services provided by A, then a Redrow 'follow the liability to pay' analysis applies to decide to whom A's supply is made. This is because the legal relationships reflect the economic reality and the outcome is consistent with the Principal VAT directive because final consumption is taxed. In other words, A's supply is to B, and B makes an on-supply to C.*

"*But where a Redrow 'follow the liability to pay' analysis does not lead to tax on final consumption, because although A makes a supply to B (of providing goods/services to C), B does not on-supply A's services to C, then C's consumption will be untaxed, and, applying Baxi/Aimia/WHA, economic reality requires the supply to be seen as made to the final consumer.*"

Here, it was clear that the clients were the final consumers of the work of the temps, and they also had the legal liability to pay for what they consumed. The day-to-day control over what the temps did was not relevant to the contractual position. The economic reality was consistent with the contractual position: that was that the temps had agreed with AUK to do what the client told them to do. The clients were the final consumers of the services, and they paid for them, and that final consumption ought to be taxed.

As a postscript (at paragraph 313), Judge Mosedale notes that this decision is consistent with fiscal neutrality: there was little difference from the client's point of view between the supply of an employed temp and the supply of a non-employed temp, so it would be surprising if there was a fundamental difference between the VAT treatments of those supplies.

First-Tier Tribunal (TC04743): *Adecco UK Ltd and others*

2.10 Second hand goods

2.10.1 Margin scheme

A second-hand car dealer sold cars with MOT certificates. Where the existing certificate had less than seven months to run, he asked a prospective customer if he wanted a fresh 12-month certificate. If he did, the dealer arranged for the test and excluded the cost from the VAT calculation on the sale of the car. HMRC ruled that this was incorrect – there was a single sale of a car, to which the MOT certificate was ancillary, rather than a disbursement arrangement.

The FTT agreed that to separate out the MOT certificate would be artificial. Although the trader's records were good and carefully maintained, they could not change the basic facts that the MOT was obtained by the dealer as a principal and included with the sale of the car. On that point of principle, the appeal was dismissed.

However, the officer raising the assessment had made certain assumptions about the numbers of cars affected that could not be explained. The officer was not available to give evidence; the judge (J Gordon Reid) accepted the trader's statement that only about 70% of the amount should be due. The appeal was therefore allowed in part, reducing the assessment by that proportion.

First-Tier Tribunal (TC04667): *Richard J Finney*

2.11 Charities and clubs

2.11.1 Relevant charitable purpose?

A charity (F) acquired and subsequently renovated a property in London, giving zero-rating certificates to its contractors. It leased the property to another charity (C), which operated a fee-paying school in the premises. HMRC decided that F had not been entitled to issue the certificates, because it intended to lease the property.

The Tribunal considered the background to the transactions and legal agreements. The charity argued that it was not in business because of the very close relationship between the two charities: in effect, the property company only existed in order to make supplies to the operating company. The Tribunal did not accept this. The property charity had broader aims, and was intended to own other sites in due course.

The Tribunal decided that the correct approach was, in line with the decision in *Yarburgh Children's Trust*, to consider whether both the lease by F to C, and the use by C, were not business use. If either was a business activity, the appeal would fail.

The Tribunal considered the principles set out in *Yarburgh*, *Morrison's Academy Boarding Houses Association*, *Lord Fisher*, and *Longridge on the Thames*. It was important to consider all of the facts and circumstances, rather than focusing on any particular aspect of the situation.

HMRC argued, as they had unsuccessfully in *Longridge*, that the existence of remuneration created a presumption that an activity was economic. After examining a number of precedents, including non-VAT cases, the Tribunal concluded that there was no such presumption. If there was no consideration the activity could not be economic; but if there was consideration, it was still necessary for the Tribunal to enquire into the nature and status of the activity in the context of the whole picture.

HMRC's next argument was that the leasing of property, being specifically mentioned in art.9 PVD, contained its own presumption of economic activity. This had been rejected in *Yarburgh* and *Longridge* in the case of an isolated letting: the Tribunal had to consider all the circumstances. This Tribunal considered itself bound by those decisions, but it also agreed with them.

Next, the Tribunal considered the taxpayer's argument that a profit motive was essential for economic activity. It found as a fact that F did not intend to make a profit: it set the rent to cover costs, but not more than that. The second sentence of art.9(1) PVD referred to "the exploitation of tangible or intangible property for the purposes of obtaining income therefrom on a continuing basis". The taxpayer tried to establish a distinction between that and the first sentence, which referred to "whatever the purpose or results of that activity". The suggestion was that the taxpayer's motive or purpose was more relevant to the exploitation of property than it was in relation to other forms of activity.

To consider this proposition, the Tribunal examined the CJEU decisions in *Floridienne* and *Banque Bruxelles Lambert*. References in *Floridienne* to the nature of a private investor in the *Wellcome Trust* decision suggested that the CJEU was not making a general point that art.9(1) is only satisfied where a person's purpose is to maximise returns on capital investment. That is a characteristic that can be shared with private investors. The *BBL* decision used "income" rather than "profit" in describing its reasons for finding that collective investment schemes were carrying on an economic activity. The Tribunal concluded that a profit motive was not essential, which was consistent with the most straightforward reading of art.9.

The charitable status of F and C was something that had to be taken into account as part of the overall context of the activities. The existence of the exemption for non-profit educational activities was also relevant but not determinative. After all of this preliminary consideration, the Tribunal finally reached the normal starting point – the "indicia" of economic activity from *Morrison's Academy*:

(a) whether the activity is a 'serious undertaking earnestly pursued' or 'a serious occupation, not necessarily confined to commercial or profit-making undertakings';

(b) whether the activity is an occupation or function actively pursued with reasonable or recognisable continuity;

(c) whether the activity has a certain measure of substance as measured by the quarterly or annual value of taxable supplies made;

(d) whether the activity was conducted in a regular manner and on sound and recognised business principles;

(e) whether the activity is predominantly concerned with the making of taxable supplies to consumers for a consideration;

(f) whether the taxable supplies are of a kind which, subject to differences of detail, are commonly made by those who seek to profit by them.

HMRC argued that factor (e) had been ruled out by the A-G in the *Wellcome Trust* case; the Tribunal agreed with the taxpayer that this had been based on a misunderstanding of the point, and the High Court and Upper Tribunal continued to apply the "predominant concern" principle in cases after that.

The Tribunal then examined the facts of the present case. It agreed with HMRC that all the above indicia were satisfied. The situation was "far adrift" from that in *Yarburgh*. This was not "a relatively informal arrangement" with a lease "substantially below" full market rent. Neither was it, at the relevant time, expected to be "an isolated letting"; instead the plan was for F to be a property company for other French schools.

As a result, the appeal could not succeed. However, the second question – whether operating the school was a business activity – was also considered, because it had been fully argued in the Tribunal. The first argument was whether the school operated in a market or not, given that there was only one other French secondary school in the UK. The Tribunal distinguished this situation from that in *Quarriers*, which ran a school for epilepsy sufferers – that offered a unique service. Although French parents might prefer to send their children to a French school, the facilities were not as distinct from other schools as those in *Quarriers*. The Tribunal held that the school operated in a market.

It was once again necessary to consider the specific circumstances, rather than to apply any overriding principle. The indicia were all met. The overwhelming impression was that of a professionally run business. That was not displaced by the fact that the parents elected half the trustees, or raised small amounts of donation income for the school. Although the lack of a profit motive, the setting of the fees below the market and the charitable status of both F and C were all pointers away from there being an economic activity, they were insufficient to offset the many indicators in the other direction: namely that the college was a substantial, professionally-run, well-managed school with fee income of over £4m paid in exchange for the provision of education. Its operation was an economic activity, and the appeal was dismissed.

First-Tier Tribunal (TC04762): *French Education Property Trust Ltd*

2.11.2 Isle of Man charities

The Autumn Statement included an announcement that the Finance Bill 2016 will amend FA 2010 Sch.6 to make it clear that Isle of Man charities qualify for UK VAT reliefs. For a charity to qualify for the VAT reliefs set out in VATA 1994, it must meet the conditions in FA 2010 Sch.6. One of these conditions is that the charity must fall under the jurisdiction of the High Court (England and Wales), the Court of Session (Scotland), or the High Court of Northern Ireland. The new legislation will refer to the jurisdiction of the High Court of the Isle of Man as well.

www.gov.uk/government/publications/vat-isle-of-man-charities

2.12 Other supply problems

2.12.1 Value of self-supply

From 1978 to 1996, General Motors (UK) accounted for self-supply charges, when it took a car from stock into its own use as a demonstrator or company car, on the basis of two-thirds of the retail selling price. It used this figure instead of the cost, which was the correct figure. This had been agreed between GM and Customs & Excise in 1978, when a change in the UK law required the use of 'cost' instead of 'open market value' for the self-supply charge. The company later made a *Fleming* claim for overpayments made between 1987 and 1996 on the basis that the 2/3 figure was too high.

In 2013, the First Tier Tribunal (TC02835) considered the underlying EU provisions and the way in which they had been implemented in the UK. It decided that the requirement was to consider the price that was, or would have been paid, on the purchase of the goods or similar goods. It was not relevant that GM was a manufacturer; it could not use the cost of manufacture unless a purchase price for similar goods could not be established. The UK legislation did not correctly implement this before 1993, but the Directive was sufficiently clear for the UK law to be overridden. The Tribunal held that, for the period between 1987 and 1993, the company could take whichever was the best option for its purposes:

- rely on the UK law, and use the manufacturing cost, if that was lower than purchase price;
- rely on the Directive, and use the purchase price, if that was lower.

The Tribunal examined what is meant by 'cost' in this context, and took expert evidence. The problem is the possibility of the allocation of different overhead and other collective costs such as research and development to particular items of production.

Before the *Italian Republic* case established that the sale of 'input tax blocked' cars should be exempt, the precise value of the self-supply was not particularly relevant. A higher self-supply charge would be matched by a lower output tax charge on the subsequent sale. After GM had received a substantial repayment in relation to the sale of ex-demonstrator vehicles, it made its *Fleming* claim in relation to the self-supplies on almost the last available day – 30 March 2009. Although it subsequently amended the details of the claim, HMRC accepted that the claim had been validly made by the deadline.

The FTT decision then examined the various mathematical calculations and models in great detail, considering the prices that a purchaser in GM's position might pay to a related company for the purchase or import of similar vehicles in similar numbers for similar purposes. It summarised the decisions in principle as follows:

1987 – 1993

373. In this period ([47]) the value of the self supply is to be calculated as the lower of:

(1) the purchase price of the cars; and

(2) the cost of the cars

1994 – 1996

374. In this period ([46]) the value of the self supply is to be calculated by reference to the purchase price of the cars.

Purchase Price

375. This means ([30]) the price at which someone in the Appellant's position would have paid for the cars had it bought them at the time of their appropriation:

(1) in the case of imported cars that means the import price payable to the relevant sister company under whatever agreement subsisted between them at the time. We set out our conclusions in relation to the cost/ list price ratio which would apply in these circumstances at [226 and 227];

(2) in the case of UK assembled cars that means the list price less the discount and rebates the appellant would have got as a bulk purchaser in its bargaining position. We found that it was not shown that that would be less than 2/3 of the list price ([118]);

(3) where a car could be purchased from a sister company for a price less than that determined under (2), that import price would be the purchase price.

Cost Price

376. This means all the expenses attributable to bringing the car to its condition at the time of appropriation and includes direct expenses of manufacture, related overheads and cost of development and design [56].

There were then further detailed conclusions about the calculation of 'cost' and the use of estimates and modelling.

The appeal was allowed in principle, and adjourned in the hope that the parties could agree the amounts on the basis of the principles set out in the decision.

HMRC appealed to the Upper Tribunal, where there was a dispute over whether the grounds of appeal were truly arguments about questions of law or were an impermissible attempt to reopen the factual issues covered by the evidence.

Upper Tribunal – background

The UT starts by reviewing the history of the dispute and the history of the legislation in the claim period. It notes some problems with the FTT decision: for example, what is now para.6 Sch.6 VATA 1994 was first enacted in 1992, so the first part of the claim period came to an end on 31 July 1992, not on 1 September 1994 when the VATA 1994 came into force. The appellant's counsel also criticised the FTT's conclusion that para.6 correctly implements the Directive: in his view, it introduces an unwarranted order of preference between the purchase price of identical goods and the purchase price of similar goods (which is only to be used if a price for identical goods cannot be obtained).

The UT went on to summarise, very briefly, the long and detailed FTT decision. The judge noted that HMRC had not appealed, and had repaid the claim, in respect of the later part of the claim period (which actually

began on 1 August 1992). For cars manufactured in the UK, the purchase price of similar items should be used, in accordance with the Directive; for cars manufactured elsewhere, the actual purchase price could be identified.

The question, then, was the price that the company would have paid if it bought the cars from a third party. The FTT had concluded that it would have obtained a total aggregate rebate and discount of more than one-third of list price. In other words, it had not been proved that the notional price would have been less than the proxy price (two-thirds of list price) on the basis of which VAT had been paid. This would mean that the claim would fail in respect of UK-manufactured cars in the later part of the claim period, because the claim depended on showing that VAT had been paid on a higher figure than that required by the law.

However, the FTT had concluded that different considerations might apply to cars purchased from sister companies. It held that 'actual purchase price of comparable vehicles from sister companies' was a valid alternative valuation basis, and as this was lower than two-thirds of list price, the claim succeeded in relation to all UK-manufactured models that could have been purchased from a sister company outside the UK. That was the conclusion that HMRC sought to challenge.

For the earlier part of the claim period, the key difference in the arguments was that the company could choose to use the cost basis in the UK law if it was beneficial. As the FTT had concluded that the cost of imported cars in this period was not less than two-thirds of the list price, the claim could only succeed in respect of UK-manufactured cars, and only if the company could show that the cost was lower than that two-thirds figure.

Upper Tribunal – arguments

HMRC's first ground of appeal was that the FTT had been wrong to conclude that the company could use the price of imported vehicles as a basis for valuation in the later part of the claim period. The basis for this conclusion was not explicitly set out in the original decision; the UT considered the FTT judge's reasoning in his leave to appeal also lacked clarity.

HMRC argued that the law required the notional purchases to be "identical in every respect", and this could not be satisfied by vehicles that were manufactured abroad. The UT rejected this argument. The place of manufacture was not a relevant attribute of the goods in deciding whether they were identical. The judge's view was that "the focus is on the physical attributes of the goods, including their age and condition". Even this reference to age and condition appeared to go further than art.11A(1)(b) 6th Directive, which only refers to "the goods".

The first ground of HMRC's appeal was therefore dismissed: the FTT had come to the correct conclusion, that the price of imported cars could be used as a measure for the output tax due on UK-manufactured cars.

HMRC's second ground of appeal related to the way in which the FTT had approached its task: it should not have 'provided a solution', but rather should have confined itself to deciding whether the claim was proved on the balance of probabilities. The UT did not agree. The FTT was not required to accept or reject a claim in its entirety. It was proper

for the FTT to consider whether the answer might lie somewhere between the two positions, and to examine how the correct answer might be found. Other criticisms of the decision of the FTT about the formula for determining cost were rejected.

The remaining three grounds were effectively procedural. HMRC argued that the FTT had been wrong to allow the submission of two 'disputed documents', or to place any reliance on them; the UT disagreed. HMRC also argued that no reasonable FTT could have come to the conclusion that it did based on the mathematical models used by the company, because they were too 'flimsy' to qualify as adequate expert evidence supporting a balance of probabilities. The UT did not deal with every point raised by HMRC, but concluded that they failed to meet the very high test set by *Edwards v Bairstow* in relation to such an appeal: the FTT had come to a conclusion that it was entitled to reach on the basis of the evidence before it.

HMRC's appeal was dismissed.

Upper Tribunal: *HMRC v General Motors (UK) Ltd*

2.12.2 Goods or services?

An appeal arrived in the FTT in July 2012 relating to a ruling on a proposed product which was requested and given in 2006. The company had proceeded on the basis that its interpretation of the product was correct: the product – a new type of finance contract called 'Agility' – was offered to customers from 1 August 2007, so the company was therefore appealing against assessments rather than merely the ruling. The amounts involved up to 2008 exceeded £10m.

The FTT decision

The question was whether the contract constituted a supply of goods (in effect, hire purchase) or a supply of services (in effect, leasing). The company considered it to be different from its existing financial arrangements, offering a customer a choice of three options at the end of the normal lease term: purchase, return, and purchase plus part-exchange.

HMRC argued that the law regarded such a contract as a supply of goods, because the contract envisaged that title could pass at the end of the agreement. The company stated that this was only a possibility, not an inevitability, and it therefore made a supply of services – the contract was a rental agreement which would only become a supply of goods if the customer chose that particular option at the end.

Art.14 PVD provides that '*the actual handing over of goods pursuant to a contract for the hire of goods for a certain period, or for the sale of goods on deferred terms, which provides that in the normal course of events ownership is to pass at the latest upon payment of the final instalment*' is to be treated as a supply of goods. The company argued that 'in the normal course of events' did not apply to the Agility contract, because it was not the most likely outcome.

HMRC responded by arguing that this was a misinterpretation of art.14. The phrase 'in the normal course of events' only referred to when the title would transfer under the particular contract, not whether it was more likely than not that tile would be transferred. Agility involved handing

over goods pursuant to a contract for hire; in the normal course of events, title would transfer – if it transferred at all – upon payment of the final instalment.

The Tribunal quoted extensively from the recent CJEU decision in *Eon Aset Menidjmunt OOD* (Case C-118/11), in which it was decided that a lease contract is normally a supply of services, but could in certain circumstances be treated as a supply of goods. The company argued that the CJEU had considered the commercial perspective when giving guidance on the borderline between goods and services, and had also suggested that the accounting treatment was relevant. Under accounting standards, in distinguishing between a finance lease (treated as a transaction in goods) and an operating lease (treated as rental), a judgement had to be made at the outset whether the transfer of title was more likely than not.

By contrast, HMRC relied on the same decision, noting that, in setting out the features of a finance lease, the CJEU had apparently only required that the transfer of ownership is provided for as a possibility in the contract. HMRC also drew support from the GMAC litigation, in which a contract which provided different terminal options was nevertheless at all times treated for VAT as a supply of goods.

The company presented a detailed explanation of the commercial rationale for the Agility product. It was not designed with the VAT treatment in mind, and the uncertainty over the VAT treatment did not affect its introduction: the company considered that it should be treated for VAT in a manner consistent with the commercial reality and accounting treatment, i.e. as rental.

The Tribunal considered the different interpretations of 'in the normal course of events'. It did not agree with the company's proposal that it involved a greater than even probability that the option to purchase should be exercised; it also rejected HMRC's suggestion that it qualified only the time at which title would pass. The Tribunal preferred to regard the expression as referring to the transfer of title as something that was central to the contract – that was envisaged by the contract as a normal outcome, not as something that would be abnormal.

The Tribunal also considered that the company's argument would offend against the principal of legal certainty, in that it would be impossible to determine whether the supply was goods or services until the conclusion of the contract.

It is interesting that the company asked for specific findings on 11 questions, and the Tribunal obliged, even though it commented that most of these matters were irrelevant to the eventual decision. Presumably these findings of fact will be pored over by lawyers in the case of an appeal. They were as follows (there appear to be only 10, but one may combine two points raised by the company):

Appellant's Proposed Finding of Fact	Tribunal's Comment
The objective purpose of Agility is the hiring of a Mercedes Benz motor vehicle to a customer who wishes to keep his options, regarding ownership of the motor vehicle, open until maturity. This is reflected in the name of the product, implying flexibility,	The Tribunal disagrees. In relation to its determination (see paragraph 79 above, and to wider circumstances see paragraph 103 above) Contradictory marketing evidence (see paragraph 101 above)

and this is how Agility is advertised/described to customers.	
And Agility is recommended both online and at dealerships to customers who wish to keep their options open; alternative products are recommended to customers who decide at the outset that they do or instead do not wish to own the motor vehicle	HMRC challenged the accuracy of this statement because the Appellant adduced no evidence to substantiate it. The Tribunal ruled that HMRC was not entitled to do this because it was an agreed statement of fact. The Tribunal, however, considers this agreed statement of fact has to be weighed against the commercial rationale (see paragraph 99 above).
The purpose of Agility is reflected in its terms: the customer hires the vehicle for a fixed period in return for monthly payments, and at maturity he has an option to purchase for a fixed price which is calculated at the outset to be equal to the market value of the vehicle at maturity.	The Tribunal disagrees. See its findings at paragraphs 79 and 80.
The calculation is genuine and expert estimate of the residual value of the vehicle; it is made partly be reference to external guides e.g. Glass's guide, and partly by reference to Mercedes Benz own knowledge about forthcoming developments which are likely to affect future values, for example, new models	Agreed. The Tribunal, however, questions its relevance for the Appellant's case of flexibility based on the wider circumstances.
The typical period of an Agility contract for a new vehicle is 3-4 years; for a second hand vehicle it is slightly less. For new and second hand vehicles, the period of an Agility contract is always substantially less than the useful life of the Mercedes Benz motor vehicle. This means that the residual value is substantial not a nominal sum.	An agreed statement of fact. The substantial sum has to be weighed against the evidence which showed that the customer's contribution in respect of monthly payments with interest and deposit exceeded the residual value by a significant sum. In the Tribunal's view, the amount already paid was important in relation to the characterisation of the agreement and the customer's decision to exercise the option.
Merely by entering into the Agility agreement, and merely by paying the obligatory monthly payments, the customer is not commercially committing himself to becoming the owner of the vehicle.	The Tribunal does not understand the term commercially committing. The Tribunal accepts that the customer has to exercise an option to purchase before ownership is transferred. The Tribunal, however, considers the monthly payments represent a significant investment in the vehicle by the customer.
Statistics show that the purpose of Agility is in fact achieved; on average around 50 per cent of vehicles are purchased and 50 per cent are returned	Hire purchase have similar high rates of return
The Appellant is neutral as to whether or not an Agility customer decides at maturity to purchase or not to purchase, the motor vehicle.	The Appellant carries no risk if the vehicle is returned.
However, because there is a very real prospect of the customer returning the vehicle, Agility, obliges the customer at maturity to pay for damage to the vehicle, and to pay for excess mileage, and also obliges him to service the vehicle at Mercedes-Benz approved workshops only.	Agreed statement of fact. Relevant to the Tribunal's characterization of Agility as a contract for sale of a vehicle (see paras 79 and 80 above).
Having regard to the terms of Agility there	Tribunal disagrees. Its findings on the

is no expectation at the outset that a typical Agility customer will purchase the vehicle	agreement and wider circumstances demonstrate that Agility is portrayed as an affordable means to purchase the vehicle.

The decision itself (to dismiss the appeal) was summarised as follows:

(1) The words of Article 14(2)(b) should be read straightforwardly which direct attention to what is provided for in the contract, not on the wider circumstances.

(2) The description of the agreement as hire purchase, the provision for a deposit payment, the specified financial information including the cash price for the vehicle, the substantial capital payment inherent in the contract structure, and the option to purchase are compelling indicators of Agility being a contract of sale of a car

(3) On a proper analysis the sole realistic option under Agility is to purchase the vehicle

(4) In the normal course of events is to be construed as a question of whether the passing of ownership was normal under the terms of the contract, rather than abnormal,

(5) The fact that ownership might not transfer under the Agility contract did not preclude it from being a contract for sale. The passing of title is central to Agility which meant that ownership would normally pass under its terms.

The Tribunal is satisfied on its findings that Agility is a contract for the sale of goods on deferred terms, which provides that in the normal course of events ownership is to pass at the latest upon payment of the final instalment. Article 14(2)(b) of the VAT Directive, therefore, applied to Agility.

The Upper Tribunal decision

The company appealed to the Upper Tribunal, which decided that the FTT had made errors of law, and overturned its decision.

First, to come within art.14(2)(b) PVD, the acquisition of the goods at the end of the contract had to be *the* normal outcome, not just *a* normal outcome.

Second, the agreement could not be characterised as, in effect, a contract for sale of a vehicle. It was a contract for hire with an option to purchase; that would only be deemed to be a contract for sale of goods if the option was normally exercised. The FTT had reached a conclusion, or a characterisation of the contract, that was not justified by its findings of fact.

A third ground of appeal, that the Tribunal had made findings of fact which had not been contended for by HMRC and had acted unfairly in so doing, was rejected.

The judge noted that there are no CJEU cases directly about art.14(2)(b). The *Eon Aset Menijdmunt* case refers to it, but is not directly relevant to the point at issue here. The judge made the following points of general application:

(1) As recital (1) to the Directive shows, the Directive is intended to harmonise the laws of the Member States relating to turnover taxes and provide for a "uniform basis of assessment".

(2) It is therefore not surprising that the ECJ has said that the notion of supply of goods is not to be determined by national law: the purpose of the Directive might be jeopardised if the requirements for a supply of goods were to differ according to the civil law of the Member State concerned: see Atktiebolaget NN v Skatteverket Case C-111/05 at [32].

(3) The concept of supply of goods is objective in nature. It applies without regard to the purpose or results of the transactions concerned and without its being necessary for the tax authorities to carry out inquiries to determine the subjective intention of the taxable person in question: see Newey v Revenue and Customs Commissioners Case C653/11 ("Newey") at [41]; Dixons Retail plc v Revenue and Customs Commissioners Case C-494/12 ("Dixons") at [21].

(4) Consideration of the economic and commercial realities is a "fundamental criterion" for the application of the common system of VAT. Since the contractual position normally reflects the economic and commercial reality of a transaction, the relevant contractual terms constitute a factor to be taken into consideration; but sometimes contractual terms do not wholly reflect the economic and commercial reality of a transaction, in particular if it becomes apparent that the contractual terms constitute a purely artificial arrangement which does not correspond with the economic and commercial reality of the transaction: Newey at [42]-[45]. This passage has very recently been referred to and relied on by the Supreme Court in Secret Hotels2 Ltd v Revenue and Customs Commissioners [2014] UKSC 16 at [29] per Lord Neuberger.

(5) In a passage cited by Jonathan Parker LJ in Tesco plc v Customs and Excise Commissioners [2003] EWCA Civ 1367 ("Tesco") at [41], the Advocate General (Tizzano) said this in his opinion in Customs and Excise Commissioners v Mirror Group plc Case C-409/98 and Customs and Excise Commissioners v Cantor Fitzgerald International Case C-108/99:

[quotation from judgment]

Jonathan Parker LJ later in his judgment made the point that the "economic purpose" here referred to by the Advocate General is not the same as "economic effect": two transactions may have the same economic effect but that does not necessarily mean that they are to be treated in the same way for VAT purposes: see Tesco at [159].

(6) In MBNA Europe Bank Ltd v HMRC [2006] EWHC 2326 (Ch) ("MBNA"), Briggs J referred to the same passage from Advocate General Tizzano's opinion in saying (at [35]) that the Court is not hidebound by the labels which the parties have chosen to apply to their transactions but must where necessary ascertain the "essential character of the transaction in issue".

The judge noted that it was not possible to decide what would be the "normal" outcome with hindsight: the very first Agility contract was, in principle, either goods or services on the day it was entered into, and that had to be decided on the information available at that time. For the judge,

the critical fact was that the option payment was substantial – that distinguished the contract from "standard HP" where at the end of the term the customer had effectively paid the whole price, including interest, and would be foolish not to pay the very small final payment to take up the option to purchase. In the case of Agility, there was a real choice at the point the option could be exercised. It was not, as the FTT had concluded, illusory.

Court of Appeal

HMRC appealed to the Court of Appeal. The judges decided that, in the absence of specific guidance in precedent cases about the meaning of "in the normal course of events" for the purposes of art.14, the Upper Tribunal had been wrong to consider that it could be sure of the correct answer (the matter was "acte clair"). It should have referred questions to the CJEU, which is what the Court of Appeal decided to do.

Court of Appeal: *HMRC v Mercedes-Benz Financial Services UK Ltd*

2.12.3 Voucher promotion

The Upper Tribunal has now heard appeals by HMRC against the FTT decisions in TC03256 (early 2014) and TC04586 (last update) concerning a promotion by a newspaper publisher involving the purchase and distribution of retailer vouchers to customers.

TC03256

The publishers of the Daily Mail and Mail on Sunday entered into a promotional scheme in which they wrote to potential customers and offered half-price newspapers for a period, at the end of which the customer would qualify for a retailer voucher (e.g. issued by Marks & Spencer) for between £10 and £100. Participating newsagents were also issued with a similar voucher (typically £5 per customer).

M&S charged a reduced rate of VAT on the supply of the vouchers. The Tribunal noted that no explanation of this was given to it; it assumed that this was a composite rate based on the average liability of sales made on redemption. The Tribunal also raised questions about whether VAT should have been charged at all on the issue of retailer vouchers: this was not answered at the hearing, so written submissions were invited to follow up the point.

In 2007, the company notified HMRC that it intended to claim back the input tax on the purchase of the vouchers. HMRC responded in November 2007 stating that they were satisfied that the input tax was deductible and that no output tax was due under SI 1993/1507 (the Supply of Services Order). However, the letter made it clear that the area was under review, and this was only a temporary ruling.

In July 2009 HMRC wrote again saying that the review was complete and the policy had changed. From that date, they regarded as the 'gift' of the vouchers as falling within the Supply of Services Order, and output tax would be due equal to the input tax deducted. Correspondence followed, leading to a formal decision in October 2011, and an appeal to the Tribunal.

HMRC's decision was based on the assertion that the customers paid nothing extra for the supply of the vouchers, so they were bought-in

services that were supplied on for no consideration. They were therefore within the terms of SI 1993/1507.

The company responded that the output tax charge only applies where such services are made available to a third party 'for a purpose other than a purpose of the business'. It argued that the use for a highly successful promotional scheme was a purpose of the business, and therefore the SI did not apply.

The Tribunal examined the CJEU precedents on 'purposes other than those of his business' – *Julius Fillibeck Söhne GmbH & Co KG v Finanzamt Neustadt* (Case C-258/95) and *Danfoss A/S and another v Skatteministeriet* (Case C-371/07). It also noted that the rules for gifts of goods and services were differently phrased in the Directive, a distinction noted by the Advocate-General in his analysis of the *Kuwait Petroleum* case – a gift of goods is chargeable simply on the basis of a disposal free of charge, whereas services must be used 'privately' or 'for purposes other than those of the business'.

HMRC argued that the *Fillibeck* and *Danfoss* decisions emphasised the business necessity of the services supplied for no consideration in those cases. It was not simply a question of there being a commercial reason for the gift: it had to be a commercial requirement.

The decision then turns to the written submissions about the propriety of Marks & Spencer charging VAT on the issue of retailer vouchers, and the question of compliance of Sch.10 VATA 1994 with the Directive. HMRC suggested that the Tribunal should disregard the implications and give a decision on the question put to it, which the judge said 'raised a metaphorical eyebrow'. However, the position appeared to be that:

- HMRC regarded the end result as the same – the company should not have deducted improperly charged input tax, and would then not have to account for output tax under SI 1993/1507;
- the amount specified by M&S on its invoices may have been the 'notional VAT' that is used by intermediaries when making onward sales of retailer vouchers – in which case there is a question (not apparently considered by the Tribunal) about whether the company actually had to pay that amount to M&S;
- the questions in the case were still wholly relevant to situations in which the company bought vouchers from intermediaries, because VAT was properly paid in relation to those vouchers;
- there were arguments that the UK's approach to vouchers in Sch.10A was not in accordance with the Directive, but HMRC argued that it was a reasonable approach in an area where the Directive was not prescriptive.

The Tribunal decided not to delay a decision on the point at issue while the issue of the correctness of the VAT charge was debated. As a preliminary point, the judge observed that para.3 SI 1993/1507 was not consistent with art.26 PVD:

- The wording of SI 1993/1507 is 'where a person carrying on a business puts services which have been supplied to him to any private use or uses them, or makes them available to any person for use, for a

purpose other than a purpose of the business...' This implies that it is the use by the recipient that is relevant in determining whether there should be a charge.

- By contrast, art.26 uses 'the supply of services carried out free of charge by a taxable person for his private use or for that of his staff or, more generally, for purposes other than those of his business'. This relates 'purpose' to 'the supply of services' – it is the trader's purpose in making the services available that determines the treatment.

The Tribunal distinguished the circumstances in *Fillibeck* and *Danfoss*, which were concerned with supplies (home-to-work transport and food) which could very easily be outside the scope of the business. The judge decided that the strictness of the wording of those judgments was due to that context. In *Danfoss*, the judge noted an assumption that food for business contacts would have a business purpose, whereas the trader would have to demonstrate a business necessity in relation to food provided to employees; this suggested that the context was important, and the approach was not as strict as HMRC suggested.

The Tribunal concluded that:

The SPICE campaign was a highly effective business promotion campaign and the vouchers were distributed as a result of binding legal commitments to do so which the Appellant undertook on a fully commercial and arms' length basis as part of that campaign in the normal course of its business. It could not, in our view, properly be said that by distributing the vouchers the Appellant has made them available to its customers for purposes other than a purpose of the business of the Appellant.

The appeal was allowed in respect of what had become a preliminary issue, subject to other potential arguments about whether the VAT should have been charged in the first place.

TC04586

The FTT considered the separate issue of the deduction of input tax on the purchase of the vouchers. The Tribunal examined precedents on vouchers and consideration, including *Argos Distributors*, *Elida Gibbs*, *Kuwait Petroleum*, *IDT Card Services*, *AstraZeneca* and *Lebara*. The judge commented that he expected his decision to be appealed, and in order to be helpful he only set out an outline of the arguments so that the appeal could proceed to the Upper Tribunal at the same time as the output tax case. The issues were:

(1) Whether or not the appellant is correctly to be treated as incurring no input VAT on its purchase of vouchers direct from retailers by virtue of paragraph 4(2) of Schedule 10A; and

(2) If the appellant does in fact incur input VAT on such purchases, whether it is entitled to set that input VAT (and the input VAT which HMRC accept it has incurred on purchases of vouchers from the intermediary) against its output tax liabilities.

The problem was that the PVD does not currently contain any rules for vouchers. A comment by the Commission in May 2012 acknowledged that this created significant inconsistencies and problems. HMRC's

representative claimed that "there was nothing in the existing UK legislation, when interpreted and supplemented by concession as HMRC did, that was inconsistent with the PVD and the case law." The company's representative responded that "there were certain crucial aspects of HMRC's interpretation and operation of the legislation which flew directly in the face of various fundamental principles of VAT and accordingly the UK legislation either needed to be re-interpreted to conform with those principles under the *Marleasing* approach or, if that were not possible, it needed to be overridden altogether by allowing the appellant to rely directly on the right to deduct input tax enshrined in the PVD."

The judge dealt with the issues in reverse order. He came to a brief conclusion on the question of recoverability of input tax: if it was incurred by the appellant at all, it must be recoverable. HMRC's various arguments led to the absurd conclusion that input tax would not be deductible on business promotions. The various cases on which HMRC sought to rely were concerned with charging output tax, not denying input tax.

The issue of whether input tax was actually incurred was more difficult. Where vouchers were acquired from an intermediary, HMRC accepted that the purchase included VAT at the "blended rate" implied by the intermediary's experience of VAT being charged when the vouchers were redeemed. Where vouchers were acquired direct from the retailer, HMRC argued that there was no VAT, because para.4(2) Sch.10A VATA 1994 disregarded that supply. The judge considered this distinction problematic, particularly in view of the principle of fiscal neutrality.

It was also hard to see how HMRC's apparent concessionary allowance of the "blended rate" was consistent with the principle of legal certainty. HMRC said their approach was necessary to preserve the integrity of the VAT system, but the judge considered that "it interposes HMRC's discretion into a fundamental area which ought to be clearly governed by law and also appears to depend upon the state of mind of the recipient of the supply when it is made to him".

The judge considered that the legislation was "imperfect" and had to be interpreted consistently with EU law in line with *Marleasing*. He was not sure how that could be done; however, he was satisfied that the issue of vouchers had to be a taxable supply under the PVD, and the right to deduct input tax was fundamental. The modification introduced by Sch.10A in the form of the "blended rate" could be followed, because it had the purpose of eliminating double taxation. The company was entitled to recover that element of what it paid for the vouchers that the retailers identified as VAT.

The appeal was allowed in principle.

Upper Tribunal

The UT referred to the two decisions as "ANL(1)" and "ANL(2)". There was no dispute about the facts. ANL(1) contradicted HMRC's policy on giving away vouchers as set out in Information Sheet 12/03, which was issued following the changes to the treatment of vouchers in the 2003 Finance Act. ANL(2) appeared to contradict the UK law. The combined effect was to create the "alchemist's dram" – recoverability of input tax

without a corresponding output tax charge. There was a further problem if the recipient of the vouchers never redeemed them: ANL would have recovered input tax without HMRC ever collecting the corresponding output tax.

HMRC argued that this produced an incoherent result. The judges commented that it was tempting to regard that as important, but their task was to determine the issues by reference to the law, not to seek economic coherence.

The judges commented that the cases of *Argos Distributors*, *Elida Gibbs* and *Astra Zeneca* were of particular relevance; the vouchers were different from those in *Lebara*, so the legislation introduced following that decision would not apply.

The issues arising from the FTT decisions were examined in reverse order, because a charge to output tax under SI 1993/1507 can only arise if input tax is deductible. There were two separate issues on input tax:

- first, whether the disregarding of the issue of face-value vouchers by a retailer meant that there was no VAT on the transaction and therefore nothing to claim;
- second, whether the intention to give away the vouchers for no consideration meant that any VAT that there was would be directly linked to a non-business activity and therefore not claimable.

The first issue is specific to vouchers. The second is of more general application, as it could arise in relation to other types of promotional activity.

The Upper Tribunal considered only the PVD provisions on the recovery of input tax, rather than examining the UK legislation. The judges noted that in *Kuwait Petroleum*, the CJEU had held that the "gift" of goods for promotional purposes was part of the company's business activities. The scheme was different, and the issues were also different (output tax and consideration rather than input tax deduction), but the particular point about the business context of the activity had "considerable force".

HMRC's counsel urged the Tribunal to follow the decisions in *Securenta, VNLTO* and *Investrand* and find that VAT on costs specifically relating to a non-economic activities was not deductible. The judges did not accept that these cases were directly relevant, because they concerned costs incurred in relation to the activities of the entity in general. They did not support a contention that a link to a gift ruled out a business purpose.

However, the judges also rejected an argument from the company's representative that there was a presumption that VAT was incurred in relation to business activities. It was still necessary for the claimant to demonstrate a direct and immediate link between incurring the cost and making taxable supplies, either in the form of a link to a particular output transaction or to the business of the entity in general.

Other CJEU decisions, including *Kretztechnik* and the very recent *Sveda* case, were considered in some detail. In the end, the decision on this issue was very brief, and described as "plain": giving the vouchers away for no consideration was not relevant, because it was not something to which the cost could be linked. Rather, it was objectively clear that the vouchers were bought for the purpose of a promotional scheme that increased the

sale of newspapers. That was the required link that justified the deduction of input tax, if there was any.

The judges turned to the argument about Sch.10A para.4(2). HMRC argued that this meant there was no VAT in the issue of the vouchers by a retailer. The trader's representative argued that the effect of the paragraph was simply to relieve the retailer of the obligation to account for the VAT at the time of issue. There would be VAT on redemption, and to deny the purchaser a deduction would infringe the principle of fiscal neutrality.

The judges did not agree. The UK law was not inconsistent with EU legal principles. The only supply on which the retailer had to account for output tax was the supply of goods or services on redemption of the voucher; that was not a supply that was made to ANL. The judges did not consider it contrary to fiscal neutrality to allow an input tax deduction where a voucher was purchased from an intermediary but to deny it when purchasing from the retailer. They included an illustrative example to show that it was only HMRC's concessionary allowance of a "blended rate deduction" to an intermediary that made the results different – under the law, the results would be the same. It appears that the judges considered "breaching fiscal neutrality by concession" was not something the trader could rely on.

The conclusions on the input tax issues were therefore that the FTT had been correct to consider that input tax was deductible on the purchase of vouchers, if it was properly chargeable; but had been wrong to conclude that there was any VAT to claim in the issue of vouchers by retailers.

It was therefore necessary to consider the application of SI 1993/1507 to gifts of vouchers bought from intermediaries. The "business purpose" conclusions of *Julius Filibeck* and *Danfoss A/S* were considered. The judges rejected HMRC's contention that *Kuwait Petroleum* was relevant: that was about free gifts of goods (art.16 PVD), whereas gifts of vouchers were covered by art.16. The wording was different, and that had to be given effect. Goods were always subject to art.16 if they ceased to be part of the assets of the business, but services were only covered by art.26 if they were used for a purpose "other than those of the business".

Astra Zeneca was also irrelevant because that concerned the question of whether the vouchers were given to staff for consideration. SI 1993/1507 has no application to that type of transaction.

The Tribunal concluded that the FTT had made no error of law. The purpose of the recipient of the vouchers, and the transaction in which they redeemed the vouchers, was not the focus of art.26. It was the purpose of the business in supplying the services (the vouchers) for no consideration that had to be determined. There was no doubt that the SPICE promotion was entirely related to the business purpose of selling more newspapers. SI 1993/1507 therefore did not apply.

HMRC's appeal was therefore allowed in respect of the input tax claim where vouchers had been issued by retailers, but dismissed in respect of other input tax and all output tax.

Upper Tribunal: *HMRC v Associated Newspapers Ltd*

2.12.4 TOGC

A company carrying on a beauty salon business filed a repayment return for the quarter to June 2012, accounting for output tax of £967 and claiming input tax of £11,044. HMRC subsequently notified a decision that output tax should be declared on a transfer of stock and assets to another company under common control. The additional VAT would reduce the repayment from £10,076 to £164.

The appellant (BAL) was incorporated in September 2009, opened for business as a beauty salon in August 2011, and registered for VAT in April 2012. The director decided that she wanted to separate two business activities – exporting beauty products, to be carried on by the appellant, and the beauty salon, to be carried on by another company (BASL). This took place in June 2012. Because she owned both companies, she did not bother to document transactions between them, so it was difficult for the Tribunal to be sure exactly what had taken place.

The director's evidence to the Tribunal was that BAL had not "transferred" assets to BASL. Rather, it had allowed BASL to use the goods indefinitely without payment. The Tribunal considered that the facts were relatively simple, but the legal consequences of the facts had to be determined. The profits of the beauty salon business accrued to BASL from the end of June 2012 onwards, even though there was no change that might have been apparent to the salon's customers. BAL simply allowed this situation to subsist, without taking any positive action.

The Tribunal noted that HMRC wanted to apply the rules for a transfer of goods for no consideration; the company's argument would trigger a different deemed supply, leading to a regular output tax charge on goods made available to another person for no charge. HMRC had not come to the hearing prepared to discuss this second possibility, which they appeared not to have considered before. The judge considered this to be "regrettable".

The judge examined the different legal principles that might recognise a legal transfer of the moveable property of the salon business and the implicit licence to occupy that BAL held for the salon premises. He concluded that there had been no transfer, and that HMRC's decision could not stand. The proceedings were adjourned for three months for the parties to agree the proper treatment or, in the absence of agreement, to present further submissions to the Tribunal.

First-Tier Tribunal (TC04683): *Beauty Angels Ltd*

2.12.5 Scale rates

The European Commission has renewed the derogation authorising the UK to continue to use flat-rate scale charges based on the car's CO_2 emission rating to account for the estimated private consumption of business fuel. The derogation has been extended until 31 December 2018.

Council Implementing Decision (EU) 2015/2109

2.12.6 Article

In an article in *Taxation*, Neil Warren suggests that HMRC are trying to increase tax collection by recategorising supplies as standard rated rather than zero rated or exempt. He illustrates the point with three FTT decisions which, he argues, reveal changes in HMRC policy.

Taxation 1 October 2015

2.12.7 Updated Notice

HMRC have updated their Notice *Barristers and advocates*. It states that the new version reflects the introduction of the new online deregistration system and changes to postal addresses.

VAT Notice 700/44

2.12.8 5p or not 5p?

An article in *Taxation* reviews the tax and VAT implications of the introduction of the 5p compulsory charge for carrier bags in England from 5 October 2015. The 5p is inclusive of output tax, regardless of whether the shop follows the government's suggestion and gives the profits from the charge to charity.

Taxation, 29 October 2015

3. LAND AND PROPERTY

3.1 Exemption

Nothing to report.

3.2 Option to tax

Nothing to report.

3.3 Developers and builders

3.3.1 Building work

A company appealed against an assessment to output tax of £51,554 in relation to works it had zero-rated as approved alterations of a protected building. The works involved conversion of a barn into living accommodation. Planning consent had been given subject to restrictions, involving a "section 106 agreement" by the owner not to occupy the new accommodation other than in connection with the existing house, and not to sell, lease or otherwise dispose of it separately; the converted barn was referred to as "the annexe", and it shared a postal address with the main (Grade II listed) house.

The building company had been unaware of the section 106 agreement. Nevertheless, they defended the zero-rating, arguing that the work constituted an approved alteration to a listed building within item 2 Group 6 Sch.8 VATA 1994 (and was carried out before the law changed in September 2012, or within the transitional period for projects in progress at that time).

HMRC argued that item 2 did not apply because the barn conversion was not a "dwelling" because of the restrictions; it could not therefore satisfy the Group 6 definition of "protected building", which had to be a dwelling. The director of the company argued that the main house and the annexe constituted a single dwelling that had been altered. Previous cases such as *Catchpole* (TC01995) and *Fox* (TC01957) showed that it was possible for a single dwelling to comprise two separate buildings. The single postal address and the terms of the planning consent showed that the two buildings were a single dwelling.

HMRC's counsel argued that these cases could be distinguished because the separate buildings only contained sleeping accommodation. The present annexe contained all the facilities required for living; it was only the planning consent that stopped it being a dwelling in its own right.

The Tribunal considered the precedents and the arguments, and agreed with HMRC. It did not matter what the subjective purpose of the purchaser or the designer was: what was important was the result, which was something that could objectively be occupied as self-contained living accommodation. As a result, it was a dwelling apart from failing the condition in Note 2, and zero-rating was ruled out.

This seems to be a Catch-22 situation: the planning consent is enough to stop the barn being regarded as a separate dwelling (when a DIY claim might have been possible), but not enough to make it part of a single dwelling (when the approved alteration argument would have succeeded).

First-Tier Tribunal (TC04679): *Carson Contractors Ltd*

3.3.2 Restrictions on occupation

A company carried out works to construct a house and zero-rated the supply. HMRC ruled that the property was not a dwelling because a s.106 agreement restricted the occupation to someone working in the neighbouring equestrian business. The company appealed.

The Tribunal noted that restriction to a type of worker did not create the necessary link to other land that would engage Note 2(c) of Group 5. The judge cited the *Shields* decision of the UT as supporting this position, even though HMRC won that case overall. Although it appeared that the planning authority had at some point considered occupation by a worker in the particular business would be required, the actual planning consent said "The occupation of the dwelling hereby permitted shall be limited to a person solely or mainly working, or last working, in the locality in agriculture, forestry or an equestrian business, or a widow or widower of such a person, and to any resident dependants." That was a general "occupancy requirement" and was not therefore a restriction on separate use.

The Tribunal went on to consider whether there was a "prohibition on separate disposal". The consent stated that the owner had to retain the property as a single parcel of land, and was not to alienate any part of it on its own "without the prior consent in writing of the Council". The Tribunal decided that the inclusion of these words meant that the Council envisaged the possibility of separate disposal if certain prior conditions were met; it was not an absolute prohibition, which is what the law required.

The appeal was allowed.

First-Tier Tribunal (TC04676): *Edmont Ltd*

3.3.3 Village hall or similar

A community association appealed against a decision by HMRC refusing to allow construction of a new pavilion, car park and all-weather pitch to be zero-rated as "for a relevant charitable purpose". The association provided facilities for the local community to engage in a number of activities. It contended that the use would be "as a village hall or similar". HMRC responded that the users would be only a segment of the community (those interested in sports etc.) and not the community as a whole. Alex Salmond, the local MSP, wrote to HMRC in support of the association's appeal.

The FTT (TC04124) considered that four tests were appropriate.

1) Were the facilities provided for the local community?

2) Was the facility owned, organised and administered by the local community?

3) Were social or recreational facilities provided or reasonably capable of being provided?

4) Was the use similar to the use of a village hall?

After detailed examination of the project, the precedent cases and the arguments of the parties, the Tribunal concluded that most of the building was suitable only for use as a sports pavilion, which was not similar to a village hall. Only one small committee room qualified for zero-rating, amounting to 4.4% of the total.

The association appealed to the UT, arguing that by requiring a large multi-purpose hall as a principal feature, the FTT had unduly restricted the scope of the statutory provision. The Tribunal had also erred in holding that only the meeting room/kitchen was capable of use similar to a village hall in providing social or recreational facilities for the local community. Even if the only use of the changing rooms was for changing, that of itself constituted use for a social or recreational purpose because sports activities on the pitch could not take place unless changing facilities were provided for players and referees. The word “similarly” in Note (6)(b) encompassed use for such a purpose. The presence of the existing village hall was irrelevant to the question whether the new building fell within the scope of zero-rating.

The UT judge considered the precedent cases and concluded that something more is required than use for social or recreational purposes for the local community. If that were all, the reference to “similar to a village hall” would be redundant. The nature of the activities must be similar to those that might be expected to take place in a village hall. In this case, the use of the building itself was not to any material extent for social or recreational purposes, nor similar to a village hall: it was ancillary to the recreational use of the adjoining sports field. The judge considered that the FTT had adopted the correct approach and come to the correct conclusion overall (although he did not agree with the comment that a large multipurpose hall was a necessity), and dismissed the appeal.

Upper Tribunal: *New Deer Community Association v HMRC*

3.3.4 Nature of building contract

A company (F) was responsible for the construction of lodges and infrastructure at a holiday development attached to a golf course in Norfolk. A separate company owned the freehold of the land. A Swedish company supplied kits which were erected by F using subcontractors and employed carpenters. The issue was whether F was making zero-rated supplies of construction services, or a composite supply that did not qualify for zero-rating.

For the first three plots, the freehold title was transferred to F which subsequently granted a lease to a customer. For later sites, a different arrangement applied. The freeholder granted the lease to the customer, who entered into a separate agreement with F. The FTT had to consider the effect and nature of this agreement in detail. The company’s solicitors had drawn it up by amending the previous version, so it used expressions such as “buyer” and “seller” even though they were not apparently strictly appropriate.

The company argued that its part of the deal was simply an agreement with the customer to construct a building designed as a dwelling. HMRC argued that it also contracted to procure the grant of the lease by the freeholder. In 11 of 15 examples, the lease and the agreement were signed on the same day, but it was not possible to know which happened first. In the other four cases the agreement was signed first; one customer's lawyer had refused to sign the lease first (so the deal fell through), on the grounds that he did not think his client should agree to lease the bare land without a binding assurance that something would be built on it.

The Tribunal reviewed various precedents and authorities on interpretation of contracts. The written contracts were the starting point for deciding what their effect would be; they would only be disregarded if they were a sham. When interpreting an agreement, the court must have regard to the words used, to the provisions of the agreement as whole, to the surrounding circumstances in so far as they were known to both parties, and to commercial common sense. When deciding on the categorisation of a relationship governed by a written agreement, the label or labels which the parties have used to describe their relationship cannot be conclusive, and may often be of little weight. The court will consider the rights and obligations of the parties as a matter of construction of the written agreement, and will then consider whether those obligations fall within the appropriate legal description (in this case, a zero-rated supply).

The Tribunal noted that the terms of the contract included F to provide a customer with proof of title to the property and proof of its ability "to procure its transfer", and the customer was entitled to issue "a notice to complete" requiring F to ensure the grant of a lease by the landowner. This went beyond the successful separation of the lease and the construction contract in *Lower Mill Estate*. F was making a composite supply, and it was therefore standard rated.

First-Tier Tribunal (TC04749): *Fairway Lakes Ltd*

3.3.5 Residential and non-residential

There has been a further twist in the long-running dispute over the proper treatment of conversion projects which turn a part-residential property (e.g. a pub) into more than one fully residential property. In *Calam Vale Ltd* (VTD 16,869), it was decided that a project that incorporated part of the previously residential part in each of two new dwellings did not qualify for zero-rating; if the upstairs had been residential and the downstairs not, then a conversion into ground floor and second floor flats would qualify for zero-rating on half, but a conversion into two semi-detached houses would not qualify at all.

This approach was not followed in the later case of *Alexandra Countryside Investments Ltd* (TC02751), where the judge noted the CA decision in relation to DIY claims in *HMRC v Jacobs* and concluded that there was no logical reason to allow a DIY claim under s.35 VATA 1994 but to disallow the zero-rating of an identical project under s.30 and Sch.8 Group 5. HMRC did not appeal that decision, but have never agreed with it, and put to the present Tribunal that it had been wrongly decided.

The present appeal related to the same kind of project – the conversion of a shop with living accommodation above into two semi-detached houses.

HMRC ruled that the sales of both houses could only be exempt. The key point is the application of Group 5 Notes 7 and 9:

7: For the purposes of item 1(b), and for the purposes of these Notes so far as having effect for the purposes of item 1(b), a building or part of a building is "non-residential" if-

(a) it is neither designed, nor adapted, for use—

(i) as a dwelling or number of dwellings, or

(ii) for a relevant residential purpose; or

(b) it is designed, or adapted, for such use but—

(i) it was constructed more than 10 years before the grant of the major interest; and

(ii) no part of it has, in the period of 10 years immediately preceding the grant, been used as a dwelling or for a relevant residential purpose.

9: The conversion, other than to a building designed for a relevant residential purpose, of a non-residential part of a building which already contains a residential part is not included within items 1(b) or 3 unless the result of that conversion is to create an additional dwelling or dwellings.

The Tribunal "respectfully disagreed" with the Tribunal in *Alexandra Countryside Investments*. The Tribunal had to consider the conversion that had actually taken place: it was clear that the building that had been converted had not been, within the definition of the law in Note 7, "a non-residential building" before the conversion. In s.35, the law used the phrase "to the extent that", which allowed a project to qualify in part. Under s.30, it had to qualify or not qualify.

To put it another way, the judge in *Alexandra* appeared to have concluded that "Note 9 requires an additional dwelling to be constructed, which has happened, so the project falls within Item 1(b)"; the judge in the present case started from the opposite direction, holding that "Zero-rating requires the project to fall within Item 1(b) to begin with, which it doesn't because of Note 7, so it doesn't matter what the outcome of the project was." Similarly, Note 10 (which deals with apportionment) was not engaged. The project was wholly exempt, and the appeal was dismissed.

First-Tier Tribunal (TC04756): *DM & DD Macpherson*

3.4 Input tax claims on land

3.4.1 DIY claim

An individual claimed £107,000 under the DIY builders' scheme. The whole amount was refused. He was, incidentally, registered for VAT, but the claim was made as an individual. He had obtained planning consent for extensions and alterations to his house; these had changed as the project went on, and some of the works exceeded those permitted, as a result of which the property was almost entirely rebuilt. A certificate from the council effectively ratified what had been done after the event.

The Tribunal agreed with HMRC that the claim failed to meet several of the conditions. The question of lawful construction had to be considered at the time the work was carried out; retrospective acceptance of the work could not validate a DIY claim for something that was not authorised at the time. In addition, the building had never been demolished to ground level and started again – the effect might be an almost completely new building, but the work had been carried out in incremental stages that never amounted to "new construction". The documentation submitted with the claim failed to meet the requirements of reg.201 SI 1995/2518.

For all these reasons, the appeal was dismissed.

First-Tier Tribunal (TC04709): *Thomas Brennan*

3.5 Other land problems

Nothing to report.

4. INTERNATIONAL SUPPLIES

4.1 E-commerce

Nothing to report.

4.2 Where is a supply of services?

4.2.1 Land-related services

The Commission has published Explanatory Notes to clarify the application of specific provisions of the VAT Implementing Regulation 1042/2013 dealing with the place of supply of services connected with immovable property, which will enter into force in 2017. It is a long and detailed document that is likely to have wider application than just place of supply of services; its analysis may also help to clarify what is sufficiently "land-related" to qualify for exemption.

ec.europa.eu/taxation_customs/resources/documents/taxation/vat/how_vat_works/explanatory_notes_new_en.pdf

4.3 International supplies of goods

4.3.1 Updated Notice

HMRC have issued a revised (October 2015) edition of their Notice *Imported antiques*. The technical content has been restructured to reflect the change from HM Customs and Excise to HM Revenue and Customs (10 years ago!), changes in VAT law and to improve readability from the August 2011 edition.

Notice 362

4.3.2 Implementation of the new Customs Code

HMRC have a paper explaining the changes to import, export and storage procedures that will follow the introduction of the Union Customs Code across the EU on 1 May 2016.

Customs Information Paper 39/2015: www.gov.uk/government/publications/customs-information-paper-39-2015-implementation-of-the-union-customs-code

4.3.3 Simplified Import VAT Accounting Scheme

HMRC have issued an Information Paper to explain revised requirements for Simplified Import VAT Accounting Scheme (SIVA) authorisation applications after 30 April 2015. SIVA allows importers to reduce the level of financial guarantee required to operate a duty deferment account for VAT purposes to 0%.

The new Union Customs Code (UCC) legislation (Commission Regulation 952/2013) comes into force on 1 May 2016. It will introduce revised criteria that economic operators have to meet before they can be authorised to reduce the level of financial guarantee required to operate a customs duty deferment account. This has led to inconsistent authorisation requirements for reduced guarantees across customs duty and import VAT.

Economic Operators who wish to reduce the VAT element of their guarantee to operate a duty deferment account must reach the criteria of Authorised Economic Operator (AEOC). There are transitional arrangements for traders who have existing SIVA authorisations that do not come up for renewal until after 1 May 2016. New SIVA applications after that date will have to meet the new standard.

Customs Information Paper 46/2015

4.3.4 Classifying imports or exports

HMRC have published an updated Notice *Classifying your imports or exports*. This explains the procedure for classifying imports or exports using the tariff; it also explains how to obtain a Binding Tariff Information decision, and points out that BTI decisions will only be valid for 3 years after 1 May 2016 (currently 6 years).

Notice 600

4.3.5 Small Non-Commercial Consignments

The Value Added Tax (Small Non-Commercial Consignments) Relief (Amendment) Order 2015 reduces the VAT exemption limit for small non-commercial consignments (e.g. postal imports sent to individuals) from £36 to £34. This is to maintain the value in euro terms (the EU legislation is based on €45).

SI 2015/2015

4.4 European rules

4.4.1 Review of VAT rules

The European Commission has “decided to give the Single Market a new boost with a number of ambitious and pragmatic actions” outlined in a press release on 28 October 2015. On this list is a “VAT Action Plan” for 2016, but no details are given in this document. It seems likely to include the outcome of the survey on the operation of the POSMOSS rules that will be completed in December.

It has been reported that the Commission is considering whether Member States should have more power to set their own VAT rates. *The Daily Telegraph* reported that this was linked to the controversy in the UK over the application of the 5% rate to sanitary protection, although it is not clear whether this is really something that would worry the Commission.

IP/15/5909; Daily Telegraph, 28 October 2015

In an annex to the work programme, there is a list of proposals that have been or will be withdrawn. These include:

- the 2007 proposals for reform of the exemptions for insurance and financial services, where "no agreement is foreseen (no Council Presidency has recently taken up discussions);
- the more recent proposal to institute a standardised VAT return throughout the EU, where "negotiations have resulted in a draft compromise text that has fully denatured the substance of the Commission proposal. In particular, the latest developments have run counter to the simplification, harmonisation and substantial burden reduction objectives of the Commission proposal."

http://ec.europa.eu/atwork/pdf/cwp_2016_annex_iv_en.pdf

4.4.2 Taxation trends in the EU

The annual report "Taxation trends in the European Union" has been published. It contains narrative descriptions and detailed statistical tables analysing the structure of the 28 Member States, together with Iceland and Norway.

ec.europa.eu/taxation_customs/resources/documents/taxation/gen_info/economic_analysis/tax_structures/2015/report.pdf

4.4.3 Crowdfunding

The Commission's VAT Committee has issued a guidance note on the VAT treatment of "crowdfunding". Crowdfunding often involves a promise of goods or services to be supplied by the person who is raising the funds, to the people who support that fundraiser's activity. The Committee suggests that:

- if the fundraiser is a taxable person acting as such, the later supply of goods or services is a supply within the scope of VAT, if it is linked to the payment by the funders;
- the tax point arises at the time payment is received, provided that the goods or services to be supplied are precisely identified at that time;
- the full amount received is taxable, even though the market value of the supply may be lower;
- in some cases, the funding may be regarded as a donation and not related to a taxable supply, where the benefit received by the contributor is negligible or totally unrelated to the amount of the contribution – in such cases, goods applied by the trader in supplying the "reward" to the funder will created deemed supplies in accordance with art.16 or art.26 PVD;
- if the rewards are in the form of sharing in the profits of intellectual property, the contribution by the funders is a taxable purchase of that intellectual property;
- if the rewards are in the form of securities rather than intellectual property, the supply may be exempt under art.135 PVD;
- "crowd-lending" is also exempt under the same provision;

- the provision of a crowdfunding platform is a taxable service supplied to entrepreneurs, although it may in some circumstances qualify for exemption as a financial service.

ec.europa.eu/taxation_customs/taxation/vat/key_documents/vat_committee/index_en.htm

4.4.4 OECD VAT/GST guidelines

At the annual meeting of the OECD Global Forum on VAT, representatives of more than 100 countries and jurisdictions endorsed the new OECD International VAT/GST Guidelines as the preferred international standard for coherent and efficient application of sales taxes to international services.

The Guidelines include recommended rules on cross-border B2C services such as internet downloads. They suggest that foreign sellers should remit tax to the country where the consumer is located, in line with the POSMOSS rules in the EU. The Guidelines also include a recommended mechanism to ensure the effective collection of VAT by tax authorities from foreign sellers.

www.oecd.org/tax/consumption/oecd-delivers-international-standard-for-collection-of-vat-on-cross-border-sales.htm

4.4.5 Overhead input tax

The CJEU has agreed with the A-G's opinion in another case about overheads and the right to deduct input tax.

A company built a "recreational trail dedicated to Baltic mythology". When completed, its use would be free to the public. 90% of the cost was funded by grants from a public body. The Lithuanian authorities denied input tax deduction on the grounds that the costs were not intended for use for taxable supplies.

The company argued that the trail would attract customers to its site, and they would buy food, drinks and souvenirs. There was a direct link between the capital expenditure and future taxable income. Questions were referred to the CJEU.

Advocate-General Kokott gave an opinion (not in English) that favoured the taxpayer. It is interesting that the UK government intervened in support of the Lithuanian government position:

- there could only be a deduction of input tax if the costs of construction were "incorporated" in the costs of the future taxable supplies as "cost components";
- the fact that 90% of the costs were covered by public grants meant that at least 90% of the VAT had to be disallowed.

The Advocate-General disagreed with both of these arguments. In an opinion that was echoed by the recent FTT decision in *North of England Zoological Society*, she accepted that the construction objectively served the purposes of the taxpayer's taxable business. The trail clearly was built to attract visitors to whom taxable sales would be made. That was a sufficient link to make the VAT into input tax. The full court agreed with this, not stating that "the matter is to be determined by the national court"

but rather confirming that it had already been confirmed by the findings set out in the order for reference.

The full court emphasised again that there is a right to deduct even "*where there is no direct and immediate link between a particular input transaction and an output transaction or transactions giving rise to the right to deduct, where the expenditure incurred is part of his general costs and are, as such, components of the price of the goods or services which he supplies. Such expenditure does have a direct and immediate link with the taxable person's economic activity as a whole.*"

Precedent cases (including *Commission v France* Case C-243/03) showed that partial funding by public grant had no effect on the deductibility of input tax. Similarly, the existence of "free to the public" use could not sever the link between the expenditure and subsequent taxable outputs. Only exempt supplies would lead to a restriction, and it was clear that there were no exempt supplies in contemplation. The input tax should be allowed in full where capital goods were purchased or provided as a means of attracting customers for a taxable business.

CJEU (Case C-126/14): *'Sveda' UAB v Valstybinė mokesčių inspekcija prie Lietuvos Respublikos finansų ministerijos*

4.4.6 Capacity of a trader

An individual, registered in Slovenia as a sole trader, bought seven parcels of land and treated them as part of his personal property rather than his business assets. In *Finanzamt Uelzen v Armbrecht*, the CJEU held that it was possible to allocate part of an asset to private rather than business use. This means that no input tax is deductible on the purchase, but no output tax is chargeable on a subsequent sale.

The trader then proceeded to develop the land into a shopping centre. He assigned five of the seven plots to the assets of his business, but maintained that the two plots he had bought first remained personal assets. He therefore excluded them from a charge to output tax when he sold the shopping centre in 2004. The national court referred questions to the CJEU, which confirmed that the intended private use could not permanently exclude part of the land from VAT; the subsequent development was economic activity, and the whole asset was subject to output tax on sale.

The decision discusses the concept of a trader "acting as such" and the extent to which all activities of the same person are brought within the scope of the person's taxable activities. It seems to be significant that there was no particular difference in the way in which this individual dealt with the two parcels he tried to treat as private: there was no particular reason to treat his actions in respect of those parcels as mere exercise of property rights, when the activity as a whole was clearly taxable property development.

CJEU (Case C-331/14): *Petar Kezić s.p. Trgovina Prizma v Republika Slovenija*

4.4.7 Missing trader rules

The Polish court referred questions to the CJEU about laws in Poland aimed at preventing tax loss through missing trader fraud. In the case,

neither the taxable person nor the tax authorities were able to establish the identity of the actual supplier of goods on which input tax is claimed; although it seems that there was an actual supply of goods, in circumstances in which it seems that output tax should have been due, the authorities would not be able to collect it from anyone. The Polish law appears to preclude an input tax claim in such a case without any requirement to satisfy the *Kittel* test – it is not necessary for the authorities to prove that the claimant had the means of knowledge that the transactions are connected with fraud. The questions asked whether this is acceptable under the PVD.

The court ruled that it was not. The tax authorities would have to prove on the basis of objective factors that the taxable person knew, or should have known, that the transaction was connected with fraud. In other words, the tests from *Kittel* are critical: it is not possible for the tax authorities to short-cut them in order to save time and trouble proving a case.

CJEU (Case C-277/14): *PPUH Stehcemp Sp. j. Florian Stefanek, Janina Stefanek, Jarosław Stefanek v Dyrektor Izby Skarbowej w Łodzi*

4.4.8 Special investment funds

A Netherlands company entered into contracts for the provision of various management services to three other companies in the same country. These companies had been established by pension funds to acquire new investors and to buy, own and manage real property. They outsourced the activities to the appellant company in the case, which provided them with portfolio management, property management, financial administration services, directorship services and managing investor relations.

The appellant company did not account for VAT on fees received for these services, taking the view that it was involved in the management of a special investment fund. The Dutch authorities accepted that some of the transactions were covered by exemptions for real property and financial services, but that the SIF exemption did not apply, so there remained a number of taxable activities. The Dutch Supreme Court referred questions to the CJEU to find out if a property investment company could fall within the definition of a SIF as mentioned in art.13B(d)(6) 6th Directive.

The CJEU recalled that SIFs are generally those collective schemes covered by the UCITS Directive. Property investment companies are not covered by that Directive, so they are not automatically SIFs. To qualify for exemption on the basis that they are identical to SIFs, a different kind of investment fund would have to display characteristics and undertake transactions that were indistinguishable from those of entities that were covered by UCITS. The CJEU examined the characteristics of the companies in the present case, and concluded that they had many similar aspects, including pooling of capital from pension funds, spreading of risk which is borne by unit-holders, and transferability of ownership. None of these factors was affected by the fact that the companies invested in property.

A crucial aspect of a SIF is the state supervision of the investment vehicle. This was originally something left to Member States, but is now harmonised by the UCITS Directive. It would be for the referring court to

determine whether the Netherlands had a system of supervision for these companies equivalent to that applicable to other SIFs. If so, it appears that they would qualify for the exemption, but only on the supply of "investment management services".

The CJEU disagreed with the A-G in holding that the actual management of property did not fall within "management of a special investment fund". It was an activity inherent in the investment itself, going beyond the activities concerned with collective investment of capital raised.

It therefore appears that the CJEU has held that the exemption is potentially wider than the tax authorities' ruling, subject to there being a regulatory regime, but exemption will not apply to all the services supplied, as argued by the company.

CJEU (Case C-595/13): *Staatssecretaris van Financiën, other party: Fiscale Eenheid X NV cs*

4.4.9 Abusive practices?

The CJEU has now given judgment in a case about international transactions, place of supply and alleged abuse of rights, a theme previously considered in the *Newey* case. The court has given guidance on the factors that are more or less relevant in determining whether an abuse has taken place.

A Hungarian individual created intellectual property (know-how relating to the provision of adult online content) through a Hungarian company. The Hungarian company licensed the content to a Portuguese company, while retaining the responsibility of "maintaining and developing" the content. Portuguese VAT rates (specifically, those applicable in Madeira) were lower than those in Hungary.

The Hungarian authorities concluded that the Hungarian company was in reality making the supplies to final consumers, which should therefore be subject to Hungarian VAT (apart from those where the customers belonged outside the EU). The authorities argued that the licensing contract had no economic or commercial reality.

The company responded that it had non-tax reasons for the arrangement. At the time the contract was entered into, Hungarian banks would not process credit card transactions for adult entertainment websites; also, the Portuguese company had experience in international online services, which the Hungarian company did not.

The Hungarian court asked 17 questions aimed at establishing whether this was an abusive practice. The A-G (Melchior Wathelet) considered the principles of the *Halifax* case and concluded that they were not satisfied here. Choosing to make supplies from another Member State was the exercise of a fundamental freedom, and could not be an abuse. The difference between the VAT rates was only 4%, which seemed too low to be a purely tax-related purpose of the arrangement. If the national court could confirm that the company's claimed commercial reasons were real, they would constitute a defence against a finding of abuse.

The A-G also considered whether the possibility that the individual exercised absolute control over the activities of the Portuguese company could be relevant. In his view this would not prevent the Portuguese

company having a real presence in Portugal and carrying on a real economic activity there. The Portuguese government had confirmed that it regarded the company as having the appropriate human and technical resources to be treated as established there.

The A-G also considered questions about the risk of double taxation, the obligation of national authorities to co-operate with each other, and the propriety of using information secretly obtained in the context of a separate criminal investigation for a tax assessment. There was a possibility that such evidence breached the Convention on Human Rights and ought to be excluded from the tax hearing.

The court confirmed that a taxable person is entitled to choose to structure his business so as to limit the tax liability attaching to transactions. There is no obligation to choose the transactions that involve paying the higher amount of VAT. The difference in applicable rates in different Member States arose from the failure to harmonise the VAT system, and could not on its own support a finding of abuse – the Directive only prescribed a minimum rate, and exploiting a lower rate elsewhere did not therefore contravene the Directive.

The CJEU agreed with the A-G that the various factors that the Hungarian authorities appeared to object to – the fact that the manager and sole shareholder of the latter company was the creator of that know-how, the fact that that same person exercised influence or control over the development and exploitation of that know-how and over the supply of the services which were based on it and that management of the financial transactions, the fact that staff and technical instruments necessary for the supply of those services was carried out by subcontractors, and the reasons which may have led the company granting the licence to make the know-how at issue available to a company established in that other Member State instead of exploiting it itself – did not appear to be enough on their own to support a finding of abuse.

Rather, the referring court would have to carry out an analysis of all the circumstances in order to determine whether the agreement constituted a wholly artificial arrangement concealing the fact that the services were not actually supplied by the company acquiring the licence, but were in fact supplied by the company granting it. This would include an examination of whether the establishment of the place of business or fixed establishment of the company (in Portugal) was not genuine, whether the company did not have the appropriate human and technical resources to make supplies, and whether it did not engage in the economic activity in its own name and on its own behalf.

If abuse was found, the fact that VAT had been paid in another Member State would not preclude the Hungarian authorities recharacterising the supplies as made in Hungary. Council Regulation 940/2010 on administrative cooperation required the Hungarian authorities to send a request for information to the Portuguese in order to help determine whether VAT should be chargeable in Hungary.

The CJEU also ruled that evidence obtained without the taxpayer's knowledge, in a parallel criminal investigation, could be used to determine the VAT liability, provided that the court was satisfied that the obtaining of the evidence did not infringe any EU legal rights. These include

proportionality, as well as a number of other specific points made by the court about the rights of defendants to see the evidence against them.

CJEU (Case C-419/14): *WebMindLicences Kft.Nemzeti Adó és Vámhivatal Kiemelt Adó és Vám Főigazgatóság v Nemzeti Adó és Vámhivatal Kiemelt Adó és Vám Főigazgatóság*

4.4.10 Unused tickets

The CJEU has ruled on the chargeability to VAT of unused, non-refundable air tickets (charged to VAT at the lower rate on domestic flights in France). From 1999, Air France (AF) stopped accounting for output tax on such tickets where the passenger failed to check in. The tax authorities ruled that tax was due, and after the French courts upheld the assessment, questions were referred to the CJEU.

The situation was not straightforward. AF subcontracted some flights to another company, Brit Air (B). AF received the price of the tickets and paid it on to B in respect of passengers actually transported. In respect of no-shows, AF paid B an annual flat rate compensation at 2% of the annual turnover of the franchised routes. B did not regard this sum as VATable.

The CJEU considered the precedent of *Société thermale d'Eugénie-les-Bains* (Case C-277/05), in which forfeited deposits for hotel rooms were considered not to be consideration for a supply. In this case, the whole price had been paid: it was not the forfeiture of a contractual indemnity, but a payment for a service that consisted of enabling the passenger to fly, if the passenger turned up.

Regarding the payment as non-VATable on a no-show made no sense, because it would change the nature of the payment at the time it was paid, and also would result in the compensation to the airline for a no-show being higher than the price charged for actually performing the service (because the airline would get the VAT back). The amount retained by the airline was not compensation for harm suffered by the airline, but was remuneration to the airline, even if the passenger did not benefit.

It followed that the tax point for the service was when the payment was received by the airline or by a third party acting on its behalf. The payment was for a specific service, and all the conditions for a taxable event were met on payment.

The same principles applied to the "compensation" paid by AF to B. It was not truly compensation, because it did not relate to harm suffered by B. Rather, it was part of the package of remuneration paid by AF to B for operating the franchised routes.

CJEU (Case C-250/14): *Air France — KLM v Ministère des finances et des comptes publics*; (Case C-289/14): *Hop!-Brit Air SAS v Ministère des Finances et des comptes publics*

4.4.11 Reverse charge

Member States have the right under art.198(2) PVD to extend the reverse charge mechanism to transactions in "gold material or semi-manufactured products of a purity of 325 thousandths or greater" by designating the customer as the person liable for paying the tax. Denmark had enacted such a rule.

A Danish company purchased 24 bars of a rough amalgam of scrap materials that contained gold (including, for example, teeth). The gold content was estimated at between 500 and 600 thousandths, but it had to be extracted. The company paid VAT on the purchase, but the supplier went into liquidation without accounting for the output tax to the authorities. The Danish authorities denied the purchaser's repayment claim on the basis that the reverse charge applied.

The Advocate-General (Kokott) has given an opinion that the goods in this case are of the kind to which art.198(2) can be applied, so the Danish ruling is permitted. She notes that the reverse charge mechanism is a necessary resource for tax authorities in closing off the opportunity for carousel fraud, and is particularly useful in relation to high value, easily transportable products such as items containing gold.

CJEU (A-G) (Case C-550/14): *Envirotec Denmark ApS v Skatteministeriet*

4.4.12 Self-supply of land

A company acquired a 20-year lease of land on which a building was in course of construction. The lease was granted for an annual payment of rent rather than for a capital sum upfront; however, under Netherlands law, the creation of the lease constituted a supply of goods, taxable on the future rents at the time the lease was granted. The grantee paid VAT and deducted it; it then completed the construction of the building, and was subject to a self-supply charge on completion, because it used the building for its own purposes. The output tax on completion was not fully deductible because part of the building was rented out as an exempt activity. It was therefore important to establish the value to be subject to output tax under the self-supply.

The company calculated the self-supply based on the costs of completing the construction, plus one year's rent that had already been paid by the time the construction was complete. The authorities argued that the full amount of the rentals payable over 20 years should be included.

The Advocate-General noted that the purpose of the provision at issue (art.5(7)(a) 6th Directive) was to prevent exempt traders from obtaining an advantage by creating goods themselves without paying VAT, instead of buying those goods from third parties who would have to charge VAT. The provision should be interpreted in line with its purpose, which is to preserve fiscal neutrality.

The A-G was satisfied that the present situation fell within the self-supply provisions. As far as the calculation of the VAT was concerned, there was no doubt that the VAT on the grant of the lease was fully deductible at that time, because the finished building was to be put at least partly to taxable use. There would either be taxable use, or an output tax charge on a taxable self-supply on completion. The question was whether the whole of that VAT, charged and deducted at the time of the grant, should be included in the self-supply charge on completion.

Under art.11A(1)(b) 6th Directive, the "purchase price for similar goods" is used in preference to the actual cost, if it can be ascertained. In this case, the national court had concluded that there was no such purchase price. It was therefore necessary to establish the correct cost price. The Advocate-General decided that the correct approach was to take into

account the costs of construction incurred by the company, together with the outstanding rental payments under the long lease – not 20 years, as argued by the government, nor 1 year, as argued by the company, but 19 years. In effect, the year's rental paid during the completion of the building was used up in that taxable activity, and should not be part of the self-supply for future partially exempt use.

CJEU (A-G) (Case C-128/14): *Staatssecretaris van Financiën v Het Oudeland Beheer BV*

4.4.13 Deduction of input tax

The Polish court has referred questions to the CJEU to determine whether a branch established in one member state, carrying out mainly intra-company transactions for a parent company established in another member state, is entitled to deduct input tax when the actual taxable activity is carried on by the parent:

Do [articles 168 and 169 PVD] not preclude, in the case of a branch registered for VAT purposes in one Member State and carrying out mainly intra-company transactions for a parent company established in another Member State and occasionally also transactions taxable in the State where the branch is registered, the taxable person from being entitled to deduct input tax in the State in which the branch is registered, despite the fact that the tax is linked to transactions carried out by the parent company in another Member State?

It appears from the summary of the case that the Polish operation is a subsidiary rather than a branch. The case may provide some useful guidance on the difference between head office/branch and holding company/subsidiary structures.

CJEU (Reference) (Case C-393/15): *Dyrektor Izby Skarbowej w Krakowie v ESET spol. s r.o. sp. z o.o., oddział w Polsce*

4.4.14 Deductible proportion

The Italian court has referred questions to the CJEU on the method of calculating the deductible proportion under Italian law:

For the purposes of exercising the right of deduction, are national provisions ... and the practice of the national tax authorities which require that reference be had to the composition of a trader's turnover, including in order to identify so-called incidental transactions, but make no provision for a method of calculation that is based on [both] the composition and the actual destination of the acquisitions and that objectively reflects the actual share of the expenditure attributable to each of the – taxed and untaxed – activities engaged in by the taxpayer incompatible with an interpretation of Articles 168, 173, 174 and 175 [PVD] which is guided by the principles of proportionality, effectiveness and neutrality, as set out in Community law?

CJEU (Reference) (Case C-378/15): *Mercedes Benz Italia SpA v Agenzia delle Entrate Direzione Provinciale Roma 3*

4.4.15 Distortion of competition

The Irish Appeal Commissioners have referred questions to the CJEU on determining whether there would be a significant distortion of competition if a public body was regarded as outside the scope of VAT in relation to tolls collected for use of a road, when commercial operators had to charge VAT on tolls for other roads. Given the specific nature of the road and the toll, there is only a hypothetical possibility of a competitor entering the market. The questions are as follows:

If a body governed by public law carries on an activity such as providing access to a road on payment of a toll and if in the Member State there are private bodies who collect tolls on different toll roads pursuant to an agreement with the public body concerned under national statutory provisions, is the second indent of [art.13 PVD] to be interpreted as meaning that the public body concerned must be deemed to be in competition with the private operators concerned such that to treat the public body as a non-taxable person is deemed to lead to a significant distortion of competition notwithstanding the facts that (a) there is not and cannot be any actual competition between the public body and the private operators concerned and (b) there is no evidence that there is any realistic possibility that any private operator could enter the market to build and operate a toll road which would compete with the toll road operated by the public body?

If there is no presumption, what exercise should be conducted to determine whether there is a significant distortion of competition within the meaning of the second indent of [art.13 PVD]?

The applicant road authority argues, in accordance with Case C-288/07 *Isle of Wight Council*, that it would be practically impossible for private operators to build a toll road; as the roads on which it collects tolls are at some distance from those of the commercial operators, there is no actual or potential competition.

CJEU (Reference) (Case C-344/15): *National Roads Authority v The Revenue Commissioners*

4.4.16 Double jeopardy

The Italian courts have referred a question to the CJEU about the propriety of Italian provisions which allow the tax authorities to impose both an administrative and a criminal tax penalty in respect of the same act or omission (non-payment of VAT). This refers to the fundamental rights under art.4 of protocol 7 of the European Convention on the Protection of Human Rights and Fundamental Freedoms and art.50 of the Charter of Fundamental Rights of the European Union.

CJEU (Reference) (Case C-350/15): *Criminal proceedings against Luciano Baldetti*

4.4.17 Right to deduct

The Hungarian authorities denied a tax deduction for certain invoices on the basis that the suppliers did not have the premises or staff required to provide the services stated, which must therefore be a sham. The company argued that it had exercised due diligence (checking the suppliers' registration numbers) and that the transactions had actually

taken place. The Hungarian court has referred questions to the CJEU asking about the level of due diligence that a tax authority can expect a trader to exercise in relation to the ability of a supplier to provide services. Further questions relate to the question of allowing input tax where it appears that a transaction has taken place, but not between the parties named on the invoice.

Overall, the Hungarian court appears to want clarification of the order of importance of the invoice and supporting due diligence. If the invoice is false, can due diligence be assumed to be inadequate? Is due diligence only relevant if it can be shown that there was a transaction between the two parties specified on the invoice? The CJEU has considered many variations on this theme over the years, and this will add a little more to the list of precedents to be argued about in MTIC cases.

CJEU (Reference) (Case C-446/15): *Signum Alfa Sped Kft. v Nemzeti Adó- és Vámhivatal Kiemelt Adó- és Vám Főigazgatóság*

4.5 Foreign refund claims

4.5.1 Claim refused

A French company carried on a trade of distilling, rectifying and blending spirits. It made a claim under Directive 2008/9 for VAT incurred in the UK during 2010; this claim was refused because it was made outside the statutory deadline, on 28 December 2011 (the deadline for that year was 30 September 2011). Correspondence followed in which the Overseas Repayment Unit explained that the statutory deadlines were strictly adhered to.

In March 2013 the company made two claims in respect of UK VAT incurred during 2012, totalling over £51,500. These claims were refused in July 2013 after the ORU concluded that the company was making supplies in the UK and was therefore not eligible for the Directive refund scheme. Following further correspondence, HMRC accepted that the claim was valid, because the transactions concerned took place within the bonded warehousing scheme (and were therefore not counted as making taxable supplies in the UK).

As a result of the letter refusing the 2012 claim (sent by ORU in July 2013), the company did not submit a further claim for 2013 by the deadline of 30 September. It only realised that it could do so in December 2013. HMRC refused this claim because it was late, pointing out that the company could have made the additional claim while continuing to appeal the earlier decisions. The company appealed, arguing that in all the circumstances, it was unreasonable that HMRC's incorrect refusal of the first two claims should lead to a loss of the refund of the third.

The Tribunal found the company's views and actions entirely understandable, but could not find in its favour. The claim was late, and there was no discretion. The judge suggested that HMRC should consider changing the wording of Notice 723A and its decision letters to make the point clearer to EU businesses in a similar position. It was possible that the company could pursue a formal complaint to HMRC in the hope of

receiving compensation, but it could not establish a claim to the VAT itself.

First-Tier Tribunal (TC04673): *SAS SVS La Martiniquaise*

4.5.2 13th Directive claim

An American company, registered in the State of Nebraska, appealed against the refusal of a 13th Directive repayment claim. The company had claimed for VAT incurred on three items purchased in the UK on 10 June 2013 (VAT £3,839.03), 19 June 2013 (VAT £350.30) and 10 July 2013 (VAT £309.20). The claim therefore spanned two prescribed years, the 12 months to 30 June 2013 and to 30 June 2014.

The claim was submitted to HMRC on 18 September 2013. Enclosed with it was a "certificate of status" from the State of Nebraska. The claim was rejected by HMRC because, according to HMRC's letter of 1 October 2013 to the company, the certificate of status was not valid. This was explained in a later letter from HMRC: the appropriate certificate of status could be obtained from the Federal Certification Unit in Philadelphia and it was this Federal form, rather than the State form that had been provided, which was required. The letter also enclosed an example of a certificate provided by the Federal Authority.

The company obtained the relevant form by 16 December 2013 and submitted the claim again. HMRC received it on 13 January 2014 but rejected it, this time because original invoices had not been supplied, and also because the time limit for the June 2013 year had expired on 31 December 2013. This was explained in a letter from HMRC dated 15 July 2014 (the decision says 2015, but it must mean 2014).

The company resubmitted the claim on 29 July 2014, enclosing the original invoices. HMRC agreed in September 2014 to repay the 2014 claim (the July 2013 purchase), but the remainder was out of time. The company requested a review, arguing that the claim had been made in time (in September 2013) and the provision of the documentation later should not affect that.

The judge agreed with HMRC that a claim is not made until it is accompanied by the appropriate documentation. HMRC's letter of 1 October 2013 stated that the claim had not been "accepted or entered as a claim". Until the appropriate documentation was provided, it had no status. Neither HMRC nor the FTT had any power to extend the time limits. The appeal was dismissed.

First-Tier Tribunal (TC04750): *Comoretel Holdings Ltd*

5. INPUTS

5.1 Economic activity

Nothing to report.

5.2 Who receives the supply?

5.2.1 Legal fees

A company claimed input tax amounting to £23,366. HMRC disallowed all of it on the basis that the company was not carrying on a taxable business and there was no link between the inputs and any taxable supplies made by the company.

The company had been incorporated on 4 January 2013, and registered as a property developer on 15 July 2013 (w.e.f. 4 January). Its first two returns claimed refunds of VAT and were rejected by HMRC. £18,000 of the tax claimed related to legal costs of defending the owner and sole director against a prosecution for false accounting. The rest related to miscellaneous expenditure including fuel, business entertainment, hotels and subsistence, as well as items not subject to VAT. In July 2014 HMRC decided to deregister the company. The company had already appealed against the input tax decisions, and although it did not formally appeal against deregistration, the Tribunal agreed to consider that decision as well at the hearing.

It is interesting that HMRC put forward four arguments, one of which they dropped at the hearing as being untenable:

Argument One: The appellant is not a taxable person and so is not entitled to be registered for VAT, this argument being the Deregistration Decision;

Argument Two: The legal fees do not have a direct and immediate link to the appellant's business, as they relate to an event, namely the fraud, that allegedly took place in 2007 prior to the incorporation of the appellant;

Argument Three: The legal fees do not have a direct and immediate link to the appellant's business having been incurred by Mr Hewart to defend himself in a criminal prosecution; and

Argument Four: The miscellaneous expenditure did not have a direct and immediate link to the appellant's business and/or was not subject to VAT.

Argument Two was dropped because the legal fees were clearly incurred at the time of the trial, not at the time of the alleged offence.

During an adjournment the appellant agreed to reduce the miscellaneous expenditure claim to about £2,430 (from £5,366). This eliminated items on which HMRC ruled there was no VAT, or the VAT was blocked, but the expenditure was still subject to the first argument and the deregistration decision.

The legal fees related to a prosecution for false accounting arising from involvement with a previous property development business. As

described in the decision, the director's connection to any alleged fraud was tenuous, and he was acquitted. The Tribunal reviewed precedent cases including *Ian Flockton Developments Ltd*, *P&O Ferries (Dover) Ltd* and *Rosner*. The case of *Becker* (Case C-104/12) provided a relevant and recent CJEU precedent: the CJEU had ruled "*In this case, the supplies of lawyers' services whose purpose is to avoid criminal penalties against natural persons, managing directors of a taxable undertaking, do not give that undertaking the right to deduct as input tax the VAT due on the services supplied*." The company's representative tried to distinguish the facts from *Rosner* and align them with *P&O*, but the Tribunal considered that *Becker* confirmed the UK legal position. There was not a clear nexus with the business. Preserving the director's reputation was undoubtedly of benefit to the appellant company, but that was not enough to make the input tax deductible.

As regards the deregistration decision, HMRC argued that in 2013 there had been no sales, no contracts with customers and no business plan. The company had successfully reapplied for registration in 2014 on the basis of projects that started to come to fruition late in that year. The Tribunal accepted that the company was engaged in taxable activities. Although there was a delay in securing income, the projects were substantial and were being diligently pursued. The appeal was allowed in respect of that decision and the deductibility of the input tax on the miscellaneous expenditure, as adjusted by agreement.

First-Tier Tribunal (TC04789): *Substantia Invest Ltd*

5.2.2 Self-insurance

A self-drive car hire company was of such a size that it effectively self-insured third party risks. It set up a captive insurance company to provide fleet insurance; the Tribunal considered that the contractual position was that "*the insurer became liable to indemnify UDL's customer in the event UDL's customer damaged property belonging to a third party while driving the car*". The premiums paid to the captive insurer were directly related to claims made; as a result, the company sometimes paid for repairs to third party vehicles directly, without making a claim.

In order to minimise costs, hirers were given a "bump card" to hand to the owner of any car with which they might be in collision. This encouraged the driver to contact UDL directly, rather than going to its own insurance company; UDL would then seek to manage the repairs, contracting directly with the car repair workshop, and so minimise the cost. UDL made a claim to recover input tax on the cost of these repairs, which HMRC rejected.

The Tribunal noted that neither the appellant nor HMRC had considered the legal position in any detail, but the judge considered it to be crucial. The situation arose when UDL believed that the customer was liable to pay compensation to the third party, and this compensation was covered by the indemnity from the captive insurer. There was no contract between UDL and the third party, but it was understood that the third party could not both claim compensation and have its repair paid for by UDL.

The Tribunal considered that the contractual position was straightforward: the garages contracted with UDL to repair the cars. However, it was not so easy to determine to whom the supply of repair services was made.

That required consideration of the legal and economic reality, in accordance with precedent cases including *Newey*, *SecretHotels2 Ltd*, *Redrow*, *Baxi, Aimia, WHA* and *Airtours*. After an extensive review of these decisions, the judge (Barbara Mosedale) concluded:

We take from consideration of all these cases that a VAT supply, ordinarily at least, requires a legal relationship between the supplier and recipient under which the supplier is obliged to make the supply and the recipient is liable to pay for it: Tolsma and Redrow. Nevertheless, where the economic reality of the legal relationship is such that it results in final consumption of goods or services by a consumer in circumstances where in effect there is no VAT charge on that consumption then this normal rule is overridden because the ultimate purpose of the Principal VAT Directive is to tax final consumption.

She explains how she intends to apply this as follows:

In conclusion, in a situation where B agrees to pay A to provide goods and/or services to C, and C agrees with B to pay for the goods and/or services provided by A, then a Redrow 'follow the liability to pay' analysis applies to decide to whom A's supply is made. This is because the legal relationships reflect the economic reality and the outcome is consistent with the Principal VAT Directive because final consumption is taxed. In other words, A's supply is to B, and B makes an on-supply to C.

But where a Redrow 'follow the liability to pay' analysis does not lead to tax on final consumption, because although A makes a supply to B (of providing goods/services to C), B does not on-supply A's services to C, then C's consumption will be untaxed, and, applying Baxi/Aimia/WHA, economic reality requires the supply to be seen as made to the final consumer.

Applying these principles to the facts, she concluded that either the company did not itself consume the garage's services, or if it did, it then supplied them on to the owner of the car (in which case an equivalent amount of output tax would have been due). She preferred the conclusion that the economic reality was that the services were consumed by the owner, and the contractual liability to pay constituted third party consideration. This was very similar to the *WHA* case, and the judge did not accept (or, in her words, understand) the distinction that the company attempted to make with that decision.

The judge included an alternative analysis as a postscript, setting out the conclusion if there was an implied contract between the company and the car owner: that would lead to a valid input tax claim, but a matching output tax charge on the barter supply.

In either case, the appeal had to be dismissed.

First-Tier Tribunal (TC04785): *U-Drive Ltd*

5.2.3 Article

In an article in *Taxation*, Neil Warren considers the basic requirements for input tax deduction, in particular the need for the business to have been the recipient of the supply. He comments on the recent case of *Robert Welch Designs Ltd* (TC4608), and relates it to the earlier decisions in *BLP*

Group plc and *Airtours Holiday Transport Ltd v HMRC* (which is under appeal to the Supreme Court).

Taxation, 29 October 2015

5.3 Partial exemption

5.3.1 Mixed-use building

Advocate-General Mengozzi has given an opinion on a case referred from Germany about the way in which costs associated with a building should be apportioned between taxable and exempt use by the taxpayer. As usual, the opinion has not been made available in English.

The appellant constructed a building which contained residential accommodation, let out exempt, and commercial premises, which were let out subject to VAT. The company applied a turnover-based method to determine the deduction of input tax on costs associated with the building.

In 2004, the company needed to adjust its allocation of input tax, because some of the commercial part of the building was now rented out as residential accommodation. It continued to use a turnover-based method. The authorities carried out an inspection and decided that, although they had approved this method in 2001 and 2002, it was no longer appropriate. Instead, an apportionment should be based on the floor areas used respectively for the two purposes.

The German VAT law on partial exemption includes a provision that:

If a trader uses any goods supplied, imported or acquired in the Community for the purposes of his business, or a service supplied to him, only in part for effecting transactions in respect of which the right to deduct is excluded, there shall be no deduction of the part of the input tax which is economically attributable to those transactions. The trader may make an appropriate estimate of the non-deductible amounts. Determination of the non-deductible part of the input tax in accordance with the ratio between the transactions in respect of which the right to deduct is excluded and the transactions in respect of which there is a right of deduction is permissible only if no other economic allocation is possible.

The Advocate-General's opinion is that this is contrary to the Directive, in that it provides for a primary method of allocation other than the turnover-based method. Although the Directive permits other methods to be used, there is no general, unconditional right to derogate from the basic method provided for by the Directive. "Another method" – that is, in UK terms, a special method – should be applied:

- only for particular transactions or situations; and
- only if the other method guarantees a more precise determination of the deductible proportion than the standard method.

As the German rule does not satisfy these requirements, it should be disregarded. The trader would then have the right to use the standard turnover-based method as prescribed in the Directive.

The A-G pointed out that the *Armbrecht* case is not relevant. That concerned a building that was partly used privately. In this case, the whole building is used for business purposes, but part of that use is to make exempt supplies.

The A-G confirmed that there would be a general right for a Member State to require an adjustment of recovery under art.20 6th Directive (the capital goods scheme), but the German law was not sufficiently clear and precise in its enactment of that provision. There also was no reason to justify a distinction in the way recovery was calculated for construction costs and maintenance costs.

CJEU (A-G) (Case C-332/14): *Wolfgang und Dr Wilfried Rey Grundstücksgemeinschaft GbR v Finanzamt Krefeld*

5.3.2 Deduction of VAT in respect of foreign branches

Following the CJEU judgment in *Le Crédit Lyonnais v Ministre du Budget* (Case C-388/11), HMRC consulted on proposed legislation to restrict the VAT deduction of VAT insofar as it was attributable to both activities within the UK and to foreign branches. The CIOT made submissions to this proposal and followed them with a meeting. HMRC have now withdrawn the proposals and issued a short consultation on new, more acceptable proposals. The CIOT has responded to these, noting that some key issues remain: these include what is meant by the term ‘sector’, what is meant by ‘separate accounts’, and how the proposals interact with HMRC’s views on *Skandia* in VAT group situations.

CIOT Technical Team Update, 9 November 2015

The Value Added Tax (Amendment) Regulations 2015 came into force on 1 January, implementing the changes that the government considers to be necessary following *Credit Lyonnais*. The changes will take effect as follows:

- changes to reg.101 (operation of standard method) – longer periods beginning on or after 1 January 2016 (in effect, 1 April 2016);
- changes to reg.102 (special methods) – methods approved or directed by HMRC on or after 1 January 2016;
- changes to reg.103 (attribution to foreign and specified supplies) – prescribed accounting periods beginning on or after 1 January 2016.

SI 2015/1978

HMRC have issued a Brief to explain the changes as follows:

Supplies from an establishment outside the UK will be excluded from “T” in the standard method under reg.101.

Businesses that make supplies from overseas establishments and currently use the standard method will no longer be able to recover related input tax on the basis of “use” under reg.101(8) and a number of options will apply:

- where such a business continues to use the standard method it will need to apply the UK recovery rate when recovering input tax used to make supplies from overseas establishments;
- where such a business continues to use the standard method, and the difference between the result of using that method and using a

method which fairly reflects the use of the tax bearing costs exceeds £50,000 (or £25,000 in the case of group undertakings), it will need to account for the difference because of the effect of the standard method override (regs.107A – 107F).

Such a business can apply to use a special method. HMRC say that they would expect a business to do so if there is a "material" (not defined) difference between the operation of the standard method and the recovery that would be appropriate based on "use", even if the standard method override is not engaged. If that is the case and the business does not apply for a special method, HMRC may direct it to use one.

Special methods that are not based on sectors cannot include the value of supplies made from overseas establishments. Presumably this means that the "overseas sector" has to be dealt with separately from "UK sectors". For partial exemption special methods, a business may only have a method based on sectors where each sector within it reflects the use made of goods and services in the business and in that sector, the structure of the business and the type of activity undertaken by that sector.

HMRC state that "for reg.103, a business may only have a calculation based on sectors where each sector that it is based on reflects the use made of goods and services in the business and in that sector, the structure of the business and the type of activity undertaken by that sector." This appears to envisage a calculation under reg.103 that is similar to a special method under reg.102, but the explanatory notes do not make it clear exactly how HMRC expect this to operate.

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5.3.3 Change of intention?

A partnership was involved in hotels and farming in the Eastbourne area. It bought a pub and claimed back the VAT on the purchase. HMRC decided that the building was not intended for use to make taxable supplies, but rather for exempt use as a nursery. The taxpayer appealed, arguing that it had intended to use the property as a retail shop.

The Tribunal considered that the partnership's witnesses were not straightforward, and stated that their evidence would not be accepted unless it was corroborated. The judge concluded that there had never been a positive intention to open a shop: that had simply been a convenient reason to claim back the VAT. In reality, there had been a firm intention to open a nursery from the time the property was purchased. The officer had considered a reg.108 clawback, but the Tribunal considered that the VAT should not have been claimed in the first place.

The Tribunal considered a number of CJEU precedents on the recovery of input tax by a taxable person in circumstances where there is a change to making exempt or partially exempt supplies. There was the possibility that recovery might have been justified because the input tax was incurred in a longer period before exempt supplies actually commenced. However, the judge was satisfied that none of the input tax could at any time have been validly attributed to an intention to make taxable supplies, so none of it should have been recovered. The appeal was dismissed.

First-Tier Tribunal (TC04653): *Sheikh Gulzar and another t/a Lions Cub Nursery*

5.4 Cars

Nothing to report.

5.5 Business entertainment

5.5.1 Article

In an article in *Taxation*, Neil Warren reviews the VAT rules on Christmas gifts and parties, including entertainment of staff and overseas clients.

Taxation 17 December 2015

5.6 Non-business use of supplies

5.6.1 Pension fund costs

HMRC have issued a further Brief on the deduction of input tax on pension fund management fees by employers. R&C Brief 43/2014 acknowledged that the CJEU decision in *PPG Holdings* (Case C-26/12) meant that HMRC's policy of disallowing VAT on investment management costs incurred by employers in respect of their pension funds was wrong; the previous policy of allowing 30% of a single bill covering asset management and administration could continue to be operated for a transitional period until 31 December 2015 while employers assessed the consequences. Then in R&C Brief 08/2015, HMRC acknowledged that it might be possible for employers and pension fund trustees to enter into a tripartite contract with fund managers so that the employer would "receive" the services for VAT purposes and so be entitled to input tax deduction. However, HMRC have now expressed doubt over whether costs paid directly for asset management would meet the "wholly and exclusively" requirement for corporation tax deduction of the expense. HMRC are therefore extending the transitional period for the continuation of the 70:30 split until 31 December 2016.

HMRC comment on options other than tripartite contracts that have been put forward by advisers and representative bodies, including:

- Supply of scheme administration services by pension trustees to an employer;
- VAT grouping of a corporate pension fund trustee with the employer, provided that the eligibility criteria in s.43A VATA 1994 are met.

If the pension trustee contracts with managers for asset management services, and invoices the employer for "running the pension scheme on the employer's behalf", then there is a chain of supply. The liability of the trustee's supply to the employer would have to be considered – if it is a compound taxable supply (which seems likely), the employer would be able to deduct input tax to the extent that it related to the employer's own taxable business.

HMRC suggest that the trustee's costs of managing assets would relate directly to its investment activities, but "may also have a direct and immediate link to the supplies made to the employer, provided part of the trustee's supply to the employer of running the pension scheme on their behalf includes asset management services". HMRC therefore consider that this would entail "dual use" of the inputs, and any input tax recovery would have to reflect this.

VAT grouping of the trustee and the employer, if possible, will lead (in HMRC's view) to similar results: the asset management costs will be "directly and immediately linked to the trustee's investment activity", but may also be directly and immediately linked to the employer's taxable activities, if they are used for those activities. This does not appear to take account of the CJEU decision in *Larentia + Minerva*, which suggested that there should not be an apportionment to "non-business activities" if there was any link to the taxpayer's economic activity.

HMRC also comment: "*Representatives have raised concerns that the effect of the joint and several liability provisions relating to VAT grouping mean that where a corporate trustee is VAT grouped, HM Revenue and Customs would be entitled to recover a VAT debt of the VAT group from the pension scheme assets. Our position is, and remains, that we are unable to recover VAT from the scheme assets except to the extent that the relevant VAT debt is attributable to the administration and operations of the pension scheme. This is set out in paragraph 4.3 of VAT Notice 700/17: Funded Pension Schemes.*"

HMRC are considering representations about alternative tripartite structures that might protect the corporation tax deduction, and will issue further guidance later this year.

In the meantime, the transitional period will be extended to 31 December 2016. The employer and the scheme trustee have to agree to the same treatment. The new treatment will apply from 1 January 2017, and taxpayers can switch to it at any time before then.

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5.7 Bad debt relief

5.7.1 Insolvency concession

HMRC consulted until 16 December 2015 on a draft Treasury order containing amendments to VAT legislation to preserve the effect of ESC 3.20, which prevents insolvency practitioners becoming liable for clawback of input tax on bad debts where the supply took place prior to the insolvency of the business for which they act.

The intention is that the existing treatment should simply continue, but on a statutory footing. Where a trader has claimed input tax on a purchase invoice, but has not paid that invoice within six months of the due date, s.26A VATA 1994 normally requires the input tax claim to be reversed. This mirrors the supplier's right to claim bad debt relief at the same time. ESC 3.20 disapplies s.26A if an insolvency procedure has commenced between the original input tax claim and the time at which the claim should be reversed. A new s.26AA is proposed to reproduce the effect.

www.gov.uk/government/consultations/extra-statutory-concessions-technical-consultation-on-draft-legislation

5.8 Other input tax problems

5.8.1 Alternative evidence

A company operating a bakery decided to outsource its payroll to a new provider after its accountant returned to Poland. A friend of the director recommended a particular company; the director met with representatives of that supplier, checked that the company existed and verified its VAT registration with the Europa website and with HMRC, and started to use its services. This involved an agreement to transfer employment of the staff to a payroll bureau; they were then effectively bought back in as staff supplies subject to VAT.

The bakery then registered for VAT and reclaimed input tax on its first return (presumably making significant zero-rated sales), including over £10,000 on invoices in respect of its staff. HMRC investigated and found that neither of the supplier companies was registered for VAT, so they disallowed the input tax claim. The company appealed; although by the time of the hearing it had accepted that the VAT invoices were invalid, it argued that supplies had undoubtedly taken place, so HMRC should pursue the supplier and allow the input tax.

The judge noted that the jurisdiction of the FTT was limited to considering whether the decision had been taken reasonably. Without going into great detail in his decision, he concludes that the officer who disallowed the claim did not take account of some irrelevant matter or disregard something to which he should have given weight. The appeal therefore had to fail.

First-Tier Tribunal (TC04694): *Ambrosia Bakes Ltd*

A trader was assessed to £124,980 plus interest for periods from 08/11 to 11/12. His business was the facilitation of a "grey market" trade in

prestige vehicles such as Porsches, Mercedes and Range Rovers. Manufacturers and dealers in the UK would not want their sales to be exported by a commercial company to Singapore; to get around this, the trader purchased the cars in his own name and sold them on to a company, Great Harvest Ltd, which exported them. To prevent the manufacturers becoming aware of the arrangement, other individuals purchased the vehicles on behalf of the trader. However, the trader claimed that the dealers were well aware of what was going on, and in some cases actively sought him out in order to make sales. The main problem was that the trader's purchase invoices were in the names of the individuals rather than the trader.

The Tribunal considered a number of precedents on the question of accepting alternative evidence to support an input tax claim. These included *Everycar Contracts Ltd and Sabrina Hammon trading as SJM Group* (TC02801), *McAndrew Utilities Ltd* (TC02406) and *ReemstmaCigarettenfabriken GmbH v Ministero delle Finanze* (CJEU Case C-35/05). It concluded that HMRC must exercise their discretion to allow alternative evidence having regard to the principles of neutrality and effectiveness under Community law.

HMRC argued that the trader had not shown that it was virtually impossible to obtain a valid VAT invoice. In effect, he had chosen not to do so. In respect of a small part of the assessment which related to road fund licences recharged to customers, HMRC argued that these were not non-VATable disbursements, but rather part of a single supply of a taxed vehicle.

The Tribunal found the trader an honest, credible and helpful witness. It made a number of findings of fact, confirming matters that were not really in dispute. It appeared that HMRC officers had only one reason for denying the input tax claim on the purchase of vehicles: they had considered exercising discretion, but had decided not to do so only because the trader had not produced valid VAT invoices in his own name.

The judge did not agree with HMRC that it was not "virtually impossible or excessively difficult" to obtain those VAT invoices. The whole point of the trade made it unlikely that the dealerships (as opposed to individual managers with whom the trader dealt) would issue replacement invoices. The Tribunal listed the matters that had led it to the conclusion that HMRC's decision was unreasonable:

(1) The inability to obtain VAT invoices in Mr Boyce's name as set out in paragraph 43 above.

(2) The Agency Agreements clearly evidenced the true relationship between the Dealerships, the Named Purchasers and Mr Boyce.

(3) Mr Boyce's bank statements evidenced the payments to the Named Purchasers and tallied with the Dealerships' invoices.

(4) HMRC had previously investigated Mr Boyce's affairs and were presumably satisfied that these arrangements constituted supplies to Mr Boyce.

The FTT noted that HMRC had won the *Everycar* case on apparently similar facts. However, that decision was not binding on the Tribunal, and the judge saw a number of differences of detail in the reasoning

underlying the two review decisions by officers. In particular, the officers' decisions in *Everycar* referred to the need to prevent fraud, whereas that was not part of the present case. Also, the dealers in *Everycar* had changed their practice so they did provide regular invoices later; here, the FTT concluded that it was and remained excessively difficult for the trader to obtain them.

The FTT agreed with HMRC that the road fund licence and registration fees were not disbursements; the trader had purchased and sold "taxed and registered cars". The appeal was therefore allowed in respect of £100,663 and dismissed in relation to £2,452. The remainder of the assessment had been agreed between the parties before the hearing.

First-Tier Tribunal (TC04651): *James Boyce t/a Glenwood*

The FTT considered yet another case about a business that purchased individual iPhones through individual purchasers, and therefore did not have "proper" VAT invoices addressed to the company to evidence its input tax claims. The decision examines the way in which this trade was carried on in late 2010 and early 2011, and concludes that the decision not to accept alternative evidence was justified. The judge noted that such evidence as was available "raised as many questions as it answered" – to the extent that it appeared the appellant had received supplies of phones, it was unclear how those purchases were paid for. The "explanations [were] commercially implausible", and the appeal was dismissed.

First-Tier Tribunal (TC04723): *Mian Global Ltd*

5.8.2 Missing traders

A rare FTT success for a MTIC appellant concerned claims for £6.3m in periods 04/06 and 05/06, and £3.5m in relation to 06/06. The initial hearing of the appeal took place in early 2012, but the release of a decision was stayed pending criminal proceedings which took place in the summer of that year.

The company clearly had a genuine trade which had been going on for some years and had been closely monitored by HMRC. The control officer was apparently unaware, when arranging an annual inspection in June 2006, that other HMRC officers were about to raid the premises with a search warrant and remove all the records – some of which appeared then to disappear altogether.

In April 2013, the FTT (TC02667) was split: the judge found the director a convincing witness, an honest businessman whose trading had many of the indications of carousel frauds (including rapid growth and banking with FCIB), but who had co-operated with HMRC throughout and had carried out genuine due diligence. His side member concluded that the *Kittel* tests were satisfied, and that on the balance of probability the company was a willing participant in a fraudulent scheme. The appeal was allowed on the casting vote of the chairman.

HMRC applied for leave to appeal to the Upper Tribunal, putting forward 8 different grounds. The FTT initially granted leave on grounds 3 and 5; following a further application to the Upper Tribunal itself, HMRC were allowed to advance grounds 2, 3, 5 and 8, but not 1, 4, 6 and 7.

Mr Justice Morgan and Judge Herrington heard the appeal. The decision criticises the way in which HMRC set out their grounds, as they contained

a mixture of claimed errors of law (which would be valid grounds of appeal) together with material that would be used in argument. Given that certain of the grounds had been excluded from the scope of the appeal, it was necessary to analyse carefully exactly what material HMRC were entitled to use, and what were valid grounds of appeal. The decision sets them out as follows:

Ground 2

(1) The F-tT applied the wrong test in deciding not to draw an adverse inference from CCA's failure to adduce evidence in respect of the matters referred to at paragraphs 22 and 30 above in that it asked itself if the failure was "a deliberate ploy to conceal matters".

(2) It also erred in taking account of the fact that the burden of proof was upon HMRC.

(3) It also took into account irrelevant factors in deciding the issue and it failed to address HMRC's arguments that CCA's evidence on the issue was not credible.

Ground 3

The F-tT erred in law in taking into account an irrelevant consideration relating to connected criminal proceedings against one of CCA's suppliers, Future Communications.

Ground 5

The Ft-T misapplied the test in Kittel in that:

(1) It considered a more onerous test than that prescribed by law;

(2) It applied the burden and standard of proof to individual pieces of evidence as opposed to considering the totality of the evidence;

(3) It adopted an overly sceptical approach to circumstantial evidence;

(4) It paid insufficient regard to the "should have known" limb of the test;

(5) It misinterpreted the case advanced by HMRC as being a case of dishonesty and, in particular, it was wrongly influenced by the opinion of the officers of HMRC as to the nature of the fraud; and

(6) It considered it relevant that the criminal investigation had paid no attention to Mr Trees.

Ground 8

The Judge erred in law in his approach to the banking evidence in that:

(1) His conclusions were inconsistent with the evidence to the extent that they were not conclusions which a reasonable tribunal could have reached;

(2) He wrongly disregarded relevant evidence;

(3) He failed to take into account the detailed submissions made on behalf of HMRC;

(4) His conclusions were based on errors of fact; and

(5) He took account of irrelevant matters;

(6) He failed to give an adequate explanation or reasons for dismissing the banking evidence.

Given the difficulties experienced by the UT in determining the grounds of appeal, the judge made some general comments about how these should

be set out, and suggested that a Practice Direction on the matter might be useful.

The UT then went through each of HMRC's grounds in turn. It dismissed Ground 2, finding no error in the way the FTT had approached its task.

In respect of Ground 3, the UT agreed that the FTT had drawn an incorrect inference from the criminal proceedings against the supplier – the FTT judge had concluded that, because he had not been called to give evidence by those prosecuting the supplier, the company's director did not know about the fraud. The state of his knowledge was for the FTT to consider, and this was an unwarranted conclusion.

In respect of Ground 5, the UT examined the conclusions of the FTT on "means of knowledge" and held that they had not been adequately reasoned – they required "much more by way of an intellectual exchange", and HMRC's list of twenty points "did not receive a coherent rebuttal from the judge". This was again an error of law.

There was not time in the hearing of the UT appeal fully to consider all the banking evidence put forward by HMRC in support of Ground 8. The UT had already decided that the case would have to be remitted to a differently constituted FTT for further examination; that part of the case could be considered by the FTT at the same time, being mainly concerned with matters of fact and therefore appropriate for a fact-finding Tribunal.

HMRC's appeal was allowed, and the case will be remitted to the FTT.

Upper Tribunal: *CCA Distribution Ltd (in administration)*

A company appealed against a FTT decision confirming HMRC's refusal to repay some £3.3m of input tax in relation to the periods 04/06 to 06/06. The HMRC refusal was issued on 21 December 2006, and the FTT hearing took place in October 2010, but it does not appear to have been reported.

The grounds of appeal were that the FTT had erred in law in concluding that the company actually knew of a connection to fraud, and in applying the *Kittel* principles to a contra-trading case. The second ground was dropped before the UT hearing following the 2015 judgment of the CA in *Fonecomp*.

The FTT had concluded that the trader actually knew of the connection to fraud, derived from a number of factors but in particular the synchronisation of payments through the chain. It was therefore not necessary for the FTT to consider HMRC's alternative argument that the trader ought to have known.

The company argued that the FTT should have applied a higher standard of proof than the normal civil "balance of probabilities". The UT judge considered that this was mistaken. The taxpayer's representative relied on an interpretation of CJEU judgments in *Mahageben* and *Bonik* that was not justified. It was necessary that the FTT should rely on "objective evidence", but that was not inconsistent with the normal UK evidential standard.

The UT also rejected an argument that the FTT conclusion was perverse. That required the company to clear the high hurdle of an appeal on a finding of fact; it could not do so. The FTT hearing had taken 13 days with many witnesses, and the FTT decision set out the reasoning from all

that evidence in some detail. It was not true that the FTT had relied only on one line of evidence (banking information from FCIB) – it had reached its conclusion quite properly on a range of evidence.

The appeal was dismissed.

Upper Tribunal: *Excel RTI Solutions Ltd v HMRC*

A company appealed against the refusal of £378,350 of input tax claimed for the period 08/06. The trader claimed that he believed the other parties were carrying out adequate due diligence, and that HMRC should have been policing his deal chains. The Tribunal could not accept that this was adequate checking, or that the director could seriously have believed either proposition. The appeal was dismissed on the usual basis that he had the means of knowledge that his transactions were connected with fraud.

First-Tier Tribunal (TC04777): *Blue Orange Information Technology Ltd*

5.8.3 VAT incurred in other countries

A company deducted as input tax some £63,000 of VAT incurred in other Member States. Although this was VAT, and was legitimately incurred in the course of business on accommodation and other travelling expenses, it could not be claimed through a UK VAT return. HMRC raised assessments to recover it, telling the trader (a mechanical engineering consultant) that he could claim it back through the electronic refund system. Once he had agreed to pay three years' worth back to HMRC, he discovered that he was out of time to claim more than the last year's worth by that route. He was therefore obliged to pay £63,000 (plus interest) but could only recover about £6,000.

He appealed, but the FTT could give him no more than sympathy. There was clearly no legal basis for his appeal. The appellant acknowledged that HMRC had been helpful and sympathetic (apart from debt management, who were less so); it was regrettable that an innocent mistake should lead to such a large financial loss. The judge suggested that the trader discuss the matter with his accountant "to make sure that such mistakes do not happen again", and to consider amending corporation tax returns to reflect the losses.

First-Tier Tribunal (TC04665): *PPIG Ltd*

6. ADMINISTRATION AND PENALTIES

6.1 Group registration

6.1.1 Grouping and *Skandia*: update

As promised in R&C Brief 2/2015, HMRC have published a list of other Member States that operate an "establishment only" grouping rule similar to the Swedish law considered by the CJEU in the *Skandia* case. Where a UK corporate group contains a company with either a head office or a branch in one of these countries and the reverse in the UK, and the foreign operation is registered as part of a VAT group in the other country, it will have to treat supplies between the head office and the branch as transactions subject to VAT, rather than applying the *FCE Bank* principle that transactions within the same entity are ignored for VAT. HMRC point out that this is the case whether or not the UK company is part of a UK group VAT registration – it applies equally to a standalone company with a foreign branch or head office.

Note that transactions in goods are normally treated as if they were supplies anyway; the main effect is on supplies of services, which will:

- require a reverse charge in the UK if they are supplied to the UK operation by the foreign operation;
- have to be entered on EC Sales Lists by the UK operation and taken into account in considering input tax entitlement if they are supplied to the foreign operation.

The anti-avoidance legislation in s.43(2A) – (2E) VATA 1994 will not apply to transactions between such foreign operations and any members of a UK VAT group (not just the branch/head office of the foreign operation), because the *Skandia* treatment will override the UK law.

HMRC also state that this change of treatment will be compulsory from 1 January 2016. Businesses may choose to apply the changes to services performed earlier than this date, provided they do so consistently for all services and establishments affected.

The Brief contains the following table outlining how HMRC expect Member States to operate VAT grouping in the light of *Skandia*. HMRC state that "*This information is provided as a guide only. It is the responsibility of individual businesses to check with the relevant member state tax authority to confirm the situation and agree how it applies to their own particular circumstances.*"

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HMRC subsequently received further information about grouping in the Netherlands and Spain, and updated their table accordingly:

Member State	latest position
Cyprus, Finland, Germany, Spain (advanced method)	At the time of publication the intention of these member states is uncertain

Austria, Ireland, the Netherlands, UK	HMRC does not expect these Member States to apply "establishment only" VAT grouping to create intra-establishment supplies
Italy, Romania, Spain (basic method)	Italian, Romanian and basic Spanish VAT grouping is purely administrative, treating each member as a separate taxable person and just amalgamating their VAT figures on a single return. Such "grouping" does not trigger the UK VAT changes above
Belgium, the Czech Republic, Denmark, Estonia, Hungary, Latvia, Slovakia, Sweden	HMRC expects these Member States to apply "establishment only" VAT grouping to create intra-establishment supplies
Bulgaria, Croatia, France, Greece, Lithuania, Luxembourg, Malta, Poland, Portugal, Slovenia	HMRC understands these Member States do not have VAT grouping

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6.2 Other registration rules

6.2.1 Cancellation of registration

A company was registered from the introduction of VAT, and had been involved in the yacht business for 40 years. In December 2013, HMRC decided to cancel the company's registration with effect from 23 June 2010 on the basis that it was no longer carrying on a business. An assessment was raised in July 2014 to recover input tax claimed from 07/10 onwards, amounting to £2,305 plus interest, plus a penalty (cancelled before the appeal hearing).

The company appealed (late) against the decision to cancel the registration. The owner of the business was unable to attend, being 80 and undergoing medical treatment, but he agreed that the hearing should proceed without him on the basis of his written submissions. He argued that the business was still continuing, even though he had sold the moulds for making a particular type of yacht to a manufacturer in the Netherlands. He was still promoting the design, and was still trying to recover the final instalment of the proceeds.

The judge noted that the law permitted HMRC to deregister a person who has ceased to be registrable; if so, they may cancel his registration with effect from the day on which he so ceased or from such later date as may be agreed between them and him (Sch.1 para.13(2) VATA 1994). As he had not agreed that he had ceased to be in business, HMRC could not

deregister him from any earlier date than the date on which he ceased to be entitled to be registered (para.13(5)).

The FTT had first to consider the extent of its jurisdiction in relation to the decision to deregister. The judge commented that there was surprisingly little clear authority on the point. Two precedents were cited: in *Anne Brookes* (VTD 11,752), in which the Tribunal considered it had a supervisory jurisdiction, but strangely seemed to regard that as "wider" than a full appellate jurisdiction; in *Gardner & Co* (TC01320), the FTT stated that it had a full appellate jurisdiction, but did not explain how it had come to that conclusion. Other cases on the nature of the Tribunal's jurisdiction on matters of HMRC's discretion were considered, including *John Dee* (on security), *BMW (GB) Ltd* and *Banbury Visionplus* (on refusal of a partial exemption special method), and *Best Buys Supplies Ltd* and *GB Housley Ltd* (on reg.29 permission to deduct input tax). The judge in this case quoted "the one principle which is clear" from the John Dee decision: "*The function and powers of a Tribunal in each case will depend in large measure on the nature of the decision appealed against and of course on any special statutory provisions.*"

The judge went on to comment that the decision to cancel a trader's registration was not similar to a decision to require a deposit of security. The registration decision depended on a factual condition (that the trader was not carrying on a business with the intention of making taxable supplies), and that seemed to be exactly the sort of question that Parliament would have intended for the Tribunal to decide on appeal. The decision about security was much more within the Commissioners' care and management powers, as it depended on their view of the need to protect the revenue.

An appeal in relation to a business splitting direction (s.83(1)(u)) is expressly restricted to a consideration of whether HMRC have made a reasonable decision (s.84(7)). There is no such cross-reference in relation to the registration or cancellation of registration of a person (s.83(1)(a)). The Tribunal took some assurance from this that the jurisdiction was appellate. After extensive consideration of all these principles, the judge decided that:

- the Tribunal could allow an appeal if it was satisfied that the trader was still in business at the date HMRC cancelled the registration;
- it could not re-make the decision for HMRC and cancel the registration from some other date – if it appeared that the business ceased on a different date, the matter would have to be referred back to HMRC for them to make a further decision.

Finally, the substantive issue was considered. The trader put forward the "*Lord Fisher* indicia" and claimed that he satisfied them. The activity of yacht brokering had been hit by the recession, but that did not mean that a business conducted on sound principles for many years had ceased. By its nature, it was a trade in which transactions would be relatively infrequent but would be large when they happened, satisfying the "substance" point.

HMRC argued that the company had made no taxable supplies after October 2007 apart from the receipt of some commission in February 2010 and the sale of some mould tools in 2010 and 2011. The sale of the mould tools related to instalments of a sale that was agreed in 2006, and

did not represent ongoing economic activity. The date of 23 June 2010 had been chosen because of the receipt of an instalment on 22 June 2010: HMRC had taken this as the last evidence of economic activity, but now were of the view that the proper deregistration date would have been earlier rather than later (as it was only an instalment relating to an earlier sale, rather than anything to do with a new supply).

The Tribunal considered the case to be finely balanced. However, it was satisfied that there was enough evidence of a continuing business intention to justify VAT registration up to October 2011. This meant that HMRC's decision was wrong and the appeal had to be allowed. It would be for HMRC to decide what to do with the decision; in the view of the Tribunal, from October 2011 to September 2013, there did not appear to be enough evidence to justify an entitlement to registration. From September 2013 onwards, it might be possible to do so, but that would be a new argument for a different Tribunal, if HMRC and the taxpayer could not agree.

The appeal against the decision and the assessments was allowed.

First-Tier Tribunal (TC04664): *David Love Marketing Ltd*

6.2.2 Registration date

A company was involved in marketing tax avoidance schemes. It registered for VAT with effect from 1 June 2009, but HMRC decided it should have been registered with effect from 1 August 2006. By the time the appeal came on for hearing the amount claimed by HMRC in respect of output tax was £324,412. In addition HMRC disallowed input tax credits of £119,521 claimed by the company in periods 09/09 to 06/11.

The assessment had originally amounted to more than £1.5m. One of the company's arguments was that the agreed reduction before the hearing showed that the assessment had been manifestly wrong and therefore not made to best judgement. However, he did not seek to use this argument to have the assessment declared invalid, but rather to question the amount.

The Tribunal reviewed the history of the tax avoidance schemes, which were the subject of extensive HMRC investigation. The current director of the appellant company had been interviewed by HMRC under COP9, implying a suspicion of tax fraud.

The investigation of the company had begun after it registered and submitted a repayment claim for its period 06/11. The visiting officer found that its accounts for the year ended 31 March 2007 showed annual turnover of £264,000, and asked why it had not registered for VAT before. The company responded that it had been a member of a LLP, and the disclosed turnover was a partnership profit share. It had only begun contracting with its own clients in June 2009.

On further investigation, the officer decided that the declared turnover was subject to VAT. She also noted that many of the expenses on which input tax were charged by companies sharing the same address, and she ruled that many of the invoices did not comply with the VAT regulations. She based the decision to backdate the registration on the annual accounts, and based the initial assessment on bank receipts. By the time of the hearing, she had accepted that some of the bank receipts were matched by bank payments, and appeared to constitute disbursements – payroll

payments on behalf of clients. That led to the reduction in the assessment for output tax to £324,000.

The Tribunal tried to reconstruct the history of the business from the evidence of the director and the investigating officer. The director's evidence was described as unsatisfactory; he did not appear to know anything about the operation of the business before he was appointed, and not a great deal more afterwards. The investigating officer suffered from a number of misapprehensions, including not apparently understanding the operation of LLPs.

The LLP had ceased to trade on 22 April 2008, and the Tribunal concluded that from that date onwards the appellant must have been making supplies directly to clients. Before that date, it was entirely possible that the company made taxable supplies to the LLP in respect of supplies of staff – payments by a LLP to a member could be VATable consideration as well as outside the scope profit share. The evidence about the appropriate date of registration was not conclusive, so the Tribunal left the matter for the parties to agree in the light of various findings of fact and principle.

The Tribunal then went through a list of invoices, considering whether they complied with reg.14. Many did not include a sequential number, but the officer stated that if that was the only defect, she would not have disallowed the input tax. Many of the descriptions were vague; although the Tribunal found that some of them were adequate to satisfy the regulation, many did not, including some of the larger ones. A description "fees on account as per agreement regarding charges" could not be adequate when not even the director could explain what the "agreement regarding charges" was.

The appeal was allowed in relation to the invoices that were held to satisfy reg.14; it was dismissed in relation to all other matters, although the parties were invited to reconsider the registration date based on findings about when the company started making supplies directly to clients.

First-Tier Tribunal (TC04775): *Knutsford Business Services Ltd*

6.2.3 Updated Notice

HMRC have updated their Notice *"Should I be registered for VAT?"* to reflect the 2015 registration and deregistration thresholds. Further changes include:

- the introduction of a new online system for registering for VAT;
- the removal of the VAT registration threshold for non-established taxable persons;
- the inclusion of all the forms associated with VAT registration;
- formatting changes to make the Notice suitable for publication on the GOV.UK website.

The Statement of Practice about artificial separation of business activities has been moved to www.gov.uk/government/publications/statement-of-practice-4-1983/statement-of-practice-4-1983.

Notice 700/1 and 700/11: Supplement

6.3 Payments and returns

6.3.1 Flat Rate Scheme

An individual operating a post office used the Flat Rate Scheme. He was assessed for using the wrong rate: the charge was for £13,869 underdeclared between 05/10 and 01/13. He asked to be able to withdraw from the FRS with retrospective effect, which would have reduced the VAT owing, but HMRC refused. The trader appealed against the assessment and the decision.

The trader had operated the FRS from 1 October 2006, and had classified his business as "retailing food, confectionary, tobacco, newspapers, or children's clothing" with a flat rate (at that time) of 2%. HMRC decided to carry out a compliance check in February 2014. Although there is a specific category for "Post Offices" with a higher rate, HMRC accepted that the retail side was the greater part of the business, so the categorisation was correct. However, the trader had failed to notice the increase in the rate from 2% to 4% that came into force from 4 January 2011.

The main ground put forward in the appeal against the assessment was that HMRC should have notified the trader of the change in rate. Leaving it so long to commence a compliance check and raise the issue for the first time meant that he would have to pay much more VAT than necessary.

The Tribunal agreed that it might be better if HMRC were under an obligation to notify traders of changes in the flat rates, but they are not. There was no question about the correctness of the assessment or its amount. There were no exceptional circumstances that might lead HMRC to depart from their normal policy of not allowing retrospective withdrawal from the scheme. "Fairness" was not within the jurisdiction of the FTT; the Tribunal could only conclude that the assessment was right and the decision to refuse withdrawal had been reasonably made. The appeal was dismissed.

First-Tier Tribunal (TC04702): *John David Pryor t/a Purfleet Post Office*

6.3.2 Updated Notices

HMRC have updated their Notice *VAT payments on account*. The main change appears to be merely an update to the address for the HMRC POA team.

Notice 700/60

HMRC have also updated their Notice *How to fill in and submit your VAT return*. The main change appears to be removal of BillPay as a means of paying the liability. The Notice now starts with the circumstances in which HMRC will accept that a trader is not required to file online:

HMRC is satisfied that:

- *your business is run entirely by practising members of a religious society whose beliefs prevent them from using computers*
- *it is not reasonably practicable for you to use a computer to submit your returns, for reasons of age, disability or remoteness of location*

If you think either of these apply to you then please contact the VAT Helpline to discuss alternative arrangements.

The Notice goes on to explain the benefits of submitting online and paying by Direct Debit, as well as how to sign up for these benefits:

- *a safe and secure method of sending your return*
- *an on-screen acknowledgement that we have received your return*
- *an option to receive an electronic reminder when your return is due*
- *automatic calculations to reduce errors when completing the return*
- *up to 7 extra calendar days to submit your return and pay any VAT due (compared with the due date for paper returns and cheques sent by post) – and if you pay by Direct Debit online at least 10 extra calendar days to pay.*

Notice 700/12

6.4 Repayment claims

6.4.1 Group claims

Another appeal has come before the FTT on the issue of the identity of the correct claimant where:

l) the representative member of a VAT group accounted to HMRC for VAT for a prescribed accounting period and brought into account an amount as output tax that was not output tax due;

2) the company whose trading activities gave rise to that overdeclaration of output tax ("the generating member") was a member of that VAT group during the relevant prescribed accounting period;

3) that VAT group remains in existence, but the generating member has ceased to be a member of that VAT group.

In HMRC's view, it is the representative member of the VAT group that has overpaid the VAT, and the "generating member" cannot make a claim. The company in the case argued that it had transferred the amounts due to the representative member to be paid on to HMRC, so it ought to be entitled to claim them back.

The claim related to mechanised cash bingo (MCB) and main stage bingo (MSB). The claimant company was the representative member of an extant VAT group that was formed in 1997; the group now contained companies that had operated MCB and MSB in the past at times when they were not members of the VAT group – they had been in a different VAT group, or had been separately registered.

HMRC accepted that a right to claim could have been transferred to the current representative member on acquiring the generating member, as long as the former registration (group or individual) had ceased, the entire trade and assets had been transferred, and a valid claim was made. However, this could not apply if the company had been a member of a

different group which still exists now; only the representative member of that other group could claim.

The hearing of this appeal had started in March 2014 and had been adjourned so that the parties could make submissions based on three other cases which were decided on similar issues: *Standard Chartered plc/Lloyds Banking Group plc* (TC03450); *MG Rover Group Ltd* (TC03461); and *Taylor Clark Leisure plc* (UT 2014). The first two of these cases have been appealed to the UT (after reaching contradictory conclusions); in March 2015 at a directions hearing, the parties to this appeal asked the FTT to make its own decision rather than waiting for those appeals.

The Tribunal adopted a summary of the earlier decisions from the company's representative's skeleton argument: in *MG Rover*, Judge Mosedale had decided that the generating member was entitled to claim; in *Standard Chartered*, Judge Berner had concluded that it should be the representative member of the group that had overpaid the VAT; and in *Taylor Clark*, Lord Doherty said he preferred the *Standard Chartered* approach.

The company advanced a number of arguments, principal among them that the s.43 group "fiction" should not survive when a company left a group. Once it had left one group and joined another, the "generating member" should no longer be regarded as part of the old representative member. If it had in the past borne the cost of an overpayment of VAT, it should be entitled to reclaim it. If a company remained in the same VAT group and the representative member made a claim, it would hold the repayment for the benefit of the generating member; if that generating member left the group, it should take the benefit of the claim with it. This argument was development with a detailed analysis of what was right about Judge Mosedale's approach and what was wrong with Judge Berner's decision.

HMRC's representative responded to these arguments line by line, and suggested that the *Taylor Clark* decision was the best starting point – a more recent, more authoritative decision that favoured their point of view. He also suggested that the *Skandia Corp* decision of the CJEU emphasised the primacy of the single taxable entity fiction as against the individual members of a group.

Judge Demack carried out a detailed analysis of the law and the arguments, and came down completely on the side of HMRC and Judge Berner. He stated that Judge Mosedale had not properly understood the EU law concept of the single taxable person. He rejected the company's claim that the generating member bore the burden of the overpaid tax. In his view, the burden was borne by the group of which it was a member at the time; that group could make any arrangements it wanted to share the burden of the tax, and it was therefore "neutralised". The person who should make any relevant claim would in all cases be the representative member that made the overpayment, regardless of the time elapsed between the supplies being made and the claim being submitted. The appeal was dismissed in its entirety.

First-Tier Tribunal (TC04674): *Gala Leisure Ltd*

6.4.2 *Bridport* claims

HMRC have issued a Brief entitled "update on supplies of sporting services by non-profit making bodies". It states that HMRC have concluded, after reviewing the many claims they have received from eligible bodies, that:

- clubs would be unjustly enriched if the full amount of output tax charged to non-members was refunded to them;
- the level of fees was relevant in determining by how much the clubs would be unjustly enriched;
- those clubs that charged over £100 per person for a round of golf should be repaid 33% of its VAT Information Sheet 01/15 compliant claim;
- those that charged less should be repaid 50% of their claims.

They will now pay claims on this basis, after receiving confirmation from claimants that:

- they have checked their claims in line with Information Sheet 01/15 (they say they have found a high level of errors in claims checked);
- their green fees are more or less than £100 per person per round or day;
- they want an interim payment, rather than waiting for final settlement.

There is a dedicated address for *Bridport* claims.

The Brief also includes reminders that:

- the recovery of VAT may have direct tax implications, if the refunds are not passed on to those who originally paid it;
- all new claims will be subject to the usual 4-year time limit;
- adjustments can be made through returns under reg.34 SI 1995/2518 if they are within the monetary limits, but claiming in this way will mean that no interest will be due under s.78.

HMRC also threaten to charge penalties where clubs have not taken due care and have as a result submitted an invalid claim.

Revenue & Customs Brief 19/2015

The Tribunal heard appeals about unjust enrichment in relation to *Bridport* claims from four representative golf clubs in June and July. The decision was not released until after the above Brief was published. The Brief appears to be based on the arguments put forward by HMRC in the Tribunal; as the Tribunal did not in the end agree with HMRC's arguments, the Brief will presumably have to be amended (unless HMRC decide to appeal).

The clubs selected as representative were The Berkshire Golf Club ("The Berkshire"), the Wilmslow Golf Club (the "Wilmslow") and The Glen Golf Club ("The Glen"). They were chosen to cover a range of geographies, levels of (local, regional and national) competition and qualities to be representative of the different types of golf courses in the

UK. As the Bridport & West Dorset Golf Club had already gathered together all the required documents it too participated in the appeal, although its claim had been settled by HMRC following the CJEU decision.

HMRC instructed Professor Stefan Szymanski, the Stephen J Galetti Professor of Sport Management at the University of Michigan, as their expert economist and also instructed an economic consultancy, Frontier, to gather evidence from the four clubs. The economics exercise concentrated on level of competition for non-member golf, price elasticity of demand, price elasticity of supply, and evidence of changes in VAT rates affecting prices charged to non-members. The professor produced a report on "The economic incidence of VAT charged on green fees by golf clubs to non-members and the economic losses borne by golf clubs".

The clubs accepted that there would be an element of unjust enrichment if their claims were paid in full. However, they disputed the extent of it, and argued that HMRC's view was not in accordance with EU law.

Apart from the question of unjust enrichment, there were other issues for the Tribunal to consider:

Whether supplies of green fee golf by the appellants which are on-supplied to individuals by tour operators are exempt or subject to VAT at the standard rate.

Whether, if the customer of the appellant is a body corporate, there is a distinction between a "corporate day" package (which all parties accept is taxable) and the supply of access to play golf.

Which categories of course maintenance costs are properly treated as residual in each of the following circumstances:

(a) The club provides advertising services from locations on the golf course but has no corporate day income;

(b) The club has neither corporate day income nor course advertising income; and

(c) The club has taxable income from the hire of other golfing equipment, including but not limited to golf buggies, trolleys or clubs.

Whether the link between course maintenance costs and taxable tee advertising, corporate day or rental income is sufficiently direct and immediate to give rise to at least partial input tax recovery and whether this depends on the category of cost incurred and is the Tribunal able to identify, on the evidence before it, which categories do give rise to a sufficiently direct and immediate link.

Unjust enrichment

The Tribunal decision starts with a rehearsal of the principles of unjust enrichment and a person's rights to receive repayment of wrongly levied taxes ("*San Giorgio* rights"). It then records a great deal of statistical and economic analysis. It is unusual for a VAT decision to discuss concepts of marginal cost, price elasticity, perfect competition and so on. The following gives a flavour of the difficulty faced by the Tribunal:

Having carefully considered the experts' written and oral evidence, there were some aspects of it that, with the benefit of hindsight, we would like to

have seen explored more. Mr Trussler, for example, did not include a cost to cover existing or future capital investment in what, as he himself argues, is a high fixed cost business. There was also no exploration in the examination in chief of the "quasi-rents" in relation to the fixed costs of entering the market which was advanced by Professor Szymanski in his report. We also felt that Professor Szymanski, when cross-examined by Mrs Brown, gave somewhat "on the hoof" responses to her questions about the "wear and tear" and "congestion" cost components which he had advanced were important elements in the make-up of marginal costs only in the hearing. We would have expected these issues to have been more fully addressed in his final report and in his oral evidence especially given the weight attached to marginal costs not only in Mr Trussler's report but also in Mrs Brown's Skeleton argument and the significant difference of opinion that there is between the experts.

The burden of showing unjust enrichment fell on HMRC. The clubs accepted that full repayment would unjustly enrich them. Having considered all the expert evidence, the judge decided that the extent of unjust enrichment for all the clubs would be 10%, "to take account of the fact that they would have incurred some costs in providing rounds of green fee golf to the additional number of visitors who would have turned up to play had the green fees been lower by the amount of VAT incorrectly imposed."

Other issues

The Tribunal examined in detail the evidence collected in respect of the other issues and came to the following summary conclusions:

(1) Other than in the case of tour operators or travel agents acting as agents and invoicing green fees directly to a golfer, supplies of green fee golf by the Clubs which are on-supplied to individuals by tour operators are subject to VAT at the standard rate.

(2) Where the customer of the Clubs is a body corporate, there is no distinction between a "corporate day" package, a supply to the body corporate, and the supply through a corporate body of access to play golf, with such a supply being subject to VAT at the standard rate.

(3) Course maintenance costs are properly treated as residual where the club has corporate day income, provides advertising services from locations on the golf course and has taxable income from the hire of golf buggies.

The Tribunal has therefore accepted HMRC's view that, even though it is always an individual who actually plays golf, payment by a body corporate or tour operator cannot benefit from the exemption because the supply is not to the individual who will participate.

The decision on course maintenance costs is fairly clear in relation to income from corporate days (because it is clearly taxable and clearly related to use of the course); HMRC might be less happy to accept that advertisements placed around tees and hire of buggies to drive on the course are sufficiently closely linked to the expenditure of maintaining the course, but the Tribunal was willing to see a connection.

First-Tier Tribunal (TC04774): *Berkshire Golf Club and others*

6.4.3 Repayment supplement

A trader in alcoholic and non-alcoholic drinks was subject to regular extended verification of its monthly returns because of the risk of MTIC fraud. The 02/13 return was submitted on 7 March, reclaiming £60,910. A meeting was held with HMRC on 19 March to discuss the information that should be provided to verify the claim; notes of the meeting record that HMRC asked the trader to provide AAD documents, and that the trader protested that these were held by the shipper, not the trader. The trader sent an e-mail on 21 March to confirm exactly what was required; HMRC responded by letter on 22 March; further correspondence followed, including the provision by the company of various items of evidence on 28 March. HMRC wrote back on 4 April stating that the information provided was not sufficient, for example because only photocopied documents had been provided.

The trader's representative responded, explaining that some supplies were indirect exports so the trader could not have the original shipping documents; others were subject to electronic recording where no hard copy was required or produced. In further correspondence, HMRC continued to ask for documents that the representative said the trader did not have and could not produce. Eventually, HMRC agreed to release the repayments on 10 May. The company claimed repayment supplement, which HMRC refused.

In the appellant's view, the "RS clock" stopped on 4 April when they received the letter stating that the information provided was not enough to validate the 02/13 return. Up to that, no specific queries had been raised about the return; the meeting and the correspondence had been about the continual monitoring in general, not about the particular claim. Also in the appellant's view, the clock should start running again on 8 or 10 May when their advisers provided the final piece of information which allowed HMRC to make a decision to repay. The repayment was not actually received until 21 May, so the total delay was well over 30 days.

HMRC's starting point was the receipt of the return on 7 March. They considered that the meeting on 19 March had included the raising of "a reasonable inquiry". They agreed that the information was provided on 8 May, but considered that the decision that they had received sufficient information was not taken until 10 May. They therefore would exclude the period from 19 March to 10 May from the RS clock. They said they issued instructions for payment to be made on 16 May; their "count" was therefore only 18 days (8/3 – 19/3; 11/5 – 16/5 inclusive).

The FTT heard evidence from the officer investigating and the director, and made various findings of fact about the significant dates:

- the first formal notification of HMRC's enquiries into the Appellant's 02/13 tax return was HMRC's letter of 27 March 2013, which was received by the director on 4 April;
- HMRC eventually accepted information other than that originally requested to support the VAT return;
- HMRC confirmed to the Appellant that it had received sufficient information about one aspect on 30 April and about the other aspect on 10 May.

The FTT stated that everyone was agreed that the clock started on 7 March with the receipt of the return by HMRC.

The stopping of the clock appears to depend on HMRC deciding to ask a question, rather than actually asking it (s.79(4)(a) VATA 1994 and reg.199 SI 1995/2518); however, the inquiry must be specific – a request for particular information that the trader can provide, rather than a general conclusion that "some extra information" is required. The FTT was satisfied that HMRC's letter of 22 March included requests for specific information; although it did not refer specifically to the 02/13 period, it was nevertheless written in response to the trader's letter of 21 March about that period's claim.

Although the trader did not explicitly include it in the grounds of appeal, the FTT considered that there was an implied suggestion that HMRC's inquiry was not "reasonable", and therefore the clock should not have stopped. The grounds for this included a change of HMRC officer leading to a requirement for information that had never previously been requested, and continued requests for documents in spite of explanations that they could not be provided. The FTT considered that this was unreasonable behaviour: HMRC's published policy in Notice 725 and Notice 197 confirmed that these documents should not have been considered relevant. The clock was therefore not stopped until 26 April, when HMRC agreed that alternative evidence could be provided. It would then restart when HMRC agreed that the alternative evidence was satisfactory.

The VATA and the Regulations are slightly inconsistent on the "restart date": the Act refers to the Commissioners being satisfied, and the Regulations refer to them receiving a complete answer to the inquiry. In either case, the FTT was satisfied that the conditions must have been satisfied on 9 May, because HMRC sent an e-mail to the trader timed at 09:49 on 10 May. The clock was therefore only stopped from 26 April to 9 May.

The regulations provide that RS will be due based on the date that a written instruction for repayment is issued by HMRC, not on the date on which the repayment reaches the trader. As the payment was received on Tuesday 21 May, normal banking time delays put the latest possible moment that the instruction could have been issued at Friday 17 May. The FTT concluded that this date should be used as the measure, even though HMRC produced ledger entries showing authorisation of the payment on 16 May. There was no evidence that an instruction had been given to the bank on that day.

In conclusion, the count of days should be 7 March to 25 April (inclusive) and 10 May to 17 May (inclusive) (i.e. including the dates on which the return was received and the authority to pay was issued, but excluding the dates on which the inquiry was raised and concluded). That was 58 days; repayment supplement was due.

First-Tier Tribunal (TC04678): *Marlico Ltd*

A farm partnership submitted its return for the quarter to 03/14 electronically on 1 April. It included a claim for a large amount of VAT incurred on the construction of a new poultry facility. An officer contacted the trader's accountants on 28 April to ask for additional supporting evidence. The accountant responded the same day by e-mail,

attaching various invoices to support the repayment claim. The officer replied on the same day, again by e-mail, stating that he was satisfied with the answers to his enquiries.

The decision to confirm the repayment had to be approved by a different officer. This was done the next day. A further electronic entry in HMRC's records on 1 May shows a further approval by a senior officer. This led to the issue of a repayment; HMRC's own systems added a 5% repayment supplement, recorded in HMRC's systems as authorised on 1 May.

The accountant e-mailed the HMRC officer on 8 May to say that the repayment had not been received. The officer responded that a payable order had been issued on 1 May, but HMRC did not have the trader's bank details on file so a BACS repayment was not possible. The accountant protested that HMRC had had the bank information for 30 years, and it had not changed. The cheque arrived in the post on 12 May and was banked on the same day.

HMRC then reviewed the situation and decided that repayment supplement had not been due. They raised an assessment on 8 August to ask for it back. The trader appealed.

HMRC argued that the day on which the inquiry was raised and answered had to be excluded from the count. 1 April to 1 May (inclusive) was 31 days; however, excluding 28 April meant that they had just issued the repayment in time.

The FTT agreed with HMRC. The "issue of a written instruction to pay" was the authorisation by the senior officer on 1 May. The date (and method) of receipt by the trader was not what the law referred to. Even though the inquiry took less than a whole day, the law does not take account of fractions of a day – the whole of that day had to be excluded from the count. It was therefore correct to calculate the delay between return and repayment as exactly 30 days.

The judge also commented that there appeared to be no requirement for HMRC to make repayments by BACS unless specifically authorised to do so. The fact that they might already have the bank details on their system did not provide that specific authorisation, nor did it create a legitimate expectation that BACS would be used.

The appeal was dismissed.

First-Tier Tribunal (TC04681): *Vogrie Farms*

6.4.4 Time limits

Leeds City Council made claims for repayment of output tax accounted for between 1974 and 2009 on a range of supplies which it argued should not have been subject to VAT. Two separate claims were made, one in May 2007 and the other on 27 March 2009. HMRC met the claims insofar as they related to periods ending on or before 4 December 1996, and for periods ending within 3 years before the dates of the claims; however, they refused to repay output tax for the intervening periods, ruling that the three-year cap on repayment claims was effective to deny repayment.

The Council appealed, arguing that the time limit should not apply. Its case was based on the assertion that the UK had failed properly to implement art.4(5) 6th Directive (now art.13 PVD), which regards local authorities and other government bodies as not taxable persons in respect of most of their public sector activities.

HMRC accepted that the article had not been implemented in the UK law, and also accepted that the Council's disputed supplies should all have been regarded as outside the scope (apart from some relating to parking). It was therefore agreed that the VAT should not have been paid in the first place. HMRC's only defence to repaying it was the operation and validity of the cap.

The Council's barrister argued that the way in which the cap had been introduced offended against the principles of effectiveness, proportionality, equivalence, legal certainty and the protection of legitimate expectations; the *Fleming* transitional period which ended on 31 March 2009 did not properly address those problems in relation to the overpayments of VAT in the periods under dispute, and the cap should be set aside until the UK implemented it properly. At the very least, questions should be referred to the CJEU to determine the matter.

On appeal in late 2013, the Upper Tribunal agreed with HMRC's representative that the manner of the cap's introduction was not relevant to the appeal. All the disputed claims related to periods after the cap was introduced by legislation; they did not relate to periods in which the time limit had been longer and was then arbitrarily reduced. It also made no difference that the Council was unaware that it was overpaying VAT, or that HMRC's published policy on the matter was wrong; that could be a common feature of s.80 claims in general.

The Tribunal examined the different EU principles which the cap was said to infringe, and found no significant breach of any of them. The appeal was dismissed.

The council appealed to the Court of Appeal. Lewison LJ summarised the history of the dispute, the different types of transaction affected, HMRC's changes of position in relation to them, and the background to capping and the *Fleming* window. He went on to confirm the reasoning of the Upper Tribunal in respect of claims for periods after July 1996: the council could not have had a legitimate expectation that an unlimited period would continue to be available to make claims, so no EU rights were infringed. A number of other points made by the council's representative were rejected, including the argument that HMRC should have given effect to a 2006 Scottish VAT Tribunal decision in *Scottish Equitable*, even though that was subsequently agreed to be incorrect.

A separate argument in relation to the principle of "equivalence" has more general application. The council argued that the difference between the time limit for reclaiming VAT (then 3 years, now 4) and reclaiming domestic taxes (generally 6 years) infringed this principle. The judges disagreed: the correct comparison was that made by the Court of Appeal in the *Littlewoods* case, between VAT claims based on EU rights and VAT claims based on domestic law. There was no requirement for equivalence between claims for different taxes.

The appeal was unanimously dismissed.

Court of Appeal: *Leeds City Council v HMRC*

A band, operating as a partnership, registered for VAT with effect from 1 June 2007, after exceeding the historical turnover threshold in the 12 months to April 2007. The VAT return for 02/09 was not submitted, so HMRC issued an estimated assessment for £7,875. The band were told by their accountant that VAT returns had been submitted; on finding out in late 2011 that this had not happened, the band instructed the accountant to calculate the 2009 liability and put the matter straight. She presented them with a calculation and the band made a payment, but in spite of her assurances, the returns for 2009 were still not filed.

Following further correspondence, the accountant finally filed the returns on 7 June 2013. The 02/09 return showed a liability of £893.20, considerably less than the estimated assessment. HMRC responded that it was too late to credit the overpayment to the account, because the four year time limit had passed.

The Tribunal cited and agreed with the precedent case of *Beds Beds Beds London Ltd*, in which Judge Sadler held that the time limit provided for no exceptions. The "relevant date" was the end of the accounting period in which the estimated assessment was raised; that was 05/09. The four year limit expired on 31 May 2013, and there was nothing that could be done to change that.

The accountant had originally agreed to give evidence on behalf of the band, but then proved reluctant to do so. It was therefore not possible to investigate her claim that the returns had in fact been filed. The judge had no alternative but to dismiss the appeal.

The judge commented that "we do appreciate that the Band would have been in a better position if the payment of £8,154 had not been made to HMRC on 27 October 2011 as the effect of s 80 is to prevent any credit being given for the difference of £6,981.80 between the estimated assessment and actual VAT liability for 02/09." This implies that the late filed return could cancel an outstanding liability, but could not lead to a repayment. As the time limit in s.80 refers to "overpaid tax", this surprising conclusion appears to be correct.

First-Tier Tribunal (TC04680): *The Holloways*

6.4.5 Article

In an article in *Taxation*, Neil Warren reviews procedures for correcting errors in returns, and the available statistics for the length of time HMRC are currently taking to process corrections. Their target is supposed to be 95% of VAT 652 forms dealt with in 15 days, but Neil believes that many are taking longer than a month. Using the reg.34 procedure to make a correction through the current VAT return is much quicker, as long as the monetary limits are satisfied.

Taxation 10 December 2015

6.5 Timing issues

Nothing to report.

6.6 Records

Nothing to report.

6.7 Assessments

6.7.1 Not to best judgement

An individual was assessed in relation to under-declared turnover for income tax, NIC and VAT. The income tax assessments were made under the "discovery" and "extended time limit" provisions for years from 2006/07 to 2010/11, and amounted to some £82,000; the VAT assessments covered the periods 04/06 to 10/12, amounting to £26,342 net (there were two credits as well as debits). There were also penalty assessments for deliberate and concealed conduct after April 2009 and conduct involving dishonesty (s.60) before that date, as well as income tax penalties.

The assessments were based on a "business economics exercise" carried out by HMRC using the VAT period 07/09 as a representative period. HMRC said that the exercise was necessary because the trader had destroyed till rolls and records of Z readings which meant that there was insufficient information on which he could rely to produce accurate tax returns.

The trader ran a fish and chip business with two outlets in Northern Ireland. A self-assessment enquiry was commenced in September 2009 into the 2007/08 income tax return, asking for full details of all the records. Various facts about the business were established at the commencement of the enquiry; the trader claimed that he recorded the cash in the till accurately, but destroyed the Z readings because they rarely reconciled. This had been his method of working for 30 years. He treated 2.5% of gross turnover as zero-rated (salads and baps), but had no till readings to justify this.

HMRC decided that the gross profit percentage in the accounts was too low. They issued revised calculations suggesting that over £580,000 had been diverted. The trader appointed a new adviser who conducted a long negotiation with HMRC, culminating in the issue of assessments against which the trader could appeal. The adviser produced a restated set of accounts for the year 2009/10 based on primary records, seeking to show that in fact the declared profits and turnover were correct. The gross profit percentage as calculated by him was 58% based on a year's records; HMRC's figure of 68% was based on only 3 months' records, and was less reliable.

The negotiations included giving HMRC a mandate to obtain copy invoices from all suppliers, to demonstrate that there were no separate purchases kept outside the books. The adviser raised the question "where is the money?" – the trader did not appear to have a lifestyle consistent with £10,000 a month of extra undeclared cash, and there was no evidence of money laundering.

The Tribunal examined HMRC's internal guidance about business economic and gross profit percentage exercises. Information obtained from a business consultancy and the Bank of Ireland was referred to, suggesting that the normal gross profit percentage for fast food outlets and restaurants was in the range 50% – 59.5%. Evidence was given on oath by the owner and his son, who managed the other shop; the former accountant and the present adviser; customers; and HMRC officers.

The grounds of appeal were summarised as follows:

i. The business economic model used by HMRC is arithmetically flawed and has been incorrectly applied. HMRC produced a mark-up exercise based on the 07/09 VAT return. In the first BEE in Nov 2010 the GP was 73% (GPR 277%), in August 2013 it became 68% (GPR 217%) and finally albeit provisionally, in September 2013, 64% (GPR 178%).

ii. The Appellant has supplied HMRC with the SRE and supporting data, based on the accounting year to May 2010 and using purchase invoices (a sample size of 89%), agreed unit sale prices, and agreed waste rates. A GP of 57% was arrived at. HMRC recognise this as being an accepted method of establishing a guidance to GP but the exercise has not been properly considered.

iii. HMRC have been offered evidence (information extracted from Companies House) showing the industry norms over the last 5 years. This indicates that the client is performing well in the industry. The industry average is 51%.

iv. The period used by HMRC in the exercise is not representative. HMRC used the VAT return for period ending 07/09. For the GPR exercise they claim that this period is representative without examining any other return. The return used represented only 22% of the recorded purchases in 2009-10 accounts. HMRC have always argued that this is a representative period but have been given extensive evidence and calculations to the contrary.

v. HMRC have not exercised best judgement. Evidence was submitted to disprove their assumptions but has been ignored. HMRC have withheld information in relation to their computations despite being repeatedly asked for it.

vi. HMRC have not followed their own published or internal guidelines.

The Tribunal concurred with most of these arguments. Although HMRC's assessments were not "spurious" or "capricious", and the whole exercise had been undertaken for good reasons (the unwise zeroing of the till, even after the trader was told not to do that), the assessments were not to best judgement. HMRC had not been able to fully explain the methodology underlying their calculations, or to respond to the various criticisms of their calculations.

The appeal was allowed. All the assessments and penalties were discharged.

First-Tier Tribunal (TC04703): *Ernest O Bustard*

6.7.2 No review, but upheld

A company appealed against an assessment for VAT and penalties covering a number of periods. HMRC had refused to carry out a review of the decision; at the hearing they accepted that this had been wrong, but the appellant did not make anything of that point in the appeal. The Tribunal centre suffered a power-cut, making it impossible to receive evidence from an HMRC witness by video link, but the Tribunal decided that this was not necessary. Various matters were agreed between the parties, leaving just one item outstanding: the VAT liability for the 07/11 period.

The company had changed from cash accounting to invoice accounting. The records were confusing, and it was difficult to establish when this change had taken place or whether it had been correctly dealt with. The officer considered that the management accounts for 07/11 showed that the true output tax on an invoice basis was £26,000 more than that shown on the VAT return.

The company claimed that it had moved from cash accounting to invoice accounting in April 2011. The 07/11 period included various invoices on which cash had been received earlier, or income had been accounted for earlier as work in progress, and including these items on the VAT return would involve double counting.

The Tribunal considered that the appellant had not provided sufficient explanations or evidence to show that the disputed items were double counted. It seems strange that the company should argue that “debtors should be excluded because cash had already been received from them in earlier periods” – if so, they would not be debtors. This point was not made by the judge, but she concluded that the company had not discharged its burden of displacing the HMRC assessments. The appeal was dismissed.

First-Tier Tribunal (TC04764): *Avenir Business Solutions Ltd*

6.8 *Penalties and appeals*

6.8.1 Default surcharge

In TC02873, a trader appealed against a surcharge of £1,900 for the period 05/12, levied at 5%, on the basis that it was 'unfair'. The FTT noted that, following the decision of the Upper Tribunal in *Total Technology*, it could not cancel the surcharge on this ground. It was noted that the correspondence showed that the appellant also referred to cash flow problems caused by delays in payment from customers who were public bodies; if the appellant had come to the Tribunal to give evidence, it might have explored the possibility of allowing a reasonable excuse because the circumstances might have been similar to those in *Steptoe*. As the trader did not appear and was not represented, this was not possible; there was no reasonable excuse, and the appeal was dismissed.

However, the judge suggested that HMRC might still reconsider the surcharge – they could yet contact the appellant and find out in more detail how the cash flow had been affected by late payments from NHS and other public body customers. That decision was handed down in September 2013, but the trader later claimed to have been unaware of the hearing or of the decision.

The company incurred further surcharges, and in TC04229 (January 2015), the director appealed against a series of these totalling £8,640. As a preliminary matter, the Tribunal considered the company's protest about the earlier decision. The director had not attended that hearing and said that he was unaware of the decision; the business had moved, and some items of post had gone astray. The judge said that he could only pursue that appeal by applying to the Upper Tribunal, but would have to explain the reasons for being late with the application.

Turning to the later periods, the Tribunal considered the trader's reliance on the *Steptoe* defence. The company's major customer was the NHS, which was often late paying. If he created too much fuss, he ran the risk of being dropped as a supplier. The company had also been pressured into buying an interest-rate hedging product by its bank, which turned out to be a financial disaster – compensation negotiations were still in progress, but the bank's offer of £265,000 was considered inadequate. The bank had unexpectedly reduced the company's overdraft facility from £150,000 to £110,000.

The FTT accepted that this combination of factors constituted a reasonable excuse for the lateness in the periods to 08/12 and 11/12. As the trader then managed to submit three returns and payments on time, and no further explanations had been offered for the period 11/13 which was late, the appeal was dismissed in respect of that period. However, that would in the circumstances only lead to the issue of a SLN and not a penalty, because there would have been five periods without a default.

The first decision was appealed to the Upper Tribunal, late but with the permission of the Tribunal, in March 2015. The case came before the Upper Tribunal (J Gordon Reid) in November 2015. Following submissions by the appellant, HMRC asked for a brief adjournment to consider the matter, and came back with a proposal for a settlement. The judge issued directions for the appellant to provide certain evidence to be

considered by HMRC (and, if necessary, the FTT again) within 30 days. This included a medical certificate confirming his health problems in 2012, and documents relating to dealings between the company and the Royal Bank of Scotland, including claims for compensation arising out of the sale of an interest rate hedging product, in spring and summer 2012. Presumably HMRC have indicated that they will accept these matters as constituting a reasonable excuse, provided that there is some evidence of the facts.

Upper Tribunal: *Robert P Slight & Sons Ltd v HMRC*

A company appealed against a £4,550 surcharge at 5% for its 04/14 period. It had paid the liability 3 days late. The money should have been in HMRC's account on Friday 6 June; it did not arrive until Monday 9 June.

The company claimed that it had authorised the payment on 6 June and expected it to be made the same day. However, documentary evidence showed a value date of 9 June. It did not appear that the bank had acted contrary to the company's instructions. The claim of disproportionality could not succeed. The appeal was dismissed.

First-Tier Tribunal (TC04660): *C A Support Services Ltd*

A trader sought to appeal against surcharges for many years together, from 04/04 to 10/07. Various disasters had occurred during the period, and these were offered as reasonable excuses; the appellant had been made bankrupt by HMRC in November 2007 for non-payment of VAT and surcharges. The bankruptcy was finally annulled in July 2014; HMRC objected to this in September 2014, referring in a witness statement to some of the surcharges from 2006/07.

The trader argued that he could not appeal against the surcharges while he was bankrupt; he did so as soon as the judge had set aside HMRC's objection to the annulment and he believed he once again had standing in the matter. He also claimed that he had not received the surcharge notices at the time, although the evidence suggested that he had. HMRC objected to his appeal being heard out of time.

The Tribunal considered the various reasons for delay put forward and decided that they were not good enough to allow such a late appeal. The trader had suffered disruption, but he could have appealed at various stages much earlier. He could also only succeed if he were permitted to amend his grounds of appeal against the surcharges, and the judge would not have accepted such an application either. The application for leave to appeal out of time was refused.

First-Tier Tribunal (TC04661): *Peter Antony Farrington*

A trader appealed against a surcharge of £142.36 for the period 01/15. This was levied at 10% after he had been late in 07/13, 10/13 and 10/14. He argued that HMRC should have sent him a reminder that his VAT was due; the judge considered that this fell short of being a reasonable excuse, given that he had received three surcharge liability notices and a trader is supposed to be aware of his quarter ends.

First-Tier Tribunal (TC04685): *Mark Heaney*

A company appealed against a 10% surcharge of £358 for period 08/14. The appeal was based on unfairness and on the assertion that "*their return was submitted by an 'alternative organisation'. The Appellant did not have a record of the date the money was due to leave their account. They explained that they had spoken to the bank and there were insufficient funds at the time to make the payment.*" It is not clear what the "alternative organisation" could be, but it clearly was not a reasonable excuse, and the appeal was dismissed.

First-Tier Tribunal (TC04695): *G Robertson Consulting Ltd*

A company appealed against a 15% surcharge of £1,950 for period 08/14. They argued that the penalty was disproportionate for being two days late (could not succeed); that their accountant had told them the payment was due by the 9th, not the 7th (HMRC pointed out that they had confirmed in a letter in 2013 that payment was due by the 7th); and that they had been assured during a visit that there were no surcharges to pay. The Tribunal noted that the company had a long history of disputes with HMRC and felt badly served, but it would have to make a separate complaint about that: the surcharge was properly issued and the appeal was dismissed.

First-Tier Tribunal (TC04696): *SCS Logistics Ltd*

A company appealed against a 5% surcharge of £546 for period 11/14. It argued that the payment was only a day late, and this had been because the administrator was ill on the due date. She had dealt with it as soon as she returned to work. The main reason, though, was poor cash flow.

Strangely, the decision makes no reference to the illness of the administrator. It simply rules out unfairness and insufficiency of funds as defences, and points out that the company had been in the surcharge regime long enough (since 11/13) to appreciate the consequences of another default. HMRC pointed out that a TTP arrangement would have avoided the surcharge.

First-Tier Tribunal (TC04707): *Jobec UK Ltd*

A partnership appealed against a 10% surcharge of £481.82 for the 02/15 period. The appellants claimed that they had paid using Faster Payments, but that a bank holiday around the due date had led to the majority of their payment being one day late. They also suggested that they had been waiting for funds to arrive, which was possibly contradictory; as this was a paper case, the judge could not obtain any further explanation of what exactly had happened.

Shortage of funds could not be an excuse; disproportionality could not be a defence; the payment was admittedly late and the surcharge was correctly calculated. The appeal was dismissed.

First-Tier Tribunal (TC04715): *RS & LR Lloyd t/a Sitting Rooms*

A company appealed against a 10% surcharge of £261.47 for its 01/15 period. The return was filed on time but the payment was only received by HMRC on 12 March. The appeal appeared to be based on shortage of funds following a downturn in trade; this could not succeed.

As the appellant is a charity selling mainly books and magazines, it is perhaps surprising that it had that large an output tax liability. However, it also sold stationery, which must have led to the VAT charge.

First-Tier Tribunal (TC04716): *Manna Christian Centre Ltd*

A company appealed against a 5% surcharge of £972.11 for its period 12/14. The company had been registered for VAT since 1 April 1973, but had sold the business on 31 December 2014. This meant that all the debt and work in progress was crystallised at that point, and the VAT liability for the period was artificially inflated. After that date the company had no employees, and the sole director was taken ill. The company had always paid its VAT on time, but was on this occasion 13 days late.

HMRC argued that this was a combination of "shortage of funds" and "reliance on another" (because there were no employees). The judge agreed that the company had not established any unforeseen or uncontrollable circumstances that might amount to a reasonable excuse. There was no doubt about the good compliance history of the company or the director's intention to do the right thing, but the appeal had to fail.

First-Tier Tribunal (TC04717): *ETB (214) Ltd*

An individual appealed against a 10% surcharge of £1,298.75 for his 02/15 period. The bulk of the VAT for the period was paid one day late. The trader was a solicitor who was heavily reliant on legal aid work. A payment was normally received on the first Monday of every month, but in that month this was a Bank Holiday; payment would then normally have arrived on Tuesday 7 April, the same day that the VAT was due, but in fact it was received on Wednesday 8 April. The solicitor had paid £2,500 in VAT before the due date, but could only afford to pay the balance of £13,000 when the legal aid funds came in.

The judge noted that this appeared at first sight to fall within the principles of the *Steptoe* case. However, the Legal Aid Board had notified all solicitors some months in advance that this payment would arrive on Wednesday 8 April; it was not therefore an unexpected late payment. The solicitor had done nothing about the anticipated cash flow difficulty. He said he was unaware that Time To Pay could be agreed, and in any case did not think that HMRC would be sympathetic as he had a history of other defaults.

In the circumstances, the judge did not accept that there was a reasonable excuse. Proportionality and fairness could not assist the trader, and the judge had no power to meet a request to shorten the surcharge liability period that would be extended for 12 months after the default.

First-Tier Tribunal (TC04729): *David Fish*

A company appealed against a 5% surcharge of £1,320 for 10/14. It appeared to have fallen into the surcharge regime because of due dates falling on a weekend or bank holiday, following which it paid on the next working day. Its appeal was essentially based only on hardship, which could not succeed.

First-Tier Tribunal (TC04736): *Groundwork (Terrocotta and Stone) Ltd*

A company appealed against a 15% surcharge of £1,199 for 02/15. The company had suffered a break-in on 8 March 2015, losing cash and

paperwork and suffering damage. An insurance claim was received after the due date for this VAT liability. The theft and the need to carry out emergency repairs caused a cash flow problem. The trader had hoped to be able to pay the VAT on time, but a heatwave just before the due date caused a slump in receipts (the company ran an indoor soft play centre for children). Nevertheless, £5,000 of the liability had been initiated using Faster Payments at 1100 on the due date (but had arrived the following day); the balance of £2,933 was paid the following day.

HMRC argued that the theft occurring a month before the due date did not constitute an excuse. The business received takings in cash, so the VAT should be available when it was due. The amount stolen was only 10% of the VAT outputs for the period. The main issue, perhaps, was that HMRC had allowed two previous appeals against surcharges, and had informed the taxpayer that any further problems should be referred immediately to the Business Payment Support Service without delay.

The FTT examined the three different statements of the judges in the *Steptoe* case – the dissenting judgment of Scott LJ, who thought that the underlying reason for a shortage of funds had to be an unforeseeable and inescapable event; and the different interpretations of Nolan LJ and Lord Donaldson, who decided that an inescapable cash flow problem could be a reasonable excuse, without it necessarily being unforeseeable (Lord Donaldson commented that foreseeability was relevant because it is more difficult to escape from the unforeseeable than the foreseeable.")

The Tribunal considered that the combination of the break-in, followed by the drop in takings, together constituted a reasonable excuse. The trader appeared to have acted reasonably in trying to meet his obligations, and it was not unreasonable to have believed that the takings would have enabled him to do so. It was also not unreasonable for him not to have asked for Time To Pay, given that there was no guarantee that it would be granted.

A separate argument about proportionality was rejected, but the appeal was allowed.

First-Tier Tribunal (TC04741): *Farmyard Funworld Ltd*

A company appealed against three default surcharges of £2,962, £3,588 and £3,582 for the periods 03/14, 06/14 and 09/14. Its main argument was that it had sought to offset Construction Industry Scheme repayments due to the company against its VAT liabilities, and HMRC had failed to do this promptly. The judge examined the history of correspondence between HMRC and the taxpayer. It appeared that the taxpayer had relied on an alleged statement by a junior PAYE officer that such an offset would be possible, when HMRC had repeatedly written to explain that CIS repayments would only be made after the end of the tax year. The company had arranged Time To Pay in the past, but did not do so in relation to these periods. The judge had some sympathy with the company and its representatives with regard to confusing replies received from different HMRC departments, but did not accept that they had acted reasonably in relation to the attempted offset of repayments against VAT debt. The appeal was dismissed.

First-Tier Tribunal (TC04742): *Quality Asbestos Services Ltd*

A company appealed against a 15% surcharge of £438 for 09/14. It had been in the surcharge regime since 06/11, paying through Faster Payments each quarter. The judge reviewed the history of late payments. The appeal was effectively based on hardship: the company was already paying off arrears to HMRC under a TTP agreement, and was having difficulty collecting receipts from customers. This could not be a reasonable excuse on its own, and the appeal was dismissed.

First-Tier Tribunal (TC04751): *Bix Ecotech Ltd*

A trader was charged a surcharge of £395 at 15% for his 01/11 period. He had been in the surcharge regime from 10/06 onwards, and had defaulted in fifteen periods in total. He had paid his VAT by cheque after the due date, when it should have been paid online in order to benefit from the 7-day extension. His defence was effectively the "unfairness" of the penalty, when he had recently taken over the business and cleared a VAT debt built up by his father.

The Tribunal did not consider that he had any reasonable excuse.

First-Tier Tribunal (TC04752): *Nasir Asghar t/a The Fashion Spot*

A company appealed against a 2% surcharge of £469 for 10/14 and a 5% surcharge of £1,431 for 01/15. The company had benefited from Time To Pay for a number of periods, but this was refused on 5 December 2014 on the grounds that the company was a consistent late payer. The company had cash flow problems, claimed to be due to late payment of bills by a client; HMRC responded that it was not using the cash accounting scheme, which would have benefited it. The 01/15 liability was paid late on a Monday, the first working day after the due date; HMRC said this was not a mistake that could be accepted as "reasonable".

The Tribunal agreed with HMRC that the company had not taken appropriate steps to deal with its problems, and did not have a reasonable excuse. The appeals were both dismissed.

First-Tier Tribunal (TC04761): *TS & B Contractors Ltd*

A landlord appealed against default surcharges of £220 levied at 10% and £330 at 15% for the periods 12/11 and 03/12. Earlier late payments had not attracted surcharges because they were below £400. The taxpayer did not attend the hearing; he appeared not to have understood the earlier notices, believing that his first surcharge had been levied at 10%; his excuse was that the tenant was consistently late paying the rent, and without that receipt he could not afford to pay the VAT. None of this could constitute a reasonable excuse.

First-Tier Tribunal (TC04766): *Vincenzo Marino*

A trader appealed against surcharges for periods 07/14 and 10/14. He had been within the regime since 11/10 and had been paying at 15% since 01/12. The appellant's payments were collected by direct debit. He did not appear to realise that he had submitted his 07/14 return late (on 9 September) because the online system did not tell him so at the time; as a result, the payment was collected late. The return for 10/14 was filed "a few hours late" on 8 December, but it was still late, leading again to late payment, and both appeals had to be dismissed.

First-Tier Tribunal (TC04767): *Anthony Joseph Hawkes*

A company appealed against surcharges for the three periods 09/11, 12/11 and 03/12 totalling £16,592.79. Time To Pay had been used in the past, but was not applied for in respect of 06/11 (when a surcharge was incurred) or in 09/11, and was applied for and refused in respect of 12/11 and 03/12. The company referred in its notice of appeal to a flood that had occurred on 23 May 2012 as causing it considerable problems, but this post-dated the periods and could not therefore be relevant to the appeal.

The company blamed slow payment by its major customer, and pleaded that it was in the same position as *Steptoe*. The judge could not accept this. The customer accounted for 45% of turnover, not the preponderant proportion of the earlier case; and the company did appear to have cash resources. The appeal was dismissed.

First-Tier Tribunal (TC04793): *Social Care 4U Ltd*

6.8.2 Deliberate, not concealed

A trader was charged a penalty at a rate of 47.25% in respect of a claim to input tax on three vehicles. He originally claimed that they were intended to be used in a chauffeuring business. HMRC said that they have not been provided with any evidence of such an intention, the cars were never used for a chauffeur business and in fact had been used for private purposes. The trader accepted that his returns were wrong and that the assessment was correct; he disputed the categorisation of his behaviour as “deliberate”.

The input tax claim was subject to a verification visit. The vehicles were parked in the drive of the trader’s house. He had no evidence of the business diversification for which he claimed he had bought the cars – no website, no advertising, no suitable insurance documentation. At a subsequent visit, the trader acknowledged that he did not have the documentation and he was happy to withdraw the claim to the input tax. As he had been told at an earlier visit about the rules for claiming input tax on cars, the officer decided that continuing to claim VAT to which he was not entitled constituted “deliberate behaviour” with a prompted disclosure, and raised a penalty accordingly. Mitigation was allowed for telling (15% out of 30%), helping (20% out of 40%) and giving (the full 30% for access to the records), so the penalty was charged at 70% minus 65% of 35% = 47.25%.

There was an additional problem in that one of the cars was purchased second-hand, without a proper VAT invoice. HMRC confirmed the penalty decision on review, and the trader appealed.

The Tribunal considered the trader’s argument that he had had a genuine intention to start a chauffeur-driven hire business, but that he had abandoned it because his father fell ill and he had been too busy with other matters. He produced a letter from a barrister with whom he claimed to have discussed the idea in 2011. He said that it was very hard to prove an intention.

The judge held that an intention was not enough in any case to justify the claim. The lack of appropriate insurance at the time of purchase made it difficult to support a firm intention to start the new business. In view of

all the circumstances, the category of penalty and the level of mitigation were appropriate. The appeal was dismissed.

First-Tier Tribunal (TC04699): *Ram Narroya*

6.8.3 Dishonesty penalty

An individual was assessed to a penalty of £3.1m under s.61 VATA 1994 in respect of VAT losses connected to a company of which he was a director. The underlying alleged fraud was a contra-trading operation carried on in period 04/06; the amount the company sought to evade was £6.97m.

The appeal commenced with an application by the appellant for the judge to "recuse herself" from the appeal, based on her involvement in various directions hearings before the substantive appeal. She refused, and proceeded with the main hearing. This followed the usual course of MTIC appeals, with the added element of considering whether the conduct involved dishonesty and that was attributable in particular to the individual director. There was a wide range of legal objections to the imposition of the penalty, all of which were rebutted in turn. The judge concluded that the penalty met the statutory criteria, and dismissed the appeal.

First-Tier Tribunal (TC04668): *Umaad Butt*

6.8.4 Information notices

An individual and a company were served with information notices by HMRC, and subsequently issued with penalties for failing to respond. Their tax agents appealed, claiming that the information had been supplied; neither taxpayer nor agent attended the hearing, at which the Tribunal concluded that the responses provided by the agent did not fulfil the requirements of the notices, and could not constitute either compliance or a reasonable excuse. The appeals were dismissed.

First-Tier Tribunal (TC04787): *Tan Cars Ltd and another*

An individual who used the same tax agents as the above appellants also appealed against an information notice penalty. The arguments were similar: the agents argued that HMRC already had all the relevant information, while HMRC said that the questions on the notice had to be answered. The Tribunal agreed with HMRC and confirmed the penalty.

First-Tier Tribunal (TC04776): *Muhammad Mahood Saify*

6.8.5 Application for strike-out

A company appealed against assessments relating to a salary sacrifice scheme it operated for its staff. HMRC demanded output tax on the basis that it was making supplies to them for consideration. The company sought to amend its grounds of appeal, and HMRC applied to have some paragraphs of these amended grounds struck out on the basis that either the Tribunal had no jurisdiction to hear an appeal on these grounds, or else that they stood no reasonable prospect of success.

The judge considered the arguments in principle, taking care not to prejudge the case itself. The main points put forward by the taxpayer were that HMRC had made public announcements to the effect that salary

sacrifice schemes would not be subject to VAT before 1 December 2012 (*R&C Brief 28/2011*), and had given specific assurances to the company that it did not have a liability. Its grounds were therefore in the area of legitimate expectations. HMRC argued that this could not succeed in the FTT because of the *Noor* decision, so the grounds should be struck out in order to save time at the main hearing.

The judge (Peter Kempster) examined the arguments and precedents, and concluded that the matter was not so clear that he would be justified in restricting the appellant's grounds of appeal. The decision of the Upper Tribunal in *Noor* was expressed in cautious language; it was possible that it would not apply universally. HMRC would no doubt challenge the factual basis of the grounds of appeal in the substantive hearing, but that was the proper course to follow. HMRC's application to strike out those grounds was refused.

First-Tier Tribunal (TC04670): *Pertemps Ltd*

An individual appealed in March 2015 against several assessments to VAT and income tax from 2007 and 2008. HMRC applied for the appeals to be struck out on the grounds that they were very late. The judge reviewed the history of the dispute and noted that HMRC had pointed out at several times that they had no record of receiving any appeal, and formal appeals were required to be made within time limits. The trader or his representatives might have taken this up in response to correspondence in 2008 or 2011 or 2012, but did not do so until 2015. There was no good reason for such an excessive delay, and the appeals were struck out.

First-Tier Tribunal (TC04662): *Alan Batson*

A VAT group had a VAT debt of about £300,000. The representative member was in administration, so HMRC declared that seven members of the group were jointly and severally liable for the tax. The companies appealed, claiming that they were not part of a group registration with the representative member and were therefore not liable for the tax. HMRC applied for the appeals to be struck out on the grounds that this was not a matter appealable within s.83 VATA 1994.

A director appeared on behalf of the appellants. He claimed that the purported group registration had been applied for by an individual who did not have the authority of the directors. He argued that the matter was within s.83(1)(a), as it related to the registration or deregistration of persons under the VATA.

HMRC pointed out that the group registration had taken effect in 2014 and the companies had dealt with their VAT affairs on that basis since then. They had not objected to their inclusion in the group until HMRC had sought to enforce the liability; two companies that had previously been separately registered had had their individual registrations cancelled at that time. Group VAT registration was subject to specific provisions in s.83(1)(k) and (ka), and the separate registration of members of a VAT group was not covered by s.83(1).

The judge reviewed precedents about the construction of rights of appeal, where an omission might be regarded as anomalous or might reflect the intention of Parliament. He concluded that the appeals were not really within s.83(1)(a) – the registration and deregistration of the companies that had been included in the VAT group had taken place in 2014 and had

not been appealed against at the time, and any appeal on that basis would now be late. In reality, they were seeking to object to the joint and several liability that followed on from inclusion in the grouping; to do so by way of s.83(1)(a) would be to bring an appeal "by the back door". It seemed more likely that Parliament had intentionally restricted the appeals about grouping to the matters set out in s.83(1)(k) and (ka). HMRC's application for strike-out was granted.

First-Tier Tribunal (TC04768): *Eco Energy Sales Ltd and others*

6.8.6 Application for postponement

An appellant received notice from HMRC that they had applied to the Tribunal for postponement of an interim hearing. He therefore told his adviser that he did not need to attend. He then discovered that HMRC's application had been refused by the Tribunal, so he applied for postponement himself. The Tribunal refused this as well, holding that it was in the interests of justice to make progress in what was a long outstanding matter.

The appeal itself clearly relates to a MTIC case. Judge Mosedale made a number of directions about case management and gave the trader specific deadlines for responding to a number of points for the progress of the appeal.

First-Tier Tribunal (TC04669): *First Class Communications Ltd*

6.8.7 Costs

HMRC imposed a "careless error" penalty under Sch.24 FA 2007 on a company in respect of its VAT return for the period to 11/13. The company appealed; HMRC withdrew the penalty the day before the hearing, after receiving an amended VAT account for the period from the company's representatives.

The company applied for costs on the basis that HMRC's behaviour was unreasonable. Although it was not represented at the costs hearing, its representative sent an explanation to be considered by the Tribunal, asserting that HMRC had had all the relevant information much earlier and should have accepted that there was a "genuine mistake" that should not have been penalised.

The judge reviewed the background to the dispute. It related to supplies made to a connected company on which no output tax had been included in the VAT return. Five such invoices had been discovered on a visit; an assessment was raised and settled, and HMRC then issued the penalty (for £4,685).

The company appealed, arguing that "no tax advantage would have been gained", and that the penalties were "grossly disproportionate". The schedule provided the day before the hearing showed that input tax and output tax had both been omitted from the return: as there was no "potential lost revenue", the penalty was cancelled.

The judge considered that the explanations given by the company in response to the penalty assessment were not sufficient on their own for HMRC to appreciate that there was no potential lost revenue. That was only clearly established when the schedule was provided. HMRC had

therefore not acted unreasonably in only dropping the matter at the last minute. The application for costs was dismissed.

First-Tier Tribunal (TC04640): *Executive Car Rentals Ltd*

Judge John Clark had to consider the rules for costs in transitional cases in a complex procedural dispute arising out of a missing trader assessment. His directions mainly accepted HMRC's proposals for the management of the case.

First-Tier Tribunal (TC04647): *Just Beer Ltd and another*

HMRC applied for costs totalling £1,834.80 on the grounds that a company had acted unreasonably in relation to an appeal. The application was made in June but only reached a judge in November, due to a Tribunal administrative mix-up for which the judge apologised to the parties.

The company had made an appeal against a decision that its self-storage services were subject to output tax. That appeal was stood over behind the *Hanbridge* case. When the Upper Tribunal decided that case in favour of HMRC in July 2014, HMRC applied to the Tribunal to relist this case. The Tribunal wrote to the company's representative to ask if he had any objection to that, and received no reply. On 8 January 2015, the Tribunal made a direction to the effect that the appeal was no longer stayed, requiring the company to confirm whether it wished to pursue the appeal, and if so to file amended grounds of appeal taking the *Hanbridge* decision into account. The representative responded to this, saying that he was no longer in contact with the company or its accountants.

The Tribunal then listed a hearing for 10 April with a view to striking out the appeal. This led to a response from a firm acting for the company (but not validly appointed to represent it under rule 11 of the Tribunals rules). The firm said that the company had no record of receiving any papers in relation to the appeal, and asked for copies.

The Tribunal sent a letter to the company stating that it would have to fill in a form to appoint the firm to represent it. This was received by the Tribunal central administration in Birmingham on 20 March. At that time, the administration of London cases was being relocated to Birmingham. On 10 April, no one from the company turned up at the hearing. The Tribunal centre contacted the firm, which stated that the company had withdrawn its appeal. A letter to this effect had been sent dated 1 April, but it only reached Birmingham on 13 April; the form authorising the firm to represent the company had not yet shown up on the Tribunal's system. In the circumstances, the Tribunal decided that it could not strike out the appeal because the January direction had not been an "unless" order, and there seemed to be a relevant difference in the facts of this case and *Hanbridge* (the original grounds of appeal stated that the storage units were fixed to the ground). An unless order was issued requiring the company either to withdraw the appeal formally, or to set out its revised position following *Hanbridge*.

HMRC subsequently applied for costs, claiming that the company's failure to deal with its appeal in an efficient manner had involved HMRC in additional expenses, in particular attending the hearing on 10 April when that was unnecessary.

The judge considered that there were three possible areas in which the company could be argued to have acted unreasonably:

(1) By failing to comply with correspondence, and directions, from the Tribunal requiring it to set out its position on *Hanbidge*.

(2) By failing to withdraw its appeal earlier than it did.

(3) By failing to notify HMRC and the Tribunal of withdrawal in sufficient time to save HMRC the costs of attending, and preparing for, the hearing on 10 April 2015.

The judge agreed that all three aspects showed unreasonable conduct. It was not possible to be sure whether the failure to respond to the *Hanbridge* decision was the fault of the company or its previous representative; however, as the appeal was stayed behind that case, the publication of that decision should have alerted them to the need to consider their position. As the new representative withdrew the appeal because it agreed that the decision determined the matter, the company should have come to that conclusion earlier. It did not matter whether the failure was the company's or the representative's – either could lead to an award of costs against the company.

Lastly, posting a letter withdrawing an appeal just 9 days before a hearing date, when the Easter weekend shortened the number of working days in the meantime, was an unreasonably slow means of communication in the circumstances. Although it was unusual to award costs to an unsuccessful applicant, and the Tribunal had decided not to strike out the appeal, the Tribunal itself had called for the 10 April hearing – HMRC were obliged to attend and make representations.

The judge confirmed that costs would be awarded, but reduced the amount of the claim in respect of the in-house solicitors' expenses. The total awarded was £1,626.90.

First-Tier Tribunal (TC04712): *Tor View Self Storage Ltd*

6.8.8 Late appeals

A trader lodged a notice of appeal on 29 October 2014 in respect of an assessment raised on 17 August 2011 for the period 05/2011. The assessment charged output tax of £26,806; it appeared from argument in the Tribunal that the appellant did not really dispute the output tax, but rather the disallowance of some input tax in the same period. The trader was engaged in the business of buying iPhones and iPads from retailers and selling them on; this is a common source of dispute about the allowability of input tax.

The judge could see no good reason for the appellant's failure to lodge an appeal when the assessment was first issued, or a year later after changing advisers. In correspondence with HMRC, the new advisers had been repeatedly told that the assessment would not be withdrawn, and reminded that any application to appeal would already require the permission of the Tribunal to proceed. The application to appeal out of time was refused.

First-Tier Tribunal (TC04711): *Mohammad Javid*

A trader appealed against a decision by HMRC to refuse £360,000 of input tax claimed between 02/07 and 05/08. The trader had produced no

purchase invoices or other evidence to support the claims. The Tribunal dismissed the appeal in a decision released on 29 August 2012. On 9 February 2015, the appellant applied for leave to appeal out of time against that decision. An earlier attempt to appeal out of time had been rejected by the Tribunal in May 2013. The appellant said that he had suffered injuries in a helicopter crash on 23 July 2008, and was only now able properly to participate in the appeals process. It had been contrary to justice to proceed with the original hearing in his absence, in the circumstances of his injuries.

The Tribunal reviewed the history of the appeals and the appellant's continual failures to meet deadlines or engage with the process. Although the description of the accident suggests it was very serious, the Tribunal noted that the appellant was able to carry on a number of activities that indicated he could have entered into the appeal in accordance with the statutory deadlines. The application was refused.

First-Tier Tribunal (TC04792): *David James Cummaford and Abcoma Ltd*

6.8.9 Categorisation of appeals

HMRC refused a deduction of £226,846 of input tax claimed by a company for the accounting periods 09/09 to 03/10. On receipt of the Trib 1, the Tribunal allocated the appeal to the "standard" category. The company applied to have it recategorised as "complex".

Judge Sinfield set out the factual background for the purposes of the application hearing only. The input tax was incurred on invoices raised by a subcontractor in relation to the supply of labour. The subcontractor went into liquidation, and subsequently issued credit notes to the company on the grounds that no supplies had taken place. It seems that the company had paid the original invoices, and will not recover in full the amounts shown on the credit notes because the supplier is insolvent.

The judge considered that the issues for the substantive hearing were simply whether the company was entitled to deduct the input tax. HMRC had two grounds to deny it: either there were no supplies, or the evidence was inadequate and it was reasonable for them to refuse to accept alternative evidence. HMRC did not allege involvement in any fraud.

Complex cases are covered by rule 23(4) of the Tribunals Rules. The Tribunal will only categorise a case as complex if it considers that it:

(a) will require lengthy or complex evidence or a lengthy hearing;

(b) involves a complex or important principle or issue; or

(c) involves a large financial sum.

The parties had agreed that six days should be provided for the hearing. Also the judge agreed with the company that this was unusually long for an input tax hearing, he did not consider that it was so out of the ordinary that it satisfied criterion (a).

The company further argued that the status of credit notes and the jurisdiction of the Tribunal in relation to HMRC imposing additional evidential requirements on traders after the event were both important points of principle. The judge accepted that they were important, but did not agree that they were complicated: the Court of Appeal's judgment in

the *Brunel* case appeared to provide strong support for the company's position on credit notes. Criterion (b) was therefore not satisfied.

The company argued that the VAT assessment on its own was a significant sum, and HMRC had also raised a corporation tax assessment for £602,000 on the grounds that the supplies had not taken place and the company had therefore overstated its deductions. The judge commented that the CT assessment was not the subject of this appeal and could not be relevant. Although there appeared to be no statistics on the median values of appeals to the Tribunal, the judge did not consider £227,000 to be a "large sum".

The judge therefore concluded that the case did not satisfy any of the criteria to be categorised as complex and dismissed the company's application.

First-Tier Tribunal (TC04641): *JSM Construction Ltd*

6.9 Other administration issues

6.9.1 Consultation on withdrawal of extra-statutory concessions

HMRC are consulting until 27 January 2016 on the proposed withdrawal of nine extra-statutory concessions with effect from April 2017. Of these concessions, four relate to income and corporation tax, four to VAT and one to excise duty.

The four VAT concessions are:

- Para 9.8 Notice 708 – Apportionment of works of approved alterations to a qualifying protected building
- 3.23 VAT: supplies by Financial Ombudsman Services Ltd to ombudsman authorities
- 3.28 VAT: supplies by Financial Services Authority to self-regulating organisations
- 3.31 VAT: supplies by Financial Services Compensation Scheme Ltd to compensation scheme authorities

The first is no longer of relevance as the transitional period for withdrawal of zero-rating on approved alterations has finished; the other three are of very limited application.

www.gov.uk/government/consultations/withdrawal-of-extra-statutory-concessions-2015

6.9.2 Compliance factsheets

HMRC have issued new versions of a number of compliance check factsheets:

CC/FS1a – General information about compliance checks

CC/FS1b – General information about checks by compliance centres

CC/FS1c – Compliance checks: large and complex businesses

CC/FS3 – Compliance checks: visits by agreement or advance notice

CC/FS7a – Compliance checks: penalties for inaccuracies in returns or documents

CC/FS7b – Compliance checks: penalties for not telling HMRC about an under-assessment

CC/FS9 – Compliance checks: Human Rights Act and penalties

CC/FS10 – Compliance checks: suspending penalties for careless inaccuracies in returns or documents

CC/FS11 – Compliance checks: Compliance checks: penalties for failure to notify

CC/FS12 – Compliance checks: penalties for VAT and Excise wrongdoing

CC/FS14 – Compliance checks: managing serious defaulters

CC/FS20 – Compliance checks: VAT dishonest conduct penalties

CC/FS21 – Compliance checks: alternative dispute resolution

CC/FS22 – Sending HMRC electronic records

www.gov.uk/government/publications

6.9.3 The tax gap

HMRC have published a paper about the "tax gap" in 2013/14 – the difference between the amount of tax theoretically due and the amount actually collected. Their latest estimate is that it stands at £34 billion, about 6.4% of the total due, down from 6.6% the previous year. The 2005/06 level was 8.4%, which would have led to a further shortfall of £11 billion if the 2013/14 gap was at the same level.

The types of behaviour listed include:

- criminal attacks £5.1 billion
- evasion £4.4 billion
- hidden economy £6.2 billion
- avoidance £2.7 billion
- legal interpretation £4.9 billion
- non-payment £4.1 billion
- failure to take care £3.9 billion
- error £2.6 billion

This shows that avoidance, even as defined by HMRC, is a trivial problem in the context of the shortfall as a whole.

The VAT gap is estimated at 11.1%, or £13.1 billion, also slightly less than the 2012 and 2013 figures. This compares to £14 billion of "lost" income tax, NICs and CGT, £3 billion of corporation tax, £2.7 billion of excise duties and £1.1 billion of other taxes.

HMRC estimate that SMEs are responsible for half the value of the tax gap: "Making errors and failing to take reasonable care in dealing with us

are the main reasons why the gap for this customer group persists. These are also relatively small amounts spread across a large number of taxpayers."

The paper sets out the use made by HMRC of these statistics, which inform compliance activity in all areas, in particular against avoidance and evasion. HMRC claim that compliance activity prevented the loss of £2 billion to avoidance and evasion in 2014/15 against a target of £1.79 billion. It is not clear how this affects the overall tax gap statistics, but that may be explained when the 2014/15 figures are published in a year's time.

www.gov.uk/government/publications/issue-briefing-calculating-the-2013-to-2014-tax-gap

6.9.4 Fraud responses

The National Audit Office has issued a report on HMRC's approach to tax evasion and fraud. The conclusion suggests that HMRC have started to take a more strategic view of its compliance business, improving its assessment of tax risks and linking this to the compliance yields it achieves and decisions on where to deploy resources. The NAO encourages HMRC to do more to move from relying so much on investigating non-compliance after it has happened, and concentrate on preventing non-compliance before it happens.

The report says that HMRC consider "smaller businesses" and "criminals" to be the groups responsible for 17 of the 21 biggest tax fraud risks. Of these, eight relate to organised crime and nine involve medium-sized, small or micro-businesses.

HMRC believe these businesses are responsible for tax losses of £17bn, but does not consider their own estimate of how much of this results from tax fraud to be robust enough for publication.

HMRC met their target to increase prosecutions by 1,000 a year by 2014/15, but recognise that they need to better prioritise the cases they select for criminal investigation. They have focused on less complex cases: many of the prosecutions relate to evasion of income tax, VAT and tobacco duty. HMRC have recognised that they need to prosecute cases which more closely correspond with their analysis of tax fraud risks.

www.nao.org.uk/wp-content/uploads/2015/12/Tackling-tax-fraud-how-HMRC-responds-to-tax-evasion-the-hidden-economy-and-criminal-attacks.pdf

6.9.5 Amazon and eBay

It has been reported that HMRC are considering ways of collecting VAT on online sales through such sites as Amazon and eBay, where overseas sellers are able to make sales to UK consumers without accounting for tax. A range of options is being considered, including the possibility of making the trading platforms account for the tax.

http://www.cityam.com/231405/hmrc-national-task-force-considering-clampdown-on-ebay-and-amazon-over-vat-fraud-by-overseas-retailers

6.9.6 Tax compliance burden

In an annual report prepared by PwC and the World Bank Group, the comparative compliance burden imposed by the tax systems of 189 countries is compared. The UK is ranked 16th, behind:

Bahrain (8), Canada (9), Denmark (12), Hong Kong (4), Ireland (6), Kiribati (14), Kuwait (11), FYR Macedonia (7), Mauritius (13), Norway (15), Oman (10), Qatar (1=), Saudi Arabia (3), Singapore (5), United Arab Emirates (1=)

It can be seen that most of these are smaller economies than the UK, and several of the best tax administrations in the world belong to oil-rich Arab countries which presumably do not need to collect a great deal of tax.

The worst tax administration in the world is reckoned to belong to Bolivia.

www.pwc.com/gx/en/paying-taxes/pdf/pwc-paying-taxes-2015-high-resolution.pdf

6.9.7 HMRC closure programme

HMRC are to consolidate their 170 offices across the UK into 13 large regional centres and 4 specialist sites over a 4-year period, beginning in 2016. The department says it expects to retain 90% of the current workforce within the new centres.

www.gov.uk/government/publications/issue-briefing-hmrc-announces-next-step-in-its-ten-year-modernisation-programme

6.9.8 OTS report

The Office of Tax Simplification (OTS) has invited comments by 31 December 2015 on a number of questions to inform its review of small company taxation. Terms of reference for the review in were published in July 2015 and the OTS expects to deliver an initial report by Budget 2016.

It appears to be a general opinion survey that will require some knowledge and effort to complete in a meaningful way. It finishes with the very general question, “If you could change one thing about the way small companies are taxed, what would it be?”

www.gov.uk/government/consultations/key-questions-for-ots-review-on-small-company-taxation

6.9.9 Ending of Business Records Checks

HMRC have announced that they are “winding down” the Business Records Checks programme. This was piloted during 2011, then suspended and re-launched in a revised form in 2012. The professional bodies have always objected to the programme as poorly targeted and ineffective; it was supposed to identify businesses with poor accounting records, but the great majority of those questioned were found to be keeping adequate books.

A BRC started with a letter announcing that the business would be subject to a check; the next step was a telephone questionnaire lasting 10 – 15 minutes. This might lead to a follow-up visit lasting up to 2 hours, which

again might lead to various instructions for improvement and sanctions if problems continued.

There were a number of technical problems with the programme, including the legal status of the questions being asked – it was never clear whether this constituted a statutory "enquiry", which would provide a legal framework.

HMRC say that no new letters will be sent out, although those who have received one already will complete the process. They say: "*Whilst HMRC will no longer initiate new business records checks, we remain committed to helping businesses to keep better records. We will continue to support businesses through our online learning packages and the investment we are making into digital tax accounts which will mean businesses can easily interface with HMRC from their own accounting software.*"

www.gov.uk/guidance/record-keeping-checks-on-your-business

6.9.10 Closure of tax enquiries

HMRC are proposing to include in the 2016 or 2017 Finance Bill a power to issue "partial closure notices", so that particular parts of an enquiry can be concluded while the rest of the enquiry continues. It is hoped that this will speed up the enquiry process. Respondents to a consultation "overwhelmingly" expressed the view that taxpayers should also have the power to force a partial closure. Further consultation will follow.

www.gov.uk/government/consultations/tax-enquiries-closure-rules

6.9.11 Updated Notice

HMRC have updated their Notice *Insolvency*. The address for submission of post-deregistration repayment claim form VAT 426 has changed. The notice also confirms that the criteria for pre-insolvency period claims using form VAT 427 are the same as for VAT 426 claims.

Notice 700/56

6.9.12 Liquidator's contribution

Three creditors of an insolvent company sued the liquidator for breaches of duty. The company had been found to have taken part in an acquisition fraud. The High Court required the liquidator to contribute just under £550,000 to the assets of the company to compensate the creditors. She appealed to the Court of Appeal, arguing that the claim was in reality a claim to recover criminal property. The CA dismissed this argument, holding that the policy of requiring liquidators properly to collect and distribute the assets of the company had to prevail; the illegality of the company's business was a legally irrelevant part of the background. The High Court judge's decision was affirmed.

Court of Appeal: *Top Brands Ltd and another v Sharma (as former Liquidator of Mama Milla Ltd) and another*

6.9.13 Reduced rate for Northern Ireland?

The Northern Ireland Affairs Committee is seeking written submissions by 11 December 2015 to help inform its inquiry into whether introduction of a reduced VAT rate could promote growth in Northern Ireland's

tourism and hospitality sector. One of the questions aims to find out what impact the Republic of Ireland's 9% lower rate has had on tourism south of the border.

http://tinyurl.com/o29vp4q

6.9.14 Confiscation

An individual was convicted of a number of offences, including handling stolen goods. Part of his business had been legitimate, but part had involved hiring out stolen plant and machinery; he had accounted for VAT on some of this income. A confiscation order had been made which included his gross turnover in the calculation of the amount "obtained by criminal conduct". The defendant appealed, arguing that this was disproportionate, as he had accounted for the VAT to HMRC, and had therefore not "obtained" it. The Court of Appeal dismissed his appeal, so it came before the Supreme Court.

The law lords noted that payment of corporation tax on illegal profits did not reduce the benefit for confiscation purposes. However, they considered that VAT on sales was different in nature: there was a powerful argument that it had not been "obtained" by the defendant as a matter of ordinary domestic legal construction. Nevertheless, the Supreme Court declined to make a ruling that would establish a binding precedent that created uncertainties about the meaning of the Proceeds of Crime Act, and rejected the defendant's argument based on POCA.

Instead, they concluded that it would be disproportionate to include in a confiscation order (which benefited the state) money that had already been accounted for to HMRC. That would not merely achieve the deterrent objective of POCA, but would be punitive.

The burden of showing how much of the gross receipts had been accounted for as output tax would fall on the defendant.

Supreme Court: *R v Harvey*

6.9.15 Autumn Statement

Apart from the announcement about the donation of VAT raised on sanitary protection to women's charities (see 2.4.1), there was very little about VAT in the Autumn Statement:

- The government will consult on legislation for Finance Bill 2016 to ensure that the application of the reduced rate of VAT on energy saving materials complies with EU law.
- As part of the government's one-off restructuring of post-16 education and training, Sixth Form Colleges in England will be given the opportunity to become academies which will enable them to recover VAT incurred on their non-business expenditure.

www.gov.uk/government/publications/finance-bill-2016-draft-legislation-overview-documents

With effect from Royal Assent to FA 2016, a new s.33E VATA 1994 will provide that the Treasury may, by order, name Non-Departmental Public Bodies and similar arm's length bodies as 'specified bodies', with the result that they will be able to recover the VAT which they incur on goods

or services which relate to their non-business activities. The aim of the measure is to prevent VAT from being a disincentive to cost-sharing arrangements between such bodies. As such bodies are likely to be government-funded, their funding will be adjusted to reflect the recovery of the VAT on their costs.

www.gov.uk/government/publications/vat-power-to-provide-refunds-to-certain-persons

The FA 2016 will extend HMRC's data gathering powers to cover business intermediaries who facilitate transactions, particularly online, and electronic payment service providers. It is intended to "future-proof" powers by using flexible definitions to cover emerging new sources of data.

www.gov.uk/government/publications/tackling-the-hidden-economy-extension-of-new-data-gathering-powers

6.9.16 Security

A company appealed against a notice of requirement to deposit security of £45,000 (or £30,000 for monthly returns). HMRC had become aware that the director had been involved in at least five other companies that had become insolvent owing various amounts of VAT, and had poor compliance records even before that.

The appeal was based on the assertion that the new business was different in scale to the one by reference to whose turnover the security requirement was calculated. The amount demanded was therefore much too high, even though it was not disputed that HMRC were entitled to require something.

The Tribunal noted that there had been significant discrepancies between the director's predictions of turnover and the actual outcome in previous businesses. It was therefore not unreasonable for the officer to consider the turnover of previous businesses as a reference point. The basis of the decision was examined in some detail, and no fault could be found.

The officer confirmed that she would reconsider the requirement if new evidence could be put before her showing that the risk to the revenue had been reduced.

First-Tier Tribunal (TC04714): *Reresby Arms Rotherham Ltd*

HMRC issued a notice of requirement to deposit security to a company that was incorporated in April 2014 and acquired a hotel from the administrators of a company that had become insolvent, owing VAT of £57,000 and PAYE of £60,000. The director and secretary of the predecessor company were also involved in the new venture.

The company's representative argued that the business had been restructured with new finance and was now trading profitably and meeting all its tax obligations. The failure of the previous business had been a one-off event, and in its lifetime it had paid far more in taxes than the debts that had gone unpaid.

The Tribunal noted that it could only consider whether the decision had been made reasonably, and it was impossible to come to that conclusion. There was no evidence available to HMRC at the time that the decision

was made to support the case that the business was in a different position to its predecessor. If the representative's claims were true, the company could ask for a later reduction in the security requirement, but the appeal against the original demand had to be refused.

First-Tier Tribunal (TC04725): *Inter Hotels Ltd*

6.9.17 Paying tax

HMRC have announced that, with effect from 1 January 2016, they will limit the number of times a credit or debit card may be used to pay tax within a certain period of time. There is no set limit – it depends on HMRC's view of what is reasonable based on payment card industry standards and guidance. The restrictions will apply to multiple card payments against the same tax – in the words of HMRC: "you can only make extra card payments if each one's for a different tax, e.g. Corporation Tax and employers' PAYE."

It is not clear why HMRC should limit such payments, if the card is honoured, as it seems hard to believe that anyone could or would use a stolen or forged card to pay tax liabilities. There is still a 1.5% fee for paying tax liabilities by credit card.

www.gov.uk/pay-tax-debit-credit-card