VAT UPDATE
APRIL 2013

Covering material from January – March 2013

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VAT Update April 2013

Contents

1. INTRODUCTION

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

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

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

1.1 Appeals pending

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

The HMRC website section which reports the progress of appeals reappeared on 21 January 2011 after lying dormant for some time. It says that it will be updated monthly, but it appears to be less frequent or regular than that. The latest update appeared on 28 February 2013 after a gap since December.

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

Awaiting the CJEU:

- *Newey (t/a Ocean Finance)*: HMRC appealed to the Upper Tribunal after the First Tier Tribunal held that a scheme was effective in reducing irrecoverable VAT on advertising costs by moving a loan broking business to the Channel Islands (Upper Tribunal has referred questions to CJEU, Case C-653/11; oral hearing 20 March 2013)
- *Bridport & West Dorset Golf Club Ltd*: the FTT decided that the UK's exemption for sporting services was not in compliance with the Directive; the UT has decided to refer questions to the CJEU
- *GMAC UK plc*: HMRC appealed to the Upper Tribunal after the First Tier Tribunal held that the company was entitled to go back for many years in a bad debt relief claim because the UK rules were too restrictive – in a preliminary decision, the UT decided not to refer questions to the CJEU but to proceed with a substantive hearing; one issue will now be referred to the CJEU, with questions for reference

being agreed (and HMRC are considering whether to appeal further on the others, once the CJEU has given its judgment)

UK appeals awaiting hearing (or announcement of decision):

- *Colaingrove Ltd*: HMRC intend to appeal the decision of the First-Tier Tribunal that is covered in this update in section 2.5.
- *David Finnamore t/a Hanbridge Storage Services*: HMRC have been granted leave to appeal to Upper Tribunal after First-Tier decided that a trader was supplying a licence to occupy land rather than storage services – hearing date to be confirmed
- *DCM (Optical Holdings) Ltd*: HMRC have appealed to the Upper Tribunal after the FTT accepted that a floor-area based special method could be appropriate (Upper Tribunal hearing was previously stated as 20 – 23 September 2011, but it now says "date to be confirmed")
- *Esporta Ltd*: HMRC have been granted leave to appeal to the Upper Tribunal after the First-Tier Tribunal decided that sports club subscriptions paid in respect of a notice period were not taxable because the club did not make its facilities available to the members during that period (hearing 13 – 14 December 2012, decision not yet released)
- *European Tour Operators Association*: Upper Tribunal has remitted case back to First-Tier Tribunal for further consideration of the facts in relation to the exemption for the association's subscriptions
- *Honourable Society of Middle Temple*: HMRC have been granted leave to appeal to the Upper Tribunal against the FTT decision that the Society was making separate zero-rated supplies of water as well as taxable land – hearing date to be confirmed
- *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 CJEU (will presumably now be addressed by the UK courts, but no details given on the website)
- *Lok'n'Store Group plc*: FTT approved a special method which gave the self-storage company 99.98% input tax recovery; HMRC have been granted leave to appeal to the Upper Tribunal
- *The British Disabled Flying Association*: HMRC are seeking permission to appeal to the Upper Tribunal after the First-Tier Tribunal decided supplies of adapted aircraft were eligible for zero-rating – FTT refused leave to appeal, so HMRC have applied directly to the UT (hearing 28 – 29 January 2013)
- *Wrag Barn Golf and Country Club*: dispute about whether a partnership had opted land and later admitted different members, or whether a different partnership disposed of the land and was therefore not bound by the option – FTT found for HMRC (bound); UT referred back for reconsideration; HMRC have been granted permission to appeal to the CA; meanwhile, the FTT re-hearing is scheduled for June 2013.

In this update from previous lists: none. However, the following significant appeals to higher authority appear in this update – they probably ought to have been on previous lists, but were not:

- Court of Appeal: *Vehicle Control Services Ltd v HMRC (2.1.1)*
- CJEU (Case C-424/11): *Wheels Common Investment Fund Trustees Ltd and other companies v HMRC (2.3.2)*
- Upper Tribunal: *British Association of Leisure Parks, Pier and Attractions Ltd v HMRC (2.3.6)*
- Supreme Court: *HMRC v v Aimia Coalition Loyalty UK Ltd (formerly known as Loyalty Management UK Ltd) (5.2.1)*
- Court of Appeal: *BAA Ltd v HMRC (5.6.1)*
- Court of Appeal: *HMRC and Ford Motor Company Ltd v Brunel Motor Company Ltd (in administrative receivership) (5.7.1)*
- Upper Tribunal: *Birmingham Hippodrome Theatre Trust Ltd v HMRC (6.4.3)*
- Upper Tribunal: *Reed Employment Ltd v HMRC (No. 3) (6.4.4)*
- Upper Tribunal: *HMRC v Abdul Noor (6.8.1)*

In addition, the following cases have disappeared from the list without apparent explanation or a published decision which resolved the issues.

- *Bilta (UK) Ltd (in liquidation) and others v Nazir and others*: the High Court decided that a company was entitled to sue its directors for damages after they had allegedly involved it in a carbon trading fraud; the Court of Appeal is to hear an appeal by the directors in May 2013
- *Croall Bryson & Co Ltd*: HMRC are appealing to the Upper Tribunal after the First-Tier Tribunal decided a car dealer was entitled to zero-rate supplies to wheelchair users on the basis of the evidence obtained (hearing date to be confirmed)

“Stop Press” – the following decision was published in mid-April and will be covered in the next quarterly update:

- *Simpson & Marwick*: HMRC have won their appeal to the Court of Session against the Upper Tribunal’s decision that bad debt relief could be claimed for the full amount of “VAT-only” invoices, rather than only the VAT fraction of them (where the invoice for the net supply had been paid by an insurance company)

2. OUTPUTS

2.1 Scope of VAT: linking supplies to consideration

2.1.1 Parking fines

A company supplied parking enforcement services for car parks on private land. It entered into a contract with a landowner to enforce parking control on the land. The landowner paid for signage and for parking permits, which the company agreed to issue to applicants nominated by the landowner. The letters accompanying the permits only carried the company's name, and set out the terms on which parking was permitted.

The Court of Appeal decision explains the source of income which led to the VAT dispute – penalty charges for a range of parking infringements. "*The warning sign sets out the requirement for valid permits or tickets to be displayed, various other rules and the charges that are imposed for failure to comply with the rules. These include a parking charge notice (£80); a wheel clamping charge (£100) and a charge for towing away (£160 plus storage). It states "You are entering into a contractual agreement. Do not park in this area unless you fully understand and agree to the above contractual terms." If a car is parked in contravention of the car park's rules, VCS issues a "parking charge notice" which is placed on the windscreen of the car. The notice sets out, through the use of a code, the nature of the contravention, and makes demand for payment to VCS. VCS enforces collection of such payments, which it retains. The appeal concerns payments arising from some only of the contravention codes (24—Not parked correctly within the markings of the bay or space; 40—Parked in a disabled space without clearly displaying a valid disabled person's badge; 81—Parked in a restricted area of the car park; and 86—Parked beyond the bay markings).*"

Up to 2007 the company accounted for VAT on some income for parking infringements but regarded other receipts as outside the scope, being penalties for trespass or breach of contract rather than consideration for a supply. HMRC ruled that the receipts were either:

- received by the company as principal as part of a contractual arrangement with the motorist; or
- retained by the company in its capacity as agent for the landowner under a contract with the landowner, and were therefore part of the consideration for services to the landowner.

In either alternative, the receipt would be taxable. HMRC's policy on car parking penalties is set out in R&C Brief 57/08: it appears that the dispute arose following the issue of this Brief, and the appeal was in effect an attempt to show that the policy given in the Brief was wrong.

The First-Tier Tribunal (TC00999) agreed with HMRC. The company did not have sufficient interest in the land to sue in its own right for trespass. It was not in the same situation as other licensees who had been held to have that right: if it could sue for trespass at all, that would only be as agent for the landowner, and the retention of the fines was then pursuant to the contract with the landowner.

The First-Tier Tribunal also rejected the contention that the payments were for breach of contract. They were still within the agreement with the motorist and were therefore VATable in principle, even if received by the company as principal.

The Upper Tribunal dismissed an appeal against this decision. The judges considered a number of cited precedents on the question of whether a "licensee in occupation" could sue for trespass, and concluded that they did not apply here – the contract between the company and the landowner did not give the company a right to occupy or possess the land. As a result, its retention of the penalties could not be compensation for trespass in its hands, because it had no right to sue motorists for such compensation.

On the contract issue, both sides appealed: the company argued that the payments were for breach of a contract that existed between it and the motorist, and HMRC argued that there was no such contract – the money was received only as a result of the contract between the company and the landowner. Neither party agreed with the FTT's conclusion that the payments were within a parking contract between the company and the motorist.

The judges agreed with HMRC. They distinguished the case of *Bristol City Council*, in which parking signs constituted a contractual offer and the purchase of a ticket from a machine constituted acceptance. Because this company had only a limited licence in relation to the land, it could not make an offer to allow access to that land. The contract for parking was between the motorist and the landowner, offered by the company as the landowner's agent, and all receipts of the company were related to its contract with the landowner.

The company appealed again to the Court of Appeal, where it succeeded. It contended that the penalty charges were either damages for a breach of a contract between the motorist and the company (which the UT had held not to exist); or else that they were damages for the motorist's trespass on the land, infringing the company's property rights (which the UT had held it did not have).

The appeal judges considered that the Upper Tribunal had confused the making of a contract with the performance of that contract. One of the judges commented, "*There is no legal impediment to my contracting to sell you Buckingham Palace. If (inevitably) I fail to honour my contract then I can be sued for damages.*" The contract between the landowner and the company gave the company the right to exploit the land by entering into contracts with motorists for parking. It was wrong to regard the motorists' contracts as entered into with the landlord, or the retained parking charges as consideration from the landlord to the company.

In addition, the company's licence from the landowner gave it the right to eject motorists from the land. If it chose to enforce its property rights by levying a charge rather than by towing vehicles away, that could be properly regarded as damages for trespass. The levy was based in property rights, and the motorist had infringed them.

Court of Appeal: *Vehicle Control Services Ltd v HMRC*

2.1.2 Private bailiffs

An individual was registered for VAT as a private bailiff. Unconnected with that work, he occasionally acted as an agent buying properties at auctions for a company. He bought the properties in his own name using the company's finance, and transferred the property to the company afterwards if successful.

The Bulgarian tax authorities ruled that he should have accounted for VAT on the income derived from this occasional activity. He appealed, arguing that it had nothing to do with his VAT-registered business (an argument that would not have succeeded in the UK). The Bulgarian court decided to refer questions to the CJEU.

The Advocate-General has given an opinion (not available in English) which confirms the basic position for VAT: a taxable person who provides occasional services outside the scope of his normal business activities is nevertheless required to account for output tax on the consideration received for those occasional supplies.

However, the Advocate-General recognised a possible argument in favour of the appellant. Art.12 Principal VAT Directive permits, but does not require, member states to regard those carrying out occasional transactions as taxable persons. Bulgaria has no specific rule on this, so it is possible that someone who carries out only occasional transactions in Bulgaria should not be regarded as a taxable person in respect of those particular transactions. The question is whether, therefore, the individual can separate out the occasional transactions and treat them as something that is not connected with the activities for which he is registered for VAT. As a subsidiary answer to the questions referred, the Advocate-General suggested that the court should consider the following issues:

- the nature and destination of the subject matter of the transactions;
- the link between the transactions and the appellant's profession, including the likelihood that the client trusted him to carry out the transactions because of his qualification;
- the importance and the type of customers;
- the volume of transactions; and
- the conditions under which consideration was paid, as well as the amount.

These factors are comparable to the "Lord Fisher tests" commonly applied in the UK.

CJEU (A-G) (Case C-62/12): *Galin Kostov v Direktor na Direktsia 'Obzhalvane i upravlenie na izpalnenieto' grad Varna pri Tsentralno upravlenie na Natsionalna agentsia za prihodite*

2.2 Disbursements

Nothing to report.

2.3 Exemptions

2.3.1 Insurance intermediary

A company was formed in 2000 to provide introductions and improved terms to insurance brokers who subscribe to its services. Its income comes from subscriptions and from commissions paid by insurers who issue policies through its subscribers. It enabled small brokers to group together into an "alliance" to secure better terms for their own commissions and for their clients' premiums.

HMRC decided that the supplies to insurance companies, remunerated by commission, were exempt. Although by the time of the appeal hearing HMRC's representative suggested that this might be incorrect, the Tribunal could not rule on it, as it was not the subject of the appeal; however, they could not regard anything relating to HMRC's concession of this issue as binding in their consideration of the other.

The issue under appeal was whether the subscriptions paid by member brokers were exempt as consideration for a service which could be regarded as an intermediary one in relation to insurance contracts. The company had asked for clearance on the matter in 2009, and HMRC had refused to give it; eventually this led to a notice of compulsory registration to take effect in 2005.

The Tribunal considered a number of precedent cases, most importantly Case C-8/01 *Assurandor-Societet, acting on behalf of Taksatorringen v Skatteminmsteriet*. The CJEU commented that "*As to whether such services are 'related services performed by insurance brokers and insurance agents', it must be stated, as the Advocate General has pointed out in para 86 of his opinion, that this expression refers only to services provided by professionals who have a relationship with both the insurer and the insured party, it being stressed that the broker is no more than an intermediary*."

Further, the judgment of Etherton LJ in Insurancewide.com was cited as defining the scope of the exemption for insurance intermediaries:

(1) The insurance intermediary exemption should be interpreted so far as possible, consistently with its terms, in a way that reflects the jurisprudence of the ECJ and the United Kingdom's obligations under the Sixth Directive and the 2006 VAT Directive. To do otherwise would, as Ms Foster pointed out, risk infraction of EU legislation by the United Kingdom.

(2) The exemption in art 13B(a) must be interpreted strictly since it constitutes an exception to the general principle that VAT is to be levied on all services supplied by a taxable person. This does not mean, however, that the words and expression in art 13B(a) and the insurance intermediary exemption are to be given a particularly narrow or restricted interpretation. It is for the supplier to establish that it and its activities come within a fair interpretation of the words of the exemption.

(3) the exemption for 'related services' under art 13B(a) only applies to services performed by persons acting as an insurance broker or an insurance agent. Although those expressions are not defined by EU legislation, they are independent concepts of the common system of VAT.

(4) Whether or not a person is an insurance broker or an insurance agent, within art 13B depends on what they do. How they choose to describe themselves or their activities is not determinative.

(5) The definitions of 'insurance broker' and 'insurance agent' in the Insurance Directive are relevant to the meaning of the same expressions in art 13B(a), to the extent, but only to the extent, that they should be taken into consideration as reflecting legal reality and practice in the area of insurance law. It is not necessary, in order to invoke the exemption in art 13B(a), for the taxpayer to perform precisely the description of activities in art 2(1)(a) or (b) of the Insurance Directive.

(6) On the other hand, the mere fact that a person is performing one of the activities described in art 2(1)(a) or (b) of the Insurance Directive or the definition of 'insurance mediation' in the Insurance mediation Directive does not automatically characterise that person as an insurance agent or insurance broker for the purposes of art 13B(a).

(7) It is an essential characteristic of an insurance broker or an insurance agent, within art 13B(a), that they are engaged in the business of putting insurance companies in touch with potential clients or, more generally, acting as intermediaries between insurance companies and clients.

(8) It is not necessary, in order to claim the benefit of the exemption in the art 13B(a), for a person to be carrying out all the functions of an insurance agent or broker. It is sufficient if a person is one of a chain of persons bringing together an insurance company and a potential insured and carrying out intermediary functions, provided that the services which that person is rendering are in themselves characteristic of the services of an insurance agent or broker.

(9) All the above principles are capable of being applied, and must be applied, to the insurance intermediary exemption in Sch 9 to VATA 1994.

The Tribunal decided that the services provided by the company constituted access to structures and facilities which enabled insurance brokers to sell insurance on more favourable terms, but that was not enough to constitute 'acting in an intermediary capacity'. It was more akin to the support services of *Arthur Andersen* in Case C-472/03. HMRC's decision in respect of the supplies to member brokers – that the subscriptions were taxable – was upheld.

First-Tier Tribunal (TC02532): *Westinsure Group Ltd*

2.3.2 Investment management

A company which provides fund management services to pension funds argued that the principles of the *JP Morgan Fleming Claverhouse* decision (Case C-363/05) should apply to exempt its services, because pension funds compete with investment trust companies and open-ended investment companies which are regarded as "special investment funds" for the purposes of the exemption.

HMRC argued that the schemes involved in the appeal, being "defined benefit" schemes (based on final salary rather than the value of a fund), are fundamentally different from investment funds which are regarded as subject to exemption. If they are not directly in competition with other special investment funds such as OEICs and investment trust companies, there is no reason to treat them in the same way for VAT.

Questions were referred to the CJEU. The court agreed with HMRC. Special investment funds were mainly those products covered by the Directive on Undertakings for Collective Investments in Securities (UCITS). The *JP Morgan* decision showed that where something which was not directly covered by that Directive competed with UCITS, it should be treated in the same way for VAT. However, a pension fund such as that managed by this company was not in direct competition with UCITS. It was not open to the public, but was an employment benefit made available to the workers of specific companies.

The features which the court identified as differentiating this pension fund from UCITS may be important for considering other *Morgan*-related arguments:

- the employees do not bear the risk arising from investment performance – their pensions are defined by their salaries and length of service, and it is the employer who will have to make extra contributions if the investments do not perform well;
- the employer is not similar to a private investor in UCITS, because he makes contributions not to maximise investment returns, but to meet a legal obligation to the employees.

The questions referred were very long, but the answer was much shorter. The court ruled that a defined benefit pension scheme is not a SIF, and the principles of fiscal neutrality do not require it to be treated as one.

The total VAT at issue in the case has been estimated at £2bn in retrospective claims (including *Fleming* claims made before the deadline) and £100m a year in current VAT. Commentators afterwards expressed disappointment with the decision, pointing out that the ongoing project to reform the financial services exemptions may well lead to the exemption for management being applied to pension funds. However, the court would not be justified in applying a possible reform retrospectively.

CJEU (Case C-424/11): *Wheels Common Investment Fund Trustees Ltd and other companies v HMRC*

Another case on the extent of the exemption for 'management of special investment funds' has come before the CJEU, referred from Germany. In this case, the services were indisputably supplied to special investment funds; the issue was whether they qualified as 'management' of those funds, as in the *Abbey National* case (Case C-169/04).

The appellant provided what appear to be advisory rather than management services. It contracted with an investment fund 'to advise in the management of the fund' and 'constantly to monitor the fund and to make recommendations for the purchase or sale of fund assets'. It was also required 'to pay heed to the principle of risk diversification, to statutory investment restrictions ... and to investment conditions.' Its remuneration was calculated as a percentage of the value of the fund. The fund managers took the final decisions on whether or not to follow the recommendations, after checking whether they would contravene any regulatory investment limits.

The Advocate-General's opinion went against the views of several governments and the Commission, and the full court has agreed. The short answer to the questions raised is:

Article 13B(d)(6) [6th Directive] must be interpreted as meaning that advisory services concerning investment in transferable securities, provided by a third party to an investment management company which is the manager of a special investment fund, fall within the concept of 'management of special investment funds' for the purposes of the exemption laid down in that provision, even if the third party has not acted on the basis of a mandate within the meaning of Article 5g of Council Directive 85/611/EEC of 20 December 1985 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) as amended by Directive 2001/107/EC of the European Parliament and of the Council of 21 January 2002.

The court considered that the relevant question was whether the service provided by the appellant was "intrinsically connected to the activity characteristic of an investment management company". Although the UCITS Directive did not explicitly describe this activity in its list of management activities, that list was not intended to be exhaustive but rather illustrative. The breadth of service included within "management" by the *Abbey National* decision suggested that these services should also fall within the exemption.

The German government had also raised the issue of fiscal neutrality – that allowing this service to be exempt, while other similar services provided to individuals were taxable, would create a distortion. The Advocate-General considered that this was answered by the recent decision in *Deutsche Bank*: the Directive provided for different treatments in the case of special investment funds, and as long as the service constituted 'management', it should be exempt.

The full court confirmed this part of the opinion, observing that the same services would be taxable if provided to anyone who was not a SIF manager. There was therefore no possibility of fiscal distortion other than that specifically provided for by the VAT Directive. It also noted that taxing these services would create a fiscal advantage in favour of SIFs using their own in-house investment advisers (although the VAT consequences of outsourcing are a common feature of the system and are hardly an overpowering reason to allow an appeal).

Lastly, a question was raised about the possible illegality of the service. The client SIF did not have regulatory authority to delegate management to the appellant. The Advocate-General did not consider this important. The SIF regulations forbidding delegation of management were using the term in a narrower sense, relating to the actual carrying out of transactions. The *Abbey National* decision showed that the meaning of the term in the VAT Directive was broader. Whether or not there had actually been a breach of the SIF rules in Germany, the service provided was still exempt. The full court confirmed this, observing that there cannot be a VAT distinction based on the lawfulness or otherwise of transactions.

CJEU (Case C-275/11): *GfBk Gesellschaft fur Borsenkommunikation mbH v Finanzamt Bayreuth*

2.3.3 Incidental to education

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 decision does 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.

The Tribunal 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 Tribunal 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 Tribunal 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).

First-Tier Tribunal (TC02569): *Brockenhurst College*

2.3.4 Healthcare and cosmetic surgery

The CJEU has considered a question which has been the subject of argument in the UK – whether cosmetic treatment and plastic surgery is exempt as "healthcare" or not. The UK government made no representations in the case.

The court ruled that such procedures are exempt if they have a therapeutic purpose – typically, if there is a medically assessed need for the procedure to be carried out, including a psychological need. That must be judged by qualified medical practitioners, rather than depending only on the subjective assessment of the person undergoing the procedures.

The full answer is as follows:

Article 132(1)(b) and (c) of Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax must be interpreted as meaning:

- *supplies of services such as those at issue in the main proceedings, consisting in plastic surgery and other cosmetic treatments, fall within the concepts of 'medical care' and 'the provision of medical care' within the meaning of Article 132(1)(b) and (c) where those services are intended to diagnose, treat or cure diseases or health disorders or to protect, maintain or restore human health;*
- *the subjective understanding that the person who undergoes plastic surgery or a cosmetic treatment has of it are not in themselves decisive in order to determine whether that intervention has a therapeutic purpose;*
- *the fact that services such as those at issue in the main proceedings are supplied or undertaken by a licensed member of the medical profession or that the purpose of such services is determined by such a professional may influence the assessment of whether interventions such as those at issue in the main proceedings fall within the concept of 'medical care' or 'the provision of medical care' within the meaning of Article 132(1)(b) and (c) of Directive 2006/112 respectively;*
- *in order to determine whether supplies of services such as those at issue in the main proceedings are exempt from VAT pursuant to Article 132(1)(b) or (c) of Directive 2006/112 all the requirements laid down in subparagraphs 1(b) or (c) thereof must be taken into*

account as well as the other relevant provisions in Title IX, Chapters 1 and 2, of that directive such as, as far as concerns Article 132(1)(b), Articles 131, 133 and 134 thereof.

CJEU (Case C-91/12): *Skatteverket v PFC Clinic AB*

2.3.5 Sporting services

A Czech municipality claimed deduction of input tax in relation to the costs associated with operating an aquatic park. The tax authority ruled that the admission charges were exempt, because the customers were paying to take part in sport or physical education supplied by a public body. Questions were referred to the CJEU about whether unsystematic and unorganised physical recreation could constitute "sport" within the meaning of the VAT Directive.

The Court commented that there should not be any limitation on the concept of "sport" based on the level at which it was practised by members of the population (i.e. wholly amateur sport qualifies, and it is not necessary for any formal competition to be involved); however, engagement in sporting activity in the context of pure rest and amusement should not qualify.

The Court then considered whether the supply should be regarded as "closely linked to sport". This required a conclusion on whether there was a single supply or a mixed supply, and what exactly the customers thought they were buying, in line with previous decisions such as *Card Protection Plan*. This would be a matter for the national court to determine; however, the judgment comments that the fact that the admission ticket gives access to all of the facilities, without any distinction according to the type of facility actually used and to the manner and to the duration of its use during the period of the entrance ticket's validity, constitutes a strong indication of the existence of a single complex supply.

The Court appeared to consider the intention of the "average customer" should determine the liability of the supplies to all. This could be gleaned from a number of objective factors, including the nature of the facilities and whether they lent themselves mainly to sporting swimming (lanes, starting blocks) or pure amusement and recreation (presumably wave machines, fountains and water slides). To determine the liability based on the actual stated intentions of individual customers would be contrary to the requirement to operate the exemptions in a straightforward manner and in line with the principle of fiscal certainty.

The answer to the main question was given as follows:

"*access to an aquatic park offering visitors not only facilities for engaging in sporting activities but also other types of amusement or rest may constitute a supply of services closely linked to sport. It is for the referring court to determine whether, in the light of the interpretative guidance provided by the CJEU in the present judgment and having regard to the specific circumstances of the case in the main proceedings, that is the position in that case.*"

CJEU (Case C-18/12): *Město Žamberk v Finanční ředitelství v Hradci Králové*

2.3.6 Subscriptions

A trade association was established in 1938 to represent proprietors of amusement parks. It registered for VAT in 1982 but later submitted a "*Fleming* claim" in respect of its subscriptions, arguing that they should be exempt under Sch.9 Group 9.

The main question was whether the association fell within Item 1(d):

"an association, the primary purpose of which is to make representations to the Government on legislation and other public matters which affect the business or professional interests of its members."

The First-Tier Tribunal examined the history of the association, its constitution and the information it sent to members about the services it provided. The chairman concluded that lobbying was not the primary purpose of the association, even if 70% of the chairman's time was now devoted to that activity.

In case he was wrong on that principal issue, Sir Stephen Oliver went on to consider whether Note 5 disqualified the association anyway. This requires that an organisation which satisfies Item 1(d) must restrict its membership wholly or mainly to individuals or corporate bodies whose business or professional interests are directly connected with the purposes of the association. About 31% of the members were agreed not to be in a kind of business that was concerned with the lobbying activities, and Sir Stephen ruled that this was too great to satisfy "wholly or mainly". In his view, that expression required "substantially all" rather than "a bare majority".

The FTT also concluded that HMRC could rely on the defence of unjust enrichment, even if it was wrong on the question of liability. The VAT had been passed on to the members, most of whom would have been able to recover it. Although the onus was on HMRC to demonstrate unjust enrichment, the burden was not excessive – it was not necessary for them to identify the status of every single member and show the extent to which the association would be enriched. In principle, it seemed more likely that the cost of the VAT had been passed on.

The Association appealed to the Upper Tribunal. It had to try to overturn the FTT's decision on all three points: the "primary purpose" of the Association; the relevance of Note 5; and unjust enrichment.

The Upper Tribunal judge could find no fault with Sir Stephen's judgment on both the first and the third issues. Even though the Association's activities had changed over time so that lobbying had become a very significant activity, it was making a claim covering the whole period. There was insufficient evidence to make out a claim that its primary purpose had been lobbying for the whole of that time.

The judge's comments on unjust enrichment may have a wider application. Again, he agreed with HMRC and Sir Stephen:

In my judgment, this was a straightforward case of unjust enrichment. As to the four questions which were agreed by the parties to be the relevant questions, on the assumption (for present purposes) that the Association ought not to have charged VAT to its members, the answers are:

(1) the Association has charged amounts of VAT to its customers (i.e. its members) which it ought not to have charged;

(2) the Association has passed the economic burden of the wrongly charged VAT to its customers (i.e. its members);

(3) the Association has suffered no loss or damage as a result of having passed the mistaken charge to its customers (i.e. its members); and

(4) the Association is unable or unwilling to reimburse its customers (i.e its members) with any amounts paid to it by HMRC; on this last point, the evidence was that the Association's Memorandum of Association prevented the Association paying a dividend to its members.

The judge was not convinced that Sir Stephen had applied the correct interpretation of Note 5. This had been considered by the Upper Tribunal in the *European Tour Operators Association* case, and that had been referred back to the FTT for reconsideration. However, after discussing the issues and the possible meaning of the provision, the judge noted that it would make no difference to the decision – as he had already decided that the Association could not satisfy the basic conditions for exemption, the exclusion was not in point.

Upper Tribunal: *British Association of Leisure Parks, Pier and Attractions Ltd v HMRC*

2.3.7 Cultural services

The British Film Institute made a *Fleming* claim in respect of tickets to the National Film Theatre and some film festivals sold between 1990 and 1996. It had accounted for output tax, believing that it did not qualify for exemption under the cultural services provisions; but it subsequently realised that it should benefit from the *London Zoo* decision, as its main management was "essentially voluntary" in nature.

The Institute argued that from 1990, the UK was no longer entitled to tax cultural services which were covered by art.13A(1)(n) 6th Directive. A transitional provision which allowed taxation had expired, but the UK had not introduced the required amendments to Sch.9 VATA 1994. The Institute therefore claimed direct effect of the Directive in the absence of any domestic implementation of the provision.

When Group 13 was inserted into Sch.9 in 1996, supplies by cinemas were not included – even though they are envisaged in the Directive. There is therefore a further area of dispute between the Institute and HMRC concerning the availability of exemption after 1996 – now, the question is whether the UK is entitled to restrict the types of supply to which exemption applies.

The Tribunal considered a number of precedent cases, including several decisions of the VAT Tribunal which had supported HMRC's view that the UK was entitled to exclude cinema tickets from exemption because the Directive referred to "certain cultural services" (i.e. selected or restricted services, such selections or restrictions to be chosen by the member state). These decisions had been taken without reference to the CJEU decision in *Commission v Spain* (Case C-124/96), in which the Spanish government had argued a similar point in relation to the similar expression "certain services closely linked to sport". The Court had ruled that this did not entitle the state a wide discretion, but only related to the fact that such services had to be supplied by “the right sort of person”.

The Tribunal concluded that the Directive was sufficiently clear and unequivocal to confer the benefit of direct effect on the Institute, and allowed the appeal.

First-Tier Tribunal (TC02490): *British Film Institute*

2.3.8 Updated Notices

HMRC have issued a new version of their Notice *Finance*, replacing the November 2011 version. The changes are stated as relating to section 5 ‘Debts and related services.’ These appear to be the inclusion of the following paragraphs which follow from the cases of *HMRC v AXA UK plc* and *Paymex Ltd*:

5.10 Debt collection

The supplies made by a debt collection agency, or by someone involved in debt collection, are taxable. Debt collection covers the collection of debts of any nature, even if payment of those debts has been received before, on, or after their due date.

Although debt collection service undertaken on behalf of a creditor company may involve some negotiation of the repayment of a debt by the debtor to the creditor this will not be an exempt debt negotiation service. For example if you:

- *issue letters to the debtor on behalf of the creditor demanding payment, or*
- *seek to chase the debt in some other form (e.g. trying to contact the debtor by phone etc.), or*
- *seek to locate a debtor on behalf of the creditor, or*
- *provide accounting services to the creditor (that is you monitor the debtor’s payment account and notify the creditor of any defaulted payments)*
- *these services will be taxable. Any debt negotiation services will be ancillary to the principal service of debt collection.*

The above list is not exhaustive.

5.11 Insolvency Practitioner services

The supplies made by an Insolvency Practitioner are normally taxable

Where an Insolvency Practitioner acts as both nominee and supervisor in any type of formal Voluntary Arrangement then the supplies by the Insolvency Practitioner are exempt.

Further details on Insolvency Practitioner services can be found in the VAT Finance manual (VATFIN3260).

Notice 701/49

HMRC have issued a new version of their Notice *Gold*, replacing the October 2011 version. The main changes relate to section 8 'Imports and exports of investment gold' and section 9 'Penalties'. In spite of the updating, section 9 still states that the penalty rate is 17.5% of the value concerned, and refers to appeals to the VAT and Duties Tribunal.

Notice 701/21

HMRC have issued a new version of their Notice *Insurance*, replacing the May 2012 version. The main changes are:

- Paragraph 10.2 (Services of Protection and Indemnity (P&I) Club managers and agents) has been updated so that it more accurately represents the services that P&I managers and agents perform.
- Paragraphs 10.3 (Pension review services) and 10.4 (Phone helplines) have been amended to reflect changes in tax treatment announced in Revenue & Customs Brief 33/12.

Notice 701/36

HMRC have issued a new version of their Notice *Betting, gaming and lotteries*, replacing the June 2011 version. The main changes are to take account of the introduction of the exemption for machines which are subject to Machine Games Duty with effect from 1 February 2013.

Notice 701/29

2.4 Zero-rating

2.4.1 Beverages

A company sold coconut water. It obtained a ruling from HMRC in July 2011 confirming that the product was zero-rated. However, HMRC changed the decision in December 2011 and ruled that it should be standard rated. The company appealed to the Tribunal.

The Tribunal had to consider whether coconut water was "food (including drink)" and therefore basically zero-rated; and if so, whether it was covered by the exception for "other beverages"; and if so, whether it fell within the overriding exception as "milk".

Coconut water is the fluid in immature green coconuts, extracted and packaged without further processing. It is not the same as coconut milk, which is made by squeezing grated coconut meat through a filter. Coconut milk is treated as zero-rated by HMRC: the Tribunal was not entirely sure why this should be so, but concluded that it was because it is a liquid food (typically an ingredient), rather than because it is "milk" and therefore zero-rated in spite of being a beverage.

The Tribunal decided that the coconut water was not "milk", whether coconut milk or any other kind. It was not the same as coconut milk, and therefore had to be considered in its own right, regardless of HMRC's policy on the other product. It was sold for drinking, rather than as a food ingredient, and therefore was a beverage. It was excluded from zero-rating. The company's appeal was dismissed.

First-Tier Tribunal (TC02512): *Chi Drinks Ltd*

2.4.2 Connection charges for water

HMRC have issued a Brief explaining a change of policy on the liability of the supply of first-time connection to water services from 1 January 2013. This follows on from, and is consistent with, R & C Brief 43/11 which changed the policy on connection to gas and electricity services with effect from 1 January 2012.

If the contract for connection is with the water supplier (or a member of its VAT group), the work will be treated as incidental to the supply of the water itself and the liability will follow from that (zero-rated for domestic customers, standard rated for relevant industrial customers).

If the connection is carried out without reference to a particular water supplier, it cannot be zero-rated as ancillary to a supply of water. However, it can be part of the zero-rated construction of a new dwelling, the conversion of non-residential property into dwellings for a housing association, or the construction of a permanent caravan park.

The Brief also contains a table setting out the liability of replacing water supply connections, which are normally standard rated unless part of an overall project that would benefit from a different rate (e.g. demolition and reconstruction of dwellings, conversion of property into multiple residential units).

R & C Brief 40/12

2.4.3 Independence payments

People who receive Disability Living Allowance are eligible to receive certain supplies zero or lower rated (leasing of motor vehicles and grant-funded installation of heating equipment among other things). The Value Added Tax (Independence Payment) Order 2013 provides that these VAT reliefs will still apply to those who receive the new benefits which will replace DLA – the Personal Independence Payment and Armed Forces Independence Payment.

SI 2013/601

2.5 Lower rate

2.5.1 Energy supplies

A company supplied holiday accommodation in chalets, static caravans and caravan pitches to customers. It made a separate charge for the provision of electricity, but this was not metered or specifically related to the amount of electricity consumed by the particular customer paying it. It was accepted that the pitch hire was standard rated; HMRC ruled that there was no separate supply of electricity that could be lower-rated, or else that the supply of electricity was incidental to the standard rated supply.

The company had made reclaims in relation to supplies to mobile caravans in the early 1990s, and HMRC had agreed and settled these. It subsequently made another claim in relation to the supplies currently in dispute, which was also settled by HMRC. For a time it made manual adjustments to its VAT returns to reflect lower-rating of the electricity charges, but then decided instead to account for everything at the standard rate and make periodic voluntary disclosures. The current dispute started when one of these disclosures was refused in 2002.

HMRC's representative argued that it would be artificial to give different VAT liabilities to the two parts of the supply when the charge for electricity was simply a flat rate amount unrelated to actual consumption. In effect, there was a single supply of "fully serviced accommodation" for a single charge, and it was standard rated. He submitted that to give separate liabilities would make a nonsense of the *CPP* precedents and would "open the floodgates" to many similar claims.

The Tribunal did not accept this. The UK's legislation appeared specifically to provide for the application of the lower rate to supplies of electricity for consumption in a caravan. That was a specific and distinct circumstance in which the law provided for the relief to apply; allowing this appeal would not have a wide effect beyond that limited circumstance. Although there might be scope for abusive value-shifting between the two types of supply, the Tribunal found no evidence that this had occurred.

On that basis – that the UK legislation specifically provided for the lower rate to apply in this situation – the appeal was allowed. However, the Tribunal went on to make other findings in case its decision on this point was appealed and overturned. As a matter of general principle, it agreed with HMRC that there would be a single supply within *CPP*, because the customer was interested in buying a package from the company of "accommodation with electricity". That single supply would, if considered without the benefit of Sch.7A, be standard rated.

First-Tier Tribunal (TC02534): *Colaingrove Ltd*

2.5.2 Cable-based transport

As announced last year, The Value Added Tax (Reduced Rate) (Cable-Suspended Passenger Transport Systems) Order 2013 has applied the 5% rate to transport in cable-based systems (cable cars, chairlifts and the like) carrying up to 9 passengers with effect from 1 April 2013.

SI 2013/430

2.5.3 Energy-saving materials

A company appealed against a ruling that its product was not "insulating materials" within the definition of Group 2 Sch.7A VATA 1994. The Tribunal accepted that it was a gel used for insulating walls, rather than merely being a waterproof paint, and therefore qualified for the relief; however, supplies of the materials themselves remained standard rated, as only the service of installing insulating materials qualified for lower-rating.

First-Tier Tribunal (TC02543): *Safeguard Europe Ltd*

Meanwhile, the European Commission is commencing infringement proceedings against the UK over the reduced VAT rate on the supply and installation of energy-saving materials. Although the UK is ending the relief in relation to charitable buildings, it intends to retain it for residential properties. The Commission argues that supplies of housing materials and services can only be eligible for the reduced rate under the Directive if they are for social policy reasons, not environmental policy. Although it supports the UK's "Green Deal" objectives, it does not believe that breaking VAT rules is an acceptable way of achieving them.

IP/13/139

2.6 Computational matters

2.6.1 Updated Notices

HMRC have issued updated versions of three of their Notices on Retail Schemes:

- 727/3: How to work the Point of Sale Scheme
- 727/4: How to work the Apportionment Schemes
- 727/5: How to work the Direct Calculation Schemes

The changes are minor – updates which were previously separately issued have been incorporated, reflecting the current capping provisions for making adjustments and a change of a relevant HMRC address.

Notices 727/3, 727/4 and 727/5

2.7 Discounts, rebates and gifts

Nothing to report.

2.8 Compound and multiple

2.8.1 Polish mixed supplies

The Polish courts referred a question that echoes a number of UK disputes – whether a charge for insurance, supplied with something else, can be treated as separate and can fall within the exemption:

(a) Must Article 2(1)(c) of [the VAT Directive] be interpreted as meaning that the service providing insurance for a leased item and the leasing service are to be treated as separate services or as one single, comprehensive, composite leasing service?

(b) If the answer to the first question is that the service providing insurance for a leased item and the leasing service are to be treated as separate services, must Article 135(1)(a) of [the VAT Directive], in conjunction with Article 28 thereof, be interpreted as meaning that the service providing insurance for a leased item is to be exempt in the case where the lessor insures that item and charges the costs of that insurance to the lessee?

The UK courts have considered this a number of times, particularly in connection with the supply of "cars and insurance". It has generally been held that the supply of insurance is absorbed within the supply of the goods and is not exempt.

However, the CJEU has ruled that the supplies of asset leasing and insurance are distinct and separate, and the supply of insurance to the lessor and its onward invoicing to the lessee is exempt. The lessor remained the owner of the asset throughout; it required the lessees to take insurance which it arranged, paid for and re-invoiced to them. The Polish authorities took the view that it was then incidental to the supply of the leases and the whole consideration paid by the customer was therefore taxable.

The following comments of the Court may have wider application:

35 In order to determine whether such elements constitute a single transaction for VAT purposes, it must be observed, first of all, that it is true that those two elements are likely to be supplied together. In fact, there is a link between the supply of a leasing service and the supply of insurance for the leased item, since such insurance for that item is only of use with respect to the latter.

36 It must be stated, in that regard, that any insurance transaction has, by nature, a link with the item it covers. It follows that there is necessarily a connection between the leased item and the relevant insurance. Nonetheless, such a connection is not sufficient in itself to determine whether or not there is a single complex transaction for VAT purposes. If any insurance transaction were subject to VAT because the services relating to the item it covers were subject to VAT, the very aim of Article 135(1)(a) of the VAT Directive, that is the exemption of insurance transactions would be called into question.

The Court ruled that it would not be artificial to divide the leasing and insurance elements: in principle, they were separate supplies. It also stated that it would be for the referring court to decide whether they were so closely linked that one could be regarded as ancillary to the other;

however, the tenor of the judgment suggests that this is not likely to be the case. The Court also confirmed that the purchase and re-invoicing of insurance did not change its nature: in line with the CPP decision, the lessor was providing insurance to the lessee which was capable of being exempt within art.135(1)(a).

The formal answers to the questions were:

1. The supply of insurance services for a leased item and the supply of the leasing services themselves must, in principle, be regarded as distinct and independent supplies of services for VAT purposes. It is for the referring court to determine whether, having regard to the specific circumstances of the case in the main proceedings, the transactions concerned are so closely linked that they must be regarded as constituting a single supply or whether, to the contrary, they constitute independent services.

2. Where the lessor insures the leased item itself and re-invoices the exact cost of the insurance to the lessee, such a transaction constitutes, in circumstances such as those at issue in the main proceedings, an insurance transaction within the meaning of Article 135(1)(a) [PVD].

CJEU (Case C-224/11): *BGŻ Leasing Sp. z o. o. v Dyrektor Izby Skarbowej w Warszawie*

2.8.2 Land and services?

A company owned premises which were used for selling antiques. It rented out about 70% of its floor space to other traders, and did not account for VAT on the receipts, considering them to be exempt as consideration for a supply of land.

If a stallholder had to be absent from the premises for some reason, the company's directors handled sales of their goods for them, putting aside cheques and cash in separate "pouches" to await their return, or processing card payments that went into a stallholders' account to be distributed later. Charges were made in respect of handling these sales.

The appellant argued that there was a single exempt supply of land; HMRC argued that there was a single taxable supply of "facilities" which did not satisfy the conditions for exemption. The Tribunal did not agree with either of these conclusions, holding rather that there were separate supplies. The renting of the pitches satisfied the conditions for being a licence to occupy land, but the sales facility was a separate matter which could not be regarded as incidental or absorbed within the main supply. The appeal was allowed in part, and the parties were invited to discuss the appropriate apportionment.

First-Tier Tribunal (TC02507): *Antiques Within Ltd*

2.8.3 Ashes to ashes

A local authority provided, for consideration, the right to a memorial plaque in a garden near where ashes of deceased persons might be scattered, or a place where an urn containing ashes might be stored behind a memorial plaque. The family of the deceased would pay for the plaque or urn to remain in place for 10 years; the period could be extended on payment of a further fee.

The local authority argued that the money was exempt consideration for a supply of land. HMRC ruled that the supply was of “commemorative focal points”, which were not essentially land, and was therefore standard rated. There was a supply of the memorial tablet as well as the place to keep it, and the rights over land enjoyed by the customer were so restricted that they could hardly constitute a “licence to occupy”.

Although the supply comprised two elements – the tablet, which could be taken away at the end of the 10-year lease term, and the right to place it on the council’s land – neither side argued that there were two separate supplies for VAT purposes. The Tribunal agreed: the customer viewed the supply as a single indivisible thing, and that was how it should be treated. The Tribunal quoted the following statement about compound and multiple supplies from the decision of the Upper Tribunal judge in *Bryce t/a The Barn*:

(a) Every supply of a service must normally be regarded as distinct and independent. However, a transaction which forms a single supply from an economic point of view should not be artificially split into separate supplies ...

(b) For this purpose, regard must be had to all the circumstances in which the transaction takes place ...

(c) There is a single supply where one or more elements are to be regarded as constituting the principal supply, whilst one or more elements are to be regarded by contrast as ancillary to that principal supply ...

(d) However the fact that one element in a package supplied cannot be described as ancillary to another element does not mean it is to be regarded as a separate supply for tax purposes. The question is whether those separate elements are to be treated as separate supplies or merely as elements in some single overarching supply ...

(e) In that regard, the test is whether the various elements supplied to the customer are so closely linked as to form, objectively, a single indivisible economic supply, which it would be artificial to split ...

(f) It is important to take an overall view of the level of generality that corresponds with social and economic reality, without overzealous dissection ...

(g) The assessment should be made from the perspective of the customer, as a typical customer, not the supplier ...

(h) The fact that a single price is charged for two or more elements is a relevant factor pointing to a single supply but it is not decisive .... Similarly, the fact that separate supplies are stipulated for various elements is not decisive where the two elements have an objective close link such that they form a single economic transaction ...

(i) The fact that the same or similar goods or services could be supplied separately from different sources is irrelevant to the question whether in the particular transaction under consideration their combination produces a different economic result ...

(j) The test is not whether the different elements in the services provided by the taxpayer to its customers have value and utility in their own right ....

The Tribunal also noted that the CJEU in *Everything Everywhere Ltd* (Case C-276/09) commented that there would be a single supply if one element was of no use to the customer without the other. Although the tablet was a physical and substantial item, the intention of the customer was never to acquire the tablet on its own.

In considering the liability of the single supply, the Tribunal drew a distinction between the situation in which one supply was ancillary to the other (as the payment arrangements were ancillary to telecommunications services in *Everything Everywhere*) and the more difficult problem when there was a package of different elements, none of which were clearly predominant. The Tribunal described its approach as follows:

In our opinion, for the reasons which follow, what is required is that the tribunal consider the essential nature of a package of services and goods and then determine whether that fits any of the statutory provisions. This is different from finding a description of the package and asking whether that description can be found within any particular statutory heading. For example if you provide me with carrots coated in chocolate, you may be said (1) to supply the service of satisfying my hunger; (2) to supply me with luxury food; or (3) to supply me with food. But the question is not whether "satisfying my hunger" or any other description falls within the ambit of the "food for human consumption" and Schedule 8 VATA, but whether providing the chocolate coated carrots falls within the words "food of a kind for human consumption" in Schedule 8. The important thing is not to be misled by attaching a description to the package when such exercise is not required by the legislation.

The Tribunal then considered a number of precedent cases where the CJEU has considered "the letting of immoveable property", and also the circumstances of the different types of memorial which the council offered. It concluded that the principal supply was exempt if it was not intended or envisaged that the memorial would be moved for the entire 10-year term; however, where the memorial could be moved, it fell within the precedent of *Sinclair Collis* (Case C-275/01) and would therefore not be exempt. The appeal was therefore allowed in part, to the extent that it related to immoveable memorials.

The Tribunal also commented on the appellant's alternative argument, that the memorials should be exempt as incidental to the disposal of the remains of the dead. The provision of the memorial was too far removed from the actual cremation (which was the essential exempt supply), and was therefore not exempt under this heading.

First-Tier Tribunal (TC02554): *Sandwell Metropolitan Borough Council*

2.9 Agency

2.9.1 TOMS

A group of travel agents made a *Fleming* claim for repayment of £156m of overpaid output tax. It covered two elements:

(i) 1 January 1980 to 4 December 1996 and 1 April 2006 to 30 September 2008 – in respect of commissions on the sale of holidays outside the EU ("non-EU claim");

(ii) 1 April 1988 to 4 December 1996 and 1 April 2006 to 30 September 2008 – in respect of commissions on the sale of holidays within the EU ("EU claim").

A further claim was made in relation to commissions received between 1 January 1997 and 31 March 2006. This claim was made in June 2009, and was the subject of a separate appeal on the question of capping.

The claims currently at issue concerned discounting packaged holidays. For example, a holiday might appear in a brochure at a price of £1,000, on which the travel agent could earn a commission of £100. To increase business, the agent might offer a discount to the customer of 5% of the brochure price. The customer would pay £950; the agent would remit £900 to the operator; the agent then accounted for output tax on the full £100 commission "received" from the operator, rather than the reduced £50 actually earned.

The arrangements are substantially the same as those considered by the CJEU in *First Choice Holidays plc* (Case C-149/01), in which it was decided that the tour operator had to account for output tax on the full amount of the margin, taking the undiscounted brochure price as the revenue. The operator would then be able to deduct the input tax charged to it by the agent on the full amount of the commission (because the selling commission does not relate to a TOMS package supply).

The essence of the appellant's argument in the current case was that the customer had only paid £950, and the VAT system was collecting output tax on £1,000, which could not be right. If the CJEU had decided that the tour operator could not recover the difference, then the agent must be able to do so. Heavy reliance was placed on the principles of *Elida Gibbs*.

HMRC put forward a number of arguments against different aspects of the claim. However, the main line was that there were separate supplies by the agent to the tour operator and by the tour operator to the final consumer. The discount was not a reduction in the value of the agent's output, because the agent was not making a supply to the final consumer. Rather it was the application of some of the (entirely VATable) consideration received from the tour operator, and the CJEU had decided that it constituted VATable third party consideration in the hands of the tour operator. *Elida Gibbs* was not relevant because the agent was not in the position of the manufacturer – it was further down the supply chain.

The Tribunal essentially accepted the HMRC arguments: *Elida Gibbs* did not apply, and the agent had received the full 10% commission before deciding to spend it on something that would not have a VAT effect – making a present to a final consumer. Although a case had been referred to the CJEU by the German courts on a superficially related matter, the

Tribunal did not consider it necessary to make a reference or to hold over the decision while waiting for that case to be decided. It was satisfied that the principles were clear, and the appeal should be dismissed.

First-Tier Tribunal (TC02493): *TUI Travel plc and others*

2.9.2 Staff agency

A trader supplied services to hauliers. His self-assessment returns disclosed turnover above the VAT registration threshold, and after enquiries he registered with effect from 1 January 2007. HMRC then backdated this to 1 January 2003; the trader submitted a return for the extended period, but on further investigation, it transpired that he had excluded invoices raised to a number of businesses. He initially claimed that these were raised to traders who had gone out of business, so he could not recover the VAT; but, when he was told that the amounts received would have to be treated as VAT-inclusive, he took advice, appealed and produced a more technical defence.

This was that many of the invoices related to drivers he had introduced to hauliers. He would receive the gross amount paid by the haulier but would pay most of it to the driver, retaining only a small commission. He considered only the commission to be his own turnover. He was a "disclosed" agent in the sense that everyone in the supply chain knew everyone else – it was clear who was doing the driving.

The Tribunal noted that there was no clear documentary evidence of the contractual relationships between the appellant, the drivers and the hauliers, and that the initial explanations given by the appellant to the investigating officers had been unsatisfactory. However, that was not surprising, given the legal complexities and the unfamiliarity of the appellant with contract and agency law. It did not indicate that the argument was false. The Tribunal was satisfied that he was in general a reliable and truthful witness, and his version of events made sense. Control over the drivers while they performed their services was exercised by the hauliers, not by the appellant. His turnover for VAT purposes was only the commission he retained, and the appeal was allowed.

First-Tier Tribunal (TC02496): *Brian Ashley Hubbard*

2.10 Second hand goods

Nothing to report.

2.11 Charities and clubs

2.11.1 Charitable purposes

A charity had as its object "the advancement of education in water, outdoor and indoor activities for young people generally". It engaged a builder to construct a new training centre on land it owned by the River Thames. HMRC ruled that the construction was standard rated. The charity appealed, arguing that the building would be used for a relevant charitable purpose. The VAT at issue was over £135,000.

HMRC's view was that the charity carried on a business, in that it charged participants for courses. The charity argued by contrast that the centre was fundamental to the fulfilment of its charitable objects, and the courses were heavily subsidised by donation income. Viewed in context, the consideration charged for the courses was not enough to make the activity a "business".

The Tribunal examined the facts in detail, including the financial information available on the costs and revenues from various activities. In many cases, courses were deliberately provided at a loss, in accordance with the charitable objects. In other cases, a surplus arose, for example on "corporate days". A schedule was provided to show the use of the disputed building. Over a period of 18 months, some 5,800 people used it, of whom just over 4% were "corporate teams".

The appellant argued that it did not satisfy the criteria of a "business" according to the *Lord Fisher* tests. Even if part of its activities were a business, the business use of the building was below the 5% de minimis test. The precedent cases of *Yarburgh Children's Trust* and *St Paul's Community Project* should be applied.

HMRC argued that the onus was on the appellant to show that it was not carrying on a business, given that it was providing services for a consideration. The VAT Directive stated that a business existed regardless of the purpose or results of the activity; and there was an implication, in the list of exemptions for charitable activities in art.132, that charities were within the scope of VAT where they provided services for consideration that were not exempt.

HMRC's counsel had the following to say about *Yarburgh* and *St Paul's*:

In the Commissioners' submission the Appellant cannot rely on the Yarburgh and St Paul's Community Project cases, where the facts were quite different, with cooperative ventures run by beneficiaries (and in the St Paul's Community Project case, the nursery undertaken for the social reasons of providing nursery education for disadvantaged and difficult children). Those cases (in the High Court) are concerned only with whether the tribunal could reasonably reach the conclusion that it did on the facts, and to the extent that they decide that a charity is not carrying on a business if its predominant concern in carrying on a particular activity is to pursue its charitable purposes, then they are wrongly decided: the question is whether the activities objectively are of a business nature, regardless of the purpose for which they are undertaken. In neither of those cases was the court directed to Articles 132 and 133 of the Directive.

The Tribunal was more willing to follow the reasoning of the judges in those cases. The reasoning of both was examined, and the *Lord Fisher* tests were applied to the current case. This was the conclusion:

Expressing the point by reference to the Lord Fisher case indicia, it is the case that the Appellant's activity is a serious undertaking earnestly pursued with reasonable continuity; and that the enterprise is substantial in size and value, and the supplies it makes (or something similar) are made by commercial enterprises; and that it adopts and applies prudent financial management. However, there are features of its activities which are not consistent with sound business principles (most obviously its use and reliance upon volunteers and its reliance upon donations to meet part of its operational costs and to meet all its capital costs); and its predominant concern is not to make taxable supplies to consumers for a consideration, but to carry out its activities in a manner which furthers its charitable objectives. The making of supplies for a consideration is incidental to its predominant concern of furthering its charitable objectives in that it is one means (admittedly an important one) by which its predominant concern is achieved.

After deciding that the overall activity of the charity was not the carrying on of a business, the Tribunal further considered the use of the building. Although the use of the upstairs for various activities which were not within the charitable objects made the question less straightforward, the Tribunal was satisfied that the overall use was for charitable purposes. The appeal was therefore allowed.

First-Tier Tribunal (TC02574): *Longridge on the Thames*

2.11.2 Red noses

The government will "give back the VAT" on this year's Comic Relief single. This is achieved by the Department for International Development making a charitable donation which is the equivalent of the VAT – it is not possible under EU law to grant a specific exemption to such a supply.

www.number10.gov.uk/news/comic-relief-single-government-give-back-vat

2.12 Other supply problems

2.12.1 Goods or services?

A company ran a website which offered goods for sale. Customers could subscribe for a "Redsave pass" which entitled them to lower prices. The pass cost £19.95 per month after an initial free period. The company accepted that this was standard rated in months during which a customer bought something at the discounted price; however, it did not account for output tax in months in which no purchases were made. HMRC disagreed, and assessed for more than £1m of unpaid tax in respect of the period from the commencement of trade on 1 September 2006 to March 2010.

The company's arguments were based on *Societe Thermale d'Eugenie-les-Bains* (Case C-277/05). Counsel argued that in the months when the discount facility was used, the £19.95 was part of the consideration for the supply of the goods which were purchased at the reduced price; when it was not used, it was in effect a forfeited deposit, or a payment of compensation to the website.

The Tribunal rejected these contentions in a very brief decision. The discount right was not related to the purchase of goods, but was a separate transaction. It constituted a standard rated supply whether it was used in a particular month or not. The company's appeal was dismissed.

First-Tier Tribunal (TC02470): *Nettexmedia.com Ltd*

2.12.2 Scale rates

The Value Added Tax (Consideration for Fuel Provided for Private Use) Order 2013 has amended the scale charges for use of business fuel on which input tax has been recovered in an employer's car. The new rates take effect for periods beginning on or after 1 May 2013. The charges have increased by a very small amount, approximately 1%.

Note that, although these charges and income tax chargeable car benefits are both based on carbon dioxide emissions, the relationship between the VAT and income tax rules has diverged very substantially in recent years. In particular, income tax now distinguishes between several bands of emissions below 120g/km, and reaches the maximum at 215g/km; there has been no change in the VAT bandings for three years, so:

- "low emissions" of up to 120g/km enjoy a special low rate;
- there are then banded increases at each 5g/km up to 225g/km, which is still the maximum for VAT.

SI 2013/659

2.12.3 Reverse charges

HMRC have issued a new version of their Notice *VAT reverse charge for mobile phones and computer chips*, replacing the June 2008 version. It has been rewritten to include details of the reverse charge procedure for emissions allowances, to address situations where supplies are disaggregated, and to improve general readability.

Notice 735

3. LAND AND PROPERTY

3.1 Exemption

3.1.1 Rooms in hotels

HMRC have issued a Brief to confirm their view on the provision of rooms in hotels for the purposes of a supply of catering. In the past, they took the view that this could be an exempt supply by the hotel, provided that the supply of catering was made by someone else; they now consider that the provision of accommodation in an hotel, inn, boarding house or similar establishment for the purpose of catering is standard rated regardless of whether the catering is provided by the operator of the hotel, etc, or by another person.

This view was published in an updated version of Notice 709/3 in October 2011. However, they do not propose to enforce it where people have treated such supplies as exempt up to the date of the Brief, 22 January 2013. No assessments will be issued and no action will be taken to correct past periods, but everyone is expected to operate the new policy from that date.

R & C Brief 02/13

3.1.2 Caravan pitches

A company which has been in dispute with HMRC before made a *Fleming* claim in respect of VAT accounted for on caravan pitches between April 1989 and December 1996. A similar claim had been made in 2004 in respect of the periods from March 2001 to December 2003 – that was allowed in the VAT Tribunal, but HMRC overturned that decision on an appeal to the High Court which was heard in 2007.

The point at issue was whether the caravan pitches were subject to a restriction preventing year-round occupancy. The taxpayer argued that the stated restrictions in planning regulations were not enforced, with the effect that there was no actual restriction. The VAT Tribunal accepted that, after the council had not taken action for some time, it would no longer be able to do so: in effect, what was written in the planning consents had become ineffective.

In the 2007 proceedings, the High Court disagreed with this approach. The clear wording of the law was that the exemption depended on there being no prohibition on year-round occupation in the planning consent. There was such a prohibition. Whether it was enforced or not was not relevant, because that was not the law.

The new case was argued mainly by a shareholder who had invested in the caravan park in 2004. He had gathered what evidence he could to support the assertion that there was no planning restriction on year-round occupation from 1989 to 1996.

HMRC argued that this was an attempt to re-litigate an issue that had been decided against the company in 2007. The Tribunal decided not to rule on that question, but examined the evidence offered by the company. It did not find it sufficient to justify a conclusion that there was no planning restriction in place. The decision therefore had to be the same as that in the 2007 case: the pitch rentals were properly standard rated, and the appeal was dismissed. The question of unjust enrichment, which HMRC also pleaded as a defence, therefore did not have to be considered.

First-Tier Tribunal (TC02575): *Tallington Lakes Ltd*

3.2 Option to tax

Nothing to report.

3.3 Developers and builders

3.3.1 Planning conditions

A company purchased a Grade 2 listed school with the intention of developing it. The company engaged a building firm to convert a separate building in the grounds into residential accommodation. The builder treated the work as zero-rated, but HMRC objected, noting that the planning permission prohibited the separate use of the building.

The Tribunal agreed with HMRC's interpretation, applying the Upper Tribunal decision in the case of *Lunn* (Upper Tribunal 2010). The decisions in *Phillips* (TC01227) and *Wendels* (TC00737) were specifically disapproved by the judge. In those cases, a requirement for the building to be occupied by someone employed in a nearby business was held to be an occupancy condition but not to impose a restriction on separate use or disposal. The judge approved a comment in a different case, *Holden* (FTT 2012 – not given a TC number and possibly unpublished), that occupancy and use are effectively the same thing.

The company also tried to make something of a change in the wording of Notice 708 between February 2008 and the November 2011 version. The planning permission had been obtained in July 2011, and it appeared that the officer had been looking at a later version of the Notice when making the decision appealed against. The Tribunal agreed with HMRC that it did not have jurisdiction to consider an appeal based on the application of an ESC (presumably misdirection) or the legitimate expectations of the taxpayer.

First-Tier Tribunal (TC02455): *Brims Construction Ltd*

3.3.2 Annexe?

An individual arranged for the construction of what was described in the planning application as a "replacement garage/guest annex" adjacent to his Grade 2 listed home. This involved razing an old garage to the ground and building a new structure on its footprint. It was not physically connected to the main building, and contained a workshop, store room, studio, bathroom and utility room.

Surprisingly, the planning consent did not impose any restrictions on separate use or disposal of the new building, and both parties agreed that it was "self-contained living accommodation". The Tribunal rejected an argument by HMRC that restrictions should be read into the planning consent: if they were not there, they could not be assumed to apply.

However, the Tribunal agreed with HMRC that the new building was an "annexe" within the meaning of Sch.8 Group 5 Note 16(c), and the builder should not have zero-rated the construction work. This was in accordance with the decisions of the High Court in the two appeals by Mr and Mrs Cantrell in respect of their construction of an additional building adjacent to a care home. The applicable principle required consideration of the two buildings together: it was not enough just to look at the new building and consider whether it could be used independently, but whether it was "*a supplementary structure, an adjunct or accessory to the main house. There is, in our view, a functional connection between the new building and the main house sufficient to render it an annexe. The new building is designed to meet the deficiencies of the main house and to operate in conjunction with it.*"

First-Tier Tribunal (TC02465): *Stephen Colchester*

3.3.3 Listed building

An individual obtained planning consent for the replacement of windows in his listed home with triple-glazed units. He applied for a ruling that this would count as a zero-rated alteration; HMRC, relying on their internal guidance at the time, decided that it was "repairs or maintenance", and was therefore standard rated. The individual appealed, and HMRC decided not to contest the appeal after a change in their guidance. The supplier of the windows charged the individual £500 for helping with the appeal, and the individual applied to the Tribunal for costs. He also asked for a hearing so that the decision could be formally ratified.

The Tribunal agreed that these were not works of repair or maintenance, not least because the existing windows were in good condition and did not need replacement. However, it was not automatically the case that any wrong statement in relation to an appeal was "unreasonable"; had the facts been found to be slightly different, HMRC's argument might have succeeded. As the only grounds on which the Tribunal could award costs would be unreasonable conduct of HMRC in relation to the proceedings, the application for costs was refused.

First-Tier Tribunal (TC02499): *Leslie Wallis*

3.3.4 Building materials

HMRC ruled that "fire curtains" (retractable fire barriers) were not "building materials" because they were not "ordinarily incorporated into buildings by builders". They could not therefore be included in a zero-rated sale of a new dwelling.

The Tribunal examined the background to the development of fire curtains as a form of fire protection which provided an alternative to fire doors. HMRC argued that they were not yet "ordinary". The Tribunal had to consider how that should be measured – whether it meant “commonly”, and whether it was necessary to consider all dwellings, or just a subset of dwellings (only exceptionally large two-storey dwellings, and dwellings of three storeys or more, require fire protection at all).

After considering a number of precedent cases, the Tribunal decided that fire protection should be regarded as something ordinarily incorporated, and fire curtains were, on the evidence, an increasingly common way of providing that protection. They therefore satisfied the definition.

Although the operation of the curtain involved electricity – they are triggered by a fire alarm breaking an electrical circuit – they then deploy under their own weight and gravity. They have an electric motor to retract them after the threat of fire has been removed, but they are not “electrical appliances”. There was therefore no reason to exclude them from zero-rating.

First-Tier Tribunal (TC02570): *Coopers Fire Ltd*

3.4 Input tax claims on land

3.4.1 Separate use or disposal: occupancy restrictions

Another case in the series considered at 3.3.1 above was decided in favour of HMRC. An individual constructed a house on land adjacent to a caravan park. The planning consent stipulated that it should only be occupied by someone who worked in the caravan park as a site manager or other essential worker.

The Tribunal came to the same decision for the same reasons: the judge approved the comment in *Holden* that “occupation and use are effectively the same thing”. The appellant asked for an adjournment while he tried to get the planning condition removed, but the Tribunal considered that this would not help him – it had applied for at least 3 years, and was in place when the construction project took place. It denied a DIY claim.

First-Tier Tribunal (TC02456): *Robert Drummond*

Another similar case was decided in favour of the claimant. An individual obtained planning consent to construct a house on some land adjacent to a lake on which he ran a fishing business (granting day licences to anglers). The consent was granted on the grounds that there was a business case for someone needing to live on the site; a condition was imposed that “*The occupation of the dwelling shall be limited to a person solely or mainly employed or last employed in Park Hall Lake Fishery or a widow or widower of such a person, or any resident dependents*.”

HMRC argued that the planning application was evidence that the building was constructed in the course or furtherance of the fishing business (which could possibly have recovered VAT as a result, but it was trading below the registration threshold and was not registered). The Tribunal accepted that what was said in the planning application was relevant, but was not necessarily conclusive for VAT. It was likely that the application would have put arguments forward in the best possible light; without saying that it was misleading, it might have overstated the connection to the business.

The Tribunal did not have access to the above decision, but rather followed the earlier Tribunal decision in *Wendels*, holding that an occupancy restriction was not a prohibition of separate use or disposal. The appeal was allowed.

First-Tier Tribunal (TC02522): *Mr Richard Burton*

Yet another case on similar facts went in favour of the appellant. This concerned the construction of a house on the site of an equestrian business run by the appellants; the planning consent provided that "*The occupation of the dwelling shall be limited to a person or persons employed in the operation of the adjoining equestrian centre*," giving as a reason "*The provision of a dwelling for unrestricted residential purposes on an isolated rural site would be contrary to planning policy.*"

As in the above case, the current Tribunal followed *Wendels* and declined to follow *Holden*. The chairman considered that the conditions in *Holden* were more specifically related to separate use or disposal; those here were merely occupancy conditions, as in *Wendels*, and did not prohibit separate use or disposal.

First-Tier Tribunal (TC02510): *Nick Bull*

3.4.2 Live/work units

A married couple owned a large house in whose grounds stood five commercial buildings. They demolished two of them and converted the remaining three into a single "live-work" unit. In effect, one of the three buildings was converted into a work space and the other two became the residential area. The planning consent imposed conditions on the relative sizes of the residential and work areas, and also required that the work use should commence not later than the residential occupation.

The district valuer decided that the commercial part was too small to warrant separate rating for business purposes, and classified the whole structure as residential. The couple applied for a DIY refund in relation to the conversion costs. HMRC refused, on the grounds that there was an implicit condition in the planning consent that the residential part could not be used or disposed of separately from the work area, and it was therefore not a "dwelling" for the purposes of the VAT law.

The Tribunal did not agree with HMRC that there was either an implicit or explicit restriction on separate disposal in the planning consent; however, there was an explicit restriction on separate use, and the appeal therefore had to fail. The Tribunal agreed with the chairman in *Holden*, who commented that it appeared unlikely that any live-work units could qualify as dwellings, and also suggested that HMRC's guidance relating to live-work units in Public Notice 708 at paragraph 15.4 is misleading.

The Tribunal also found that the occupation of the property was in breach of the planning consent, because it was not being used in connection with a business carried on from the work area. This was also enough to deny the DIY claim.

First-Tier Tribunal (TC02513): *John and Susan Kear*

The opposite conclusion was reached in another case. Here, there were two commercial buildings on a site. One was converted to residential use, while the other remained subject to commercial use planning permission. There was a restriction on the occupation of the commercial building – it was only to be used by the occupier of the residential property. The effect of the condition was that in practical terms it was extremely unlikely that the residential dwelling would be used or disposed of separately from the commercial dwelling. It did not however on its face impose any express restriction on the separate use or disposal of the residential dwelling.

When asked to undertake a statutory review of their decision to disallow the DIY builder's claim, HMRC wrote to the council, asking for an explanation of the planning condition. The council replied:

"*Your interpretation of the planning condition is correct, and the Local Planning Authority consider the two buildings as a single live/work unit, and the separate disposal of the dwelling would not be permitted.*"

The Tribunal considered the *Kear* decision above. The appellant argued that it was irrelevant, because in that case the planning consent was more explicit: it placed a restriction on the residential part. This consent only placed a restriction on the commercial part, which was not the subject of the DIY claim. It was possible – even if probably not sensible – to sell the residential part and retain the commercial part, leaving it empty, and still comply with the planning consent as it was written.

The Tribunal agreed with the appellant. The views of the planning authority carried no weight: they had not put any prohibition on separate use or disposal of the residential part in the planning consent, and they could not afterwards claim that it was implied by what they had included in relation to the commercial part. The appeal was allowed.

First-Tier Tribunal (TC02601): *Anthony Barkas*

3.5 Other land problems

Nothing to report.

4. INTERNATIONAL SUPPLIES

4.1 E-commerce

4.1.1 Special scheme

HMRC have issued an Information Sheet to inform those registered under the special scheme for e-traders that the standard rate of VAT in Finland increased from 23% to 24% with effect from 1 January 2013.

Information Sheet 19/12

HMRC have also published the usual table of exchange rates to be used by those registered under the special scheme for the quarter to December 2012.

Information Sheet 01/13

4.2 Where is a supply of services?

4.2.1 Cross-border storage facilities

Following the cases about self-storage services in the UK, and the HMRC statement about changes to their policy on the treatment of services connected with land in Revenue & Customs Brief 22/2012, the Advocate-General has given an opinion about the place of supply of cross-border storage facilities.

The company provides services for the storage of goods to undertakings established in other Member States of the European Union and in non-member States. Those services include admitting the goods to the warehouse, placing the goods on storage shelves, storing the goods, packaging the goods for the customer, issuing the goods, unloading and loading. The service may also include repackaging materials supplied in collective packaging into individual sets.

The Polish authorities took the view that this was a supply connected with immovable property and would therefore be taxable in Poland. The company appealed, contending that it was a standard business-to-business supply which would be subject to VAT where the customer belonged. Questions were referred by the Polish courts to the CJEU.

Advocate-General Kokott considered first whether there was a single supply or a series of independent individual supplies. She considered that this was primarily a question for the referring court; however, it seemed compelling that the warehousing of goods was a principal supply to which the various other aspects would be ancillary, with the possible exception of repackaging goods if that was not simply to achieve a better storage solution.

She went on to discuss whether there was a "sufficiently direct link" between the immovable property and the services to satisfy the requirements of art.9(2)(a) 6th Directive/art.47 PVD. It would not be enough for there to be a requirement that the services were supplied in a particular place – that would be common for supplies of services which would be carried out in the business premises of the supplier. Rather, "specifically determined immovable property must also be the subject-matter of the service, that is to say, the immovable property is the object of the supply."

Her proposed answers to the questions referred were as follows:

1. Application of Article 47 [PVD as amended by the VAT package] requires that the subject-matter of the service be the use of, work on or assessment of specific immovable property or that the service be explicitly listed in that provision.

2. Complex services relating to the storage of goods fulfil these requirements only if the storage of the goods is the principal supply of a single service and it is connected with a right to use specific immovable property or a specific part of such property.

CJEU (A-G) (Case C-155/12): *Minister Finansów v RR Donnelley Global Turnkey Solutions Poland Sp. z o.o.*

4.2.2 Budget changes

HMRC have published a list of questions and answers relating to the changes to VAT place of supply rules which are due to be introduced in the Finance Act 2014 to take effect on 1 January 2015, in accordance with the VAT Package.

The first of two changes is described as follows: "*The first affects the VAT place of supply rules and will mean that supplies of telecommunications, broadcasting and e-services made by a business established in one EU member state to a private consumer located in another member state ("intra EU B2C supplies") will be taxed in the member state in which the consumer is located. These services are currently taxed where the business is established. This will ensure that these supplies are taxed fairly in the member state of consumption.*"

The second change is the introduction of the "Mini One Stop Shop", which is an IT system being developed that will give businesses the option of registering in the UK from where they can account for VAT due in all member states by submitting a single return to HMRC.

Few details are given at this stage, but a consultation is promised.

http://www.hmrc.gov.uk/budget2013/vat-place-supply-rules.pdf

4.3 International supplies of goods

4.3.1 Onward Supply Relief

A UK company acted as a marketing arm of a French sister company, distributing products such as popcorn and snacks for it in the UK. In a one-off transaction in June 2009, it imported some goods from outside the EU into the UK. They were paid for by the French company, which also arranged for them to be transported from the UK to France. The UK company was not party to the contract of purchase and did not have title to the goods at any time. The UK company only telephoned a freight forwarder in Felixstowe to pass on instructions from the French company.

The goods were declared at importation under the code for Onward Supply Relief, and the company did not include them in its EC Sales List or VAT returns. HMRC wrote to the company in October 2010 asking for further information about its OSR claim, and subsequently issued a post-clearance demand for £1,000 on the grounds that the transaction did not qualify.

In line with the decision in *Brooklands International Freight Services Ltd* (TC00587), the Tribunal agreed with HMRC that Onward Supply Relief is only available if the importer takes title to the goods and makes a supply. The chairman expressed sympathy with the appellant's director, who described the import VAT as a "penalty which unjustly enriched HMRC", but there was no flexibility in the law.

First-Tier Tribunal (TC02454): *Finger Foods Ltd*

Meanwhile, HMRC have issued an updated Notice on the subject, replacing the April 2010 version. The new version makes it clearer that a VAT registered importer acting as agent in an onward supply must be "acting in his own name" in relation to that supply, which seems to relate specifically to the problems in the above case and the *Brooklands* dispute that preceded it.

It has also been changed to address changes to the way VAT identification numbers are entered in box 44 of the import declaration.

Notice 702/7

4.3.2 Relief on importation?

An individual imported a motor-cruiser from Jersey for use by his disabled son. HMRC ruled that import VAT was due; he appealed, arguing that it should be zero-rated by reason of Sch.8 Group 12 Item 2(i).

The Tribunal observed that the adaptations to make the cruiser useable by the son had not been carried out at the time of importation. As a result it did not qualify for the relief at the relevant time. The appeal was dismissed.

The appellant argued that the public notices (371 and 701/7) were not sufficiently clear. He had been given misleading advice on the telephone. However, the Tribunal observed that he had not read the notices, nor received the advice, before he had bought and imported the boat. He could justifiably feel aggrieved that he had been led to believe that he would not have to pay the VAT (and HMRC then appeared to forget about it for over a year); however, that did not mean it was not due.

The Tribunal also considered that the alterations in fact made to the boat were not sufficiently substantial to qualify for zero-rating; that the fact that the boat would be used by the family in general, as well as by the disabled son, meant that it was not "supplied to" or "for the personal use of" the disabled person.

First-Tier Tribunal (TC02515): *William Cadbury*

4.3.3 New rules for road vehicles

The Value Added Tax (Amendment) Regulations 2013 give effect to legislation introduced in FA 2012, s 202 from 15 April 2013. A person bringing a land vehicle into the UK will, subject to certain specified exceptions, have to notify HMRC within 14 days of the arrival of the land vehicle in the UK. This is intended to cut down on fraud involving the movement of vehicles between countries.

SI 2013/701

4.3.4 Updated Notices

HMRC have issued an updated version of the *Intrastat General Guide*. It includes advice that Croatia is expected to join the EU with effect from 1 July 2013. From that date, goods moving between the UK and Croatia will be subject to intrastat declarations.

The threshold for the low value consignment simplification procedure has been changed to £160 from 1 January 2013.

Notice 60

HMRC have also updated their *Guide for international post users*. This shows the reduction in the relief for small items sent as gifts from £40 to £36 from 1 January 2013 (resulting from exchange rate movements – the figure is supposed to be fixed in euro).

Notice 143

HMRC have updated their Notice *Valuation of imported goods for customs purposes, VAT and trade statistics*. The amendments include:

- changes to the treatment of buying commission for import VAT purposes;
- how to revalue goods that have devalued whilst in a customs warehouse;
- the treatment of surcharges relating to Air Transport Costs.

The notice is now available online only – there is no printed version.

Notice 252

HMRC have updated their Notice *Customs: Export Procedures*. The amendments listed are:

- The low value threshold will be reduced from £900 to £800 on 1 January 2013 (paragraphs 10.1 and 10.4);
- A CHIEF change has accommodated the full ARC number for excise goods (paragraphs 11.2 and 11.3).

Notice 275

4.4 European rules

4.4.1 Right of deduction

A Bulgarian company claimed input tax in relation to several invoices which purported to describe purchases of goods. The authorities rejected the claims on the grounds that there was insufficient evidence that the transactions had taken place; the "suppliers" had subsequently been deregistered. There were discrepancies in the records of the transactions submitted by claimant, and the suppliers had not complied with their reporting requirements.

The company appealed, contending that they had an absolute right to deduct the input tax. The authorities had issued tax adjustment notices to the suppliers which did not correct the disputed transactions, so the company argued that the authorities had in effect accepted that the transactions had taken place as described.

The CJEU pointed out that the supplier and purchaser are not treated identically for VAT purposes. A supplier who mentions VAT on an invoice is liable to pay it whether the transaction took place or not, but the authorities can refuse a deduction to a purchaser if the invoice does not reflect the facts. This apparent inequality can be allowed for by the supplier issuing corrective documents and claiming back any VAT accounted for in error. The failure of the authorities to correct the supplier's declaration could not be taken as confirmation or acceptance that the transactions had taken place.

The general principles for deduction of VAT in such circumstances applied: if the purchaser could not reasonably be expected to know or have the means of knowing that the transactions had not taken place as described in the invoices, the input tax should be allowed. It would be for the referring court to determine whether this was the case.

CJEU (Case C-643/11): *LVK-56 EOOD v Direktor na Direktsia 'Obzhalvane i upravlenie na izpalnenieto' – grad Varna pri Tsentralno Upravlenie na Natsionalnata Agentsia za Prihodite*

A similar decision was reached in another case on similar facts.

CJEU (Case C-642/11): *Stroy Trans EOOD v Direktor na Direktsia Obzhalvane i upravlenie na izpalnenieto – Varna pri Tsentralno upravlenie na Natsionalnata agentsia za prihodite*

4.4.2 Spanish reduced rate

Spain has allowed a reduced rate to be applied to a range of healthcare supplies, including appliances and ingredients for medicines, and treatments for animals as well as humans. The Commission took infringement proceedings, arguing that this was not in accordance with the VAT Directive (in particular, art.98 and Annex III).

The CJEU has upheld all four of the Commission's complaints:

- that the Spanish rules allowed relief on too general a basis – the exemption was intended to benefit only final consumers, not manufacturers of medicines;

- that the Spanish definition of "pharmaceutical products", which included appliances as well as medicines, was too broad – appliances could be reduced-rated only if they were for the alleviation of disability, not merely illness;
- that the Directive only authorised a reduced rate for appliances intended for disabled humans, not for treating disabilities in animals (although animal medicines can be lower rated);
- that the Directive only authorised a reduced rate for apparatus and accessories essentially or primarily used to treat human disabilities, which are intended for the exclusive personal use of the disabled person – again, Spain allowed the rate to apply to a wider category of goods.

CJEU (Case C-360/11): *European Commission v Spain*

4.4.3 Building land

In the Netherlands, a supply of "building land" is not exempt from VAT, in accordance with the provisions of the VAT Directive (the UK continues to exempt building land, subject to the option to tax, under transitional rules in force when the 6th Directive was implemented). If a land transaction is exempt from VAT, a transfer duty applies; to avoid double taxation, the transfer duty is not charged where VAT is due.

An organisation purchased a piece of land from a local authority with the intention of building houses. The vendor authority undertook to demolish an existing building and to remove the rubble. The question was whether the result was "building land", chargeable to VAT and exempt from transfer duty, because there was an intention to build on it; or whether it was not building land, because it had previously been built on.

The court noted that this was one of those situations where it was necessary to interpret the terms used in an exemption. These should be interpreted strictly, but not so strictly as to deprive them of their intended effect. In that light, it was in accordance with the purpose of the provision to exclude from exemption a transfer of land where there was an intention to build on it, even if there had been a previous building on the land which had been demolished, and even if (as in the present case) there was a car park on the land which was intended to be removed in order to make further construction possible.

It was for the referring court to determine whether there was in fact an intention to build on the land at the time of the transfer; that appears to be what makes something "building land" for the purposes of the Directive.

CJEU (Case C-543/11): *Woningstichting Maasdriel v Staatssecretaris van Financiën*

4.4.4 Deferral of VAT

A Romanian company imported goods from France under a temporary admissions procedure which allowed deferral of import duty and VAT. The importation took place in 2006, before Romania joined the EU. The conditions for deferral of the VAT expired, and the Romanian authorities demanded the tax two years later, after the country had joined the EU.

The company argued to the CJEU that the conditions for deferral of import VAT in Romania were unduly restrictive and discriminatory (requiring the importer to obtain a particular certificate from the authorities), and were therefore not in compliance with art.211 Principal VAT Directive. The Court disagreed: art.211 allows member states to impose detailed rules for payment of import VAT, and requiring a certificate was within the scope of a state's discretion, as long as it was exercised in accordance with the principles of fiscal neutrality.

A separate argument, that the rules contravened the Treaty on the Functioning of the EU, was struck out as inadmissible.

CJEU (Case C-79/12): *SC Mora IPR SRL v Directia Generala a Finantelor Publice Sibiu, Directia Judeteana pentru Accize si Operatiuni Vamali Sibiu*

4.4.5 Penalties

A Swedish national was found to have been involved in serious VAT evasion. He was charged a tax penalty under administrative rules, then prosecuted and charged a criminal penalty as well. He argued that this was in contravention of art.50 of the Charter of Fundamental Rights of the European Union, which provides that a person cannot be prosecuted twice for the same offence (referred to as 'ne bis in idem').

The CJEU ruled that this was not so, as long as the first penalty was not a criminal one, which it was for the national court to determine in line with various precedents and principles set down by the Court. It was open to member states to levy civil or criminal penalties for tax evasion, or a combination of the two.

CJEU (Case C-617/10): *Åklagaren v Hans Åkerberg Fransson*

4.4.6 Hot dogs (and horses)

The CJEU has agreed with the Commission that Ireland was in breach of the Directive in applying a lower rate of VAT (4.8%) to various supplies of dogs and horses that were not intended for human consumption, and to the hire of horses and artificial insemination.

Art.110 Principal VAT Directive allows Member States which, at 1 January 1991, were granting exemptions with deductibility of the VAT paid at the preceding stage or applying reduced rates lower than the minimum laid down in art.99 (5%) may continue to grant those exemptions or apply those reduced rates.

The exemptions and reduced rates referred to in the first paragraph must be in accordance with Community law and must have been adopted for clearly defined social reasons and for the benefit of the final consumer.

The Irish Finance Minister had made statements about the introduction of an exemption in 1973 and the lower rate in 1990 that suggested that the rules were for the economic protection of the sectors concerned rather than for "clearly defined social reasons".

In addition, it appeared that many of those who benefited from receiving supplies charged at the lower rate were economic operators (including farmers subject to the flat-rate scheme) rather than final consumers.

As art.110 was an exception to the general rules of VAT, it had to be strictly interpreted. As a result, the Commission's case was well founded, and its application for a declaration that Ireland was in breach of its treaty obligations was granted.

CJEU (Case C-108/11): *Commission v Ireland*

4.4.7 French navigation

The Commission has also succeeded in an action against France over the rules for exempting supplies for ships which are used for carrying passengers for reward, without requiring that those ships are used for navigation on the high seas as required by art.148 Principal VAT Directive. The French authorities changed the tax law in 2011 to include this wording, but maintained an administrative interpretation that allowed traders to continue to benefit from the old wording. The CJEU declared that this was unacceptable.

CJEU (Case C-197/12): *Commission v French Republic*

4.4.8 Proportion for partial exemption

A French bank included loan interest charged to its foreign branches in its calculations of input tax recovery. The authorities objected, arguing that the branches were part of the same legal entity (*FCE Bank*), so interest charged to them had to be ignored for VAT purposes. The bank countered by arguing that, in that case, the turnover of the branches should be included in the pro-rata calculations for recovery in France. Questions were referred to the CJEU.

The Advocate-General has given an opinion that member states are not obliged to have rules which include foreign branches' turnover in a domestic input tax recovery calculation. EU branches will be subject to their own pro rata calculations in the states in which they are established; branches outside the EU are effectively separate sectors for the purposes of partial exemption, and should therefore not be included in a French calculation.

CJEU (A-G) (Case C-388/11): *Société le Crédit Lyonnais v Ministre du budget, des comptes publics et de la réforme de l'Etat*

4.4.9 References

The Swedish court has referred questions to the CJEU about the VAT consequences of supplies purchased by its US parent company and transferred to it:

Do supplies of externally purchased services from a company's main establishment in a third country to its subsidiary in a Member State, with an allocation of costs for the purchase to the subsidiary, constitute taxable transactions if the subsidiary belongs to a VAT group in the Member State?

If the answer to the first question is in the affirmative, is the main establishment in the third country to be viewed as a taxable person not established in the Member State within the meaning of Article 196 of the Directive [1], with the result that the purchaser is to be taxed for the transactions?

These questions appear to relate to the problem of the foreign holding company being part of the domestic VAT group by virtue of having an establishment in the country. This was dealt with by legislation in the UK some years ago, and a concession in relation to the detailed workings of the rules has recently been incorporated in the law.

CJEU (Reference) (Case C-7/13): *Skandia America Corporation USA, filial Sverige v Skatteverket*

The French appeal court has referred a question about the operation of the 8th Directive to the CJEU:

Does Article 2 of [the] Directive [79/1072/EEC of 6 December 1979] infringe freedom of establishment in that it limits entitlement to a refund to just moveable property?

Presumably one possible answer is that the acquisition of immovable property creates a presence in the member state that ought to deal with VAT in the same way as other established businesses, by registering and completing VAT returns. The CJEU will have to decide whether it is acceptable to treat businesses mainly established abroad differently from those mainly established in the country.

CJEU (Reference) (Case C-618/12): *Reggiani SpA Illuminazione v Ministre de l'Économie et des Finances*

Questions have been referred by the Belgian courts about the operation of the "standstill clauses" which allowed member states to keep certain rules which were in force before the adoption of the 6th Directive. Belgium changed its legislation on 1 December 1977 to tax supplies of transport outside the EU. This was before the 6th Directive came into effect (1 January 1978), but after it had been adopted and its terms were known. The change was therefore specifically to circumvent the new law and to attempt to take advantage of the standstill clause.

CJEU (Reference) (Case C-599/12): *Jetair and BTW-eenheid BTWE Travel4you*

The Polish court has referred an interesting question about the place of establishment of a business which provides facilities to another business in another member state:

For the purposes of the taxation of services supplied by company A, which is established in Poland, to company B, which is established in another Member State of the European Union, in circumstances where company B carries out its economic activity by making use of company A's infrastructure, is the fixed establishment within the meaning of Article 44 of Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax situated in the place in which company A is established?

CJEU (Reference) (Case C-605/12): *Welmory Sp. z o.o. v Dyrektor Izby Skarbowej w Gdańsku*

A number of detailed questions have been referred by the Bulgarian courts to clarify the rules relating to tax evasion. The underlying situation appears to be one in which a business has raised invoices for services that it could not possibly have supplied. It seems likely that the UK authorities would robustly agree with the proposition that a fictitious supply cannot possibly give rise to a right of deduction on the basis of documentation alone.

CJEU (Reference) (Case C-18/13): *'Maks Pen' EOOD v Direktor na Direktsia 'Obzhalvane i izpalnenie na proizvodstvoto' pri Tsentralno Upravlenie na Natsionalnata Agentsia po Prihodite - gr. Sofia*

4.5 Eighth Directive reclaims

Nothing to report.

5. INPUTS

5.1 Economic activity

5.1.1 Statutory body

The South African Tourist Board registered for VAT and reclaimed input tax. HMRC ruled that it was only entitled to 15% of its claim, on the grounds that it was a statutory body which was 85% funded by grants from the South African government. To that extent, it did not make supplies for a consideration.

The Board appealed, arguing that it was not like a government department – "it was entrepreneurial and target-focused with considerable autonomy from the South African Government. It acted like a public company, just one which happened to have the South African Government as its major customer (and shareholder)." It should therefore be regarded as making supplies of marketing services to its shareholder, rather than acting in the capacity of a state-funded non-economic entity.

After a detailed examination of a number of precedent cases and the structure of the Board's operations, the Tribunal agreed with HMRC's analysis. It followed the decision of the VAT Tribunal in *Turespana* (VTD 14,568) and disagreeing with those in *Netherlands Board of Tourism* (VTD 12,935) and *Austrian National Tourist Office* (VTD 15,561). The funds provided by the governments in those cases had been earmarked for particular purposes and could not be used for anything else: there did not appear to be "economic activity" or a direct link between "supply" and "consideration". In respect of what it did for the government, the Board was not "primarily concerned with making supplies for consideration".

The judge commented that the decision was not based on art.13 PVD (government bodies being treated as non-taxable persons). That provision was engaged when a government body was involved in making supplies for consideration, usually to third parties. In the present case, she had decided that the Board was not making supplies for consideration when it received funding from the South African government, so art.13 was not applicable.

First-Tier Tribunal (TC02431): *South African Tourist Board*

5.1.2 Home electricity production

Questions were referred by the Austrian court about the possible VAT liability of a householder who installs solar panels on his house. The Advocate-General has given an opinion that this is economic activity – and therefore capable of input tax deduction and a liability to output tax, subject to local rules on registration – where the electricity generated is sold to the national grid for consideration.

The Advocate-General suggests that there is an important difference between a situation in which a householder installs solar panels which only reduce electricity bills (not an economic activity) and one who does so in order to generate income by selling surplus electricity to the grid, whether that is achieved by selling all the electricity and buying back what is needed, or by selling only the surplus at any particular time, and topping up a shortfall by buying electricity from the grid. The second situation is subject to all the rights and obligations of a taxable person in the member state concerned.

The opinion goes on to consider the effect of the private consumption on the right to deduct input tax – the Advocate-General points out that the expenditure was incurred in 2005, before the introduction of art.168a which allows member states to make adjustments to input tax on capital goods dependent on the extent of business and private use. It seems that the *Lennartz* approach would have been appropriate in 2005 – full deduction followed by output tax charges to reflect private consumption.

Lastly, the opinion considers the relevance of a substantial grant which was paid to the individual. Precedent case law on grants suggested that this should be ignored in determining the right to deduct input tax.

CJEU (A-G) (Case C-219/12): *Finanzamt Freistadt Rohrbach Urfahr v Unabhängiger Fianzsenat Außenstelle Linz*

5.1.3 No activity

A company registered for VAT in August 2011, stating that its activities would be "accountancy services". In its first VAT return it claimed input tax of £12,518; £12,500 was disallowed by HMRC. Of this, £11,600 related to the purchase of an industrial freezer which was installed in Malawi, and £900 related to the purchase of a car.

The Tribunal agreed with HMRC's view. It was not clear that the company had made a supply of the freezer to a customer in Malawi. If it had, the documentation suggested that its own supplier had made the supplier of the freezer outside the UK, so VAT should not have been charged, and it could therefore not be reclaimed. The car was subject to the input tax block in the normal way and for the normal reasons: it was available for private use.

First-Tier Tribunal (TC02474): *Myaccounts.com Ltd*

5.2 Who receives the supply?

5.2.1 Loyalty points win in the end

The Court of Justice gave its answer in the *Loyalty Management* case (now called *Aimia*) about Nectar points in the third quarter of 2010. The decision appeared to have gone against the taxpayer, as explained below. Nevertheless, it was for the referring court to come to a final decision; the House of Lords has now done so, and has held (by a 3-2 majority) that the input tax was deductible.

The Court of Appeal gave judgment in the case (mainly favouring the taxpayers) in late 2007; the House of Lords referred questions to the ECJ in 2008, and HMRC published Revenue & Customs Brief 46/08 to set out their view on what people involved in loyalty schemes should do while waiting for a decision.

The following notes set out the background to the dispute before analysing the court's decision. It is not yet clear what has happened to the *Baxi* appeal, which was joined with *LMUK* by the CJEU.

5.2.1.1 Loyalty Management

A company ("promoter") operated a sales promotion scheme designed to reward regular customers of a variety of different retailers. Customers who bought goods or services from certain suppliers ("sponsors") received "loyalty points" which could be used to obtain goods or services from other specified suppliers ("redeemers"). The promoter paid the redeemers for the goods or services, and claimed input tax on these costs.

HMRC argued that the input tax was not recoverable by the promoter, because the supplies were made to the customers, not to it. The Tribunal allowed the company's appeal: "*the proper analysis of the transaction under which a supplier provides goods to a customer in return for points is that the supplier is providing a service to the appellant in assisting it to discharge its obligation to customers that they can acquire rewards in return for points*". The company was "*a taxable person in the chain of supply so that the supply of the secondary goods is from the supplier to the appellant in the course of the appellant's business for a consideration and from the appellant to the customer*".

HMRC appealed, and the High Court upheld their original decision. The judge ruled that the supplies under the scheme were "*rewards to collectors rather than a supply to [the promoter]*". One consideration had to be identified for one supply: the judge did not accept that consideration could be for more than one thing simultaneously. The payment was for goods to be supplied to customers, and could not also be for services supplied to the appellant promoter.

The Court of Appeal allowed the company's appeal. Its analysis of the situation was slightly different from both the Tribunal and the High Court. The promoter did not undertake to provide rewards for customers: it promised only to make arrangements so that they could obtain rewards. So, when it paid the retailers for redeeming points, it was in fact paying them for the service of redeeming points, rather than for the rewards themselves. The "redemption service" was a taxable supply made for consideration by the redeemer to the promoter: input tax was recoverable.

HMRC also raised the issue in the Court of Appeal that some of the supplies of redemption goods are made for no payment by the customer – only for points. If the payment by the promoter was not consideration for the goods (but rather was consideration for a supply of redemption services by the redeemer to the promoter), it could be argued that the supply is "for no consideration" and is therefore within Sch.4 para.5.

Court of Appeal [2007]: *Loyalty Management UK Ltd v HMRC*

5.2.1.2 Revenue & Customs Brief 46/08

HMRC issued a Brief in late 2008 explaining their policy following the Court of Appeal's decision.

HMRC maintained that the payments by the promoter were third party consideration for goods and services supplied by redeemers to individuals; as the promoter did not receive those supplies, it could not claim input tax.

Pending the outcome of the litigation in the ECJ, HMRC intended to maintain that position by issuing protective assessments where necessary.

The Brief pointed out that some redeemers were adversely affected by the Court of Appeal's ruling: even if they supplied zero-rated goods, they would have to account for output tax because redemption services were not a zero-rated supply. This should not have been a problem because the promoter would be able to recover the full amount as input tax. However, in case the ECJ's decision changed the analysis of the transactions, HMRC suggested that redeemers might wish to make protective claims for repayment in respect of possibly overpaid output tax.

Redeemers who supplied goods only for points (as opposed to part payment) were also, under the Court's view of the law, making supplies within Sch.4 para.5 (business gifts). HMRC said that they would protectively assess for output tax on that basis (presumably where the cost of the goods exceeded £50).

The Brief also stated that HMRC regard the litigation as particular to the facts of LMUK's scheme. Until the litigation is complete, it would not be clear what the correct treatment of other loyalty schemes should be.

Revenue & Customs Brief 46/08

5.2.1.3 CJEU decision

The CJEU joined the cases of LMUK and Baxi Group together at a hearing on 21 January 2010. Representations were made by the Greek government and the Commission as well as by the taxpayers and the UK government. The court decided to proceed to a judgment without publishing an Advocate-General's opinion. The Supreme Court judge Lord Reed notes that "[Baxi] *was concerned with a loyalty scheme of an entirely different character…* [but the CJEU] *appears to have considered that both cases alike involved the straightforward application of established principles, since it determined them without a submission from the Advocate General. In terms of article 20, paragraph 5 of its Statute, it may do so only 'where it considers that the case raises no new point of law'.*"

The judgment said that the questions must be answered having regard to "the economic realities" of the promotional schemes. According to the judges, these are that "goods and services are supplied by the redeemers to the customers".

The judgment goes on to refer to the decision in *Kuwait Petroleum* (Case C-48/97), another case about a promotional scheme that went against the taxpayer. The relevant point was that the acquisition of rewards points by the customer has to be treated as a transaction which is separate from the transfer of the rewards to the customer. Applying that principle, the transfer of rewards – viewed in isolation – could only be a supply of goods or services which was made for third party consideration.

In *Baxi*, the court noted the taxpayer's argument that the supply was "in reality" a complex advertising service supplied by the promoter to Baxi Group. The court considered that there was a mixed supply of goods to the customer and services to Baxi: the consideration had to be apportioned between the two. The promoter made a profit margin by charging Baxi the full retail price (plus delivery costs) of rewards goods, while acquiring them for a lower cost. The profit margin would be the promoter's charge for services to Baxi (on which Baxi can presumably claim input tax). The reimbursement of the cost to the promoter of acquiring and delivering the goods would be third party consideration for the supply to the customer.

In *LMUK*, the court noted that the company asserted that the supply was a single supply of services. The judges said that this was an issue for the referring court to decide, but if there was only a single supply, it was made to the customers and not to the promoter.

The decisions, therefore, effectively supported HMRC's line and went against the taxpayers in both cases.

ECJ (Case C-53/09): *Loyalty Management UK Ltd v HMRC*

In his leading judgment, Lord Reed starts by summarising the network of contracts on which the scheme depends:

- Aimia contracts with "collectors" (the consumers) to operate their accounts and to make arrangements for the redemption of points;
- Aimia contracts with "sponsors" (issuers of points) to credit their customers with points in return for payments by the sponsors to Aimia (which are VATable);
- Aimia contracts with "redeemers" to pay part or all of the cost of goods and services which collectors receive in return for points;
- sponsors also contract with collectors in the initial supply which generates points;
- redeemers also contract with collectors in the second supply which involves redemption of points.

He observes that the use of the word "points", and the words "issue", "purchase" and "redeem" in relation to points, is metaphorical: they refer to changes in the contractual rights of the parties arising under the agreements between them.

Surprisingly, he then goes on to note that the reasons for the reference by the House of Lords – when the Tribunal and the Court of Appeal had declined to make a reference – were not recorded. In addition, the reference did not direct the CJEU to the specific circumstances of the case as found by the Tribunal, instead asking its questions in general terms. Lord Reed considered that this was a mistake, because the facts were unusual and highly relevant. In particular, it was not pointed out to the CJEU that Aimia accounts for output tax on the "issue of points" – or, to be more precise, on the transaction in which "the right to receive rewards" was supplied to collectors.

A key section of his judgment is as follows:

In relation to the issues emerging from the judgment of the Court of Appeal, one such was what might be described as the Redrow issue: that is to say, whether, considering the transactions in question in the context of the scheme as a whole, the payments made by LMUK to the redeemers were most aptly regarded as the consideration paid for the supply of services to it by the redeemers, which it required for the purposes of its business: services which included the provision of goods and services to collectors. A second issue, closely related to the first, was whether the *principle that VAT is neutral in its effect upon taxable persons required that LMUK, having accounted for VAT on its supply of the right to receive the goods and services provided by redeemers, should be able to deduct the VAT element of the costs which it incurred in order to satisfy that right.*

Lord Reed notes that the CJEU itself commented that the reference was restricted in scope, and did not touch on the relationship between the sponsors and LMUK. In the light of that limitation, he considered that the judgment of the CJEU – on its face, entirely favourable to HMRC's position – was determinative of the issue. The CJEU's analysis of the transactions was based on *Kuwait Petroleum*, when the factual background was quite different. In particular, there was a direct and immediate link between:

- the creation of the right to obtain rewards when a collector bought something from a sponsor – a transaction on which the sponsor made a specific payment to Aimia, and Aimia accounted for output tax; and
- the redemption of those rights in accordance with the agreements between the parties – the cost of meeting Aimia's obligations was borne out of the taxable revenue earned on the first transaction, which meant that the redemption was an essential cost component of a taxable supply, and the VAT was deductible.

The CJEU stated in its judgment that "*consideration of economic realities is a fundamental criterion for the application of VAT.*" This was more relevant in applying its decision than the rest of its answers to the limited reference, because those answers were not directed to the economic realities of the transactions.

Lord Reed also considered the authority of the *Redrow* case, which Aimia sought to rely on, and which HMRC argued was shown by the CJEU decision to have been wrongly decided. He considered that there was nothing in the CJEU ruling to negate *Redrow*, but that it would be necessary in future to emphasise the "economic realities" point when applying it. In *Redrow*, Lord Millett said that the question should be whether the claimant of input tax "*obtained anything – anything at all – used or to be used for the purposes of his business in return for that payment?*" This question should involve a "realistic appreciation" of the transactions, which presumably means that "anything at all" should not be taken to include advantages which are negligible in comparison to the amount paid.

The result is also, as observed by the Court of Appeal, in accordance with the general rules of VAT – if Aimia is allowed to deduct the input tax on redemption, the system will collect the exact proportion of the consideration paid by the final consumer. If Aimia had to account for output tax on the issue of points, but could not deduct input tax on redemption, the VAT collected would not be proportional.

Lord Hope also gave a detailed judgment, concluding that there was nothing in the CJEU judgment which precluded a finding that there was a taxable supply by the redeemer to the collector, but at the same time and as part of the same transaction, a supply of different services by the redeemer to Aimia; and that Aimia was entitled to input tax credit on the consideration it paid to obtain that supply.

Lord Walker gave a relatively brief judgment concurring with Lords Reed and Hope. Lord Carnwath gave the dissenting judgment, which was agreed by Lord Wilson. He considered it improper to go back to the reference and find fault with it; the terms of the reference had been agreed by Aimia at the time, and the judgment of the CJEU clearly agreed with HMRC's position. He explained in detail why he did not find the CJEU ruling difficult to follow or agree with, and concluded that he would have allowed HMRC's appeal against the Court of Appeal ruling.

Supreme Court: *HMRC v Aimia Coalition Loyalty UK Ltd (formerly known as Loyalty Management UK Ltd)*

5.2.2 Legal costs

A family partnership dismissed an employee, who sued the partnership for wrongful dismissal. The County Court ordered the partners to pay the employee's legal costs. The partnership reclaimed input tax on this (totalling over £8,000). Following a visit, HMRC raised an assessment to claw back this input tax on the basis that the supplies had been made to the employee rather than to the partnership. The Tribunal dismissed the partners' appeal against this decision.

There was further assessment in respect of legal fees payable to Post Office Counters Ltd following a dispute over a sub-post office that was run by the partnership, and the firm's appeal against this was dismissed for the same reason.

A third set of legal fees related to a dispute with a contractor who had sued the firm after it refused to pay his bills. He had won the dispute and the settlement paid to him had included payment of his legal costs. The Tribunal observed that input tax could be claimed in respect of the supply that had been made by the contractor, if there were appropriate invoices to back it up; the partner was given extra time to look for such invoices, but failed to produce any compelling evidence that input tax had been properly incurred. The Tribunal dismissed the appeal on this point as well.

First-Tier Tribunal (TC02458): *Mohamed Saheid and Sherifan Neisha Saheid*

5.3 Partial exemption

5.3.1 Supplies made under finance leases

The case of *EON Aset Menidjmunt* (Case C-118/11) concerned the disallowance of input tax on the leasing of cars which were used by employees for commuting. Although it was not apparently the main point of the case, the CJEU considered whether the input supply of leasing was a supply of goods or a supply of services, which would affect the question of recovery if it was found that the lessee supplied the cars on to its employees for no consideration. The court concluded that a leasing supply is ordinarily regarded as a supply of services, but that a finance lease could be regarded as a supply of goods. Where "*the lessee is to possess all the essential powers attaching to ownership of that vehicle and, in particular, that substantially all the rewards and risks incidental to legal ownership of that vehicle are transferred to the lessee and that the present value of the amount of the lease payments is practically identical to the market value of the property, the transaction must be treated as the acquisition of capital goods.*"

HMRC have responded to this decision with a Brief. Some confusion has arisen as to whether the distinction between goods and services is relevant to the UK's treatment of cars on finance leases, in particular to the application of the input tax block. HMRC say that they are considering the matter, but do not believe that there will eventually be any change of treatment – even if a car is acquired as "goods" under a finance lease, it will still be a "letting on hire", and that is the phrase in the law which applies the 50% block rather than the 100% block.

While HMRC consider the matter, taxpayers should continue to apply the rules as they have previously been understood.

R & C Brief 37/12

5.4 Cars

Nothing to report.

5.5 Business entertainment

Nothing to report.

5.6 Non-business use of supplies

5.6.1 Bid costs

In Spring 2006 a Spanish company formed a new subsidiary (ADIL) to make a takeover bid in respect of BAA plc. After this bid was successful (July 2006), the new holding company joined BAA's VAT group registration (September 2006). BAA then claimed an input tax deduction for some £6.7m incurred in respect of the costs of making the bid and in refinancing the group operations afterwards. HMRC refused the claim, arguing that there was no direct and immediate link between these inputs and any taxable supplies made or to be made by the group.

The company appealed, contending that the activities of a holding company are "economic activity" in European law, and the preliminary activities of the bidder were regarded as such in line with cases going back to *Rompelman*. The new holding company actively managed the acquired business, and obtained finance to fund the group's capital expenditure programme.

The First-Tier Tribunal accepted this argument and allowed the appeal. Even though the new holding company never made any supplies in its own right, it was regarded as a single taxable entity with BAA, and the arrangement of group finance facilities was an economic activity linked to the whole trade. The decision includes a detailed consideration of the meaning of "economic activity" in the context of holding companies. Fiscal neutrality also required that the input tax was deductible.

The Upper Tribunal summarised the issue as follows:

Put shortly the main question is whether the VAT incurred by ADIL on the professional services supplied to ADIL have a sufficiently direct and immediate link to taxable supplies made by ADIL (or which may be attributed to ADIL) in the course of an economic activity. If so, and to that extent, the appeal fails (and the VAT incurred by ADIL is recoverable). If not (again to that extent), the Commissioners' appeal succeeds. ADIL also pleads that the application of specific provisions (Regulation 111 of the VAT Regulations) demands that ADIL recover the relevant VAT.

HMRC offered three reasons why the FTT's decision was wrong:

- ADIL was only an acquisition vehicle which never intended to make taxable supplies in its own right;
- the FTT failed to take account of its own findings that ADIL did not make or intend to make taxable supplies;
- the FTT relied on an analogy with the *Faxworld* case (C-137/02) which was inappropriate because the facts were materially different.

The company offered four reasons to uphold the FTT's decision, any one of which would, in its contention, be enough to dismiss HMRC's appeal:

- the FTT correctly found a link between the input tax incurred by ADIL and the supplies made by the company that it acquired and always intended to manage;

- whatever its subjective intentions at various stages, ADIL objectively did use the inputs in making taxable supplies after the takeover, once it had joined the VAT group;
- reg.111 SI 1995/2518 required that input tax in this situation should be recoverable;
- ADIL always intended to join the VAT group (contrary to a finding of the FTT – the taxpayer cross-appealed on this particular finding of fact).

The Upper Tribunal examined the arguments and the FTT's findings in considerable detail. The judges concluded that ADIL did carry on an economic activity rather than an investment activity, but that:

- there were no taxable supplies made, or intended to be made, by ADIL before the takeover succeeded, and as a result none of the fees – which related solely to the takeover – could be directly and immediately linked to an onward taxable supply;
- as HMRC argued, the correct time to consider deductibility of input tax is when it is incurred, not retrospectively when the output to which it is allegedly related (i.e. after ADIL has joined the group) takes place;
- the deeming of all inputs and outputs of group companies to be made by a single entity only applies once all the companies are members of the group, and it therefore does not automatically bring in input tax incurred before the company joined the group;
- reg.111 was of no assistance because the VAT was not attributable to making onward taxable supplies;
- the FTT had found no evidence in relation to an intention of ADIL to join the VAT group before the takeover – so it was not possible to conclude that its decision was unjustified on the evidence, because it concluded that there was no evidence to support such a conclusion.

HMRC's appeal was allowed, and the cross-appeal was dismissed.

The company appealed to the Court of Appeal. The Court ruled that the FTT and UT had both been wrong to conclude that the company had carried on an economic activity at the relevant time. That time was when it incurred the liability to pay the VAT; at that point, its only intention was to take over BAA, which was an investment transaction within the principles of the *Polysar* case, rather than relating to an intention to make taxable supplies of goods or services.

The FTT had been wrong in law to find any connection between the inputs incurred by ADIL and the outputs later made by the BAA group. The inputs were only incurred in connection with the takeover of BAA, and were unconnected with any outward supply that either ADIL or BAA had intended at that time to make.

The company sought to rely on *Faxworld* (Case C-137/02) to support the idea that BAA could stand in the shoes of ADIL to recover the input tax incurred. The Court did not agree that the circumstances were sufficiently similar: that involved a transfer of a business from one entity to another, so that the inputs of the predecessor might be considered to be related to the outputs of the successor. However, there was no business in ADIL that was transferred to or continued by BAA after the takeover. There was no link between ADIL's inputs and BAA's supplies.

Court of Appeal: *BAA Ltd v HMRC*

5.6.2 Deductions

The Advocate-General has given an opinion which is consistent with UK case law on the situation in which a company pays for the defence of its employees in criminal proceedings. The A-G considered that there was no link between the taxable activities of the business and the defence of its managing director and principal executive officer, who were being prosecuted for their personal conduct and were seeking to avoid personal penalties. The company itself was not a party to the proceedings, and could not deduct input tax on the lawyers' fees.

The formal answer to the question set is that "*the existence of a direct and immediate link between a given transaction and the taxable person's activity as a whole for the purposes of determining whether the goods and services were used by that person 'for the purposes of taxable transactions' ... depends on the objective content of the goods or services acquired by that taxable person.*" Although "purpose" suggests subjective intention, nevertheless the nature of the supplies can be used to provide an objective measure of the link between the input and any output of the business. Here, there was none.

CJEU (A-G) (Case C-104/12): *Finanzamt Köln-Nord v Wolfram Becker*

5.6.3 Funded pension schemes

HMRC have updated their Notice on *Funded pension schemes*, replacing the November 2011 edition. It provides guidance for both employers and trustees about claiming input tax on funded pension scheme expenditure.

Paragraph 2.9 has been amended to include guidance on the recovery of VAT on management costs by professional trustees who are appointed to run a pension scheme:

If you cease trading, and therefore cease to be an employer, you no longer have any entitlement to input tax on management of the pension scheme. Where, however, the trustees are themselves VAT registered on account of business activities carried out by the pension scheme they may treat the tax incurred on services connected with the continuing management of the scheme as their input tax, subject to the normal rules. This means that where the trustees are required to restrict recovery of input tax because they make exempt supplies not all the tax on the management services may be recovered – see paragraph 1.5.

Where a professional trustee is appointed to run a pension scheme e.g. where the sponsoring employer ceases to exist. VAT incurred on the management of the pension fund can only be recovered by the trustee insofar as it is a clear cost component of an onward supply of that management of the pension fund.

This presumably follows on from the case of *JIB Group Ltd* (TC02224) reported in the October 2012 update, which dealt with this situation.

Notice 700/17

5.7 Bad debt relief

5.7.1 Credit note or bad debt?

A car dealership company (B) sold Ford cars. B had no corporate relationship with Ford. In 2002 B went into receivership. It held a number of cars for which it had not paid F. In accordance with the supply agreement between the two companies (which was terminated if either party went into an insolvency procedure), F reclaimed the cars and issued credit notes. The supply agreement contained a “retention of title” clause which was legally effective and which entitled F to recover its cars in priority to other creditors.

B’s receivers needed to continue the business in order to try to sell it as a going concern, for which they needed stock. They agreed with F that, after the credit notes had been issued, F would re-sell the same cars to the receivers on the same terms. In effect, F exercised its rights under the supply agreement by issuing the credit notes, but then decided to carry on a new informal supply agreement with the receivers. The cars were not physically repossessed by F.

B’s receivers subsequently submitted a claim for repayment of input tax in respect of these cars. The Commissioners rejected the claim and B appealed, contending that the credit notes should not have been treated as effective for VAT purposes (cancelling the input tax entitlement in the pre-insolvency period), and that F should have claimed bad debt relief instead. This would have benefited B because B would not have had to repay the input tax under the usual bad debt rules if an insolvency procedure commenced between the input tax claim and the six month deadline at which F would make its claim.

This was particularly important to the administrative receiver from Baker Tilly, who was being sued by a secured creditor for accepting the credit notes at face value. The creditor, NatWest, argued that the proper treatment would have resulted in a much higher recovery for itself. The administrator therefore claimed back the VAT essentially in order to pay NatWest, using the argument put forward by NatWest in its lawsuit.

In 2007, the VAT Tribunal rejected this contention and dismissed B’s appeal, holding that the credit notes had been correctly issued and that F could not have claimed bad debt relief since it had legally (if not physically) “recovered” the cars in accordance with the supply agreement. The original supply had been reversed, so there was no input tax for B to claim. However, it was not a straightforward case: the company’s counsel had argued strongly from precedent cases that the supply did not cease to be a supply because of the retention of title clause, and the reclamation of the cars by F was not a supply either.

In 2008, the High Court confirmed the Tribunal’s decision. The parties had agreed that the first supply agreement had been rescinded, cancelling the original supplies, and the credit notes were validly issued.

In early 2009, the Court of Appeal remitted the case to the Tribunal for reconsideration. The credit notes would only have the effect of cancelling the original supply (and therefore cancelling the associated right to input tax) if there was a contractual agreement between B and F that the supply should be cancelled. The original Tribunal did not consider this question:

it appeared to accept that the credit notes must be assumed to reflect such a contract, rather than questioning whether the credit notes did so.

As the Tribunal's primary findings of fact did not justify its conclusions, it should examine the case again. It was possible that it would come to the same answer, but it was also possible that it would accept the taxpayer's argument: F acted unilaterally in repossessing the cars and issuing the credit notes, and B accepted that conduct not because of a contractual agreement but because it had neither the power nor the commercial incentive to do anything else.

The case was further complicated by the death of the original Tribunal chairman to whom it was remitted; when the FTT at last came to hear it in 2011, Judge Nowlan then could not agree with his Tribunal member, Julian Stafford, and had to reach a decision based on his own casting vote. The FTT decision therefore rehearsed the facts and the possible legal analyses in considerable detail and reached the conclusion that there was no agreement to rescind the contract. This meant that the dealer won – if there was no rescission, the credit notes were ineffective, and bad debt relief should have been claimed instead.

HMRC, supported by Ford, appealed to the Upper Tribunal, arguing that the FTT had erred in concluding that there was no agreement to rescind the original supply. It appears that Ford no longer had any financial interest in the outcome of this case because their VAT returns for the periods concerned were long beyond the time for assessment, but as the situation arises from time to time, they wanted a determination of the correct outcome (there may be other cases where they have VAT at risk after following the same line as they did here).

The Upper Tribunal judge, Mr Justice Henderson, starts with a rehearsal of the history of the case and some of the reasons for the remission by the Court of Appeal for rehearing in 2009. He then emphasises that the decision of the FTT, while not unanimous, was nevertheless one of fact, and could only be overturned by the Upper Tribunal on limited grounds. The alleged errors of law on which HMRC's and Ford's appeal was based were described as follows:

The first contention is that the FTT proceeded on the mistaken basis that the original contracts of supply could be cancelled otherwise than by a legally binding subsequent agreement between Ford and Brunel, and that it was odd or surprising to expect to find any such agreement on the part of Brunel. The second contention is that, although it was common ground between the parties that the question whether there had been a legally binding agreement to vary or rescind the original contract had to be determined objectively, the FTT wrongly looked solely to the subjective understanding of Mr Mackay [the Baker Tilly administrator] *and the absence of any positive witness evidence from Ford in reaching their conclusion. It is said that each of these alleged errors infected and vitiated the FTT's consideration of the evidence, and that had they directed themselves correctly they ought to have found that, viewed objectively, there was an offer by Ford to rescind the original contracts of supply, thereby cancelling or reducing the debt owed by Brunel to Ford, and that Brunel then accepted this offer by their conduct in accepting the credit notes and the re-supply of the same vehicles under new tax invoices.*

It was agreed between the parties that the original contract could only have been varied or rescinded by agreement. The question was whether there was such an agreement, evidenced by Ford issuing the credit notes and Brunel accepting them in exchange for the further agreement to make the new supplies of the cars, or whether Ford's action was unilateral and Brunel could do nothing about it.

The judge considered the findings of the FTT, in particular the reasoning adopted by Judge Nowlan, and could find no reason to depart from it. In spite of the apparent interest of the administrator in giving his evidence – the outcome indicated by his version of events meant that the negligence action against his firm was avoided – the FTT had been right to attach weight to his expressed explanations, and had not unreasonably chosen to believe him. There were some aspects of the analysis of the original contract between Ford and Brunel that could be criticised, but if anything Judge Nowlan's understanding of the contract was more likely to lead him to conclude that there had been a rescission than otherwise. There was no error of law in the FTT's decision.

Upper Tribunal: *HMRC and Ford Motor Company Ltd v Brunel Motor Company Ltd (in administrative receivership)*

5.7.2 Reference

The questions for reference in *GMAC* have been published:

To what extent is a taxable person, in relation to two transactions concerning the same goods, entitled both (i) to invoke the direct effect of one provision of [the Sixth Directive] in respect of one transaction and (ii) to rely on the provisions of national law in relation to the other transaction, when to do so would produce an overall fiscal result in relation to the two transactions which neither national law nor the Sixth VAT Directive applied separately to those two transactions produces or is intended to produce?

If the answer to Question 1 is that there are circumstances in which the taxable person would not be entitled to do so (or would not be entitled to do so to a particular extent), what are the circumstances in which this would be so and in particular what is the relationship between the two transactions which would give rise to such circumstances?

Do the answers to Questions 1 and 2 differ according to whether or not the national treatment of one transaction is in conformity with the Sixth VAT Directive?

CJEU (Reference) (Case C-589/12): *HMRC v GMAC UK plc*

5.7.3 Updated Notice

HMRC have updated their Notice *Relief from VAT on bad debts*. The previous edition was dated December 2002. The notice has been rewritten for current time limits and VAT rates, and "to remove historical rules which are no longer relevant." In spite of this statement, the notice still contains details of the notification of a customer that a claim is being made, which has not applied for many years.

Notice 700/18

5.8 Other input tax problems

5.8.1 Invalid invoices

A company appealed against the disallowance of input tax on a number of invoices over a series of periods from 09/05 to 03/07. The reason for disallowance was that the invoices were invalid, being issued by a deregistered trader, and showing the wrong address for the company to which the registration number had belonged (i.e. the registration had been "hijacked" by another supplier). The appeal had to be heard in two sections, with a long gap between the two, because not enough time had been allowed for the first hearing, and a series of case directions further delayed the second one.

The Tribunal was satisfied that the invoices had been issued fraudulently. Although there was no evidence or allegation that the director of the company had been complicit in the fraud, the Tribunal did not consider that he had done enough to satisfy himself that the supplier was genuine. In those circumstances, it was not unreasonable of HMRC to refuse to exercise their discretion to accept alternative evidence instead of proper VAT invoices. The appeal was dismissed, apart from in respect of one invoice which appeared to have been double-counted in the assessment.

First-Tier Tribunal (TC02603): *Arkeley Ltd (In Liquidation)*

5.8.2 Missing traders

A trader appealed against the disallowance of some £350,000 of input tax in the period to July 2006 which related to a purchase of 17,500 iPod nanos. The Tribunal considered that the only reasonable explanation for the transactions was that they were connected with fraud, and a reasonable businessman would not have entered into those transactions in the way in which the director did so. The appeal was dismissed.

First-Tier Tribunal (TC02428): *H S Tank & Sons Ltd*

Another company was denied deduction of £1m in respect of 12 transactions in mobile phones in the period to April 2006. The decision was the same. There were subsequent points about which costs regime should apply, and the Tribunal only awarded costs to HMRC for the period up to 31 March 2009, because the department had not made it clear from the outset that costs would be applied for under the new regime.

First-Tier Tribunal (TC02437): *Global Enterprise (GB) Ltd*

A company was denied input tax of just over £250,000 in respect of the period to May 2006. The Tribunal concluded that the director was a dishonest witness and he had been aware that the transactions were connected with fraud. The appeal was dismissed.

First-Tier Tribunal (TC02441): *Mail A Mobile Ltd*

Another case heard at the same time as the above concerned just over £400,000 of input tax for the period to April 2006. The counterparties for the fraudulent transactions were the same, and so were the conclusions of the Tribunal.

First-Tier Tribunal (TC02442): *Club Mobile Ltd*

Another company was denied repayment of £6.4m for the periods April and May 2006. The Tribunal made the usual detailed examination of the circumstances and found inadequate due diligence, contrived mark-ups, circular payments and clear connections to VAT losses through fraud. It concluded that the directors knew that the transactions were connected to fraud; if not, they certainly should have known.

First-Tier Tribunal (TC02535): *Trans Global Trade (Europe) Ltd*

A recent MTIC case was unusual in that it featured satnavs rather than phones or CPUs, and related to the middle of 2005 rather than 2006. The amount of VAT at stake was £1.4m, Evidence was taken from an employee of the manufacturer, Garmin, which cast doubt on the possibility that this company could have obtained that many of its satnavs (for example, over 16% of the worldwide sales of one particular model that year).

The Tribunal went on to discuss whether HMRC had discretion under reg.29 to accept “alternative evidence” when it appeared that there was no underlying transaction, and concluded that it did not. Even if there were in fact supplies of goods, but goods which did not fit the descriptions on the invoices, the Tribunal did not believe that the failure to exercise a discretion to allow deduction was in any way unreasonable. The appeal was dismissed.

First-Tier Tribunal (TC02584): *Future Phonic Ltd*

An appeal related to a slightly later period than most of the MTIC cases up to now - £327,000 of input tax refused for the period 09/06 – 11/06. Perhaps the Tribunal is finally working through the backlog of the middle of 2006. T

The director admitted by the time of the hearing that the company’s transactions were connected with fraud, but denied that he knew this at the time, arguing that HMRC only decided to disallow the input tax after 14 months of enquiries, using hindsight and resources that were not available to the company. The Tribunal examined the background to the business and the deals and declined to accept this, concluding that the director was well aware that his transactions were part of an organised VAT fraud. Costs were awarded to HMRC.

First-Tier Tribunal (TC02585): *Global Corporation Trading Ltd*

Back to the normal periods, 04/06 – 06/06, a company was denied a deduction of £6.7m. The Tribunal found as a fact that the company knew at the time of entering into the transactions that they were connected with fraud, and dismissed the appeal.

First-Tier Tribunal (TC02595): *Libra Tech Ltd and related appeal*

Another company was denied input tax of £275,000 in its periods to 09/06 and 12/06. The Tribunal decision includes the following analogy to illustrate the “means of knowing” test:

199. Without trying to be frivolous, we can perhaps clarify the different situations in relation to “means of knowledge” by giving three variations on the Nelsonian example.

200. If Nelson has seen the French and Spanish ships with his good eye, and then aimed the telescope in their direction but to his blind eye, that is plainly a case of knowledge.

201. If Nelson knew that a particular course had to be set to engage the enemy; had not seen the ships, but nevertheless scanned the horizon with the telescope to his blind eye, he would still have been deliberately ensuring that he failed to ascertain the relevant facts. That involves the deliberate lack of knowledge that we attribute to Mr. Patel in this case.

202. If Nelson was incompetent and misread the compass and looked with his good eye in the wrong direction, when any more competent admiral would have seen the ships immediately, that is negligence. We make no comment, though other authorities have done, on whether in that situation it would have been apt to conclude that Nelson should have known that the ships were indeed on the other horizon.

203. We simply say that it is our judgment that Mr. Patel deliberately sought to know the minimum about the surrounding circumstances of the transactions and he deliberately refrained from considering and analysing the information that he did have. In answer to the obvious question of whether he would have known of the connection to fraud had he not deliberately sought to know the bare minimum, and had he not shut his mind deliberately to all sensible enquiry, our decision is that he would have done.

First-Tier Tribunal (TC02535): *Celltec Computers Ltd*

5.8.3 Company car advisory fuel rates

The fuel-only advisory mileage rates now appear to change quarterly, although only by very small amounts. For the month following an announced change (i.e. the month of March) employers may use either the old or the new rate.

The rates from 1 March 2013 (1 December 2012 in brackets) are:

Engine size	Petrol	LPG
1400cc or less	15p (15p)	10p (11p)
1401cc – 2000cc	18p (18p)	12p (13p)
Over 2000cc	26p (26p)	18p (18p)

Engine size	Diesel
1600cc or less	13p (12p)
1601cc – 2000cc	15p (15p)
Over 2000cc	18p (18p)

Although the rates now change quarterly, the actual adjustments are very small – in this case, 1p on one figure.

http://www.hmrc.gov.uk/cars/fuel_company_cars.htm

6. ADMINISTRATION AND PENALTIES

6.1 Group registration

6.1.1 Retrospective grouping

A group of companies operated as if two subsidiaries were included within its group registration. When HMRC discovered that the group was not accounting for VAT on supplies to and from these companies, which had not been formally included, the company applied for the grouping to be recognised retrospectively, as the VAT would then be correct in all periods.

There was a separate issue in relation to an assessment arising from a failure to notify an option to tax, and HMRC's refusal to accept a belated notification. A misdeclaration penalty was levied in addition to this assessment.

The property on which the option was to be exercised was purchased by the group and transferred to one of the subsidiaries, C28. If C28 had been a member of the VAT group registration at that time, the option to tax would have had no immediate effect. As it was not, HMRC assessed to disallow the input tax that had been claimed on the transaction (over £2m), together with the misdeclaration penalty, and ruled that this could not be corrected. HMRC also raised a separate alternative assessment, charging output tax on the intra-group transaction, in case it should turn out that the belated notification of the option to tax was accepted on review.

The Tribunal decision examines the history of the transactions and the discussion of their consequences between HMRC and the taxpayer companies. Evidence was produced of a board meeting at which the purchase of the property and its transfer to the SPV subsidiary were considered; an option to tax was explicitly mentioned. Nevertheless, HMRC were not persuaded to accept a belated notification. They also explained that they could only accept a retrospective application for grouping in "exceptional circumstances", which did not apply here. As the reviewing officer pointed out, it appeared from the minutes of the board meeting that the directors had been told that VAT would have to be charged on the intra-group transaction as a result of the option to tax, so they could not reasonably have believed that a group registration was in place.

Retrospective grouping

The company had written to HMRC setting out the following grounds for allowing a retrospective admission to grouping:

(a) it has (acting as the representative member of the VAT group, on behalf of CUK [ie CPUKL]) consistently acted since 30th July 2007 in a manner consistent with its mistaken belief that C28 was already included in its VAT group;

(b) had the application been made before rather than after the transfer of property to C28, there would have been no grounds for refusing the application;

(c) while unfortunate the omission to make the application at the right time was solely due to an administrative slip-up such as can occur in the best regulated organisation;

(d) no prejudice to the Revenue or loss of tax has been caused by the delay in making the application to group;

(e) on the contrary, the belated inclusion of C28 in the group will enable Copthorn Holdings to get its tax affairs in order;

(f) the potential loss of a tax windfall to HMRC is not a relevant consideration.

We would be grateful if HMRC allow the retrospective inclusion of C28 in the Copthorn Holdings VAT group, effective from 30 July 2007. This is right, sensible and in the interests of all parties.

The other subsidiary, C26, had purchased a company which owned a property. Similar problems arose because C26 had not been included in the group registration at the time, and a similar request was made and refused.

The argument for the company was summed up as follows:

The essential question before the Tribunal was this: where there has been an innocent administrative oversight, does the law – interpreted in the light of the public interest, ie what is reasonable – require the damage to be reparable or irreparable? Administrative mistakes were regrettable, but they did occur. Specifically, should HMRC admit the two companies concerned to the CHL VAT group with retrospective effect? If the answer to this question was "Yes", all the costs, legal issues and complications would disappear at the stroke of a pen. This would produce a sensible commercial result. It would also accord with EU law. CHL's essential submission was that this outcome would best accord with the will of Parliament.

HMRC's representative characterised the omission of the subsidiaries from the group registration as something that had been deliberately done, so that the company was now trying to rewrite its VAT history to achieve a better result with the benefit of hindsight. This led to exchanges between counsel on whether HMRC were now effectively alleging fraud on the part of the company, when this had not been included in any of the correspondence or legal arguments up to this point. The Tribunal balanced the evidence and arguments on both sides and concluded that there was no basis for HMRC's suggestion that the company had followed a "conscious process". The company had made mistakes, rather than deliberate decisions.

The Tribunal then considered the reasons for refusing retrospective grouping. S.43B(4) VATA 1994 allows HMRC to accept an application for grouping to take effect from a date earlier than the application is made, but does not say in what circumstances that might apply. HMRC argued that it was therefore a matter for their discretion and not subject to appeal.

The Tribunal considered that it did have jurisdiction to consider appeals about the refusal of HMRC to allow a grouping application, and that extended to s.43B(4). That was the decision of the High Court in the *Save & Prosper* case, and it was inherently unlikely that the law had been reversed by the consolidation of the grouping rules which was carried out in the FA 1999. The Tribunal also noted that HMRC had simply refused the grouping applications, rather than stating that they were acceptable but could not be applied retrospectively. This suggested that the refusal was within s.83(k) VATA 1994 and appealable.

Further, there were special rules in s.84(4A) VATA 1994 which limited the Tribunal's jurisdiction specifically when HMRC took a decision to refuse grouping on the grounds of protection of the revenue. That legislation included specific provisions about the effect of allowing an appeal: the group registration would then have effect from the date the application was made. Normally, when a Tribunal exercises a supervisory jurisdiction and decides that HMRC have not made a decision in the correct manner, it still cannot replace HMRC's decision with its own – it can only require HMRC to reconsider the matter.

The Tribunal concluded that it had jurisdiction at least in the terms of the decision in *John Dee*, that it could overturn the decision if it was satisfied that the Commissioners had acted in a way in which no reasonable panel of Commissioners could have acted or whether they had taken into account some irrelevant matter or had disregarded something to which they should have given weight, or erred on a point of law. It could so find and yet dismiss the appeal if satisfied that the decision would inevitably have been the same, even if the Commissioners had not committed the error that possibly undermined the validity of their process.

VAT Notice 700/2 includes the following explanation of HMRC's view of the scope of their discretion:

Can I backdate my application for more than 30 days?

Only in exceptional circumstances:

- *if we lose your application and you can supply details of your original application and your attempts to follow it up; or*
- *if the delay was caused by lack of action on our part.*

The company's representative argued that this was almost impossible to achieve. HMRC were effectively making ineffective a right, envisaged by the law and by Parliament, which would achieve the correct result under EU law of removing the burden of VAT from businesses. The Tribunal accepted the argument that HMRC could not restrict their own discretion by publishing guidance as if it were law; the possibility of other circumstances in which discretion might be exercised should be mentioned.

The Tribunal concluded that it should construe s.43B as follows:

(1) HMRC must register a qualifying group or candidate group member;

(2) The normal timing for the effective date of registration is the date of receipt of the application;

(3) HMRC has a discretion to permit group registration to take effect from an earlier or later date, but may decide that the effective date should be some date other than that requested by the applicant. There is no statutory time limit for "retrospective" applications, the question of timing being a matter for HMRC's discretion;

(4) If an applicant wishes to challenge HMRC's decision to grant the application with effect from a date other than that requested, the applicant may appeal on the basis of the principles set out in John Dee;

(5) HMRC may (within the 90 day period) refuse the application for any of the reasons in s 43B(5);

(6) There is a separate appeal regime for an appeal against a refusal pursuant to s 43B(5)(c) (the other reasons set out in s 43B(5) being based on lack of eligibility, against which it would not be appropriate to permit any appeal).

In those terms, the letters refusing the application for retrospective grouping were unacceptable. They did not explain that HMRC was exercising a discretion, nor give the reasons for doing so; they gave no response to various points raised by the director of the company in applying for retrospective grouping. The appeals were allowed, but the result of that was to remit the applications to HMRC for reconsideration, which may lead to the same decision being given again. The Tribunal noted that it was no longer open for HMRC to refuse on the basis of the protection of the revenue, because that has to be done within 90 days of receiving the application.

Belated notification

It seems that HMRC did not accept the belated notification of the option to tax because the company had made a transfer without accounting for output tax, i.e. had treated an output as exempt. However, as pointed out by the director in correspondence, this was a different error: it had failed to account for output tax because it had treated the transfer as one made within a VAT group registration. The company's representative argued that there was clear evidence that the group had intended to tax the property from the outset; the subsequent mistakes were not inconsistent with that.

The Tribunal considered here that HMRC had not unreasonably exercised their discretion on the basis of the information that had been presented to them at the time the decision was taken. Subject to a possible revised decision on grouping (which would remove the intra-group transaction from being treated as exempt and "blocking" the input tax), the appeal against the refusal to accept that the option was in place – so the input tax was not deductible. 65% mitigation of the misdeclaration penalty was considered to be reasonable.

Overall conclusion

The overall conclusion was that the group had not opted to tax, and was therefore not entitled to recover input tax, even if HMRC decided to allow retrospective grouping. For some reason, the Tribunal considered that the blocking of input tax would then fall in a different period, which would mean that the misdeclaration penalty would have to be cancelled. However, it is not clear why that should be.

There is a lengthy postscript arising from a further set of submissions received by the Tribunal just before it released its decision. It seems likely that this will be appealed by both sides.

First-Tier Tribunal (TC02605): *Copthorn Holdings Ltd*

6.2 Other registration rules

6.2.1 TOGC

An individual owned a large residential property in which a licensed restaurant operated in the basement. For some years she and her sons ran it as a family business; in 2006, she leased the basement to the then chef, who ran it as his own business. He registered for VAT and made a number of substantial amendments to the property.

The lease provided for a break after 3 and 7 years. The chef decided his future lay outside the restaurant business, so he gave notice and surrendered the lease in June 2009. There was some dispute about the length of notice given and the length of time between the chef closing his business and one of the sons reopening it again, but the Tribunal found that 3 months' notice had been given and the restaurant was only shut for about 10 days.

A payment of £6,000 was made by the son to the outgoing chef. The nature of this payment was disputed: the chef said it was for the fixtures and fittings, while the son claimed it was a pure goodwill gesture. The mother claimed not to have been party to the discussions over the payment, and had been against paying it.

Although there were some differences in the way in which the restaurant was run (style of cooking, opening times), and a need for complete restocking of inventory, the Tribunal was satisfied that the mother had acquired the means to carry on a business as a going concern. She was therefore liable to be registered from the date of the transfer on the basis that she took over the chef's turnover history.

First-Tier Tribunal (TC02520): *Brenda Massey t/a The Basement Restaurant*

6.2.2 Late registration

A sole trader failed to register for VAT when he should have done: his turnover for the 12 months to 31 October 2008 exceeded the then threshold of £67,000, imposing an obligation to register with effect from 1 December 2008. Around that time his wife, who had previously kept his books, took a job, and his accounting fell into arrears. He did not notify liability to register until November 2011, when he gave the correct date for exceeding the threshold. After initially giving the wrong EDR in correspondence, HMRC apologised and revised the EDR to 1 December 2008; they then notified that a penalty would be levied.

His accountants then asked for the registration to be cancelled, on the basis that turnover had been below the threshold since August 2009. However, he exceeded the threshold again in June 2010. His turnover continued to fluctuate around the level at which registration would be required. However, HMRC agreed to deregister the trader with effect from 19 December 2011.

HMRC had asked for details of the trader's turnover, with a proposal to calculate the penalty on the basis of the flat rate VAT that would be due on turnover for the penalty period. This information was not provided, so HMRC issued a penalty of £1,698 on an estimated basis in January 2012 (calculated at 15%, with 25% mitigation).

The trader made a single VAT return, using the flat rate scheme, covering the whole period from December 2008 to December 2011, in March 2012. The VAT shown was £13,692. He had not paid the tax or the penalty by the time of the hearing of an appeal against both.

The Tribunal examined the accounting information available and concluded that it was not possible to contradict HMRC's decision not to allow exception from registration as at December 2008. In accordance with the precedent in *Gray & Sons*, and as confirmed recently in the case of *Mark Mills-Henning*, exception had to be applied for at the time. Only information that was available to HMRC at the time could be taken into account, and they had none.

The HMRC officers explained to the Tribunal that there is a policy called "Liable Not Liable" under which a trader in this circumstance may be "forgiven" VAT for periods in which he should technically have been registered, but for which he could have deregistered. It appears that this policy only applies to traders who have not actually registered and deregistered: it could not be used to reduce the liability apparently due from the trader. He regarded this as "adding insult to injury", because he felt he had done what he was obliged to do and had been advised to do, and now found that he would be treated more harshly than he would have been if he had taken no action and waited for HMRC to find him. The Tribunal acknowledged that this was not within its jurisdiction, but it urged HMRC to consider whether there was anything within its care and management powers that would enable the department to reduce the harshness of the burden on the trader.

The Tribunal did consider itself able to mitigate the penalty to zero. It could not take into account the good faith of the appellant, nor his insufficiency of funds to pay the tax or the penalty; but it did feel able to take into account the extreme harshness of the conclusion that he would have to pay VAT for periods in which he could have been deregistered, and would now have to pay more VAT than if he had not voluntarily registered.

First-Tier Tribunal (TC02571): *Michael Robert Haynes*

6.2.3 Right to register

The Latvian authorities refused to company which stated on its application that it intended to carry out construction services. The reason was that it did not have the material, technical and financial capacity to carry on such an activity. The appeal court ruled that this was not a sufficient reason on its own to deny VAT registration. It was also irrelevant that the shareholder had already obtained VAT registration in respect of a number of other entities which had not traded under his ownership, but had been transferred to other parties. The tax authority appealed, and the following questions were referred to the CJEU:

1. Is Directive 2006/112 … to be interpreted as prohibiting refusal of the individual registration number that identifies a taxable person, on the basis that the holder of the taxable person's shares previously obtained on various occasions an individual number for other undertakings which did not carry out any real economic activity, and the shares of which were transferred by the holder to other persons immediately after obtaining the individual number?

2. Is Article 214, in conjunction with Article 273, of Directive [2006/112] to be interpreted as permitting the tax authority, before assigning the individual number, to verify the capacity of the taxable person to carry out the activity that is subject to tax, where this verification is intended to ensure correct collection of the tax and prevent tax evasion?

The CJEU noted that the system of inspection and control of traders' records should be used to prevent evasion. It was not enough on its own to find that an applicant for registration did not have the resources to carry on a trade, or to conclude from the existence of previous VAT registrations that VAT fraud was being facilitated. It was for the national court to determine whether the authorities had provided sufficient evidence to support these conclusions, but the reasons given on their own were insufficient to do so. The answer given was:

Articles 213, 214 and 273 of Council Directive 2006/112 EC of 28 November 2006 on the common system of value added tax must be interpreted as meaning that the tax authority of a Member State may not refuse to assign a value added tax identification number to a company solely on the ground that, in the opinion of that authority, the company does not have at its disposal the material, technical and financial resources to carry out the economic activity declared, and that the owner of the shares in that company has already obtained, on various occasions, such an identification number for companies which never carried out any real economic activity, and the shares of which were transferred immediately after obtaining the individual number, where the tax authority concerned has not established, on the basis of objective factors, that there is sound evidence leading to the suspicion that the value added tax identification number assigned will be used fraudulently. It is for the referring court to assess whether that tax authority provided serious evidence of the existence of a risk of tax evasion in the case in the main proceedings.

CJEU (Case C-527/11): *SIA Ablessio v Valsts ieņēmumu dienests*

6.2.4 Registration online

The government has issued a press release urging businesses to register for VAT online rather than using the old paper system. "Registering for VAT online is easier, more secure and faster than using a paper form, says HMRC, which is urging new businesses which need to register for VAT to do so online, rather than on paper. As well as avoiding postal delays, the online system provides on-screen help plus an immediate on-screen acknowledgment that HMRC has received the application. Around four out of five new businesses now register online for VAT."

Online applicants will be automatically enrolled for online filing, and VAT Online now offers the facility to amend registration details and to deregister.

rnn.cabinetoffice.gov.uk/Press-Releases/New-businesses-urged-to-register-for-VAT-online-68926.aspx

HMRC have published a Tax Impact and Information Note in which they analyse the effect of changes to VAT online registration and the 1 December 2012 removal of the registration threshold for non-UK established businesses.

http://www.hmrc.gov.uk/tiin/vat-online.pdf

6.2.5 Non-established persons

In an article in *Taxation,* Neil Warren considers the new rules requiring registration of non-established persons who make any supplies in the UK, without the benefit of a registration threshold. It points out that for most supplies of services, there will not be a problem – B2B will be reverse charged by the customer, and B2C will be charged to foreign VAT where the supplier is established.

Taxation, 14 February 2013

6.3 Payments and returns

Nothing to report.

6.4 Repayment claims

6.4.1 Mileage allowances

A market research company made a *Fleming* claim on 27 March 2009 in respect of the VAT element – totalling £126,000 – of mileage allowances it paid to market researchers between January 1986 and April 1997. At a preliminary hearing, the Tribunal decided two matters:

- HMRC should be allowed to amend their original statement of case;
- the Tribunal's jurisdiction was appellate, not supervisory, on the question of whether the appellant had already claimed a deduction for the input tax through its VAT account.

HMRC's amendments to the statement of case had not been sent promptly to the appellant, and the revised statement had not been marked up with the changes as HMRC had promised; however, the Tribunal did not consider that there was any serious prejudice to the appellant, and allowed the amended statement of case to stand.

HMRC then argued that the question of whether input tax had already been claimed was one on which they should exercise their discretion under reg.29 SI 1995/2518, so the Tribunal would only have supervisory jurisdiction – it could not form its own decision on the basis of the evidence, but should only find for the appellant if HMRC had exercised its discretion in an unreasonable manner.

The Tribunal did not agree. The question of whether input tax had already been claimed was one of fact, not one over which HMRC had discretion. Accordingly, the Tribunal had a full appellate jurisdiction to consider the evidence and come to a decision. The substantive hearing will presumably follow.

First-Tier Tribunal (TC02428): *Market & Opinion Research International Ltd*

6.4.2 Fleming claim by a group

The representative member of a VAT group (T) made a claim in respect of output tax accounted for on the takings of gaming machines between 1973 and 1996. Initially, this claim was made in November 2007 by the company that owned the gaming machines (C), which had left the VAT group under a management buy-out in 1998. T applied on 31 March 2009 for the VAT group to be formally disbanded; although it did not make a formal claim under s.80 for the repayment of the output tax, and appeared to have no knowledge of the claims made by C, in April 2009 HMRC paid to T the amount due under the one *Linneweber* claim made by C that HMRC accepted (repaying about £667,000 with almost as much in statutory interest). Presumably this was because C would have used the group's VAT number in relation to its claim, and HMRC paid the claim to the representative member which still owned that number.

HMRC then assessed (in July 2009) to claw back the repayment, having decided that it had been paid to the wrong company – C was the correct person to receive any refund. Following a protest, HMRC changed their view again in October 2009, stating that they then believed that T was the correct claimant, so the assessments would not be enforced, but noting that C had also made a competing claim. By September 2010, they had gone back to the earlier view, and decided to uphold the July 2009 assessment against T.

The situation was further complicated by the fact that the appellant company had originally carried on the trade itself; it had entered into a group reconstruction in 1990, changing its name and transferring the trade to the other company. The claim therefore related to VAT that had been accounted for at one time or another by both companies.

The Tribunal reviewed the complex background and a number of precedent cases. It concluded that T could not take over C's timely claim when it had not itself made any claim at all. Any claim made by T as part of the appeals process was after the *Fleming* time limit; C had not made the claim on behalf of T or acting as its agent, and T could not take the benefit of the fact that C had made a claim in time.

The Tribunal went on to consider the consequences of the assignment of the trade in 1990 and the management buy-out in 1998. The 1990 assignment of trade from T to C carried with it any rights to reimbursement of overpaid VAT. At that time, T was the representative member of the VAT group, so it would have made any such claim; but when C left the group in 1998, it took with it the rights to make claims in respect of its own VAT overpayments, including those rights that had been assigned to it in 1990. Accordingly, it was the correct person to receive repayments.

The Tribunal considered that the disbandment of the VAT group, which seems to have been coincidentally applied for at about the same time, had no effect. C was not a member of the group in 2009, and T could no longer act as its representative. Even if that was wrong, HMRC had agreed to give effect to the cancellation of the group registration with effect from 28 February 2009, when T had ceased to trade; that was before the repayment was incorrectly made to T, and confirmed further that C was the company entitled to repayment.

The company was given leave to apply for a further hearing to consider the question of legitimate expectation. Presumably that will be founded on the confusion in HMRC about who ought to have received the money.

First-Tier Tribunal (TC02443): *Tailor Clark Leisure plc*

6.4.3 Offset of claims

A charitable theatre trust supplied tickets which were exempt under the cultural services exemption. It had accounted for output tax on these tickets before a change in the understanding of the law following the *London Zoo* decision of the European Court. In 2007 it made a *Fleming* claim for output tax overpaid between 1990 and 1996.

HMRC argued that the company had reclaimed input tax on theatre renovations in 2000 and 2001. If the supplies had been correctly classified as exempt, this input tax would not have been repaid; the overpaid output tax should be set against the overclaimed input tax. The First-Tier Tribunal accepted this contention and dismissed the appeal. The taxpayer had argued that s.81(3A) VATA 1994 did not allow HMRC to offset amounts from different periods (in this case a 1990 – 1996 overpayment against an excessive refund from 2000 – 2001); if it did, it was a draconian provision that allowed HMRC to extend time limits for assessment unreasonably. The Tribunal agreed with HMRC’s view that the rule was only capable of “defensive” use by HMRC and was reasonable, proportional and as intended by Parliament.

HMRC also argued that the claim was “abusive”, but the Tribunal did not agree. It failed on the technical ground rather than on the anti-avoidance ground. Costs were nevertheless awarded on the pre-April 2009 basis to HMRC, who were left to decide whether they would not enforce the award because the Tribunal had decided that the “abuse” argument did not succeed.

The company appealed to the Upper Tribunal, which considered the construction and application of s.81(3A) in detail. It was necessary to balance the general right of taxpayers to make corrections to their declarations, and the general right of the authorities to raise assessments, with the practical need for finality which the CJEU had recognised in judgments which permitted the imposition of time limits. The interpretation of s.81(3A) by HMRC and the FTT in the present case satisfied the objectives of the Directive. There had been a single “mistake” – treating the ticket sales as taxable – and that had led both to the overpayment of the output tax and the overclaim for input tax. Offsetting those two amounts was exactly what was prescribed by s.81(3A). The decision of the FTT was upheld.

The UT summarised its conclusions as follows:

129. The discussion above addresses each of the five issues raised before us: (1) properly construed s. 81 (3A) does not permit HMRC to pick and choose; (2) set-off is limited to the same mistake, not to items linked in any other way; (3) no time limitation is required, although some modification of normal procedural rules may be needed; (4) it is unhelpful to characterise the mistakes by asking the question 'one mistake or two?' but the same mistake was made; and (5) no transitional period was required for the implementation of s. 81 (3A).

130. S. 81 (3A) is to be construed subject to the conditions, (1) that all relevant previous years need to be considered and (2) that in relation to the consideration of years in which the taxpayer is not required to keep records, the onus should be on HMRC to show that any adjustment should be made. However the operation of s. 81 (3A) is not precluded by the principles of legal certainty, equality, equivalence, or the supremacy of Community law.

131. So applied the effect of s. 81 (3A) is not incongruent with Community law. The issues of incongruence raised by HMRC do not arise.

Upper Tribunal: *Birmingham Hippodrome Theatre Trust Ltd v HMRC*

6.4.4 New claim?

Reed Employment Ltd won a dispute with Customs in 1997 which established that it should only have accounted for VAT on the commissions it received from clients, not on the whole of the consideration. It submitted a claim which went back to 1991, originally capped but paid by HMRC in 2003 following the first *Marks & Spencer* ruling in the ECJ.

The company then made a further claim, going back to 1973, in relation to customers who were wholly or partly exempt and who would therefore not have been able to recover the VAT that had been charged to them. As this was a new claim, HMRC refused it, and the company appealed.

In March 2009, the company made further claims going back to 1973 in respect of supplies to clients who were taxable. HMRC argued that these repayments would unjustly enrich the company. The rules on unjust enrichment were found to be faulty by earlier court decisions and were rectified in 2005. The amounts claimed were in total £140m, made up of two separate amounts – about £64m which was expressed as an amendment to the 2003 claim (which was only £4m), and the other which was an additional claim for about £76m.

In 2011, the FTT examined the contracts and the history of the dispute, and concluded that the 2003 claim had to succeed. It was based on the same arguments as the 1997 claim and was made before the unjust enrichment rule was rectified. However, the 2009 claims were new claims, not amendments of the 2003 claims, and they failed to satisfy the new unjust enrichment rule. HMRC were able to refuse them.

The company appealed to the Upper Tribunal, which has upheld the FTT decision. The judge noted that he was only considering the question of whether the 2009 claims were "new claims" – he did not address the further question of whether the revised unjust enrichment rules would indeed prevent the company enjoying the repayment. In his view, the FTT's finding that the 2009 claim was not an amendment was not a mere amendment of the 2003 claim was a decision of fact which it was entitled to reach on the evidence, and was manifestly correct.

Reed also argued that the unjust enrichment defence itself contravened the EU principles of effectiveness, equal treatment and fiscal neutrality. This was because the problem with unjust enrichment up to 2005 was dealt with by correcting the law with immediate effect from 26 May 2005, in effect removing traders' rights in the same way that the introduction of the 3-year cap had removed them in 1996. If it had made its claim in early May 2005, it would have succeeded; it only delayed doing so until 2009 because it had believed in 2005 that the 3-year cap prevented it from claiming at all.

The judge did not agree that the correction of the unjust enrichment rules was comparable to the introduction of the cap. He considered that Reed's right was "*to obtain repayment of overpaid VAT subject to an unjust enrichment defence that has been properly introduced into UK law. Reed's claims were made in 2009, at the time when there was a valid unjust enrichment defence and it is the subsequent payment of those claims which could cause Reed to be unjustly enriched (see in that regard M&S 2 at para 52). Reed's EU law right is not the right to be put back in the position that it would have been in while the invalid three-year cap was in force when there was no valid unjust enrichment defence.*"

There was no infringement of the principles of equal treatment or fiscal neutrality. On all the preliminary grounds, therefore, Reed's appeal was dismissed.

Footnote on the technical issue

Following the 1997 case, HMRC introduced the staff hire concession as a temporary measure to reduce the possibility of distortion of competition between different employment businesses which structured their contracts in different ways; the ESC was withdrawn in 2009 because HMRC believed it was no longer needed: changes in the law affecting temporary workers eliminated the possibility of distortion.

The FTT also considered the fundamental question of whether Reed was supplying the services of its workers as principal, or rather supplying an introductory service. If it was supplying introduction only, its taxable income would only include its commission, rather than the whole amount paid by the client. The concession allowed an employment business to account for output tax only on the commission, as long as certain conditions were met.

The FTT decided that the proper construction of the various contracts meant that Reed was supplying agency services as a matter of law, not as a concession. The workers supplied no services to Reed; the payment of their wages did not constitute a cost component of Reed's supply. Even if Reed invoiced the client for a single composite amount, nevertheless the worker made the supply of services direct to the client in return for the payment of their wages.

This appeared to undermine the basis on which HMRC withdrew the staff hire concession, but as HMRC had won the case they could not appeal. They stated in *Revenue & Customs Brief 32/2011* that they did not accept the decision and would not pay other claims based on it. Since then, no other cases on this point have proceeded to the First-Tier Tribunal.

Upper Tribunal: *Reed Employment Ltd v HMRC (No. 3)*

6.4.5 Direct claim by persons suffering the tax

Following the CJEU judgment in *JP Morgan Fleming Claverhouse*, HMRC made repayments of VAT charged by investment managers to investment trust companies. This would have been subject to the principles of unjust enrichment – i.e. the managers would have had to pay the money back to their clients, the ITCs – and also subject to capping, in that only 3 years' worth would be repaid.

A group of ITCs are claiming compensation directly from HMRC in respect of the amounts which were not repaid because of the cap. In early 2012, the High Court considered that the issues are similar to those in a group action brought by other companies in respect of corporation tax (the "FII Group Litigation"). In that case, the Court of Appeal had held that the claims were time-barred because they were made more than 6 years after the periods concerned.

The judge decided to hold over the current litigation pending consideration of the FII Group case by the Supreme Court. In the light of that judgment, which was issued later last year, and also the CJEU ruling in *Littlewoods Retail Ltd*, both parties made further submissions to the court.

The judge has given a further judgment following these submissions. It seems likely to be appealed further, partly because the FII Group case will involve a reference to the CJEU, and partly because the judge held that one of the claims succeeded and another two failed – therefore making sure that both parties were likely to be looking for reasons to disagree with him.

The judge was concerned that a claim by someone who bore the burden of the tax, but was not liable to pay it to the authorities (i.e. a customer rather than a registered trader), should be a last resort rather than a freely available alternative. In his view, the precedents showed that, as a matter of EU law, those people should have an effective right to recover tax suffered in breach of the Directive, if no other right was available to them. They could not recover the tax outside the capped period through the suppliers, because those suppliers were subject to the cap; therefore they ought to be able to recover it directly from HMRC.

This meant that one of the claimants succeeded; the other two were making claims in respect of VAT incurred during the three years in which the supplier could claim, and their claims therefore failed.

High Court: *Investment Trust Companies (in liquidation) v HMRC*

6.4.6 Capping

A livestock farmer failed to make returns for 03/02 and 06/02. A centrally issued assessment for £64,500 was raised in 02/05; amounts paid by the taxpayer were allocated against these assessments. She eventually filed the returns in January 2009, showing a total amount due of £3,700.

Her VAT advisers based an appeal on the argument that the time limit for a "claim" should run from the period in which an assessment was raised, rather than from the original period to which the return related. They appear to have attempted to argue that the four-year cap should apply, and it was therefore possible in January 2009 to correct the assessment which was made in February 2005.

The Tribunal chairman appears to have accepted as a matter of principle that the starting date for the cap is the period in which the assessment was raised, not the return period itself. However, he noted that the three-year cap operated up to 31 March 2006, so it would have been necessary to make a claim by 31 March 2008 in respect of an assessment raised in the return period 03/05. Clearly, this had not been done, so the appeal was struck out.

First-Tier Tribunal (TC02547): *Edith Dianne Hitchen*

A trader failed to file VAT returns on 48 occasions over 17 years of registration. He received central assessments for the periods 12/06 and 02/07 which he paid, and subsequently asked for repayment when in February 2012 he had filed returns showing one much smaller liability and one repayment due.

The Tribunal chairman expressed regret that an appeal hearing was necessary, as it was clearly impossible for the Tribunal to do anything other than confirm HMRC's refusal of the repayment. The four-year cap applied, and there was no scope for entertaining a reasonable excuse for failing to file returns, even if there was one. The fact that HMRC's system allowed the trader to file outstanding returns online even after the four-year deadline might have misled him into believing that there was some point in submitting them, and the chairman suggested that HMRC should make it clearer on their website that the cap would apply.

First-Tier Tribunal (TC02552): *Anthony Geller*

6.4.7 Golf club claim

A members' golf club (ET) paid a neighbouring club (GC) for use of its facilities by its members. VAT was charged on these fees. Following the CJEU decision in *Canterbury Hockey Club*, ET asked GC to claim the VAT back from HMRC and return it to ET. ET also claimed directly from HMRC, but this was refused on the grounds that ET was not a person who had overpaid VAT within s.80.

GC made a claim and paid £20,400 to ET, apparently after deducting expenses of making the claim; but ET claimed further that HMRC had reduced the repayment by restricting GC's input tax, and this unfairly deprived ET of some of its proper reimbursement. The total amount of VAT paid by ET to GC and reclaimed was £41,500. ET appealed against HMRC's refusal of its claim.

HMRC applied for the appeal to be struck out on the grounds that ET had no standing under s.80. It could only claim money back from GC, which would then have to claim from HMRC.

The Tribunal noted that no evidence had been produced by either side to explain what had been repaid by GC to ET. The chairman agreed with HMRC that the primary route to claim back VAT lay through GC; only if relief was "impossible or excessively difficult" would ET have a direct right against HMRC. However, until the CJEU ruled in the *West Bridport Golf Club* case (expected in the summer of 2013 at the earliest), it would not be possible to know to what extent GC's repayment claim had been correctly restricted by HMRC.

Accordingly, HMRC's application to strike out the appeal was refused, and the case was stood over pending the outcome of the *West Bridport* case in the CJEU.

First-Tier Tribunal (TC02602): *The Earlsferry Thistle Golf Club*

6.5 Timing issues

Nothing to report.

6.6 Records

6.6.1 Self-billing

A scrap metal dealer had operated a self-billing system for VAT for many years. There were no formal agreements in place with any suppliers, but HMRC had carried out a number of visits and were well aware of how the company operated. Between 2006 and 2008, HMRC deregistered four of the company's suppliers, and subsequently assessed to disallow £337,000 of input tax claimed by the company on its self-billing invoices in respect of supplies from these suppliers.

The Tribunal examined the background and concluded that the absence of self-billing agreements, combined with the regular visits, meant that HMRC had exercised discretion under reg,29 to allow the company's input tax claims on invoices which did not meet all the conditions of the regulations. Given that this discretion had been exercised for so long, it was not reasonable to withdraw it in relation to these particular invoices, where the company could not have been expected to know that the suppliers had been deregistered.

The case of *Boguslaw Juliusz Dankowski v Dyrektor Izby Skarbowej w Lodzi* (Case -438/09) was referred to as authority for the proposition that a member state cannot disallow input tax just because a supplier is not registered for VAT: a trader who has received a taxable supply from a taxable person is basically entitled to deduct the input tax, unless other conditions are met (e.g. knowledge or means of knowledge of connection to fraud).

First-Tier Tribunal (TC02548): *G B Housley Ltd*

6.7 Assessments

6.7.1 Knowledge of facts

In TC02170, a supermarket was assessed to VAT and a s.60 penalty on the basis of a till roll taken away on a control visit that indicated underdeclarations over several periods. The total assessment was for VAT of £82,859, increased by a penalty of 80% – another £66,287.

The FTT examined the evidence, which included 24 hours of CCTV footage to provide evidence of the level of trade. It concluded that a particular "clerk 4" button had been deliberately used to suppress reported sales, and that someone in the business knew the amount of the "clerk 4 sales". The assessment had been made to the best of the officer's judgement, and the appeal was dismissed, except in relation to two periods in which it appeared that HMRC had sufficient information to raise the assessments over 12 months before they were issued. HMRC were given the opportunity to make further representations on this issue if they wished.

At a further hearing, the Tribunal considered new representations made by HMRC. It accepted that the assessments finally made were in time; HMRC could have raised assessments in respect of the periods earlier, but they could not have raised these assessments, because they did not receive sufficient evidence until certain information had been provided by the supermarket's accountants. Accordingly, the assessments were valid.

First-Tier Tribunal (TC02464): *Bounds Green Supermarket (a partnership)*

6.7.2 Best judgement

An individual took over the running of a pub for a short period. He discovered that the records were in a mess, and withdrew from the business fairly quickly; however, in the meantime he had signed VAT returns which an HMRC officer decided were unreliable. Assessments were raised on the basis of estimated mark-ups following an extensive correspondence between the officer and the publican's accountants.

The Tribunal found the publican to be an honest witness, but he did not have the evidence available to discharge the burden of proof that rested on him to show the assessments to be unsound. The Tribunal suspected that the accountants may have underestimated the costs and the split of food and drink sales may have been unreliable, but in the absence of any proper evidence, it was not possible to make any findings of fact. The officer's approach had been an honest and reasonable one, and the assessments were upheld.

First-Tier Tribunal (TC02469): *Peter Whitehouse t/a Freemasons Arms*

A local shop was assessed for underdeclaring its takings. It disputed the basis of HMRC's assessment, but its own figures suggested that it rang up a "no sale" on the till (enabling the drawer to be opened without recording takings) 44,000 times out of about 131,000 total transactions in a six-month period. The Tribunal did not consider that there was any reasonable explanation for this, or evidence to support the explanations that were given; it concluded that there was reason to suppose that the takings were understated, and the assessment was raised to the best of the officers' judgement. The appeal was dismissed.

First-Tier Tribunal (TC02546): *Thambithurai Sanjeevraj t/a Cambridge Food & Wine*

6.7.3 Default interest

A company appealed against the imposition of default interest of £11,000 in respect of a VAT liability that should have been paid by 31 July 2007, but which was eventually paid on 21 December 2010.

The company's argument was that HMRC had not been short of the money. It had claimed input tax which was due to another company in its group; it had therefore repaid that money to HMRC, who had in turn repaid it to the group company.

The Tribunal noted that there had been significant problems with the group's tax compliance, leading to two threats of winding-up petitions from HMRC during the period. This might explain why HMRC paid close attention to the individual liabilities of individual companies. The Tribunal accepted that each company's VAT must be assessed and settled separately, and dismissed the appeal as without merit.

There was no mention of the policy of HMRC to charge interest only where there is a need for "commercial restitution". The policy is still current, and is set out in the online manuals at VDIM3000.

First-Tier Tribunal (TC02495): *Dudman Group Ltd*

6.8 Penalties and appeals

6.8.1 Legitimate expectations

Back in 2011, a trader had a rare success with the "legitimate expectation" argument in a dispute about pre-registration input tax (solicitors' bills in relation to disputes with builders who were working on a restaurant he intended to open). The Tribunal accepted that he had telephoned the Advice Line and had been told that there was a three-year window for claiming pre-registration tax. This created a legitimate expectation of repayment.

The trader had visited an office of HMRC, taking with him the invoices for the supplies concerned, and had asked very specific questions about when he should register for VAT in order to recover the input tax on these specific invoices. Although there was no record of the telephone conversation, the Tribunal accepted the trader's evidence of the content of the discussion, and held that it satisfied the basic conditions for the creation of a legitimate expectation: he had given the relevant information and made it clear that he would rely on the resulting advice. The fact that he had failed to ask for written confirmation did not fatally undermine the argument.

The chairman went on to consider whether he had jurisdiction to allow an appeal on this basis, quoting at length from the *Oxfam* decision in which the point is discussed. He concluded that he did, and allowed the appeal.

HMRC have now succeeded in overturning this decision in the Upper Tribunal. The judges (Warren J and Judge Colin Bishopp) considered in great detail whether the FTT has jurisdiction to consider the legitimate expectations defence, and decided that it does not. They commented at the outset that their decision should not be considered as being as authoritative as it might have been had the appellant been legally represented; it had been expected that the appeal would be heard together with another on the same issue where the taxpayer had instructed leading counsel, but that case was settled shortly before the hearing. As a result, this appellant had to rely on the judges themselves and on HMRC's counsel acting properly in bringing all the arguments to the Tribunal's attention. Even though the decision contains this reservation, it is nevertheless binding on the FTT, so it seems that legitimate expectations cannot now be a ground of appeal by that route.

In effect, Sales J in the *Oxfam* case appeared to hold that any ground at all could be brought forward in an appeal about the deductibility of input tax under s.83(1)(c). The UT explained in detail why they considered that this was wrong:

a. If Parliament had intended to confer this jurisdiction on the VAT Tribunal, we would have expected it to say so clearly. Even as late as the passing of VATA 1994, a fortiori when the VAT Tribunal was first set up and given a statutory appellate jurisdiction, it would have been exceptional for an inferior tribunal to have a judicial review jurisdiction or an appellate jurisdiction allowing it to adjudicate on public law issues other than in the course of its statutory jurisdiction. VATA 1994 does not use words which clearly confer such a jurisdiction, reliance instead having to be placed on the words "with respect to".

b. In cases where an inferior tribunal is intended to have a judicial review function, express provision has been made. See, for instance, the powers given to the newly-created (and now abolished) Charity Tribunal under section 8 Charities Act 2006.

c. We have referred to the structure of the tribunal system put in place by TCEA 2007 at paragraph 29 above. Parliament decided that the F-tT should not have a judicial review function; and although the Upper Tribunal does have a judicial review function, its jurisdiction usually comes into play on the transfer of a case commenced in the Administrative Court. It is only in a very limited class of case that a judicial review application can properly be commenced in and heard by the Upper Tribunal. It is well known that there was significant opposition even to these powers being conferred on the Upper Tribunal. It is simply inconceivable that Parliament would have contemplated conferring a similar power on the F-tT notwithstanding the two factors which Sales J identified and of which legislators were well aware.

d. Just as it was inconceivable that the F-tT should be given a judicial review jurisdiction, so to it was not plausible, in our view, that Parliament, when enacting section 83 VATA 1994, intended to confer a judicial review function on the VAT Tribunal.

e. We are bound to say that, if it was plausible in the way which Sales J suggests, it is very surprising that the point was not raised in litigation or otherwise many years before Oxfam came before the court. In fact, it was not raised as a plausible result before the VAT Tribunal even in Oxfam itself. As Sales J acknowledged, he was departing from a widely held view, a view which, on his approach, was entirely at odds with what Parliament is to be supposed to have wished to achieve. Although Sales J describes the view as widely held (and we do not know on what he based that description) we ourselves know of no contrary view being promoted as a correct view prior to the decision of Sales J himself.

f. Further, if Parliament's intention had been as Sales J suggests, we would have expected the same Parliament to have introduced secondary legislation in the form of suitable tribunal rules to govern the procedure (and in particular rules concerning permission to bring judicial review and time-limits) applicable to public law claims.

That meant that the appellant should not have succeeded before the FTT. However, he could perhaps have made a different appeal to the UT, and the UT considered the merits of his case on the basis of the facts. Although it was clear that HMRC had made mistakes, the judges did not consider that these were so great that to enforce the law, contrary to the advice they had given, amounted to an abuse of power. As a result, the appeal on judicial review grounds would fail.

Possibly the taxpayer could now try claiming compensation through the Adjudicator's Office.

Upper Tribunal: *HMRC v Abdul Noor*

6.8.2 Late appeals

A working men's club made a *Linneweber* claim by voluntary disclosure on 15 August 2006, covering the periods from 1 July 2003 to 30 November 2005, and applying for £6,752. HMRC rejected the claim by letter of 19 July 2007. The letter offered a reconsideration; the club's accountant said that he had intended to apply for one but overlooked it. The accountant admitted that he and the club's officers had taken a deliberate decision not to appeal, believing – as it turned out, incorrectly – that an appeal would involve committing an impractical amount of the club's funds to arguing with HMRC. He had not realised that it would have been possible merely to make the appeal and have it stood over behind *Rank*.

The club asked for the matter to be reconsidered by letter of 13 October 2010. HMRC replied on 3 November 2010, stating that the claim had already been rejected. After some further correspondence, the club eventually lodged an appeal on 3 December 2011. HMRC applied for the appeal to be struck out as made out of time.

The Tribunal considered that there were factors in each direction to be balanced; however, the length of the delay, and the culpability of failing to find out that merely making an appeal would not involve any great expense, outweighed the effect on the club and the fact that the claim probably had some merit. The appeal was struck out.

First-Tier Tribunal (TC02436): *Moulton Working Mens Club*

The same accountant also acted for another club which also had a claim rejected. Although the dates were different, the facts were very similar, and so was the result: the appeal was made out of time, and would not be heard.

First-Tier Tribunal (TC02435): *Wilby Working Mens Club*

Demonstrating admirable political balance, a similar decision was made in a separate case involving a claim in respect of gaming machines at a Conservative Club.

First-Tier Tribunal (TC02435): *Rosary Conservative Club*

A variation on the normal gaming machine situation arose in a case where a voluntary disclosure, made on 2 July 2007 and refused on 31 July 2007, had been "appealed" on 22 August 2007. The trader asked for the appeal to be stood over behind *Rank*. HMRC then wrote on 20 October 2009 to say that it was no longer HMRC policy to allow such appeals to be held over, and a formal appeal to the Tribunal would now be necessary.

The traders sent an appeal within 30 days, but directed it to HMRC's office rather than to the Tribunal. In August 2010, they closed their business and emigrated to Australia. The status of the "appeal" was not followed up until their agents wrote to HMRC in March 2012 to find out what was happening before closing their files.

The Tribunal had some sympathy with the appellants; if the only factor had been the failure of HMRC to redirect the appeal form to the Tribunal, or to point out that the wrong procedure had been followed, leave to appeal out of time might have been granted. However, given that the traders had in the meantime closed their business and deregistered, and had failed at that time to follow up the status of the appeal they claimed to believe was in progress, there was more than a mere administrative error. The agents and the taxpayers had not exercised proper diligence in pursuing the matter. Leave to appeal out of time was refused.

First-Tier Tribunal (TC02504): *Tamar Leisure Spot*

An unusual argument in a hearing about leave to appeal out of time concerned an individual who had registered for VAT and submitted repayment returns claiming input tax on expenditure on premises. HMRC refused to make the repayments, holding that the individual's intention was to let the premises rather than to make taxable supplies. The individual claimed not to have received the ruling, but produced no evidence to support this; HMRC produced no evidence to prove that the ruling had been posted, other than the existence of copy letters on the file. The Tribunal therefore decided to consider whether the appeal would have any merit if leave to appeal was given.

The Tribunal examined the "management agreement" between the individual and the person who occupied the shop. It appeared relatively clear that this was in reality a rental agreement, and the profits of the shop accrued to the "manager", not the owner. Combined with the significant delay in following up the non-receipt of the repayments claimed – regardless of whether the letters had been received explaining why – this counted against the appellant in excusing a late appeal. Leave was refused.

First-Tier Tribunal (TC02519): *Touqueer Ahmed Khan*

Another unusual appeal concerned the confiscation of a car which had contained 14.5kg of hand-rolling tobacco when about to cross from France to the UK. Goods on which duty appears likely to be evaded are subject to forfeiture, and this extends to any vehicle or other form of transport which is used to convey them. After the car was seized in June 2011, there was some correspondence about it, leading to a decision by HMRC on 7 September 2011 not to return the vehicle; the owner appealed two months after this decision, one month late.

The Tribunal reviewed the background and the policy underlying the law on confiscation. It was intended to produce hardship; the vehicle was usually only restored where an owner had been a wholly innocent party. In this case, there had been inconsistent explanations and some doubt about the true ownership of the vehicle. Combined with the delay in making the appeal, this counted against allowing an appeal out of time, and leave was refused.

First-Tier Tribunal (TC02536): *Fahmi Hakim*

An appellant wrote in September 2010 to find out what had happened to a claim allegedly sent in August 2006, claiming repayment of output tax on *Linneweber* grounds for the period from August 2003 to December 2005. HMRC could find no trace of the earlier letter, and refused to entertain any such claim.

The Tribunal examined the evidence, which for the appellant mainly turned on the recollections of two officials of events taking place some five or six years earlier. The chairman was not satisfied that they could show that on a balance of probabilities the letter had been signed and mailed to HMRC at the time they claimed. HMRC's decision to refuse to entertain the claim was confirmed.

First-Tier Tribunal (TC02582): *H & W Staff Sports & Recreation Association*

A different problem arose in a case in which a trader had appealed against the disallowance of over £1.8m of input tax for the periods 03/06, 04/06 and 05/06 on "missing trader" grounds. A hearing commenced on 16 April 2012, but on the first day the appellant withdrew its appeal on counsel's advice. It later tried to reinstate it.

The Tribunal wrote to the appellant's representatives on 17 April 2012 with the information that it could reinstate the appeal within 28 days. The director claimed that this letter was not passed on. No action was taken until he wrote to apply to reinstate the appeal on 16 October. HMRC sought to have this further appeal struck out as being out of time. There was a separate appeal in progress about the withdrawal of the company's registration under the Warehousekeepers and Owners of Warehoused Goods Regulations (its "WOWGR" licence). This appears to have arisen because of the withdrawal of the appeal – HMRC had not taken action to collect the debt that now fell due, but issued a notice stating that the company was no longer regarded as a fit and proper person to hold a licence because of that debt.

It appeared that the appeal had been withdrawn because there had been other irregularities with the director's personal tax and the company's direct tax. There was evidence of dishonesty which counsel had advised would make it hard to persuade the Tribunal that there was no knowledge or means of knowledge in the VAT case. The director claimed not to have appreciated the consequences of withdrawing the appeal, which he had considered well-founded, and also claimed that it had been dropped because of a personal issue between himself and counsel, not because of any problem with the appeal itself.

The Tribunal was not satisfied that any of this provided an excuse for the late application to reinstate. The chairman concluded that the director had withdrawn the appeal in full awareness of the consequences at that time; the fact that the WOWGR licence was later withdrawn because the VAT debt had not been paid was not such an unexpected outcome that it should give the company more time to continue the original appeal. The application was refused.

First-Tier Tribunal (TC02587): *Pierhead Purchasing Ltd*

6.8.3 Appealable matter?

A trader had dealt in used cars from 2000. It was discovered that he was using the margin scheme even though some of the cars were "qualifying cars" on which VAT should be accounted for under the normal rules. He appealed against an assessment for some £34,500 (including interest). He did not have a technical defence: he argued that HMRC should have noticed his mistake earlier, and the assessment would lead to bankruptcy.

HMRC applied to have the appeal struck out on the grounds that such an argument was not within s.83 VATA 1994. The chairman had some sympathy for the trader, but observed that it was the responsibility of taxable persons to familiarise themselves with the requirements for their trade. The appeal was dismissed.

First-Tier Tribunal (TC02589): *Stuart Cross t/a Euromarques*

6.8.4 Dishonesty penalty

A company registered for VAT in 2008. HMRC ruled that it should have registered earlier; when it went into liquidation, they charged a s.60 dishonesty penalty, and allocated it to the controlling director under s.61. She appealed against the penalty and its imposition on her.

It appears that this was another case in which the company's accounts were prepared once a year; the accountant therefore realised some time in arrears that the company had exceeded the registration threshold, and should at that time have approached HMRC to negotiate retrospective registration, or possibly to claim exception from registration; the accountant had believed or hoped that turnover would fall again, and had therefore not taken either action; and when turnover in fact increased, he advised registration from some 15 months after it should have taken place.

The Tribunal examined the background, hearing witnesses including the director and the accountant. It commented that putting the company into liquidation and not answering HMRC's questions was "a most curious way to proceed and not advisable"; however, HMRC had not discharged the heavy burden of proving that the director had acted dishonestly, either in accordance with the standards of a "reasonable person", or subjectively in relation to her own intentions. The appeal was allowed.

First-Tier Tribunal (TC02544): *Glenda Candy*

6.8.5 Costs

A trader in a MTIC case applied for the "old costs rules" in relation to an appeal which straddled 1 April 2009. The Tribunal considered the Upper Tribunal precedent case of *Atlantic Electronics Ltd* and decided that it would not be appropriate to accept the trader's application: it had been made very late in the proceedings, and it was therefore not fair on HMRC who would by that stage have been entitled to assume that the new costs rules would apply.

First-Tier Tribunal (TC02425): *Hillcraft Trading Ltd and related appeal*

The same precedent was considered, but with the opposite outcome, in another case involving anti-dumping duty and import VAT. The Tribunal observed that the case had been held in abeyance for long periods, both before and after 1 April 2009, at HMRC's request. It was an unusual case, but it was reasonable in the circumstances to allow the appellant the benefit of the old costs regime, and the case was remitted for taxation by the Auditor of the Court of Session.

First-Tier Tribunal (TC02444): *Usha Martin (UK) Ltd*

A company (HP) appealed against a VAT decision in similar circumstances to those of *Harrier LLC*. After that company won its case, HP applied for the old costs regime. Harrier had made its own appeal in 2010, but HP's was a transitional appeal. Once again, the precedent of *Atlantic Electronics* was considered; although the taxpayer argued that it should be distinguished for various reasons, the Tribunal ruled that there was no compelling reason to allow the old regime to apply. The application for costs had only been made after the substantive decision had been released, which suggested that it was "opportunistic".

First-Tier Tribunal (TC02459): *Hewlett Packard Ltd*

6.8.6 Procedure

In relation to a MTIC hearing scheduled to run for 4 weeks from 4 February 2013, the appellant applied for an adjournment on the basis that the main director's mental state was such that he would not be able to give instructions or to give evidence. In December the First-Tier Tribunal allowed this application; in January, HMRC appealed against it as a matter of urgency, arguing that the FTT had been wrong in concluding that the director was incapable, and that there would be significant wasted costs if the matter was not considered in accordance with the schedule.

The Upper Tribunal considered the evidence and upheld HMRC's appeal. It should be possible to "*accommodate Mr Wager's needs with the 'slow and patient approach' advocated in* [an independent psychologist's report] *and frequent breaks in his evidence as advocated in his conclusions.*"

Upper Tribunal: *HMRC v Purple Telecom Ltd*

6.9 Other administration issues

6.9.1 Privilege

The Supreme Court has ruled, by a 3-2 majority, that “legal advice privilege” (LAP) only extends to advice given by a member of the legal profession (a solicitor or barrister) and not advice given by a chartered accountant, even if the advice relates to a legal matter on which the accountant is qualified to advise and where such advice would be subject to privilege if it had been given by a lawyer.

The principle of LAP allows a person to refuse to disclose to the authorities information which constitutes advice given by lawyers. It enables lawyers to give advice in confidence, knowing that they cannot be forced to “shop” the client.

The dispute in the case related to advice given by a firm of accountants in relation to a tax planning scheme designed for some clients in 2004. HMRC obtained authorisation from the Special Commissioners (predecessors of the First-Tier Tribunal) to issue notices under the Taxes Management Act requiring the claimants to disclose certain documents. They applied for judicial review of this authorisation, arguing that it was illogical to give LAP to advice that happened to have been given by a lawyer, but to withhold it in circumstances in which the same advice was given by someone else.

The lower courts found against the applicants. The Supreme Court noted that there was some logic behind the application, but extending LAP beyond its widely understood scope was a matter for Parliament, not for the judiciary. Parliament had enacted laws on LAP, and had therefore had the opportunity to include circumstances such as the present case. Although the application related to a specific situation, allowing the application would create a precedent which would have much wider possible implications, and would create uncertainty.

Supreme Court: *R (on the application of Prudential plc) v Special Commissioner of Income Tax*

6.9.2 Alternative Dispute Resolution (ADR)

HMRC has concluded from the two-year pilot of ADR that this should be offered as a standard approach for small and medium enterprises in future, and may be extended to large and complex cases. Over 400 applications for ADR have been received, and favourable feedback has been received from SMEs, advisers and professional bodies.

HMRC Release NAT 20/13

HMRC have updated the April 2012 guidance for staff on the use of ADR in resolving tax disputes. The revised guidance has been expanded on the typical ADR timetable and process, and includes new annexes setting out a model facilitation agreement and guidelines for the “facilitated discussion”. It includes practical examples of the types of dispute in which ADR could be useful.

HMRC Release 7 February 2013

6.9.3 Advice

The government has publicised an online tutorial developed by HMRC to help farmers to understand their tax obligations. The "Starting your own Business" e-learning tutorial includes:

- an overview of tax, National Insurance contributions and VAT
- information on registering as self-employed
- guidance on keeping business records
- help with completing tax returns
- information on paying HMRC

The guide is aimed at those new to farming, who may be unaware of their tax obligations, and at experienced farmers who are currently diversifying, which can change their tax obligations. Although it is aimed specifically at farmers, it may be of benefit to others who are starting out in business.

rnn.cabinetoffice.gov.uk/Press-Releases/Tax-guides-give-advice-to-farmers-68756.aspx

6.9.4 Simplification?

The March Budget included the confirmation that small businesses – those with turnover below the VAT registration threshold – can prepare income tax accounts on a "cash basis" rather than an accruals basis from 6 April 2013. Some expenses can be deducted on a flat rate basis rather than using the actual figures. If the business grows, it will not have to leave the cash accounting scheme until the turnover is twice the VAT registration threshold.

Note that it is therefore possible to be registered for VAT and within the cash accounting scheme for income tax, whether below the threshold and registered voluntarily, or above the threshold and registered compulsorily. The rules for income tax are not exactly the same as those for VAT, so it will not necessarily be a simplification to use them.

Note also that this scheme is not available to companies, which must prepare accounts using proper accounting policies, whether they are above or below the VAT registration threshold.

There are transitional rules for moving into and out of cash accounting.

www.hmrc.gov.uk/budget2013/tiin-2014.pdf

6.9.5 Spotlights

HMRC have updated the "avoidance spotlights" section on their website. This warns taxpayers to be wary of tax saving schemes where:

- It sounds too good to be true.
- Artificial or contrived arrangements are involved.
- It seems very complex given what you want to do.
- There are guaranteed returns with apparently no risk.
- There are secrecy or confidentiality agreements.

- Upfront fees are payable or the arrangement is on a no win/no fee basis.
- The scheme is said to be vetted by a top lawyer or accountant but no details of their opinion are provided.
- The scheme is said to be approved by HMRC (it does not follow that this is true).
- Taxation of income is delayed or tax deductions accelerated.
- Tax benefits are disproportionate to the commercial activity.
- Offshore companies or trusts are involved for no sound commercial reason.
- The involvement of professional trustees is claimed to guarantee that the arrangements succeed.
- A tax haven or banking secrecy country is involved without any sound commercial reason.
- Tax exempt entities, such as pension funds, are involved inappropriately.
- It contains exit arrangements designed to sidestep tax consequences.
- It involves money going in a circle back to where it started.
- Low risk loans to be paid off by future earnings are involved.
- The scheme promoter lends the funding needed.
- There is a requirement to take out insurance against the failure of the tax planning to deliver the tax benefits.

The latest addition involves the reduction of the taxable benefit on an employee's company car. No new VAT spotlights have been added since February 2011 (supply splitting avoidance and relocation of telecommunication service providers).

http://www.hmrc.gov.uk/avoidance/spotlights.htm

6.9.6 Data mining

The Budget included an announcement that HMRC will be given powers to require card payment processors to provide bulk data about business taxpayers to provide greater effectiveness in assessing those card-payment processors which do not declare their full tax liability. This will enable HMRC to find out about the turnover of traders who receive payments for sales through card companies, which are not currently included in the categories of "data holder" on whom HMRC can serve notices.

www.hmrc.gov.uk/budget2013/tiin-2019.pdf

6.9.7 Campaigns

HMRC have announced a new campaign in their series of crackdowns on specific types of non-compliance: from 28 February, they intend to investigate businesses which, despite reminders, have one or more VAT return outstanding. HMRC expect to have to chase some 50,000 businesses in the "VAT Outstanding Returns" campaign. The press release states that more than 600,000 businesses have to put in VAT returns "each month" – presumably that is the average, with some 1.8m total VAT-registered businesses in the UK. 50,000 therefore represents about 3% of the total.

HMRC state that they have raised nearly £540m from their campaigns so far, and £137m from follow-up activity.

HMRC Release NAT 05/13

HMRC have issued two reminders that the disclosure campaign aimed at direct sellers, which opened in September 2012, closed on 28 February 2013. After this date, any undeclared tax will no longer receive favourable penalty terms. HMRC offered a YouTube video to help direct sellers to comply with their responsibilities.

HMRC Press Releases 28 January 2013, 21 February 2013; http://bit.ly/PtpzVO

6.9.8 Managing serious defaulters

HMRC have renamed their "Managing deliberate defaulters" programme, which has been in place since 2011, as "managing serious defaulters" from 1 April 2013. The new scheme will now include those who, since 2009:

- have become insolvent as a way of dodging their tax obligations;
- have received a civil evasion penalty for dishonestly evading VAT; or
- are required to give a security deposit for VAT, environmental taxes, PAYE or NICs.

A person who is under close scrutiny within the programme can expect:

- unannounced visits by HMRC
- asking for records so they can be checked
- carrying out in-depth compliance checks into persons tax affairs
- observing and recording business activities and cross-checking details in accounts.

Defaulters who fail to keep their tax affairs in order may face criminal proceedings.

A set of questions and answers about the programme has been published on the HMRC website.

www.hmrc.gov.uk/news/msd-q-and-a.pdf; www.hmrc.gov.uk/news/tax-defaulters.htm; www.hmrc.gov.uk/compliance/cc-fs14.pdf

6.9.9 Naming and shaming

HMRC have published details of the 32 worst tax evaders on the Flickr image hosting site. They include four men jailed for one of the biggest alcohol smuggling frauds uncovered in the UK, and dealers in fake carbon credits as well as MTIC fraudsters. They were sentenced to a total of nearly 153 years in prison during 2012.

Guardian, 5 January 2013

HMRC has published its first list of deliberate defaulters in accordance with the provisions of s.94 FA 2009. It contains those who have received a relevant penalty for, among other things, inaccurate returns or documents, failing to notify HMRC of a tax liability, or a wrongdoing in relation to VAT, and the tax involved exceeds £25,000. The names can only be published for a year and details must be published within a year of the penalty becoming final. There are just four companies and five individuals on the published list, which HMRC say will be updated each quarter.

HMRC Press Release 22 February 2013; http://www.hmrc.gov.uk/defaulters/index.htm

Rohan Pershad, a QC, has been convicted of one count of cheating the public revenue between 1 June 1999 and 24 September 2011. He failed to pay VAT for 12 years, resulting in retention of over £600,000 which should have been paid to HMRC. He was sentenced to three and a half years imprisonment, but he has announced an intention to appeal. He claimed that he believed his chambers had dealt with the VAT, and he had not acted dishonestly.

www.cps.gov.uk/news/press_statements/qc_convicted_of_gbp_600k_vat_fraud

The owner of a security firm was sentenced to 18 months' imprisonment for failing to pay minimum wage rates to his employees, and for failing to account for at least £72,000 of VAT.

rnn.cabinetoffice.gov.uk/Press-Releases/Security-firm-owner-sentenced-for-minimum-wage-failings-68888.aspx

Three individuals were banned from acting as directors for a total of 20 years for filing incorrect VAT returns in respect of a company they ran, selling small electrical goods on eBay. The returns filed had disclosed liabilities of about £3,000, when the true liability was 100 times greater. The company went into creditors' voluntary liquidation with an estimated deficiency of £311,000.

news-insolvency.bis.gov.uk/Press-Releases/20-year-ban-for-Liverpool-on-line-traders-6860f.aspx

On 7 January 2013, 14 suspects (including 8 members of the same family) were arrested by Hungarian authorities. €4.8 million in cash, as well as luxury motor vehicles and real estate, were seized. The organised criminal group had been trading scrap metal between Hungary, the Czech Republic and Slovakia, using missing traders in the chain to illegally acquire massive amounts of VAT from the authorities of several EU member states.

The estimated VAT losses for the Slovakian authorities exceed €17m, and the Czech losses are nearly €3m.

www.europol.europa.eu/content/press/four-million-euros-seized-14-suspected-vat-fraudsters-arrested-1981

Two men who imported wine from Italy and sold it on without paying more than £5 million in duty and VAT have both been sentenced to more than six years' imprisonment. The men used the same delivery documents multiple times to take advantage of the UK's duty scheme and were extradited from Italy in 2012 after fleeing the UK while on bail in 2009.

www.gov.uk/government/news/wine-smugglers-sentenced-in-5m-wine-fraud

Four members of an organised crime gang, who are currently in prison for their part in a £17 million VAT fraud, have been ordered to pay back £4.38 million of their criminal profits or face a further 18 years in jail.

rnn.cabinetoffice.gov.uk/Press-Releases/Payback-time-for-Surrey-multi-million-VAT-fraudster-68933.aspx

A man has had ten years added to the seven-and-a-half year prison sentence he is already serving after he failed to satisfy a confiscation order for £14,019,439 to be paid by 28 February 2013. He was originally sentenced to prison in 2008 for his role in a conspiracy to steal £38m in a MTIC VAT fraud.

hmrc.presscentre.com/Press-Releases/Extra-10-years-in-jail-for-38-million-fraudster-688bb.aspx

In the first prosecution for film tax relief fraud, five men have been jailed for a total of over 20 years at Southwark Crown Court for their parts in a VAT and film tax credits scam. The men pretended to be filming a £20m Hollywood blockbuster to be produced in the UK. The fraud was based on a bogus film entitled ‘Landscape of Lies’, under which the men submitted fraudulent claims totalling £2.8 million.

When HMRC started to investigate, the conspirators actually produced a film on a budget of £90,000 in an attempt to make the claims appear genuine.

www.cps.gov.uk/news/press_statements/five_sentenced_for__extraordinary__attack_on_public_purse/

6.9.10 Prosecution procedure

An individual was prosecuted in Scotland in connection with a missing trader fraud. He claimed that the prosecution had failed to carry out the same disclosure of all relevant materials to the defence as they would have done in England and Wales, and that this therefore invalidated the prosecution. This argument was rejected by a judge at first instance, and has now been rejected by the Scottish Appeal Court as well.

Scottish Appeal Court: *Ramzan v HM Advocate*

6.9.11 Security requirement

An individual was the director of a security company which had a very poor compliance record. Between October 2005 and the commencement of liquidation in June 2009, it ran up a VAT debt to HMRC of £270,000 in assessments, surcharges and penalties. In January 2009 a new company was set up with a similar name; the VAT registration application was submitted by the director’s wife. The address and telephone number were the same as for the previous company. That company was put into liquidation in October 2011 owing HMRC nearly £70,000 in VAT. The director was made bankrupt in March 2011.

A new company was incorporated in May 2011. The only director was the son of the bankrupt owner of the former businesses. It applied for VAT registration, which was subjected to considerable delay, causing the company financial difficulties. When HMRC eventually registered it, they issued a notice of requirement to deposit security. The company's accountants asked for a review of this decision, pointing out that if – as they suspected – the notice was issued because of the involvement of the father, he was only an employee with no access to the bank account and no control. The responsibility for the VAT lay entirely with the son, who had no previous record of non-compliance.

The father appeared before the Tribunal to give evidence; the chairman records that he "cast a clearer light on matters." However, this evidence was not available to the HMRC officers who had taken the decision or reviewed it, and so it could not be relevant to the Tribunal's conclusion on whether those decisions had been reasonably made. In view of the history and the information available to the officers at the time, it could not be said that the decision was unjustified. The appeal was dismissed.

First-Tier Tribunal (TC02509): *Shand Security Ltd*

A company appealed against a notice of requirement to deposit security. HMRC were able to point to the poor compliance record and financial failure of a company with the same controlling director and line of business. The Tribunal concluded that the decision to require security could not be faulted.

First-Tier Tribunal (TC02553): *Kingsway Lifts Ltd*

HMRC have published two new factsheets explaining notices requiring a deposit of security:

- Securities in respect of releasing a VAT credit
- Securities in respect of VAT at risk

They explain the background to notices, how they may be complied with, and the trader's rights of appeal:

SS/FS2b, SS/FS2a