VAT UPDATE
APRIL 2016

Covering material from January – March 2016

Notes prepared by Mike Thexton MA FCA CTA

No responsibility for anyone acting upon or refraining from acting upon these notes can be accepted by the course presenter or author of the notes.

VAT Update April 2016

Contents

1. INTRODUCTION 1
   1.1 Appeals pending 1
2. OUTPUTS 5
   2.1 Scope of VAT: linking supplies to consideration 5
   2.2 Disbursements 5
   2.3 Exemptions 5
   2.4 Zero-rating 15
   2.5 Lower rate 16
   2.6 Computational matters 17
   2.7 Discounts, rebates and gifts 20
   2.8 Compound and multiple 20
   2.9 Agency 20
   2.10 Second hand goods 23
   2.11 Charities and clubs 23
   2.12 Other supply problems 26
3. LAND AND PROPERTY 30
   3.1 Exemption 30
   3.2 Option to tax 30
   3.3 Developers and builders 31
   3.4 Input tax claims on land 35
   3.5 Other land problems 37
4. INTERNATIONAL SUPPLIES 38
   4.1 E-commerce 38
   4.2 Where is a supply of services? 39
   4.3 International supplies of goods 39
   4.4 European rules 42
   4.5 Foreign refund reclaims 48
5. INPUTS 49
   5.1 Economic activity 49
   5.2 Who receives the supply? 52
   5.3 Partial exemption 52
   5.4 Cars 53
   5.5 Business entertainment 53
   5.6 Non-business use of supplies 53
   5.7 Bad debt relief 53
   5.8 Other input tax problems 54
6. ADMINISTRATION AND PENALTIES 63
   6.1 Group registration 63
   6.2 Other registration rules 63
   6.3 Payments and returns 65
   6.4 Repayment claims 66
   6.5 Timing issues 75
   6.6 Records 75
   6.7 Assessments 75
   6.8 Penalties and appeals 77
   6.9 Other administration issues 101

1. INTRODUCTION

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

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

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

1.1 Appeals pending

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

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

Several of the "appeal will be dropped" items are still on the website list, but where they have already been reported in the update they are not reproduced below.

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

1.1.1 UK appeals awaiting hearing or decision

- *The Chancellor, Masters & Scholars of the The University of Cambridge*: HMRC are seeking leave to appeal against the UT's decision that VAT incurred on investment management was residual input tax of the whole operation.
- *Colaingrove Ltd*: HMRC's list used to contain four separate appeals, but this has been reduced to just TC02534 (fuel – UT decision in favour of HMRC; in April 2015 the CA started to hear the company's appeal against the UT's decision that it was not entitled to apply the lower rate to electricity supplied as part of a compound supply of "caravan with electricity"). This therefore appears to be the only remaining "live" issue, but the CA hearing is not mentioned in the HMRC list. The cases about removable contents/definition, removable contents/apportionment and verandas are now resolved.
- *Copthorn Holdings Ltd*: HMRC are seeking leave to appeal against the FTT's decision that they should reconsider their refusal to allow retrospective grouping.

- *Davis & Dann Ltd and Precis (1080) Ltd*: HMRC have received leave to appeal to the Court of Appeal against the Upper Tribunal's decision that the companies did not have the means of knowing that their transactions were connected with fraud (hearing listed for 24 November 2015).
- *Finmeccanica Group Services SpA*: taxpayer has been given leave to appeal to the Court of Appeal against the UT's ruling that it was making supplies in the UK and was therefore not entitled to a refund under the 8th Directive.
- *GMAC UK plc v HMRC*: the UT reaffirmed its own decision in favour of the taxpayer on the basis of the CJEU decision (Case C-589/12). HMRC have been granted permission to appeal to the CA.
- *Investment Trust Companies (in Liquidation) v HMRC*: after the CA effectively reversed the High Court's decision in relation to the companies' direct claims for overpaid VAT, both parties have been given leave to appeal to the Supreme Court (hearing listed for May 2016).
- *Iveco Ltd*: HMRC have been granted leave to appeal to the Upper Tribunal against the FTT's ruling that a claim for repayment was not subject to the cap (hearing listed for 24 – 25 November 2015).
- *Kati Zombory-Moldovan t/a Craft Carnival*: HMRC have been granted leave to appeal to the Upper Tribunal against the FTT's ruling that the trader was making exempt supplies of land.
- *Littlewoods Retail Ltd*: HMRC have been granted leave to appeal to the Supreme Court against the CA's decision in favour of the company on the question of compound interest on long-term repayments. HMRC are appealing on both liability and amount.
- *Longridge on the Thames*: HMRC have been granted leave to appeal against the UT's dismissal of their HMRC appeal against the FTT's ruling that a charity was not in business and could receive building services zero-rated (appeal scheduled to start in the Court of Appeal 19/20 April 2016).
- *MG Rover Group Ltd*: HMRC have been granted leave to appeal against the FTT's decision about who is entitled to claim a refund where an overpayment was made on a group VAT return – case management decisions on this case and *Standard Chartered/Lloyds Banking Group* were issued in March 2015, hearing listed for July 2016.
- *Newey t/a Ocean Finance*: HMRC have been granted leave to appeal to the Court of Appeal against the UT's decision that the FTT was correct to find that the appellant's offshore business arrangements were not an abusive practice, hearing listed for July 2016.
- *National Exhibition Centre*: Upper Tribunal has referred questions to the CJEU.
- *Open University*: HMRC have been granted leave to appeal to the Court of Appeal against the UT's decision that the FTT was correct to find that supplies by the BBC to the OU qualified for exemption on

the basis that the BBC was "another organisation defined by the UK as having similar objects", hearing listed for February 2016.

- *Pacific Computers Ltd*: the FTT found in favour of a MTIC appellant. HMRC have been given leave to appeal to the UT.
- *Privin Corporation Ltd*: the FTT found in favour of a MTIC appellant. HMRC are seeking leave to appeal to the UT.
- *The "Spotting the Ball" Partnership & Others*: the taxpayers have been granted leave to appeal to the CA against the UT's overruling of the FTT decision in their favour in relation to the exemption of "spot the ball" competitions (hearing listed for November 2015 has been postponed – new date awaited).
- *University of Huddersfield Higher Education Corporation*: the company has been granted leave to appeal to the CA against the UT's decision that its scheme was abusive.
- *Vodafone Group Services Ltd*: HMRC have been granted leave to appeal against the FTT's decision that the trader could replace the reasons for an in-time but disputed claim with the grounds for an accepted but out-of-time claim (UT hearing listed for December 2015).
- *Whistl UK Ltd*: the Court of Appeal will hear a further application for judicial review after the High Court held that the UK's amendments to the VAT exemption for postal services were compatible with EU law (hearing April 2016).

1.1.2 Unresolved cases not on the list

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

- *HMRC v Atlantic Electronics Ltd*: the Court of Appeal reserved judgment in a dispute about the admissibility of evidence in a MTIC fraud case.
- *Airtours Holidays Transport Ltd v HMRC*: in February 2016, Supreme Court heard taxpayer's appeal against Court of Appeal ruling upholding FTT's decision that it could not deduct input tax on professional fees associated with reports from accountants to persuade lenders to continue to finance the company (hearing concluded 25 February, judgment reserved).
- *John Wilkins Ltd and others*: Supreme Court refused HMRC permission to appeal one aspect of the case, in which the Court of Appeal decided that motor dealers were entitled in principle to claim compound interest on VAT repayments. Substantive issue stayed pending the *Littlewoods* decision in the Court of Appeal (High Court applied the CJEU's judgment in Case C-591/10 in favour of the taxpayer, but HMRC have appealed).
- *R (on the application of Rouse) v HMRC*: HMRC appealing against Upper Tribunal's decision that they were not entitled to set off a credit against money owing from the taxpayer under s.130 FA 2008.

- *Shop Direct Group Ltd*: the company is continuing to appeal against the ruling that VAT repayments and interest are subject to corporation tax (Supreme Court hearing concluded 10 December 2015 with judgment reserved, but the case is no longer on HMRC's list).
- *Volkswagen Financial Services (UK) Ltd v HMRC*: HMRC have been granted leave to appeal to the Supreme Court against the Court of Appeal's upholding of the FTT's decision that the company's partial exemption special method, recovering overhead input tax on a "transaction count" basis, was more fair and reasonable than HMRC's method which treated the trader as wholly exempt.
- *Wilton Park Ltd*: company will appeal to CA against FTT and UT decisions that its charges to dancers for redeeming "Secrets Money" were standard rated (hearing listed for 5/6 October 2016).

1.1.3 Cases in the current update

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

- *British Film Institute*: on HMRC's appeal to the Court of Appeal against the UT's confirmation of the FTT's decision that the Institute was entitled to rely on the cultural services exemption in the period 1990 – 1996 in support of a *Fleming* claim, questions will be referred to the CJEU.
- *Finance and Business Training Ltd v HMRC*: taxpayer is applying for leave to Court of Appeal against UT's upholding of FTT's decision that it was not an "eligible body" by being so closely connected with the University of Wales that it became a "college of the university" – oddly, the list says that "HMRC is appealing", even though the decisions below went against the taxpayer (hearing 7/8 October 2015, decision awaited).
- *Wakefield College*: HMRC have been granted leave to appeal against the FTT's decision (itself a finding on remittal from the UT) that the college's buildings were used for non-business purposes (hearing 27 – 28 July 2015, decision awaited).

1.1.4 Other reported developments on appeals

The following cases appear to have reached the end of the appeal trail:

- *Massey and another trading as Hilden Park Partnership v HMRC*: the Court of Appeal refused the trader's application for leave to appeal against the UT's decision that its arrangements (exploiting the sporting exemption) were abusive and should be disregarded by HMRC.
- *United Grand Lodge of England v HMRC*: Court of Appeal refused taxpayer's application for leave to appeal against the UT's confirmation of the FTT's ruling that it did not qualify for the exemption for a body with civic aims.

2. OUTPUTS

2.1 Scope of VAT: linking supplies to consideration

Nothing to report.

2.2 Disbursements

Nothing to report.

2.3 Exemptions

2.3.1 Claims handling not exempt

A Polish company provided claims handling services in the name of and on behalf of an insurance company, although it had no legal relationship with the insured person. The company received and processed claims, and enquired into the circumstances in order to agree the amount to be paid under the policy.

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

The full court has agreed with this opinion. "Insurance transactions" can include supplies under a block policy, as in *Card Protection Plan*, but that still requires a relationship between the supplier and the insured person in that the supplier ensures that the insured person is covered by the policy. In circumstances such as those in the present case, the services might be an essential part of the insurance transaction, but they did not fall within the scope of "insurance transactions" when supplied by the appellant to the insurer outside of any legal relationship with the insured person.

The CJEU acknowledged that "related transactions" could cover what the appellant did, and that the required relationship with the two principals could be indirect (as in the case of *Beheer*, where a sub-agent was held to qualify for exemption). However, the work of the supplier must include the essential aspects of the work of an insurance agent, such as the finding of prospective clients and introducing them to the insurer – "the conclusion of insurance contracts", rather than the settling of claims later.

The answer to the question referred is very brief – it simply says that "claims settlement services, such as those at issue in the main proceedings, provided by a third party in the name and on behalf of an insurance company, do not fall within the exemption". The reasoning

underlying that answer is likely to lead to changes in law and practice in the UK.

CJEU (Case C-40/15): *Minister Finansów v Aspiro SA, formerly BRE Ubezpieczenia sp. z o.o.*

2.3.2 Supply of credit?

A company operated health and fitness clubs, and accounted for VAT on all subscriptions received. In 2012 it submitted a repayment claim for £434,880, contending that some of the money received should have been treated as exempt consideration for a supply of credit. The periods concerned were 11/08 to 09/12. HMRC accepted part of the claim in July 2013. The rest of it proceeded to the Tribunal.

The judge (Jonathan Cannan) noted that there was no real dispute of fact and no need for witness evidence. The outcome would depend on the terms of the contract between the appellant and the members. The appeal was concerned with a category of membership ("Results") for which a lump sum annual fee of £593.45 could be paid in advance; alternatively, a monthly direct debit of £53.95 for 12 months would give a total for the year of £647.40 (in effect, the lump sum made the 12th month "free"). HMRC accepted that this gave rise to an exempt charge for credit in the first year, amounting to £4.50 per month.

The issue was what happened after the first 12 months. The contract specified that 12 months' payments had to be made as a minimum, but after that 3 months' notice was required for cancellation of the contract. The company argued that, where a member in this category continued to pay the monthly DD, the amount received continued to contain £4.50 for an exempt supply of credit.

The judge noted that there was nothing in the contract to deal with a member who paid by DD for the first year, but wished to change to a lump sum payment for the second year. A Results member who paid by lump sum for the first year would, by implication, cease to be a member unless a new contract was entered into. The company said that such members received a letter as the end of the year approached offering renewal (which would not involve paying a joining fee).

The judge examined the contractual clauses which provided that the company had the right to vary the charges by giving 10 days' notice; and that after the first year the membership "shall continue monthly" subject to giving 3 months' notice. In his view, the situation of a member was different after the minimum period of 12 months. There was no explicit alternative offer of a year's membership for a lump sum; the Results member was in a better position than a different category ("Lifestyle") who also had to give 3 months' notice, but without the first 12 month minimum period, who paid £61.95 per month.

HMRC's argument was that a charge for credit required there to be a charge for deferment of a sum that would otherwise fall due immediately. In other words, there must be a sum for which credit is given, a period over which it is given, and a charge for that credit. Whilst the company's counsel identified £4.50 per month as the charge for credit, he did not seek to identify the sum for which credit was given or the period over which it was given. He also suggested that a Results member would have

the option of paying an annual fee for the second year of £593.45. The judge did not consider that was a term of the agreement. The Appellant might accept £593.45 as payment by way of a lump sum, but that would be a separately agreed extension to the original agreement on whatever terms might be agreed as to joining fees and periodic payments. The actual terms and conditions did not include the option and it was not necessary to imply such a term.

The appeal was dismissed.

First-Tier Tribunal (TC04836): *Sports and Leisure Group Ltd*

2.3.3 College of a university

A college claimed that it should benefit from exemption under Group 6 Sch.9 because it was a "college of a university". It would be taxable in relation to courses supplied to some other clients, but it believed that it was an eligible body where it was supplying education within the context of the university to which it was affiliated (the University of Wales). HMRC accepted that it was exempt in relation to certain grant-funded training it provided under Item 5 Group 6.

The FTT (TC02066) considered comparisons to the earlier cases of *School of Finance and Management* and *HIBT Ltd* in which commercial companies had been held to be acting as parts of universities. Although many of the factors identified in *SFM* were also present here, the Tribunal did not accept that the link between the company and the university was close enough. The company was one of 140 accredited learning centres for the university; clearly they were not all colleges of the university. The link was not enough even if it was right to consider only the courses which were run for the university; if the totality of the company's activities was considered, it was clearly not an eligible body. Its appeal was dismissed.

The company appealed to the Upper Tribunal. Its main contention was that the FTT had erred in concluding that it was not possible to be an "eligible body" in relation to only part of an entity's activities: the FTT ruled that it was "all or nothing". There was no case law on this question. If the UT agreed that this was an error of law, it would be necessary to reconsider the other conclusion of the FTT, that the relationship between the company and the university was not close enough to make it "a college" of the university.

The UT examined the precedent cases that touched on the concept of "an eligible body", and also the detailed wording and purpose of article 132 and Schedule 9 Group 6. He concluded that the ground of appeal was mistaken: it was not possible to be an eligible body in respect of some activities, and not be an eligible body in respect of others. Rather, it was possible for an eligible body to have some activities that did not qualify for exemption. As the company accepted that, taking all of its activities into account, it could not qualify as an eligible body, its appeal had to be dismissed.

The company appealed to the Court of Appeal, arguing that a more recent CJEU judgment showed that the decisions below were incompatible with EU law. The main point of its argument was that the decisions infringed the principle of fiscal neutrality: they suggested that universities could be

exempt in respect of some activities and not others, but for a college such as itself, it was "all or nothing". The CJEU had held in the *MDDP* case (Case C-319/12) that a profit-making entity could still benefit from the education exemption; it was the purpose of art.132 to lower the cost of access to education by exempting it.

The Court of Appeal considered that Member States were required, under art.132, to define those non-public bodies that could qualify for the exemption. The UK had decided to allow exemption for those bodies that provided education in a similar manner to those governed by public law – there had to be a public interest element in their work; and in the case of universities, the UK had restricted the exemption to colleges that were integrated into the universities and were therefore governed by the objects of the larger body.

The college also argued that the UK law infringed the principle of legal certainty. The Court agreed that Sch.9 Group 6 item 1 ("education") on its own might be unclear in its scope, but when it was read with Note 1(b) and the factors set out by the courts in *SFM*, the position was clear enough. The law was consistent with the Directive, and the FTT had applied it in a sensible way. The appeal was dismissed, and an application for a reference to the CJEU was refused.

Court of Appeal: *Finance & Business Training Ltd v HMRC*

2.3.4 Education questions

The questions for reference in the *Brockenhurst College* case have been confirmed (unchanged from the draft questions included in the last update) and the case has been given its reference number:

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

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

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

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

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

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

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

CJEU (Reference) (Case C-699/15): *HMRC v Brockenhurst College*

2.3.5 Scope of education exemption

The BBC made charges to The Open University in respect of the cost of broadcasting its educational programmes. Following a Tribunal decision in 1982 (VTD 1,196), these supplies were treated as taxable; from August 1994, Customs accepted that they were exempt under Sch.9 Group 6 Item 4 VATA 1994 (the wording was changed, and the exemption extended, on consolidation of the VATA 1983). In 2009, the BBC made a *Fleming* claim in respect of the VAT charged (just under £21m) between 1978 and 1994. When HMRC refused, The Open University appealed to the FTT. It was entitled to do so as it was the recipient of the supplies, and would be entitled to reimbursement if the claim succeeded. The FTT decided for the taxpayer, and HMRC's appeal to the Upper Tribunal failed. The Court of Appeal has now confirmed the decisions below.

First-Tier Tribunal

The 1982 Tribunal had decided that supplies of "services closely related to education" had to be made by a person supplying education itself in order to be exempt. As the BBC was not supplying education to the OU's students, it could not qualify. The 2005 CJEU decision in *Horizon College* (Case C-434/05) showed that this was (and always had been) wrong in principle; however, it was binding on the parties in relation to the VAT at issue before the Tribunal, so the *Fleming* claim did not include the quarter to September 1981, because that appeal had determined the tax finally for that exact return period.

The FTT judge considered that there were three issues to be determined:

(1) was the BBC a body governed by public law for the purposes of Art.13A(1)(i); and

(2) did the BBC have the educational aim required by Art.13A(1)(i); or

(3) if the BBC was not a body governed by public law with the required educational aim, was it another organisation defined by the United Kingdom as having similar objects?

In respect of the first question, the judge considered himself bound by the ruling of the High Court in the *Cambridge University* case: a body governed by public law must be, for this purpose, part of the public administration of the country. The BBC did not satisfy this condition. The BBC is subject to a range of laws and is a creation of the law, but it does not appear to fall within the type of organisation that the Directive envisages as enjoying this exemption.

The second question was dependent on the first, which meant that it was not strictly relevant, once the judge had decided that the BBC was not a body governed by public law. However, he considered it, in case the

point was important to an appeal. Although the BBC has education, in a broad sense, as one of its aims, the judge did not accept that its involvement in educational broadcasting was of the kind envisaged by the CJEU in *Horizon College*.

However, the judge did accept that the BBC was "*another organisation defined by the United Kingdom as having similar objects*." The law had changed in the VATA 1994 to go beyond just state organisations, and Customs had accepted in 1997 that this applied to the OU Production Centre, which was part of the BBC. The judge concluded that the change in the VATA 1994 had correctly implemented a directly effective Directive provision that applied both before and after 1994, rather than extending an exemption that it was within the power of a member state to restrict. The situation was comparable to that in *JP Morgan Claverhouse*, where the government had argued it was allowed to "define" special investment funds for the purposes of the VAT exemption. The CJEU ruled that such definitions had to be applied in accordance with the concept of fiscal neutrality – it was not permitted to distinguish between organisations or products that were essentially the same.

The OU's appeal was allowed on that basis.

Upper Tribunal

The judge set out the background and identified the same issues as those considered by the FTT. HMRC were appealing on the third point (organisation having similar objects); as part of its objection to that appeal, the OU argued that the first two issues should have been decided in its favour. The judge therefore reconsidered all three issues.

On the question of whether the BBC is a body governed by public law, the judge examined the precedents and further arguments put forward by the OU's counsel. He rejected the OU's reliance on the UK domestic legislation: according to CJEU precedent, "body governed by public law" has an autonomous EU law meaning.

He went on to consider the CJEU decision in *MDDP* (Case C-319/12), in which the court set out the purpose of the education exemption in clear terms. This post-dated the FTT hearing, and the OU's counsel argued that it supported his case – he contended that the CJEU had drawn a clear distinction between public sector bodies and private sector enterprises. However, the judge did not accept that this point had been relevant in the case: it was rather about whether a profit motive was fatal to a claim for exemption.

Counsel further sought to rely on a definition of "body governed by public law" in the Procurement Directive – that would certainly apply to the BBC. However, the judge concluded that the purposes of the VAT and Procurement Directives are different, and the roles of the concept of public law bodies in each of them are likewise different.

The judge noted that his first impression had been that the FTT had asked the right questions and had come to the right answer on this point; his more detailed consideration had not changed that.

On the second issue, the judge considered the problems of applying the *Horizon College* decision to distance learning. He drew a distinction between a mere provider of materials (who would be in the same position

as Horizon College, which provided only teaching staff), and a provider of materials in the context of a self-contained course. In his view, the BBC did more than provide support to others who supplied education; the BBC had an educational aim.

He decided that this was one of the rare cases in which an appellate Tribunal should overturn a decision below in relation to the facts. His conclusion on the second issue was as follows:

I think that the FTT took too narrow a view of what Horizon College requires, in the context of distance learning provided by a public sector broadcaster. Secondly, I think the FTT's analysis failed to do justice to the scale and variety of the forms of distance learning provided by the BBC throughout the Appeal Period, as reflected in the annual reports from which I have quoted. Thirdly, this led the FTT to state, wrongly in my view, that the BBC always provided "only a part of the package". Finally, the question is not one which turns in any way on the oral evidence, or on the FTT's assessment of the witnesses. In the light of these considerations, I am satisfied that the FTT's conclusion on this issue is erroneous in law; that there would be no point in my remitting it to the FTT for reconsideration; and that I should re-determine the issue myself, under section 12 of the Tribunals, Courts and Enforcement Act 2007, so as to hold that the BBC did at all material times have the requisite educational aim.

This meant that the conclusion on the third issue was simple: if the BBC had the requisite educational aim, it clearly had "similar objects". The judge was satisfied that the conclusion of the FTT – that the definition of such bodies was a matter of EU law rather than relying on specific domestic "definition" – was correct, and was in accordance with the purpose of the exemption as set out by the CJEU in *MDDP*.

HMRC's appeal was dismissed.

Court of Appeal

The Court confirmed again that the powers of the Secretary of State, Parliament and the government in relation to the BBC did not make it a body governed by public law. The precedents had been correctly applied by the Tribunals.

The Court went on to agree with the Upper Tribunal judge. The BBC did not only supply course material, or individual stand-alone programmes, which might not be enough on their own to demonstrate an educational object following *Horizon College*. Rather, it provided the whole framework of educational facilities to deliver distance learning direct to children and young people: these involved teaching materials, technical resources, educational policy and organisational infrastructure. The supply of education was part of the BBC's objects.

It was therefore unnecessary to conclude the question of whether it had "similar objects" – it was supplying education, and the supply was exempt under the direct effect of art.13A(1)(i) 6th Directive, which the UK had failed to implement in the national law. To exclude the BBC from exemption would be contrary to the objective of the Directive and the principle of fiscal neutrality.

Court of Appeal: *HMRC v Open University*

2.3.6 Extent of welfare services

A commercial company constructed a property for use as a serviced residence for persons over 60. Its activities were profit-oriented and the residents did not receive any form of state funding. The company regarded its activities as taxable and claimed a deduction for the input tax on the cost of the construction project. The Belgian tax authorities ruled that the activity was exempt within art.13A(1)(g) 6th Directive.

Advocate-General Bot agreed with the authorities. The taxpayer should be regarded as "a body devoted to social wellbeing". The serviced residence had to meet regulatory standards and to obtain licences. Previous case law showed that profit-making entities could fall within this exemption. The presence or absence of state funding was just one factor in deciding whether a body was exempt, not a crucial consideration.

The A-G went on to conclude that the taxpayer was providing services "closely related to welfare". The A-G considered that the normal strict interpretation of terms in the exemption provisions should not deprive them of their intended effect. The purpose of the welfare exemption was to reduce the cost of welfare services to members of the public who might rely on them. Although the provision of independent living required fewer services than residential care, nevertheless the residents were provided with certain amenities that were appropriate to their specific needs (e.g. lifts, elements of home automation). This was enough to bring them within the scope of the exemption.

The full court agreed with the opinion. The exemptions in the Directive should be autonomous concepts of EU law with an EU-wide effect: to make them dependent on the provision of public financial assistance would lead to variation based on the domestic legislation in each country. That could not be right.

The services provided by the company were capable of being exempt, in particular where the services which serviced residences were obliged to offer pursuant to the relevant national legislation were intended to achieve the support and care of elderly persons and corresponded to the services which old people's homes were also obliged to offer in accordance with national legislation. Other optional services such as hairdressing and beauty services could not be regarded as essential to operating a serviced residence, and would not benefit from exemption. It should be for the national court to decide whether particular services fall one side of the line or the other.

CJEU (Case C-334/14): *Les Jardins de Jouvence SCRL v Belgian State*

2.3.7 Political club membership

A not-for-profit organisation had as its main object "to promote by all proper means the principles of Conservatism, and the implementation of the Conservative Party's policies." It claimed exemption for its membership subscriptions under Sch.9 Group 9 item 1(e) as a body whose objects were in the public domain and of a political nature. The context of the claim was a repayment claim made in March 2011 for overpaid output tax in respect of the previous four years; the original claim was revised downwards shortly after it was made, to recognise the fact that the club had already treated one-third of its subscriptions as exempt under an

agreement with HMRC that this proportion related to the provision of sporting facilities and was therefore covered by Group 10. The claim was further reduced to reflect a claim for exemption under Group 9 for 30% of the subscription, recognising that some of the objects of the club were not political.

HMRC ruled that the subscriptions were taxable, because the actual activities of the club were social rather than political. The appeal against this decision became a lead case, with appeals by four other Conservative clubs dependent on it.

The Tribunal heard from the chairman of the Association of Conservative Clubs and from the manager of the appellant club. It also examined the minutes of the club's AGM. The judge commented: "*Reading the minutes gave the Tribunal the strong impression that the social and not political aspects of the club were what were predominant: whatever the purpose for which the Club had been established, at the period in question the main activity was the provision of social events and not the provision of participation in political activity.*" The club's website and Facebook page had no political entries in an election year, apart from a video posted the day before the election and a brief thank you to the public for voting conservative the day after. The judge found as a fact that the original purpose of the club may have been political, but that it was in reality and in the present a social club.

The judge (Barbara Mosedale) examined the basis for Sch.9 Group 9 and agreed with HMRC that an organisation can only qualify if its main aim is political and if its supplies are referable to that aim, and that this was the test that had to be applied to the subscriptions. The rights the members obtained in return for their subscriptions were principally access to the social facilities, including a cheap bar, and the sporting facilities.

The subscription constituted consideration for a single supply that it would be artificial to divide. HMRC allowed exemption of the sporting element by concession under ESC 3.35, but the Tribunal had no jurisdiction to insist that this should be extended to any other aspect of membership, either in accordance with the UK law or with the principle of legitimate expectations, given that it appeared to be contrary to the EU law.

As is common with Judge Mosedale's decisions, there is a very detailed analysis of precedent (including the recent decision of the Upper Tribunal in *United Grand Lodge of England*) and legal issues. She concludes that the club might have a claim for legitimate expectations on the basis of the ESC, but that this would have to be pursued by an application for judicial review, not by appeal to the Tribunal.

First-Tier Tribunal (TC04923): *Shanklin Conservative and Unionist Club*

2.3.8 Sport

Questions have been referred to the CJEU by the FTT in relation to the sporting exemption. A local authority is appealing against a ruling by HMRC that it has to charge VAT on admission to leisure centres, and is not entitled to a refund of output tax accounted for in the past. HMRC's grounds for refusal are that allowing the exemption would lead to a

distortion of competition and a competitive disadvantage for commercial enterprises that provide similar supplies subject to VAT.

The questions for reference are:

1. *Is the UK entitled, pursuant to the final paragraph of art.133 PVD, to impose the condition contained in paragraph (d) of that article on bodies governed by public law, (i) in circumstances where the relevant transactions were treated by the UK as taxable on 1st January 1989, but other Sporting Services were subject to exemption on that date and (ii) in circumstances where the relevant transactions had not first been granted exemption under national law before the UK sought to impose the condition contained in Article 133(d)?*
2. *If the answer to (1) above is in the affirmative, is the UK entitled to impose the condition contained in paragraph (d) of art.133 PVD on non-profit making bodies governed by public law without also applying that condition to non-profit making bodies which are not governed by public law?*
3. *If the answer to (2) above is in the affirmative, is the UK permitted to exclude all public non-profit making bodies from the benefit of the exemption contained in art.132(1)(m) without having considered in each individual case whether the granting of exemption would be likely to cause distortion of competition to the disadvantage of commercial enterprises subject to VAT?*

There appears to be a potential interaction between *Isle of Wight Council* on distortion of competition and *Bridport & West Dorset Golf Club* on fees paid for participation in sport.

CJEU (Reference) (Case C-633/15): *London Borough of Ealing v HMRC*

2.3.9 Cultural exemption

The Court of Appeal has decided to refer questions to the CJEU in the *BFI* case. The FTT and Upper Tribunal have both allowed the taxpayer's appeal against a refusal of a *Fleming* claim for repayment of output tax accounted for in the early 1990s. The claim is based on the direct effect of the 6th Directive exemption for cultural services provided by eligible bodies.

The questions referred are:

1. *Are the terms of art.13A(1)(n) 6th Directive , in particular the words "certain cultural services", sufficiently clear and precise such that art.13A(1)(n) is of direct effect so as to exempt the supply of those cultural services by bodies governed by public law or other recognized cultural bodies, such as the supplies made by the Respondent in the present case, in the absence of any domestic implementing legislation?*
2. *Do the terms of art.13A(1)(n) 6th Directive, in particular the words "certain cultural services", permit Member States any discretion in their application by means of implementing legislation and, if so, what discretion?*
3. *Do the same conclusions as above apply to Art.132(1)(n) PVD?*

CJEU (Reference) (Case C-592/14): *HMRC v British Film Institute*

2.4 Zero-rating

2.4.1 I can't believe it's not ice cream?

HMRC issued a decision that a company's products were standard rated because they were "similar to ice cream, ice lollies, frozen yoghurt and water ices". The company appealed, arguing that they should be zero-rated because they were predominantly frozen fruit, and were therefore not similar to the excepted items listed in Group 1 Sch.8.

The company's representative argued that the product should be zero-rated in the same way that frozen fruit is zero-rated. The judge commented that "*one cannot describe a cake as being nothing more than flour, butter, sugar and eggs. The frozen fruit is subjected to a process in order to make the Product and describing the Product by reference only to its ingredients ignores that process.*" HMRC did not argue that the product was ice-cream, only that it was "similar". The company's advertising and packaging all suggested that it was. The judge weighed the number and significance of factors of similarity and dissimilarity, and concluded that it was "similar to water-ice" (something made with fruit and sugar and no added dairy products – in this case, the sugar came from the fruit itself, rather than being added).

The appeal was dismissed.

First-Tier Tribunal (TC04819): *The Frozen Fruit Company Ltd*

2.4.2 Powders

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

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

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

The first conclusion concerned the interpretation of "beverage" and the interaction between excepted item 4 and overriding item 6: the items were specific, rather than general rules of interpretation, and the exception was not to be interpreted as "beverages other than milk and preparations and extracts thereof". A powder that is sold separately and has to be mixed

with milk is not the same as milk. There was no indication that Parliament must have intended the provision to be extended that far.

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

The Tribunal considered that the social policy underlying Group 1 was not "to promote the health benefits of milk", but rather "to remove VAT from basic foodstuffs such as milk". There was nothing to indicate that a powder sold separately was subject to the same considerations.

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

At the conclusion of 210 paragraphs, the Tribunal rejected the appeal.

First-Tier Tribunal (TC04944): *Nestlé UK Ltd*

2.4.3 Updated Notice

HMRC have issued a revised version of their Notice *Food*. It now specifically describes marshmallow "snowballs" and confirms that they are zero-rated, following the *Lees of Scotland/Thomas Tunnock* decision.

Notice 701/14

2.4.4 Sanitary products

Press reports at the time of the Budget suggested that the government has obtained the Commission's approval of the removal of VAT from sanitary protection. However, no further details have been given yet.

Independent, 18 March 2016

2.5 Lower rate

Nothing to report.

2.6 Computational matters

2.6.1 Market value direction

Two connected companies appealed against the issue of a Sch.6 para.1 direction requiring transactions between them to be accounted for at open market value. One also appealed against an assessment based on the imposition of the standard method override to reduce its input tax recovery. The VAT assessed as a result of the direction was £4.25m for the periods concerned, and the override adjustments were nearly £600,000 over two years.

As well as asserting that HMRC's decisions are wrong, the appellants argued that the assessments made on 4 June 2013 and 5 July 2011 were made out of time. One aspect of that argument related to the question of whether those assessments were single "global assessments" or multiple assessments in relation to different VAT periods.

The two companies (TFL and TRL) were separately VAT-registered fellow subsidiaries of a UK holding company (PerfectHome). The precise nature of their respective activities was disputed, and the Tribunal had to make findings of fact. The group as a whole operated from 67 showrooms located in various parts of the UK. It sold household goods, furniture and electronic appliances to consumers. Its customers were generally unable to use credit cards; 98% of its sales involved hire purchase, with the customers making weekly payments, typically over three years. Customers often purchased insurance and extended warranties as well as their goods.

Some 40% to 50% of customers terminated their HP agreements early. The company tended to repossess goods rather than taking legal action against the customer. Goods were refurbished and resold.

The business of the group was carried on by the two companies acting in accordance with an "intra-group services agreement":

- TRL was the tenant of the leasehold showrooms;
- TRL bought advertising services;
- TRL bought goods for resale, and in the 2% of sales that were for cash, was the only group company involved in transactions with the customer;
- in relation to HP sales, TRL sold the goods to TFL for 97% of the advertised price (standard rated);
- TFL entered into the HP contract with the customer and treated 100% of the advertised price as its standard rated sale;
- TFL entered into the contracts for insurance and extended warranties;
- TFL paid TRL for delivery of some bulky items to customers (a standard rated service).

TRL was a fully taxable business for VAT purposes. TFL was partially exempt. HMRC were concerned that this provided the opportunity to manipulate the VAT recovery of the group as a whole. On 31 May 2012, an officer issued a direction to TRL requiring market value to be applied to supplies of shop advertising and launch costs in relation to the stores

from 1 June 2009 until the direction. The assessments were issued in June 2013 and May 2014 on the basis that HMRC were not satisfied that the company had complied with the direction.

HMRC considered that OMV of the intra-group supplies should be calculated as follows:

- costs associated with the stores should be split 25% to TRL and 75% to TFL, and recharged by TRL to TFL with a 10% mark-up;
- advertising costs should be split in the ratio of cash and HP sales (2:98), and again recharged by TRL to TFL with a 10% mark-up.

HMRC also considered that the standard method was unduly favourable to TFL, on the grounds that have been applied to other HP companies – including the selling price of the goods significantly increases the taxable turnover in relation to the "real" income of the company, which HMRC consider to be the exempt finance charges and insurance commissions.

Judge Richards considered that the burden of proof lay on the companies to demonstrate that the directions should not have been issued. The Tribunal had a full appellate jurisdiction to substitute different figures for those used by HMRC, if it considered that the supplies were indeed made at below market value.

He went on to examine the UK law and its basis in art.80 and art.72 PVD. Before applying them to the facts, he commented on an objection raised by the taxpayers' representative that use of the words "artificial" and "contrived" in HMRC's statement of case were prejudicial and tantamount to allegations of dishonesty, that ought to have been more specifically pleaded and raised at an earlier point in the proceedings (the SOC was filed four days late). The judge rejected these objections, holding that they were relevant arguments and implicit in the basic assertion that the transactions were at less than OMV.

The judge also had to consider objections by the taxpayer to the admission as evidence of an All Party Parliamentary Group on the PerfectHome business (objection overruled) and by HMRC to the admission of transfer pricing reports prepared by Grant Thornton. HMRC argued that GT were not independent (as they were advising the companies in the appeal) and their reports were irrelevant, because they were based on OECD guidelines rather than the principles of OMV for VAT. The judge said he would admit their reports as evidence, but as they were not prepared for the Tribunal itself, they would not be given the same weight as expert witness statements.

The judge then examined the way in which the two businesses operated, both with customers and with each other. He concluded that they were separate businesses, but commercially intertwined. PerfectHome was set up to deal with credit-constrained customers in particular, and was not operating in the same marketplace as other retailers of similar goods. The judge analysed and listed out what he regarded as the activities of each company.

HMRC argued that TFL was the "primary" user of the stores, because 98% of the customers bought on HP terms. The judge agreed with the company's finance director that this was the wrong way of looking at the business. Customers came to the stores seeking to buy goods, not finance.

HMRC further argued that the present owners of PerfectHome had bought it as a single company, and had divided it into two businesses with the object of reducing the irrecoverable VAT by making intra-group supplies at less than market value. The finance director denied this, claiming that there were various commercial reasons for the two-company structure. HMRC's representative pointed out that the two-company structure created irrecoverable VAT on certain recharged costs, and argued from this that "the savings elsewhere must have been greater in order to justify this inefficiency". The judge did not accept this either. In his view, VAT savings were not the motivation for the two-company structure.

HMRC's representative asked the group tax manager if he had ever disclosed a tax avoidance scheme. He said that he did not believe he had. The following day, HMRC's representative told the judge that HMRC had evidence to suggest that this was not true, but taxpayer confidentiality prevented them producing that evidence to the Tribunal. The judge declined to recall the witness and explicitly accepted his evidence.

The Sch.6 para.1 direction applies to supplies that are made for less than their OMV. HMRC argued that some supplies were made from TRL to TFL for more than their OMV – in particular, the supply of the goods. This would not lead to any irrecoverable VAT (because it would be directly attributable to the onward taxable supply of those goods), and was to compensate TRL for undercharging in other areas. HMRC considered that TRL should be regarded as a "wholesaler" in respect of these goods. The judge did not accept this. TRL was not a wholesaler; the *VW Financial Services* appeal showed that it was normal for a HP finance company to buy goods at 100% of the retail price.

An argument about recharges for repair services was also rejected. HMRC's calculations of the "mark-up" on those repair services omitted the most substantial cost of TRL in providing them – the cost of staff carrying out the repairs, which would not generate any irrecoverable VAT. Delivery charges, where TRL charged 5% of the price to TFL but TFL did not charge the customer, were part of the overall commercial activity of TFL, and should not be looked at in isolation. The judge was satisfied that TRL did not overcharge TFL for any of the inter-company transactions, so that there was no inference to be drawn that a compensating undercharge arose on other supplies.

The judge then examined in detail the professional advice that the companies had received from GT and from a consultant about inter-company charges. He approved of the approach GT adopted to the calculation of "store charges", and disapproved of HMRC's approach; in his view, the actual charges might be argued to be lower than "at the high end of the range" suggested by GT, but that did not mean they were below OMV.

The judge was less satisfied with GT's approach to the charges for advertising, preferring HMRC's conceptual analysis. However, HMRC's application of its analysis ignored the fact that TRL made a retail sale with a 37% mark-up every time TFL made a sale. Their calculation of the OMV was therefore wrong. He set out how he considered it ought to be done; presumably the parties will go away and recalculate the results.

The standard method override (SMO) argument was significantly affected by the 2015 decision of the Court of Appeal in *VWFS*. Although that had

been about the proposed imposition of a special method on a HP finance company, it nevertheless cast light on the question of what such a company's overheads were "used" for. For the same reasons as the Court of Appeal, the judge considered that TFL's business consisted in selling both taxable goods and exempt services, and its overheads were consumed in making both supplies. The SMO did not apply.

There was a separate argument about whether certain assessments were issued in time. If they were "global assessments", the time limit rules would strike down the whole document unless the earliest return period comprised within it was still "in time". If they were separate assessments shown together on the same piece of paper, the individual periods could stand or fall individually. The matter was examined in great detail, and involved hostile questioning of the HMRC officers by the company's representatives – references to "an assessment" were taken as indicating that the officers had intended to raise a global assessment, which they denied. The judge explicitly found that he regarded the officers as honest witnesses who used the expression "an assessment" without any inference.

The judge was satisfied that the assessments, which analysed the outstanding VAT by period, were not global in nature. HMRC accepted during the hearing that numerous periods were out of time, leaving just one period (06/09) in dispute. As the company had not had enough notice to prepare a case in the light of this change of approach by HMRC, the judge left this point undecided, and issued directions to the parties in an attempt to bring them to a conclusion.

The end result was that the appeal was allowed in part: the SMO was not appropriate, and store fees should not be included in the Sch.6 para.1 direction. The advertising recharge was in principle subject to the direction, but the amount involved should be recalculated.

First-Tier Tribunal (TC04840): *Temple Finance Ltd and another*

2.7 Discounts, rebates and gifts

Nothing to report.

2.8 Compound and multiple

Nothing to report.

2.9 Agency

2.9.1 TOMS applied

A company appealed against three assessments for £408,000, £88,000 and £171,000, covering the periods from 2011 to 2013. By the time of the hearing, it had gone into liquidation, and was not represented. The judge decided that the hearing should proceed in the interests of justice, but the lack of evidence meant that some facts remained unknown.

The company had three grounds of appeal: that the assessments were raised out of time, that the supply should be treated as mixed rather than composite, and that there was an inconsistency between the treatment of the supply made by the company and the onward supply made by its customers.

One of the company's businesses was the organising of conferences. It sold on a packaged supply to other businesses, which sold them on again to businesses who wanted delegates to attend the conference. The decision states that "*VAT rules in this area changed in 2011. After this point, the wholesale supply of conference packages became subject to the 'business to business' general rule, and were therefore liable to VAT at the standard rate, with the place of supply being where the customer was based. HMRC believes that TIME's customers operate, or should operate, the Tour Operators Margin Scheme, which would disallow the input VAT on conference services. As a result of this change in legislation, therefore, a large amount of irrecoverable VAT is created by the operation of business in this way (using a middleman, here TIME), compared to the direct sourcing of the elements of the conference by the TOMS business.*" There seem to be two separate points here – one concerning place of supply, and one concerning the operation of TOMS.

The appeal concerning the time limit was dismissed. The burden was on the appellant to show that HMRC had had sufficient information to raise the assessments for over a year before they did so; in the absence of any witnesses, it was not possible to do that. HMRC's notes of correspondence and meetings suggested that they were correct in asserting that they did not have sufficient information in May 2012, as claimed by the appellant, but only received that information at a meeting in November 2012.

As regards the second ground of appeal, the appellant contended that it was making a mixed supply comprising 90% travel services and 10% conference arranging. The overseas travel services would be outside the scope of UK VAT. HMRC argued that there was a single supply which was all chargeable where the customer belonged. An overseas conference arranged for a UK customer would therefore be fully chargeable to UK output tax. The Tribunal considered a number of arguments raised by the company in its grounds of appeal, but found that the whole purpose of the customer was to buy "a conference" – it was a single supply, to which the travel services were ancillary.

The third ground of appeal related to the fact that HMRC wanted the company's customers to operate TOMS (meaning they could not recover the output tax charged by the appellant), but the company not to operate TOMS (which meant that it had to charge output tax on the full consideration to a UK customer, without deducting outside-the-scope costs of overseas travel and accommodation).

HMRC argued that the company only supplied businesses making an onward sale, whereas its customers supplied end users. The Tribunal considered that this was not the correct treatment following *Commission v Spain* (Case C-189/11), a decision that was quoted at length. The Tribunal sought further representations about the case from the appellant and from HMRC, and makes the following comments:

HMRC agree that UK policy has not yet implemented this judgment. We were referred to Revenue & Customs Brief 05/14 which mentions this and accepts that it is open to any business to apply the direct effect of the judgment of the European Court should they so wish. We note that the brief was issued in January 2014, and HMRC intended to review this after 1 year, but as yet no new guidance is forthcoming.

We are aware that this distinction that HMRC draws between supplies to the end customer and wholesale supplies has led to the business model operated by TIME becoming problematic or unworkable. We are aware that HMRC are aware of this.

We find it difficult to understand why HMRC chose to bring this current case (and in doing so, force the business into administration) at a time when it is clear that UK policy around implementing the judgment may need to change, and at a time when similar cases were already going through the European Courts while HMRC were investigating this case.

While TIME did raise the ECJ case in their correspondence with HMRC, HMRC dismissed its relevance, and did not mention the case in their submissions or evidence at the hearing. In their subsequent submissions, HMRC advised that they considered the case to be irrelevant, because while TIME did have the option of applying direct effect to the EU law, the use of TOMS must be on an all or nothing basis. TIME would have to use it for ALL supplies of conference services (including those wholly within the UK), or for none of them.

The Tribunal issued a stinging criticism of HMRC for directly bringing about the liquidation of a company that had previously contributed corporation tax, PAYE and NIC, through a blinkered approach to VAT in an area in which the department was aware there was uncertainty over the law. If the company had been allowed to operate TOMS from 2011, it would have been able to treat its margins for conferences outside the EU as outside the scope, and within the EU it would only have charged VAT on its profit margin. The appeal was allowed.

First-Tier Tribunal (TC04833): *Travel Incentives Meetings Exhibitions Ltd*

2.9.2 Tour operators margin scheme

HMRC have issued a February 2016 version of their Notice on the TOMS. Sections 9 (Cost-based calculation: annual adjustment) and 10 (Accounting for VAT on the provisional value of designated travel services and margin scheme packages) have been updated.

Notice 709/5

2.9.3 Article

In an article in *Taxation*, Elman Wall discusses a number of tax issues arising in the holiday industry, including the TOMS as well as problems of corporation tax and income tax.

Taxation, 25 February 2016

2.10 Second hand goods

2.10.1 Updated Notice

HMRC have published a January 2016 version of their Notice *The VAT Margin Scheme on second-hand cars and other vehicles*. The "what's changed?" section only says that it has been revised to make it suitable for publication on GOV.UK, and to change an address in paragraph 11.4.

Notice 718/1

2.11 Charities and clubs

2.11.1 Relevant charitable purpose

The *Wakefield College* case was heard by the FTT (TC03108) in late 2013 after being remitted by the UT early in 2012. The second FTT decision was appealed by HMRC to the UT, which has agreed with HMRC.

Background

The college appealed against HMRC's refusal to agree to the issue of a zero-rating certificate in relation to the construction costs of a new campus building. The question was whether the buildings would be used for a "relevant charitable purpose", i.e. other than for a business purpose (as it was accepted that the appellant was a charity for the purpose of this rule).

The college argued that the nature of its funding, its mode of operation and its general characteristics were such that it was not in business at all so far as the activities intended to take place at the new campus were concerned.

First FTT

The First-Tier Tribunal considered the facts of the case in detail, and then applied a number of legal principles to those facts. First, everyone agreed that the provision of grant-funded education is not a business for VAT purposes. This is backed up by the CJEU decision in *Commission v Finland* (Case C-246/08), where charging contributions for legal aid based on a means test broke the link between consideration and service and was therefore not a business activity.

However, there were a significant number of students who paid fees for their education. 11% paid up to half the cost, and 16% paid the full amount. Applying the *Lord Fisher* tests to these activities, the FTT chairman found that the college was engaged in business. HMRC were therefore correct to refuse the zero-rating certificate, and the appeal was dismissed.

First UT

The college appealed to the Upper Tribunal, arguing that the FTT had failed to appreciate that business use which was de minimis could be ignored. The FTT chairman appeared to have believed that this was only an extra-statutory concession and he could not therefore allow the appeal on that ground; however, as set out in RCB 39/09, HMRC regard the de minimis business use of buildings by a charity as a matter of interpretation

of the statutory word "solely". It was therefore open to the chairman to allow the appeal if he had concluded that the business use was no more than 5% of the total. He had not drawn such a conclusion because he did not think it necessary. The Upper Tribunal remitted the case to the FTT for consideration of this point.

The college also appealed on the basis that the chairman had not reached a conclusion on a particular part of its skeleton argument. HMRC contended that the chairman had considered it and dismissed it. The Upper Tribunal judge decided that it was not entirely clear whether the chairman had reached a final conclusion – he appeared to indicate that more information was necessary. As the case was being remitted anyway, the chairman could clarify that issue at the same time.

The college had also argued before the First-Tier Tribunal that it was at the relevant time "a body governed by public law" in the sense required by art.13 VAT Directive, and it was therefore not to be regarded as a taxable person. Although this point was rejected by the High Court in the *Cambridge University* case in 2009, the Tribunal was asked to rule on the issue so that the college could argue in an appeal that the earlier case was wrongly decided. In the event, it did not appeal this point to the Upper Tribunal, as it must have decided that such an appeal would not succeed.

Second FTT

The FTT chairman admitted to being puzzled by the remittance of the de minimis issue. If the statutory de minimis level was 5%, it appeared clear that this was exceeded in the present case. Also, the facts predated the HMRC Brief in which the 10% de minimis concession was replaced by the 5% statutory interpretation. However, the parties appeared to have agreed that a decision on a different unresolved issue would determine the appeal: if that was in favour of the appellants, HMRC would accept that the de minimis rule was satisfied.

This point was whether income from students who paid part, rather than all, of their fees should be treated as business or non-business. The judge said that he had originally considered the matter settled – he intended that the parties should go away and agree the result based on the principles he set out in his decision. However, as it had been remitted to him for determination, he heard further evidence and reconsidered the evidence from the first hearing.

The chairman reviewed the categories of student who paid some of their fees. The college relied on the decision in *Commission v Finland* (Case C-246/08), in which legally-aided individuals had to pay some lawyers' fees. The amount they paid was linked to their ability to pay, not to the services they received, so it was not consideration for the services. Although the criteria used to determine the payment of college fees were different and not related to income levels, the chairman was satisfied that they were analogous to the *Finland* case. Accordingly, this income should be classified as non-business. Although this was a decision of principle which did not formally determine the appeal, the chairman believed that the parties would now be able to agree the outcome between them, based on the application of the de minimis principle.

Second UT

HMRC appealed on three grounds:

- the FTT had failed to provide a properly reasoned decision, which said nothing about HMRC's case or the evidence;
- the FTT had failed to consider whether there was a relevant distinction between students who were liable to pay the fee in the prospectus, but who were eligible for partial or total remission, and those who paid the fee without any remission – this was an important part of HMRC's case, and the FTT had failed to explain why it had rejected it (if it had);
- the FTT had been wrong to consider as relevant the fact that the fees did not cover the costs, but were subsidised by block grants. That did not stop the fees being business income (*Hotel Scandic Gåsabäck AB v Riksskatteverket* (Case C-412/03)).

The Upper Tribunal agreed with HMRC on all three points. It was not clear whether the judge had rejected HMRC's argument about the different types of students, or had simply overlooked it. That was an error of law that warranted the intervention of the UT. The fact that the fees did not cover the costs was not enough to prevent them representing consideration for the services. There was a direct link between the payment and the supply: if there was no remission based on income levels, the *Finland* case did not apply. Where fees were charged to students who paid, or whose employer paid, the amount stated in the prospectus, the college was receiving income in the course or furtherance of business, and it could not issue the zero-rating certificate.

HMRC's appeal was allowed. However, the Upper Tribunal concludes with the following comment:

We cannot leave this appeal without expressing some disquiet that it should have reached us at all. It is common ground that the College is a charity, and that the bulk of its income is derived from public funds. Because that public funding does not cover all of its costs it is compelled to seek income from other sources; but its doing so does not alter the fact that it remains a charity providing education for young people. If, by careful management or good fortune, it can earn its further income in one way rather than another, or can keep the extent of the income earned in particular ways below an arbitrary threshold, it can escape a tax burden on the construction of a building intended for its charitable purpose, but if it is unable to do so, even to a trivial extent, it is compelled to suffer not some but all of that tax burden. We think it unlikely that Parliament intended such a capricious system. We consider it unlikely, too, that Parliament would consider it a sensible use of public money for the parties to litigate this dispute twice before the FTT and now twice before this tribunal. We do not blame the parties; the College is obliged to maximise the resources available to it for the pursuit of its charitable activities, just as HMRC are obliged to collect tax which is due. Rather, we think the legislation should be reconsidered. It cannot be impossible to relieve charities of an unintended tax burden while at the same time protecting commercial organisations from unfair competition and preventing abuse.

Upper Tribunal: *HMRC v Wakefield College*

2.11.2 Isle of Man charities

As previously announced, with effect from Royal Assent, FA 2016 will amend Sch.6 FA 2010 to include a reference to the High Court of the Isle of Man to make it clear that charities subject to that court's jurisdiction will qualify for UK VAT reliefs.

OOTLAR Budget 2016; Red Book 2.153

2.12 Other supply problems

2.12.1 Unused vouchers

A company offered access to genealogical websites which it owned or in respect of which it held licences. Access could be by way of a subscription, which lasted for a certain period, but which was not otherwise limited as to use. Alternatively the sites could be accessed by a Pay As You Go system ("PAYG"): a lump sum was paid, for which a number of units or vouchers giving opportunities to download information were issued, and which had to be used up within a certain time.

The company reclaimed output tax on unused PAYG credits for the period from 09/08 to 10 May 2012. It argued that there had been no taxable supply and therefore no liability for output tax. The claim totalled £434,000. On 10 May 2012 the law changed with respect to the issue of "single purpose vouchers" to make it clear that the time of supply fell on issue, not on redemption.

The appellant argued that the face-value voucher rules before that date should have been applied: there should have been no tax point on issue of the PAYG "vouchers", but rather VAT should have been accounted for on use.

The FTT (TC04133) agreed with HMRC that in reality the company supplied a package of services that was taxable at the time of purchase, and it was not possible to separate out any unused element that should be treated as subject to the FVV rules. The documents issued by the company were in reality simply receipts, not vouchers for redemption. A number of other precedents, including *BUPA*, were considered, but none helped the company in its efforts to delay the tax point.

The company appealed to the Upper Tribunal. The judge set out a number of key issues to be determined. First, there was a difference between the parties' views of what was supplied by the appellant:

- the company argued that it supplied the genealogical records viewed or downloaded by the subscriber – until the subscriber did that, there was no supply;
- HMRC argued that the customer acquired a "package", which afforded him the facility to take advantage of the work done by the appellant in gathering and publishing information – the package was supplied as soon as the credits were purchased.

The appeal would fail if HMRC were correct about the nature of the supply. The appellant also needed to sustain an argument that either:

- the PAYG credit was a face-value voucher within Sch.10A para.1(1); or
- the PAYG credit was not a prepayment for the service provided by the appellant, capable of advancing the tax point to the time of receipt.

The company argued that it was like a virtual bookshop. The search facilities on the website were ancillary services, whereas the downloading of documents was the principal supply. What the customers were paying for was the downloading of specific documents that they selected as relevant to them. It would be artificial to regard anything else the company did as a separate supply or as changing the nature of that supply into some different kind of "package".

HMRC relied on the *Lebara* decision in support of the contention that the PAYG credits were a prepayment for access to a facility, taxable at the time that payment was made. There was a clear contract setting out the terms, which included the fact that refunds were only possible within 7 days of payment, and then only if no documents at all had been downloaded. The search functions were an essential part of the package that the customer was paying for, because the publication of the documents would be useless without them.

The judge considered that the FTT's findings on the nature of the supply, which had agreed with HMRC's view, were inconsistent with the company's contracts. The judge noted that the FTT decision did not reproduce the company's contracts (which he did), but was clearly based on them. The findings about the nature of the supply were decisions of law based upon findings of fact about what the company did.

The judge did not agree with the conclusions. The search function was free: it was not necessary to buy PAYG credits to enter the website and search for documents. A customer could search for as long as he liked, find the documents that he wanted, and then buy PAYG credits only to download them. It followed that the search functions were not part of any "package" paid for by the customer, even though a customer might use the search functions after buying credits. It would not be artificial to split the search function and the downloading of documents into separate supplies (one free, one paid for): that reflected the reality. It also reflected the link between the payment and the service that was supplied in exchange.

The judge went on to consider whether the credits satisfied the definition of "face value voucher" in Sch.10A. In his view they did so. Although the monetary value was only recorded in the records of the company, it was clear enough that the credits reflected a monetary value that had been paid for them. They gave the right to receive services up to that value, and the value was recorded in the records of the company in order for the company to know what it was obliged to supply. The FTT had rejected the appellant's argument on this point because it did not think that the customer would be readily able to translate credit units into money, but the UT judge disagreed. He considered the precedent cases of *Leisure Pass* and *Skyview Ballooning* supported the treatment of these vouchers as FVVs.

The FTT had also decided that the credits were prepayments for the services, which meant that a tax point was fixed. The nature of the

services was known, so the *BUPA Purchasing* decision did not apply. Again, the UT judge did not agree. It was possible for the company to change the price for downloading documents – the amount of credits required could be increased or reduced. That meant that the purchaser of credits could not be certain of the documents that could be accessed for a particular amount of credits. The services to which the customer was entitled were not clearly identified at the time of purchase. It only became fixed when the documents were identified and the credits used.

The appellant therefore succeeded on all the points – the supply was that of downloading documents, not a "package"; the PAYG credits were FVVs; and even if they were not FVVs, they were not prepayments that were capable of fixing a tax point.

Upper Tribunal: *Findmypast Ltd v HMRC*

2.12.2 Fuel scale rate

HMRC assessed a company £1,386 in respect of fuel scale rates not declared. The company appealed, arguing that there was no private use of the fuel. The Tribunal noted that the law applied where a vehicle was allocated to an employee by reason of that person's employment, and fuel supplied to the employer was provided for private use.

HMRC's representative argued that the scale charge would be due if there was any private mileage during a period. The Tribunal did not agree: there was a prior condition, that the vehicle had to be "allocated to the employee". If it was a pool car, no scale rate could apply.

After examining the facts, the Tribunal concluded that for periods up to April 2012, the cars were pool cars. They were used by sales reps who came to work in their own vehicles. Very rarely, after a late appointment, they would take the car home for the night, but this was considered incidental.

After April 2012, the sales reps became home-based, with remote access to the company's computer. They now kept the vehicles at home. HMRC argued that their travel from home to office, on the occasions they had to go in, was "private", triggering the scale rate; the judge disagreed. They now had a normal place of work at home, and he was satisfied on the evidence that there was no private use of the cars. The scale rate did not apply.

The appeal was allowed, except for a section conceded by the company.

First-Tier Tribunal (TC04886): *Broadsteady Ltd*

2.12.3 Reverse charge for electronic communications services

The Value Added Tax (Section 55A) (Specified Services and Excepted Supplies) Order 2016 has extended the reverse charge that applies to some domestic transactions to prevent missing trader fraud. Up to now, the charge has mainly applied to wholesale transactions in mobile phones and computer chips, trading in emissions allowances, and some supplies of gas and electricity. From 1 February 2016, it will apply to wholesale supplies of electronic communications services, including calls and data over landlines, mobile networks and internet.

SI 2016/12

HMRC have issued a Brief to explain this change. They say it will be of importance to:

- airtime carriers
- network operators
- message hubbing providers
- short messaging service (SMS) and voice aggregators.

The Brief explains the type of services that will be covered, and also describes “wholesale supplies” as “business to business supplies where the intention is to sell on the supply with no or negligible consumption of the supply by the businesses concerned”. There is also a list of exceptions.

HMRC note that some “bundled” supplies may be hard to separate into reverse charge and non-reverse charge supplies. They say that it is then acceptable to apply the reverse charge to the whole supply.

The administrative rules that apply are the same as for the emissions allowances reverse charge: there is no £5,000 de minimis limit, and the business is not required to complete a Reverse Charge Sales List. The supplier will not enter output tax in Box 1, but will still record the sale in Box 6 of the VAT return; the customer will enter VAT in Box 1 and Box 4, and will also enter the figures in Boxes 6 and 7.

The Brief also explains the invoicing requirements:

When making a supply to which the domestic reverse charge applies, suppliers must:

- *show all the information normally required to be shown on a VAT invoice*
- *make a note on the invoice to make clear that the domestic reverse charge applies and the customer is required to account for the VAT*

The amount of VAT due under the domestic reverse charge should be clearly stated on the invoice but shouldn’t be included in the amount shown as total VAT charged.

Revenue & Customs Brief 01/2016

The Government has published a Tax Impact and Information Note to explain the background and expected effect of the change. It is purely a revenue protection measure and is not expected to have any significant economic impacts.

www.gov.uk/government/publications/vat-reverse-charge-for-electronic-communications-services

3. LAND AND PROPERTY

3.1 Exemption

3.1.1 Pitches for mobile homes

A company (KL) owned a mobile home park. Someone buying a mobile home (to live in – not holiday accommodation) entered into a tripartite agreement with KL and an associated company, A: A supplied the mobile home, while KL supplied a licence to occupy the pitch. Pitches were constructed with a concrete base by an unconnected company which charged VAT on the work. A and KL were not part of a VAT group.

KL deducted the input tax on the cost of constructing pitches. HMRC disallowed it (£717,000 in total), and charged misdeclaration penalties (£136,000 in total), on the basis that it was solely referable to the exempt supply of licences to occupy.

Judge Bishopp had to piece together the arrangements between the companies and the customers from evidence that he described as "incomplete" – some of the documentation was missing, some was undated or in draft form. However, he was satisfied that he had enough evidence to build up a clear picture of what was, in fact, quite a simple arrangement. The customer contracted exclusively with A for the supply of the mobile home, and with KL for the right to occupy the land. There was no supply of the base from KL to A.

The Tribunal agreed with HMRC that it was not possible to regard any part of the input tax as associated with the taxable supply of the mobile home. That was being made by another company. The fact that the transactions were commercially linked was not enough; nor was the "but for" argument that, without the construction of the base, it would not have been possible to supply the mobile home. The company's representative tried to build an argument based on *Redrow* and *Sveda*, but the judge concluded that the relationships were different – the company claiming the input tax was not making any taxable supplies to a customer. Several other precedent cases were also distinguished: there was no link between the inputs on the bases and any taxable supplies.

The penalty was also confirmed. The Tribunal accepted the taxpayer's counsel's argument that the law was complicated – HMRC's statement of case started at 26 paragraphs running over 9 pages, and was later amended to 135 paragraphs over 31 pages. The judge might have been minded to accept a reasonable excuse defence if the company had recovered some of the VAT, apportioning it on the basis that it was referable partly to the exempt and partly to the taxable supply; but 100% recovery was clearly wrong. The defence amounted to little more than a "plea for mercy".

The appeal was dismissed in its entirety.

First-Tier Tribunal (TC04877): *Kings Leisure Ltd*

3.2 Option to tax

Nothing to report.

3.3 *Developers and builders*

3.3.1 As we were on pub conversions

The last update reported the FTT decision in (TC04756): *DM & DD Macpherson*. This appeared to settle a long-standing argument about the application of zero-rating to projects involving the conversion of partly commercial, partly residential premises into more than one dwelling.

Background: Calam Vale and Alexandra Countryside

In *Calam Vale Ltd* (VTD 16,869), it was decided that a project that incorporated part of the previously residential part in each of two new dwellings did not qualify for zero-rating; if the upstairs had been residential and the downstairs not, then a conversion into ground floor and second floor flats would qualify for zero-rating on half, but a conversion into two semi-detached houses would not qualify at all.

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

Macpherson

The *Macpherson* appeal related to the same kind of project – the conversion of a shop with living accommodation above into two semi-detached houses. HMRC ruled that the sales of both houses could only be exempt. The key point is the application of Group 5 Notes 7 and 9:

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

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

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

(ii) for a relevant residential purpose; or

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

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

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

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

The Tribunal "respectfully disagreed" with the Tribunal in *Alexandra Countryside Investments*. The Tribunal had to consider the conversion that had actually taken place: it was clear that the building that had been converted had not been, within the definition of the law in Note 7, "a non-

residential building" before the conversion. In s.35, the law used the phrase "to the extent that", which allowed a project to qualify in part. Under s.30, it had to qualify or not qualify.

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

Languard

Now another FTT judge (Jane Bailey) had disagreed again. She was considering a similar situation to *Macpherson*, and was aware of the decision that the FTT had reached in that case – this is not a parallel case that happened to come to a different decision, but a subsequent case that disagreed.

The project converted a three-storey pub into a four-storey building containing four dwellings. The two lower floors became maisonettes that incorporated part of the ground floor (formerly pub) and first floor (formerly manager's accommodation); two more "upper maisonettes" comprised the old top floor (formerly manager's accommodation) and the new top floor (new construction).

The appellant treated the sale of major interests in all four properties as zero-rated in 2011. It was subsequently agreed that the sale of the upper maisonettes was exempt, but the company appealed to the Tribunal in relation to the lower maisonettes.

The taxpayer's representative criticised the decision in *Macpherson* for a lack of any indication of when Note 9 would, or could, be engaged. He suggested that the reasoning of the Court of Appeal in *Jacobs* was compelling in relation to s.30, even if not binding as it would be in relation to s.35.

The judge posed the question as "*whether the ground floor was converted 'into a building designed as a dwelling or number of dwellings'*". She noted that the Tribunal in *Calam Vale* had decided this kind of project was not within Item 1(b), because it refers to "converting a non-residential building or a non-residential part of a building into a building designed as a dwelling or number of dwellings" rather than "converting a non-residential building or a non-residential part of a building into a building or part of a building designed as a dwelling or number of dwellings".

The judge commented that if this was correct, Note 9 could have no application. If item 1(b) could only apply to buildings that were wholly non-residential before the conversion, then there would always be a new dwelling or dwellings afterwards, because there would be no dwellings beforehand – so Note 9, which was drafted at the same time as item 1(b), would be meaningless. HMRC's representative was invited to suggest when it might apply, but could not come up with an example.

The judge also commented that a conversion would appear only to satisfy Note 9, under the reasoning in *Macpherson* if it not only was "horizontal rather than vertical" (creating two flats rather than two maisonettes) but also did not touch the formerly residential part at all – a project that affected the whole building would not be "a conversion of a non-residential part of a building", but would be "a conversion of a building containing a residential part". This seemed unnecessarily strict.

Given the confusion that these provisions have continued to cause, it is worth reproducing the careful reasoning of the judge in full:

37. We consider that the purpose of Note 9 is to exclude from Item 1(b) any conversion of a mixed use building into dwellings unless additional dwellings (when compared to the building as a whole before conversion) have been created as a result of the conversion of the non-residential part of the mixed use building. The draftsman of Item 1(b) must have considered that the conversion of the non-residential parts of mixed use buildings into dwellings would fall within Item 1(b) in order to have considered it necessary to draft Note 9 to exclude some of such conversions.

38. As the effect of converting the non-residential part of a building alone (that is to say the non-residential part not combined with any residential part) into a dwelling would always be to create more dwellings than previously existed, we conclude that the draftsman must have contemplated the possibility that one or more new dwellings would be created from bringing together residential and non-residential parts of the mixed use building. We bear in mind that to achieve the social purpose of creating additional housing it does not matter from what constituent parts the new dwellings are created provided that additional dwellings are created as a result. However Note 9 would be required in order to ensure that relief is available only in those situations where additional housing is created.

39. If we are correct in our understanding of Note 9 then a mixed use building which previously contained one dwelling would be excluded from Item 1(b) if the result of converting the non-residential part was to create one large dwelling. However, the conversion would be included in Item 1(b) if the building was converted into two or more moderately sized dwellings. In the second case, housing stock is increased and so relief under Section 30 would be available. This is in accordance with our understanding of the social purpose behind Group 5.

40. Looking at Item 1(b) in the light of our conclusions regarding Note 9, we conclude that "converting … a non-residential part of a building into a building designed as a … number of dwellings" should be construed as meaning that the non-residential part of a building has changed its character and now forms part of a building designed as a number of dwellings. It follows that we agree with the Appellant and prefer the careful reasoning of the Court of Appeal in Jacobs and of the Tribunal in Alexandra Countryside. It seems to us that this is the better interpretation of Item 1(b) as it enables Group 5 to be interpreted as a coherent whole.

The comparison exercise was between the situation before (non-residential part of a building) and the situation afterwards (building containing four dwellings); the non-residential parts had changed their

nature, and the supply of the major interest grants in the lower maisonettes fell within item 1(b).

That suggests that the whole supply is zero-rated, and the VAT incurred on work relating to the conversion of the first floor should also be recoverable – there is no scope for a claim "to the extent that", as there was in *Jacobs*.

First-Tier Tribunal (TC04917): *Languard New Homes Ltd*

3.3.2 Ancillary buildings

In TC04132, the FTT decided that certain charitable residences were to be used as a relevant residential purpose institution providing personal care. The same site was the subject of a second appeal, this time concerning the liability of certain building works carried out by a subsidiary of the charity. Various other disputes had been settled by agreement between the parties.

The outstanding issue related to the construction of a workshop at the same time as the RRP buildings, and used together with them. The company argued that a construction supply is zero rated where ancillary buildings are used with the main building or buildings, which are used solely for a relevant residential purpose, and there is no requirement that the ancillary buildings are solely used in conjunction with the main relevant residential purpose building or buildings.

HMRC disagreed. In their view, the workshop was not used as a unit with the newly constructed RRP building only, but with all the buildings on the site. It was therefore not "constructed at the same time" with what it was "a unit" of, as required by Group 5 Note 5.

The Tribunal examined the precedents and HMRC's policies on ancillary buildings that are part of a larger RRP complex. It is recognised that non-residential buildings can qualify if they used together with others for a residential purpose, for example dining halls or laundry facilities in student accommodation. At the end of this consideration, it summed up the issue between the parties as follows:

Perusal of the correspondence between the parties indicates that the parties would agree:

(1) If the Workshop had been used exclusively with Holme Terrace it would have been eligible to be zero rated pursuant to Note 5.

(2) If the Workshop had been constructed on its own for use with the previously constructed buildings on the site it would not have been eligible to be zero rated.

The Respondents contends that "as a unit" requires that the Workshop be used exclusively to service Holme Terrace. The Appellant contends that provided that the Workshop is used in conjunction with Holme Terrace it is used as a unit with it.

The Tribunal considered that the result contended for by the appellants was the most sensible one. The main difficulty in arriving at it was the use of "used together as a unit" in the legislation, rather than simply "used together". Nevertheless, the Tribunal was satisfied that the workshop was an integral part of offering safe and suitable living accommodation for the

elderly, and other uses were de minimis. The workshop was therefore deemed to be used for a RRP, and the appeal was allowed.

First-Tier Tribunal (TC04851): *TGH (Commercial) Ltd*

3.3.3 Demolished?

A builder appealed against a decision by HMRC that certain works to a house did not qualify for zero-rating. The planning consent for the works envisaged extension and alteration, but the work actually involved demolishing the whole of the property apart from a small part of the facade. The builder argued that this was part of an understanding between the architect and the planning officer: the work had become more extensive during the project, and there was an implicit requirement in the planning consent that the facade should be retained.

The FTT (TC03951) did not consider that this was enough to satisfy the conditions for zero-rating, which have to be applied strictly. In substance, the work done might have amounted to the construction of a new dwelling, but the conditions were not satisfied. The planning consent did not refer to demolition at all, and therefore did not set a requirement to retain certain parts of the existing building. That would have had to be explicit to meet the conditions in the law.

The trader appealed to the Upper Tribunal, arguing that the retention of a bay should be regarded as de minimis, and that the planning consent reflected an understanding between the owner and the authority that the facade would be retained. The UT confirmed that such an "understanding" is not enough: the consent must formally require retention, rather than simply permitting it. Anything that was capable of being a "facade" for the purposes of Note 18(b) could not be regarded as de minimis for the purposes of Note 18(a). In this case, the project could not be regarded as demolition and reconstruction, but had to be standard rated as alteration and extension.

Upper Tribunal: *Boxmoor Construction Ltd v HMRC*

3.4 Input tax claims on land

3.4.1 DIY claims

There have been a number of cases about planning restrictions on the use or occupation of what might otherwise be a "dwelling". In early 2013, TC02522 was decided in favour of a DIY 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 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.

HMRC appealed to the Upper Tribunal, which heard the case in January 2016. The UT considered several of the cases on the issue, and came to the conclusion that condition 4 of the planning consent clearly did prohibit separate use, particularly if read in the context of the rest of the document and the purpose underlying the restrictions. "*The aim of Condition 4 is manifestly to ensure, by means of the occupancy restriction, that the accommodation is retained for the purposes of the Park Hall fishery business. Indeed, the relevant reason set out in the Inspector's Decision expressly says so. This is confirmed by the planning consent as a whole, which explains in detail how certain important requirements of the Park Hall fishery business are to be met through the occupation of the Building.*" The class of possible users was wider than in some other cases, but they all had to have a close connection with the fishery, and that was enough to engage Note 2(c).

HMRC's appeal was allowed. The judge noted that HMRC had expressly ruled out applying for their costs, because they wanted an authoritative decision to clarify the legal principles for similar cases.

Upper Tribunal: *HMRC v Richard Burton*

An individual made a DIY claim in 2014, 20 years after a certificate of completion had been issued in respect of his house (and 32 years after obtaining planning permission for the construction of the house). He claimed that he had only just completed the garage, and it was all part of a single continuous project that had taken many years. He probably did not help his case by apologising for the late submission of the claim – an invitation to refuse it, which HMRC duly did.

The Tribunal examined the facts, which included the laying of a slab to form the base of the garage only five weeks after the completion of the house. There was a separate planning consent for the garage, but the Tribunal regarded it as a variation of the original plan, rather than a completely separate project. It had been granted in 1993, 18 months before completion of the house. HMRC accepted that, in principle, it was possible for a DIY project to take 30 years; a claim would still be "in time" if submitted within 3 months of the final completion. They did not accept that a six-month overlap in working on house and garage was enough to make them a single project.

The Tribunal decided that the house and garage had been built as part of a single continuous project, so the claim was in time. The facts are relatively unusual and were considered in some detail by the Tribunal.

First-Tier Tribunal (TC04800): *B Bowley*

A DIY claim was rejected because planning consent had not been obtained at the time the work was carried out. Retrospective consent was obtained some 11 months afterwards, but this was not enough to validate a VAT claim. Evidence of planning consent has to be submitted with the claim in accordance with reg.201, and this is clearly impossible if it has not yet been obtained. The Tribunal agreed with HMRC that the legal requirement was strict, and dismissed the appeal.

First-Tier Tribunal (TC04973): *Scott Kernohan*

A married couple carried out a DIY project and claimed £12,543, which was refused by HMRC on the basis that the previous structure had not been completely demolished. They appealed, arguing that they had been misled by HMRC's guidance, and the conditions for a repayment were "effectively" met.

The plans for the project had initially involved the retention of three exterior walls and one interior wall. As the work progressed, it became necessary to demolish everything except one gable end. When the work was nearly completed, the husband enquired about making a DIY claim, and was advised that it would be possible. He submitted the forms when the work was complete; the claim was initially refused because the plans still showed the retention of the interior wall, and also because the gable end was not a "facade". The taxpayer appealed.

The Tribunal noted that it had no jurisdiction to hear an appeal on misdirection. However, the judge commented that it did not appear that the alleged misdirection had had any effect on the building work or on the actual possibility of making an effective claim – it had, if anything, simply encouraged the couple to make a claim that could not succeed.

The judge considered whether the decision in *Astral Construction* had any significance for this kind of project. The UT had decided that it was necessary to consider whether, as a matter of fact and degree, the new structure was a completely different building to what had been there before. The Tribunal did not consider that the two cases were analogous: in Astral, the new building had a very different size, shape, function and character from the original. Here, it was the same sort of thing – a dwelling – and Note 18 applied. The only question, therefore, was whether the gable wall was "a facade" whose retention was required by planning consent.

The judge distinguished the *Boxmoor* decision above. In this case, the retention of the gable wall was clearly indicated on the plans, and that was more than a mere tacit understanding between the architect and the planning officer. The judge was satisfied that the retention of the wall was required. However, the normal meaning of a "facade" was the front of a building facing the street: that did not apply here. Accordingly, the project failed the test of "new construction", and the DIY claim was rightly rejected by HMRC.

First-Tier Tribunal (TC04980): *Andrew David Reeves*

3.5 Other land problems

Nothing to report.

4. INTERNATIONAL SUPPLIES

4.1 E-commerce

4.1.1 MOSS rules

The UK government has responded to the Commission's consultation on the MOSS rules, urging the Commission to reduce the burdens on small and micro businesses by introducing a threshold for application of the cross-border registration requirements. The government also suggests reducing both the evidence needed to establish customer location and the 10-year record-keeping requirement. Progress is anticipated on the Commission's wider Digital Single Market Strategy paper.

www.gov.uk/government/publications/vat-in-the-digital-single-market-eu-consultation-response

HMRC have announced a further simplification of the MOSS rules for those businesses registered for MOSS but below the UK registration threshold. They can make nil UK VAT returns, but have to file MOSS returns and account for output tax on their EU consumer sales.

Most businesses are supposed to collect two pieces of non-contradictory evidence to show where the customer is located. From the start, HMRC allowed these specially registered UK businesses to base their customer location decisions on a single piece of information provided to them by their payment service provider. HMRC are now extending this, to allow the business to use its own judgement to decide what piece of evidence to collect. HMRC will accept one single piece of evidence, chosen by the trader, such as the address given by the customer.

HMRC also suggest that some of those who have registered for MOSS might not really be "in business", and therefore should not be registered at all. Although there is no registration threshold for MOSS supplies, if an activity is only carried on as a hobby, it would not lead to a registration liability.

Revenue & Customs Brief 04/2016

These points are included in an updated version of the HMRC *Guide to VAT on supplies of digital services to private consumers: Register and use the VAT Mini one-stop-shop for digital supplies*.

www.gov.uk/government/publications/vat-supplying-digital-services-to-private-consumers

4.1.2 VAT MOSS exchange rates

HMRC have published the usual table of exchange rates for use by those registered under MOSS for the quarter to December 2015.

VAT Information Sheet 1/2016; www.gov.uk/government/publications/vat-information-sheet-0116-vat-moss-exchange-rates-for-period-ending-december-2015

4.2 Where is a supply of services?

4.2.1 Place of supply of repair services

HMRC ran a consultation until 29 February 2016 on a draft order to change the place of supply rules for "indemnity repairs" to moveable goods carried out under insurance contracts. The change is aimed at countering avoidance involving the provision of repair services to insurers located outside the EU. The order introduces an exception to the usual place of supply rules, which will treat supplies as taking place where they are effectively used and enjoyed, rather than in the country where the recipient is located. It will require UK service providers to charge VAT at the standard rate on their repairs, irrespective of where the provider of the insurance cover for the goods is located.

www.gov.uk/government/publications/draft-legislation-vat-use-and-enjoyment-provisions-for-insurance-repair-services

4.3 International supplies of goods

4.3.1 Imports

An individual retired from the police force and set off with his wife on what was intended to be a period of long-term travel. They bought a motorhome in the USA. He fell ill, and discovered that it might be related to a pre-existing condition that he had not reported to his insurers because he had not thought it was relevant: there was therefore uncertainty about whether his insurers would pay for medical treatment abroad. In the circumstances, they decided to return to the UK from Canada, where they were at the time.

The motorhome then proved a significant problem. They could not store it in Canada without local insurance, which they could not obtain; they could not return it to the USA without a new visa; they could not sell or scrap it in Canada because it was US registered. They were left with no obvious alternative but to ship it to the UK. This cost $2,950. On arrival, it was subject to customs duty of $1,200 and VAT of £2,640. There was further expense in making it legal for use on UK roads.

The individual then applied for repayment of the duty and VAT on the grounds of Transfer of Residence Relief. This was eventually accepted not to be due, but he applied instead for remission of the duties under art.239 of the Customs Code, which covers "special situations" in which there has been no "deception or obvious negligence" on the part of the importer. In the view of the Tribunal, HMRC sought to apply this provision far too narrowly, treating the individual as if he were a trader rather than a traveller. The equitable relieving intention of the provision should be applied, and the duty repaid.

On the other hand, some of the appellant's claims – that he should have been repaid the duty because he had been out of the country for 185 days; that the valuation had been arbitrarily arrived at by the officers; and that he had been poorly treated by the Customs officers at the port – were rejected. His appeal was allowed.

First-Tier Tribunal (TC04806): *Brian Hughes*

An individual was stopped in the Green Channel at Heathrow on 1 January 2015. He was found to have three uncut diamonds in his luggage – one was "certified" (i.e. could be legally sold) and two were not. All were confiscated. The individual sought restoration of the certified diamond on the basis that it was to be re-exported shortly after to the USA. There was no customs duty on diamonds, and the VAT at 20% of the $35,000 value could have been avoided by temporary import procedures, or by paying it and then reclaiming it on leaving the country.

The Tribunal was satisfied that there had been an intention to re-export the diamond. However, the Tribunal was also satisfied that the decision to refuse restoration was entirely reasonable – the carrier had attempted to pass through the Green Channel, had told several material lies and could not explain the presence of the other two diamonds. Although the owner of the certified diamond, who was in New York throughout, claimed that he had issued instructions to the carrier to go through the Red Channel, it seemed inherently unlikely that this could have been the subject of a misunderstanding in the context of such a valuable item.

In the context of the attempt to smuggle two uncertificated diamonds and the lies that had been told, the refusal to restore was entirely reasonable, and the appeal was dismissed.

First-Tier Tribunal (TC04954): *George Akay*

4.3.2 Indirect export

A UK company supplied a hydraulic excavator to a Belgian company and zero-rated the supply. However, before the goods left the UK, the Belgian company sold it on to another UK company, which exported the machine to an Australian company. HMRC therefore refused zero-rating of the original supply on the basis that the conditions for zero-rating a despatch had not been met.

The company appealed, arguing that it had met the conditions for zero-rating in Notice 703, and that it did not and could not know anything about the subsequent transactions by its customer. HMRC did not allege any impropriety, but ruled that the conditions were not satisfied.

The problem was that the company was relying on the customer to provide evidence of the goods leaving the UK. The original evidence was provided to the second UK company, and the appellant did not have the documents required by law. It could not zero-rate the despatch on the basis of a supply to Belgium, because the goods did not go to Belgium – the invoice that said they did was incorrect, and it appeared that the company had always known that the goods would instead be shipped to Australia. It also could not zero-rate the supply as an export because the goods had been supplied on before they left the UK – the transport was not part of the appellant's supply.

The Tribunal considered the facts, the law, and the *Teleos* case. This was not a case where HMRC were satisfied that the goods had been exported and were disputing one of the formal requirements. Nor was it a question of whether the company had failed to provide the required evidence within 3 months. The transactions were not really in dispute, and they did not qualify for zero-rating under the detailed requirements of paras. 6.5

and 6.6 of Notice 703. Although para.6.6 does not have the force of law, para.6.5 does.

There was also some dispute about whether the assessment had been raised for the right period. The company argued that it should have fallen in 09/11, at the end of the three-month period for providing evidence. The Tribunal agreed with HMRC that it was correctly raised for 06/11, when the supply took place, because zero-rating had never been available. The circumstances were therefore different from those in *Musashi Autoparts*, when goods had been zero-rated but this had to be reversed because of a failure to provide the evidence. In that circumstance, Notice 703 requires the output tax to be accounted for on the return following the period in which the supply was made; it can be recovered later, when the evidence is obtained, but interest will be due in the meantime.

The assessment was raised within 1 year (just) of the officer visiting the appellant in February 2013 and obtaining a redacted copy of the Bill of Lading – it was this that showed that the supply should not have been zero-rated by the appellant. Information had been obtained from the other UK company at an earlier date, but on its own that would not justify the raising of the assessment.

First-Tier Tribunal (TC04925): *K J Services Ltd*

4.3.3 Intrastat

The *Intrastat General Guide* has been updated. The large limits are unchanged (arrivals threshold £1.5m, despatches threshold £250,000, delivery terms threshold £24m); the low value consignment threshold has been reduced from £160 to £150 with effect from 1 January 2016.

Notice 60

4.3.4 Updated Notices

HMRC have updated their Notice *Imports*. “What’s changed?” notes that “the C18 team have moved from Grimsby to National Clearance Hub (NCH) Salford” and paragraph 8.8 on Isle of Man VAT registered importers has been deleted.

Notice 702

HMRC have updated their Notice on *Deferring duty, VAT and other charges*. The central deferment office address has been updated.

Notice 101

HMRC have updated their Notice *Visiting forces*. It has been updated for the introduction of a new ‘Allied Command Operations Purchase Card’.

Notice 431

4.3.5 Updated import/export Notices

HMRC have updated their Notice *Classifying your imports or exports*. It explains the new procedures for applying for a BTI ruling applicable from 1 April 2014 and updates HM Revenue and Customs (HMRC) contact numbers. It also now contains more information on the Tariff Classification email service, which replaced the telephone service from

September 2015. From 1 May 2016, Binding Tariff Information decisions will be valid for 3 years (formerly 6 years).

Notice 600

HMRC have updated their Notices *European Union: Binding Origin Information (BOI) and European Union preferences – export procedures*. The only changes appear to be to replace the expression "European Community" and its abbreviation "EC" with "European Union" and "EU".

Notice 831, Notice 827

HMRC have updated their Notice *Tariff preferences – rules of origin for various countries*. It explains the rules of origin if goods are to qualify for a preferential rate of duty when exported to or from Mexico. The terms European Union and EC are longer used and are replaced by European Union and EU.

Notice 828

HMRC have updated their Notice *Imported goods – end-use relief*. The Notice has been re-written to improve readability. It also has:

- A new paragraph on civil penalties.
- Additional clarification on the policy for shipwork end-use including the Continental Shelf.
- A new section on Chinese Bicycle parts and Anti dumping duty.
- Updated details on how to contact HMRC.

Notice 770

4.3.6 Changes to customs procedure codes

HMRC have issued a paper to explain some of the more significant changes to customs procedure codes used for special procedures under the Union Customs Code from 1 May 2016. These will in particular affect imports for Processing Under Customs Control and Inward Processing Drawback.

Customs Information Paper 6/2016;
www.gov.uk/government/collections/customs-information-papers--2

4.4 European rules

4.4.1 Future of VAT

In February, the Commission held an "orientation debate" on the future for VAT in the EU. This was in preparation for the publication of an Action Plan in March. The Commission wants to narrow the VAT gap, the difference between the expected VAT revenue and VAT actually collected in Member States, which was almost €170 billion in 2013. Cross-border VAT fraud is estimated to cost €50bn a year across the EU. The burdens on business, particularly digital businesses, need to be reduced.

http://europa.eu/rapid/press-release_MEX-16-398_en.htm

4.4.2 Registration thresholds

The Commission has published a list of the VAT registration thresholds applied by EU Member States updated to January 2016. This includes the 'regular' VAT registration threshold for small locally established businesses, as well as the thresholds for intra-Community acquisitions and distance sales.

The UK still has the highest registration threshold for small enterprises – Sweden, Spain and the Netherlands have no threshold at all. The threshold for registration in respect of acquisitions by businesses not entitled to input tax recovery and by non-taxable legal persons is about €10,000 in most other countries, as against £82,000 in the UK.

http://ec.europa.eu/taxation_customs/resources/documents/taxation/vat/traders/vat_community/vat_in_ec_annexi.pdf

4.4.3 Investment gold

The Commission has published a list of gold coins eligible for VAT exemption in 2016 under the special scheme for investment gold. A coin that is not listed still qualifies for exemption if it satisfies the criteria of art.344 PVD.

http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52015XC1126(01)&from=EN

4.4.4 Issue of invalid invoices

A German company was discovered on a VAT inspection to have deducted input tax on the strength of non-compliant invoices. The company obtained corrected invoices, but the tax authority maintained that deduction was still not possible. Questions were referred to the CJEU.

The A-G has given an opinion that the principle of neutrality requires that a trader who has met the substantive requirements for deduction should be allowed to correct defects in invoices and retroactively qualify for deduction. An absolute denial of deduction appeared disproportionate, and rendered the exercise of rights either impossible or excessively difficult.

Part of the question related to the period in which the deduction could be made. The German authorities accepted a deduction in the later period in which the corrected invoice was obtained, but then an interest charge (and possibly penalties) could arise in the meantime. The German government regarded that as the application of the judgment in *Terra-Baubedarf-Handel* (Case C-152/02). The A-G considered that the correction should fall in the period in which the supply was received, in line with the principle that the right to deduct arose immediately on receiving an input. The A-G distinguished the earlier case in that it concerned the original issue of an invoice: the company did not have a right to deduct until it held one. In the present case, the company had an invoice, but it was defective. The A-G considered that a crucial distinction.

The recommended answer includes the following: "*the Member States may adopt measures to penalise failure to provide the required details, as long as they comply with the principle of proportionality, and also*

measures placing a temporal restriction on the possibility of correcting an incorrect or incomplete invoice, provided they apply in the same way to similar rights in tax matters based on domestic law and to such rights based on EU law (principle of equivalence) and do not render impossible in practice or excessively difficult the exercise of the right of deduction (principle of effectiveness)."

CJEU (A-G) (Case C-518/14): *Senatex GmbH v Finanzamt Hannover-Nord*

4.4.5 Required contents of invoice

A-G Kokott has considered a question that has been before the Tribunal in the UK in recent quarters – how detailed a description of the supply is required for an invoice to comply with the law. In her view, descriptions such as 'legal services rendered from such a date until the present date' or 'legal services rendered until the present date' are not sufficient to satisfy the law and therefore to justify input tax deduction for the customer.

The question referred noted that the authority might be able to obtain more information about the nature of the supply "in accordance with the principle of collaboration". The A-G considered that the supplier has to make the correction – it cannot be provided by the person claiming a deduction, or by the authorities.

The purpose of the description is to make sure that the correct provisions are applied to the supply. For example, some legal services are subject to a lower rate under Portuguese transitional provisions. The description is therefore insufficient to enable the authorities to carry out their monitoring function.

CJEU (A-G) (Case C-516/14): *Barlis 06 — Investimentos Imobiliários e Turísticos SA v Autoridade Tributária e Aduaneira*

4.4.6 Compromise with the tax authorities

An Italian company was in financial difficulties and proposed a compromise with its creditors. Certain preferential creditors would be paid in full; others, including the VAT authorities, would only receive partial payment. The Italian court referred questions to the CJEU to determine whether it would be acceptable to enter into such an arrangement, or whether a Member State has an obligation to pursue the full amount of the debt.

A-G Sharpston has given an opinion that such an arrangement would be acceptable, provided that an expert has given an opinion that the State will receive no greater amount by proceeding with bankruptcy to enforce the full debt. The arrangement should also be approved by a court. This contrasts with the two cases in which the Commission took infringement proceedings against Italy for allowing a general and indiscriminate amnesty for past VAT debts; there, the CJEU held that this was incompatible with a Member State's obligations.

CJEU (A-G) (Case C-546/15): *Degano Trasporti S.a.s. di Ferruccio Degano & C., in liquidazione*

4.4.7 Public body

The Czech court referred questions to the CJEU asking whether a public broadcaster could be exempt from VAT in respect of broadcasting financed by a statutory fee payable by anyone in possession of a radio receiver (i.e. similar to the BBC licence fee).

A-G Szpunar concluded that the activity is not "business" and is therefore not exempt under what is now art.132(1)(q) "the activities, other than those of a commercial nature, carried out by public radio and television bodies." There was no direct link between the payment and the supply: in line with *Tolsma* and with *Apple & Pear Development Council*, the payment was not consideration for what the broadcaster did or for what the listener received.

The broadcaster had claimed an additional repayment of VAT by excluding the licence fees from its partial exemption calculations; the authorities insisted that they constituted exempt income and should therefore be included. Although it was not part of the questions for reference, the A-G commented that there should be no right of deduction for VAT incurred exclusively in relation to activities that were financed by income that was outside the scope of VAT. Although the Directive does not prescribe detailed rules for apportioning VAT in relation to "business/non-business" activities, Member States must have regard to the broad logic and aims of the Directive in determining appropriate methods of apportionment.

CJEU (A-G) (Case C-11/15): *Odvolací finanční ředitelství v Česky Rozhlas*

4.4.8 Transitional exemption

Under a transitional provision, the supplies of lawyers' services in the course of their usual activities were exempt from VAT in Belgium up to 31 December 2013. They had been exempt when the VAT Directive entered Belgian law in 1971, and remained so under a derogation in accordance with art.371 PVD. The exemption was abolished by Belgian law with effect from 1 January 2014.

Some lawyers argued that this would lead to a number of problems that made it unlawful – in particular, the possible 21% increase in the cost of lawyers would reduce access to justice. The questions referred were many and detailed, covering a number of possible "solutions". A-G Sharpston has given an opinion that the transitional exemption accorded with the Directive, and it could have been restricted without being wholly abolished; but having abolished it completely, Belgium cannot reintroduce any aspect of it. There was no scope for exempting legal services under any other provision of the PVD; in particular, legal aid work could not be brought within "welfare and social security work" under art.132(1)(g). The charging of VAT on lawyers' services did not breach any principles of international law or agreements.

CJEU (A-G) (Case C-543/14): *Ordre des barreaux francophones et germanophone and Others v Conseil des ministres*

4.4.9 Freedom to provide services

In a corporation tax case, A-G Kokott has given an opinion emphasising that tax rules cannot discriminate against businesses resident outside a particular Member State. The Portuguese rules refused a deduction of operating costs for a non-resident taxpayer subject to limited taxation (but allowed a lower rate of tax), with the effect that the tax burden on profits was likely to be significantly higher than for a resident taxpayer. This could not be justified by the allocation of taxing powers to the Member States, nor the need to ensure efficient tax collection or supervision.

The A-G drew on VAT cases by analogy in order to support the conclusion that costs incurred in earning revenue should be deductible from that revenue in calculating tax.

CJEU (A-G) (Case C-18/15): *Brisal — Auto Estradas do Litoral S.A., KBC Finance Ireland v Fazenda Pública*

4.4.10 Double jeopardy?

The Italian court has referred a question to the CJEU about whether a person who has been subject to a civil penalty for unpaid VAT can also be subject to criminal prosecution. The UK law generally envisages such a possibility, although s.60 VATA 1994 specifically provided that a s.60 penalty could not be levied if the taxpayer had already been the subject of a criminal penalty. HMRC guidance on conduct that may give rise to either or both a civil penalty and criminal prosecution is set out in their manuals at CH300600.

The question referred is:

Does Article 50 of the Charter of Fundamental Rights of the European Union, interpreted in the light of Article 4 of Protocol No 7 to the European Convention for the Protection of Human Rights and Fundamental Freedoms and the related case-law of the European Court of Human Rights, preclude the possibility of conducting criminal proceedings concerning an act (non-payment of VAT) for which a definitive administrative penalty has been imposed on the defendant?

Article 50 of the Charter of Fundamental Rights states: "*Right not to be tried or punished twice in criminal proceedings for the same criminal offence- No one shall be liable to be tried or punished again in criminal proceedings for an offence for which he or she has already been finally acquitted or convicted within the Union in accordance with the law.*"

CJEU (Reference) (Case C-524/15): *Criminal proceedings against Luca Menci*

4.4.11 Extent of medical profession

The Portuguese court has referred a question about whether osteopathy can be regarded as a branch of the paramedical profession qualifying for exemption. The UK already recognises registered osteopaths as within the exemption – the UK defines the medical profession as including all those entered on statutory medical registers, and there is such a register provided by the Osteopaths Act 1993.

The question referred is:

For the purposes of the interpretation of art.132(1)(c) PVD, should non-conventional therapies, in particular osteopathy, be regarded as paramedical activities? Must a taxable person who is authorised under national law to practise a paramedical activity, namely physiotherapy, but who in the context of his professional health activity uses either indistinctly or complementarily both therapies characteristic of physiotherapy and therapies characteristic of osteopathy be regarded, for the purposes of art.132(1)(c) PVD and, consequently, for the purposes of [the Portuguese VAT law], as a professional who, overall, carries out a paramedical activity which is, accordingly, exempt from VAT?

CJEU (Reference) (Case C-555/15): *Bernard Jean Marie Gabarel v Fazenda Pública*

4.4.12 Place of supply of emissions allowances

In the context of dealing with the consequences of a carousel fraud, the German court has referred a question to determine whether emissions allowances are covered by art.56(1)(a) PVD:

Is art.56(1)(a) PVD to be interpreted as meaning that an allowance under Article 3(a) of Directive 2003/87/EC of the European Parliament and of the Council of 13 October 2003 establishing a scheme for greenhouse gas emission allowance trading within the Community and amending Council Directive 96/61/EC which confers a right to emit one tonne of carbon dioxide equivalent during a specified period is a 'similar right' within the meaning of that provision?

This relates to art.56 as it originally was – the list of services "supplied where received". Art.56(1)(a) referred to "transfers and assignments of copyrights, patents, licences, trademarks and similar rights". Since the implementation of the VAT package in 2010, art.56 has been about hiring of means of transport.

CJEU (Reference) (Case C-453/15): *Criminal proceedings against A, B*

4.4.13 Margin scheme

The Lithuanian court has referred questions to the CJEU on the operation of the margin scheme for second-hand goods under art.314 PVD. It appears that the trader in the case bought cars in Denmark and sold them in Lithuania, Belarus and Russia. The questions are about the consequences of irregularities in the paperwork which the trader did not and could not know about, and whether the margin scheme can still be applied.

CJEU (Reference) (Case 624/15): *Litdana UAB v Valstybinė mokesčių inspekcija prie Lietuvos Respublikos finansų ministerijos*

4.4.14 Effectiveness of Italian deterrents

An Italian company was late paying VAT and associated penalties, and was therefore subject to a fine and criminal proceedings. The Italian law was then changed, raising the threshold below which criminal proceedings are not instituted, effectively removing the criminal sanction against this taxpayer. The threshold is now higher for VAT than for Italian income tax. The Italian court has referred questions to the CJEU to establish whether such a difference is permitted under the Directives, which require

Member States to implement effective deterrents to enforce the collection of VAT.

CJEU (Reference) (Case C-574/15): *Criminal proceedings against Mauro Scialdone*

4.4.15 Response to evasion risk

The Bulgarian court has referred questions about the determination of taxable amounts in the context of possibly fraudulent transactions. The first question asks whether the authorities are entitled to infer from the absence of goods that have been supplied to a trader, that they have been supplied for consideration by the trader. It appears that Bulgaria has implemented laws to counter VAT evasion that do not correspond to the Directive; the questions ask whether the measures are permitted as a proportional response to the risk of fraud and evasion.

CJEU (Reference) (Case C-576/14): *ET 'Maya Marinova' v Direktor na Direktsia 'Obzhalvane i danachno-osiguritelna praktika' Veliko Tarnovo pri Tsentralno upravlenie na natsionalnata agentsia za prihodite*

4.4.16 Oxygen in different forms

The Belgian court has referred questions about whether it is permissible to apply a reduced rate (6%) for oxygen treatment by the provision of oxygen in cylinders, whereas oxygen treatment using a compressor is standard rated (21%). Annex III points 3 and 4 allow lower rating for "pharmaceutical products of a kind normally used for health care, prevention of illnesses and as treatment for medical and veterinary purposes, including products used for contraception and sanitary protection" and "medical equipment, aids and other appliances normally intended to alleviate or treat disability, for the exclusive personal use of the disabled, including the repair of such goods, and supply of children's car seats".

CJEU (Reference) (Case C-573/15): *État belge v Oxycure Belgium SA*

4.4.17 Permitted penalty?

The Hungarian court has referred questions about the lawfulness of imposing a penalty for choosing the wrong method of accounting for a reverse charge transaction, where the tax authority has not incurred any loss of revenue and there is no evidence of abuse. It appears that a supplier has raised a VAT invoice for a supply that ought to be subject to a reverse charge and has accounted for output tax; the customer has deducted input tax (without also accounting for the reverse charge). The tax authorities must have levied the penalty and assessed for the VAT, disregarding the fact that the supplier had already accounted for it.

CJEU (Reference) (Case C-564/15): *Tibor Farkas v Nemzeti Adó- és Vámhivatal Dél-alföldi Regionális Adó Főigazgatósága*

4.5 Foreign refund reclaims

Nothing to report.

5. INPUTS

5.1 Economic activity

5.1.1 Holding company recharges

In TC03698, a UK company appealed against an assessment to claw back £81,000 of input tax recovered in its VAT returns from 10/07 to 01/09. The FTT's decision of principle would also apply in other periods, but these were not considered directly.

HMRC had concluded that the company was not carrying on any economic activity and was therefore not entitled to be registered. It was a UK registered company, listed on the Alternative Investment Market (AIM). Its operating subsidiaries carry on gold mining activities in Australia.

When the company applied for registration in 2007, it stated that its activities were "mining". Following correspondence with HMRC it was accepted that this was a mistake: it was the company's own activity that was relevant, not that of the group. HMRC must have been satisfied by the responses given concerning management services being supplied to the Australian subsidiaries, because they registered the company under the classification "management consultancy".

The judge was satisfied that the directors of the holding company spent material amounts of time in managing the subsidiaries' activities. In principle, therefore, it was possible that the holding company was "active" and making taxable supplies of management services. However, at the time that the "supplies" were made, no price or payment terms had been agreed. Although the facts of *Tolsma* were somewhat different, the judge agreed with HMRC that the principle was of assistance: any payment would have been voluntary, and would therefore not have been consideration for a supply. The agreement of payment terms only finally took place after the last of the disputed periods, and that could not change the correct treatment, which should be based only on the conditions subsisting at the time the claims to input tax were made.

A separate argument about whether the assessments were in time was also considered. The appellant claimed that HMRC had had sufficient information to raise assessments following a meeting more than a year before they were raised in August 2010. According to the company, no new information had been obtained by an officer who visited the company in August 2009; in particular, the officer had discovered for the first time that the holding company was not itself operating a gold mine, but that information was already in HMRC's possession. The time limit depended on what "the Commissioners" knew, not a particular individual officer.

The FTT disagreed. Although the officer might have found out about the activities of the company by reading the correspondence rather than the initial registration application, his discovery at the meeting led him to ask further questions about the arrangements between the holding company and the subsidiaries. It was this further information that led to the assessments – he found out, which no one at HMRC previously knew, that there were no formal arrangements in place to enforce payment for the

management services. The assessments were therefore not raised outside the statutory time limits.

Upper Tribunal

The company appealed to the Upper Tribunal. The UT judge was equally unconvinced by the vagueness of the company's arrangements. There had to be a direct link between a service supplied and the consideration for it; an intention to make supplies was not enough to justify input tax recovery, but rather there had to be an intention to make supplies for a consideration. The decision not to charge until the subsidiaries could afford to pay amounted to a gratuitous supply (particularly following the *Finland* case). There was no specific recognition that supplies made in any period would be paid for in the future: in that case, any payment received in the future would not be consideration for those supplies, because the necessary link would be missing.

After a very detailed examination of many precedent cases on the nature of consideration and the entitlement to recover input tax, the appeal was dismissed.

Upper Tribunal: *Norseman Gold plc v HMRC*

5.1.2 Single Farm Payment Entitlements

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

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

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

The Tribunal agreed with the taxpayer that the purchasing of SFPEs was not a separate activity, but an integral part of the farming business. Given that the purchase was carried out in the context of a fully taxable business,

there was no reason to deny the deduction of input tax. It was a fully recoverable overhead cost.

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

HMRC considered the purchase of the SFPE units to be "artificial" because it was so out of proportion to the actual farming activities. However, their counsel confirmed to the judge that HMRC regarded any level of SFPE purchases as falling foul of their view that they were linked to activities outside the scope of VAT – it was not just the quantity that created the problem. The judge concluded that HMRC's view was simply wrong. The FTT had come to a justifiable decision of fact on the basis of evidence that the purchases were connected to the taxable business, and that led inevitably to the conclusion that the VAT was deductible as input tax.

Upper Tribunal: *HMRC v Frank A Smart & Son Ltd*

5.1.3 Lennartz considered

The Wellcome Trust is a charity that carries on some business and some non-business activities. On 30 March 2009 it made a *Fleming* claim, seeking to recover VAT on certain buildings using the *Lennartz* mechanism – that is, allocating the whole of the cost of the buildings to the business and so recovering VAT at the time the cost is incurred, and then accounting for output tax on "non-business use" over the life of the building. It could only recover 3% of the VAT incurred on the building, so a 100% recovery followed by repayment would represent a substantial interest-free loan from HMRC.

The history of the *Lennartz* mechanism is a series of twists and turns. The case of *Seeling* in 2003 showed that tax authorities were not permitted to deem the self-supply to be exempt, so appearing to confirm that the initial recovery would be justified. HMRC introduced legislation in that year to try to close down this "loophole", but following the 2006 decision in *Charles and Charles-Tijmens*, they accepted that this legislation was ultra vires. However, in 2009 the CJEU in *VNLTO* restricted the application of *Lennartz*: it only applied where VAT deduction was justified in the first place on the basis of business use, and the intended self-supply charge could not be used in an effectively circular manner to justify the initial recovery. The "private use" subject to the output tax charge had to be separate from the purposes of the business – the "non-business" activities of many charities and similar organisations would not fall within that category. HMRC relied on *VNLTO* to deny the *Fleming* claim.

The taxpayer's counsel put forward two arguments: first, that *VNLTO* was narrow in scope, and its facts did not apply to Wellcome Trust, because the present case was about an enduring asset rather than the use of revenue items; and second, that the CJEU, in the case about Wellcome

Trust's share sale, had described it as "acting like a private investor", so it was within *Lennartz* even as restricted by *VNLTO*.

HMRC also argued that it was necessary for a trader to allocate costs to the business in order to claim the *Lennartz* mechanism, which Wellcome had not done – in effect, it was not possible to claim *Lennartz* in arrears. The taxpayer argued that its intentions were always clear, but at the time that it had purchased the building in question, HMRC did not accept that the approach could be used for buildings.

The judge agreed with HMRC's main contention, that Wellcome's investment activities did not constitute "private use". The *Wellcome Trust* decision concerned the borderline between economic and non-economic activity, and the expression had been used in that context. The property was entirely used for the purposes of the entity in the sense required by *VNLTO*.

Turning to the timing of the claim, the judge considered that accounting for output tax was an essential part of choosing to apply the *Lennartz* mechanism. There was evidence from a 2008 Tribunal case about an adjacent building that the finance director had considered and rejected the operation of *Lennartz* as posing too many practical difficulties. It appeared that the charity had considered the possibility and rejected it, rather than being prevented from adopting the method because of HMRC's policy.

The appeal was refused.

First-Tier Tribunal (TC04855): *Wellcome Trust Ltd*

5.2 Who receives the supply?

Nothing to report.

5.3 Partial exemption

5.3.1 Cars as capital assets

A car dealer made a Fleming claim for output tax accounted for on the sale of demonstrator vehicles at a time when input tax was blocked on their purchase (an "*Italian Republic*" claim). HMRC repaid £160,000. HMRC then decided that the repayment had been excessive, because it did not restrict input tax recovery on account of the exempt turnover from the demonstrator vehicles. The UK courts had decided that demonstrators were "capital assets" to be omitted from standard method calculations in the *JDL Ltd* case, but the CJEU judgment in *Nordania Finans* suggested that this was wrong where assets were a fundamental part of the everyday transactions of the trade. The clawback was £13,094 plus statutory interest of £25,245. The company appealed; the case was the lead appeal for a large number of other motor traders.

The company argued that the demonstrators were capital assets, and that *JDL* remained good law, binding on the Tribunal. HMRC argued that *Nordania* showed that JDL had been wrongly decided; they also argued that the cars in this case were materially different from those considered in *JDL.*

Judge Cannan considered a number of precedents concerning the meaning of the expression "capital goods". He was satisfied that HMRC were correct: the cars were bought with the intention of sale, and the fact that they were used for a short time in the business first did not change that. The mileage on them was kept low and monitored in order to maximise their sale value. They were not capital assets.

He did not consider that *JDL* was binding following *Nordania*; however, in case it was, he also considered that there was a material difference. Some of the cars in that case had been held for over a year, whereas all the cars in the present appeal were sold within 2 to 6 months.

The appeal was dismissed.

First-Tier Tribunal (TC04803): *Cleckheaton Holdings Ltd*

5.4 Cars

Nothing to report.

5.5 Business entertainment

Nothing to report.

5.6 Non-business use of supplies

Nothing to report.

5.7 Bad debt relief

Nothing to report.

5.8 Other input tax problems

5.8.1 Updated Notice

HMRC have updated their Notice *Local authorities and similar bodies*. It appears that the main change is a revised postal address for VAT refund claims by public bodies. It has also been rewritten to improve readability, but the technical content has not changed since the 2000 version.

Notice 749

5.8.2 Pre-registration VAT

A trader appealed against a decision to refuse certain amounts of pre-registration VAT in relation to services. In opening the appeal, the appellant's representative made it clear that the appeal was against a refusal to backdate the effective date of registration. HMRC's representative claimed that this had not been included in the grounds of appeal, and argued that the Tribunal should not consider it. However, the judge said that it was clear in the correspondence with the Tribunal, which might not have been passed to HMRC. He decided to consider the matter, giving both parties 30 days to make representations.

HMRC then decided to concede the point, which would decide the appeal in the taxpayer's favour. The judge decided to issue a full decision, on the basis that "HMRC's forms and their accompanying notes relating to registration for VAT do not seem to fully follow or correctly explain the law." He commented that as the VAT 1 form is prescribed by law, it is important that it should reflect the law.

The company had been formed to acquire a disused petrol station and bring it back into service. In the autumn of 2013 it submitted a VAT 1, requesting a registration date of 1 November 2013. Following correspondence, some of which went astray, a second form was submitted, with 1 March 2014 as the requested registration date. This was incomplete in some respects, so HMRC sent a follow-up letter. In the reply to this, the owner put in yet another date, 1 April, possibly by mistake.

The first VAT return was filed for the period to 07/14, claiming a substantial repayment. HMRC carried out checks, and disallowed VAT claimed on invoices for services dated 18 September 2013 and 27 September 2013.

The point on which the judge requested representations is in relation to VATA 1994 Sch.1 para.9, which states that a person who is not registered or required to be registered, but who makes taxable supplies or intends to do so, can request voluntary registration. The law states that the Commissioners "shall, if he so requests, register him with effect from the day on which the request is made or from such earlier date as may be agreed between them and him." This appears to allow a backdated registration, but not a later date. The judge read it as allowing a two-way choice only. The second (incomplete) VAT 1 was submitted on 20 February and received on 25 February: it appears that, as the trader did not request an earlier date, one of those two dates would have to be used.

The judge noted that the normal procedure – to allow an applicant to choose a later date – may be convenient both to HMRC and the taxpayer;

but, if it was important to a trader, it would be possible to rely on the strict legal position. If he had to be registered from 20 or 25 February, the pre-registration VAT became deductible.

The judge also commented that the questions put in response to the incomplete VAT 1 were unsatisfactory. They should not have asked again for the date on which the trader wished to be registered, when an answer had already been given to that question (even if it was a later date, which in the judge's view was not permitted under the law).

He also noted that further confusion arose about the question of whether the trader had applied for a backdated registration: "*We do not need to deal with the question of backdating the date of registration, save to say that it seems to us that the appellant did not make any request for registration to be backdated until after HMRC had give a ruling on the matter. This was because HMRC had interpreted a letter from the appellant relating to Ms Turnbull's refusal to allow the two invoices as a complaint (which it wasn't) and the Complaints Unit had then passed the letter to the office dealing with registration issues who issued the ruling on the assumption that the appellant had sought backdating (which at that time it hadn't).*"

The appeal was allowed, on the basis that the two invoices were within six months of the correct date of registration, which ought to have been 20 or 25 February.

First-Tier Tribunal (TC04929): *Lepton Service Station Ltd*

In an article in *Taxation*, Richard Staunton considers the latest news on pre-registration VAT on fixed assets. He was running a case that he hoped would be a test of HMRC's policy, but they pulled out at a late stage. He provides evidence that HMRC's view (that expenditure on fixed assets should be depreciated for the purposes of a reg.111 claim) does represent a change of policy, and should therefore be subject to different procedures from those that HMRC are currently applying (i.e. stating that "this has always been our policy and people have misunderstood it").

Taxation, 10 March 2016

5.8.3 Refunds to museums and galleries etc.

As announced in advance, and following a consultation, The Value Added Tax (Refund of Tax to Museums and Galleries) (Amendment) Order 2016 came into force on 1 April 2016 to add three new bodies, and four new sites connected with existing bodies, to the list of museums and galleries entitled to claim refunds of VAT they incur in providing free admission to their collections. The three new bodies are the LSE, University of Essex and Teesside University, which have museums and galleries allowing free access to their collections.

SI 2016/235

The Old Oak and Park Royal Development Corporation has been specified as a government body entitled to recover input tax under VATA 1994 s.33 on non-business supplies with effect from 1 April 2016.

SI 2016/307

With effect from 16 March 2016, the VAT refund scheme for museums and galleries, contained in s.33A VATA 1994, is to be extended to any museum or gallery that:

- is open to the general public for at least 30 hours per week, without exception;
- offers free entry, without prior appointment;
- holds collections in a purpose-built building;
- displays details of free entry and opening hours on the museum website

Museums and galleries must apply to the relevant body, i.e.:

- the Department for Culture, Media and Sport;
- the Welsh Assembly Government;
- the Northern Ireland Assembly;
- the Scottish Government;
- the Ministry of Defence;

and must support their application with a specific business case.

www.gov.uk/government/publications/vat-refunds-for-museums-and-galleries; Red Book 2.151

As previously announced, with effect from Royal Assent to the Finance Bill 2016, a new s.33E VATA 1994 will provide that the Treasury may add to the list of "specified bodies" for the purposes of VAT recovery in respect of non-business activities. This is intended to prevent VAT from being a disincentive to cost-sharing arrangements between such bodies.

OOTLAR Budget 2016; Red Book 2.152

5.8.4 Alternative evidence

HMRC assessed a construction company to deny input tax credit claimed in respect of invoices raised by a supplier that had been retrospectively deregistered. The invoices were dated between 2 October 2012 and 29 January 2013; the deregistration was ordered by HMRC on 12 March 2013 to take effect from 1 October 2012. The total was for supplies of £108,066 plus VAT of £21,613.

In correspondence with the company's accountants, HMRC asked for various items of alternative evidence in relation to the expenses. The company provided some, but not all. Further information was requested, including names, addresses, national insurance numbers of subcontract labourers provided by the subcontractor, and the sites on which the individuals were engaged and the supply being made e.g. labourer, bricklayer, carpenter etc. The accountants replied that the company had never held this information and was not required to do so.

At the hearing, the company's accountant argued that the invoices issued by the subcontractor before and after 1 October 2012 were identical. Those before were accepted by HMRC, those after were not. It was impossible for the client to know the difference.

HMRC originally stated that the invoices were invalid both because of the retrospective deregistration and their failure to comply with reg.14. Before the hearing, they withdrew the first ground, following the CJEU judgment in *Mecsek-Gabona* (Case C-273/11) – if a customer did not and could not be expected to know that a supplier would be deregistered, the authorities could not deny deduction on the basis of a retrospective deregistration.

The main deficiency in the invoices was a failure to describe the supplies sufficiently to satisfy reg.14(1)(g). They referred to "labour and trade supplied at the following sites: various sites". The company had either not received or not retained supporting timesheets to back up the invoices, and HMRC considered that there was therefore insufficient information to be sure that the supplies had actually taken place. The Tribunal agreed that the invoices did not satisfy the regulation in this respect.

As regards the reasonableness of HMRC's refusal to accept alternative evidence, the judge noted that very little information was provided to HMRC about the construction project involving the subcontractor. Nothing was provided in response to the request about the sites at which the services were supplied, nor about the nature of those services.

HMRC had not asked all of the questions in their own statement of practice (VAT Strategy: Input Tax Deduction without a valid VAT invoice, March 2007). The judge considered whether the failure to follow their own published procedures rendered the decision unreasonable, and was satisfied that it did not. The previous acceptance of similar invoices was not a relevant matter that should have affected HMRC's decision in relation to the later invoices.

The appeal was dismissed.

First-Tier Tribunal (TC04935): *Gradon Construction Ltd*

5.8.5 Missing traders

Two companies were denied input tax of £2.2m each in relation to purchases of razor blades in April and May 2006. The companies were established traders which dealt in a range of household goods, so the transactions were not in themselves unusual. However, there were factors that were suspicious, including the size of the deals and the fact that the companies had been approached by unsolicited customers wanting large quantities of the same product at the same time. The companies had been involved in other deals in the previous year which had resulted in follow-up visits and warnings from HMRC, and as a result they had asked the customers for declarations that they were not involved in MTIC fraud.

The company's counsel put forward over 60 pages of detailed submissions to the FTT, summarised in the following questions:

(1) what could/should the Appellants have done differently?

(2) What would additional/alternative actions have revealed?

(3) Why would such additional/alternative steps have caused the Appellants to realise that the only reasonable explanation for the transactions was fraud?

(4) How were HMRC's allegations sustainable when all the "indices" of fraud which HMRC pointed could just as easily be characterised as the usual incidences of international trade?

The First-Tier Tribunal (TC01752) discussed the meaning of the "only reasonable explanation" test and gave detailed reasons for finding that the traders ought to have known that their transactions were connected with fraud. Among these was the fact that the deals involved 159% of the global sales of the razor blades for the month concerned – it was surely impossible that these were normal commercial transactions. The razor blades were sold to a Spanish customer but shipped on its instructions to a French company which was registered as "Wholesalers of wood, construction materials and sanitary equipment". Given that the company was on notice that it might be involved in MTIC fraud, the Tribunal concluded that these and other factors should have alerted it to the extreme risk it was taking.

The company appealed to the Upper Tribunal, where its representative launched an "extensive attack" on the FTT's conclusions. Although he subdivided his objections into three sections, the third of which had nine subsections, the judge summarised his argument as "*that the Tribunal had erred in law by going beyond HMRC's pleaded case and arriving at findings of fact and a conclusion on the facts that were not supported by the evidence that HMRC had adduced in support of its case.*"

The judge examined the basis for the FTT's decision, and allowed the company's appeal. In his view, the Tribunal had not been entitled to come to the conclusion that "the only reasonable explanation" was fraud on the basis of the facts that it had found. It seemed that one of the most important factors for the FTT was the high volume of razor blades involved; however, it had been accepted that the razor blades actually existed, and the quantity had not been exaggerated by circulating them in a "carousel". The company routinely dealt in high volumes of various goods in the "grey market" for consumer items, and this was within the normal bounds of its trade. The appellant had reasonable explanations for the various features that HMRC argued were unusual, and the FTT should not therefore have concluded that the only possible explanation was fraud.

HMRC appealed to the Court of Appeal, which overturned the UT's decision and restored that of the FTT. HMRC argued that the UT had failed, unlike the FTT, to stand back and look at the cumulative effect of the evidence; had failed to take into account the traders' prior knowledge of the characteristics associated with MTIC fraud; and had been wrong to conclude that there was no evidence to suggest that these were other than normal market transactions.

The Court agreed with these propositions. The "no other reasonable explanation" test was satisfied if a reasonable person, mindful of all the circumstances, ought to have concluded that the transactions were connected with fraud. Even though HMRC had not alleged fraud against the immediate counterparties of the appellants' transactions, the standard still applied (the fraud was further up the supply chain). The UT had also not given weight to the fact that HMRC had warned the taxpayers about the risks of MTIC fraud. That had to be relevant to the consideration of what a reasonable person would have concluded, and failing to take it into account was an error of law.

The UT's finding that the transactions were in the ordinary course of business was also flawed. That had to be considered in general (ordinary for a theoretical grey market trader) and in particular (ordinary for this trader). The trader normally only dealt with authorised dealers, but in this case the supplier was not authorised. The terms of credit were unusual. In the circumstances, the burden of proof had moved to the taxpayers to show that the transactions were normal, and they had not adduced any evidence to show this. The "ordinary course of business" defence therefore had to fail.

HMRC's appeal was allowed.

Court of Appeal: *Davis & Dann Ltd and another v HMRC*

A MTIC appeal concerned an assessment to claw back £1.625m repaid by HMRC for the 02/06 period, and a decision to refuse repayment of £1.819m for the 05/06 period. The Tribunal described the facts as "relatively simple", but considered it still difficult to judge the state of mind, intentions and level of knowledge of the director.

The Tribunal examined a number of assertions put forward by the director to justify his method of trading. These were hopelessly confused, and often were "the wrong way round" (i.e. identifying something as indicating honest deals when it was indicative of fraud, and vice versa). It was hard to tell "whether in the years since 2006 Mr. Jafar had woven together a web of nonsense and even eventually persuaded himself that some of his thoughts were valid, or whether he was just hopelessly confused and out of his depth, or finally whether he was delivering a quite convincing sounding picture of theories that he knew perfectly well were largely incoherent." If he genuinely believed these theories, that might be relevant to the Tribunal's conclusions.

The Tribunal had no hesitation in concluding from the manner of transactions that the trader had the means of knowledge of connection to fraud. The Tribunal also concluded that the director knew that he was following a series of pre-ordained and instructed steps; however, it was possible that he was confused, and found himself swept into participating in transactions that he did not fully understand. Even so, the Tribunal was satisfied that by the 02/06 and 05/06 periods, he must have been aware of the fraudulent nature of the trading.

Both limbs of the *Kittel* test were therefore satisfied, and the appeal was dismissed.

First-Tier Tribunal (TC04839): *GSM Inter Trade Ltd*

A company appealed against the refusal of credit for £330,000 in total for the periods 07/06 and 08/06. The Tribunal noted that the appeal was relatively unusual in that it appeared that the trader had actually purchased mobile phones and sold them on under his own control; they were not part of a pre-ordained or circular chain of dealing. However, they had been traced to a supplier further up the chain who had not accounted to HMRC for output tax charged.

The Tribunal decided that the trader had carried out poor due diligence, but was still entitled to believe that transactions with suppliers he had visited and had prior dealings with were genuine. HMRC had not provided convincing evidence that he knew, or ought to have known, that

these transactions were connected with fraud. His appeal was therefore allowed in respect to a number of deals. Transactions with a new supplier were different – he knew about the risks of MTIC fraud, and should have carried out far more due diligence. With regard to this supplier, therefore, he "had the means of knowledge".

The appeal was allowed in part.

First-Tier Tribunal (TC04770): *Electrade 247 Ltd*

A company appealed against a refusal of input tax of £758,000 for its period 07/06. There was a preliminary issue: the appellant argued that HMRC had never issued a formal assessment, and were therefore unable to collect any money. The Tribunal would have no jurisdiction to consider the matter, and should strike the case out. The judge examined a number of precedents, and was satisfied that the Tribunal did have jurisdiction over whether an assessment existed, and that HMRC's actions in this case constituted the making of one.

From that point, the appeal followed the usual course: an exhaustive examination of deals and explanations for deals, and the eventual conclusion that there was no other reasonable explanation for the transactions apart from their connection to fraud. The appeal was dismissed.

First-Tier Tribunal (TC04888): *Aria Technology Ltd*

A company appealed against a refusal of credit of £1.749m for its 05/06 period. An application for adjournment a few days before the hearing was refused, and refused again at the beginning of the hearing. The appeal proceeded with very little input from the appellant. The appellant had lost two previous MTIC appeals under a previous name (Balmoral Ltd) and had not paid the debts of some £2m plus interest. The director and owner had no assets and survived on benefits. He claimed that he had found possible sources of funding for the present appeal, and wanted the adjournment to secure representation. The Tribunal considered that the individual had not cooperated or made any effort to pursue the appeal for many years, and rejected the application to adjourn.

The burden of proof rested with HMRC. In spite of the lack of appellant's representation or defence, the Tribunal assured the director that it would consider all the evidence to decide whether HMRC had discharged that burden. The judge commented that this was in effect hearing the appeal in the absence of the appellant, and considered whether it was appropriate to do so in that context.

The Tribunal then examined the evidence in detail, considering not only HMRC's arguments but those that might have been advanced by the appellant, had he been willing to participate. It concluded that it was more likely than not that he had full knowledge of the fraud; it considered the evidence overwhelming that he was aware of the risks of dealing in mobile phones, having been warned repeatedly by HMRC (warnings he had ignored), and therefore "had the means of knowledge". The appeal was dismissed.

First-Tier Tribunal (TC04946): *Walmley Ash Ltd*

A company appealed against the refusal of credit amounting to £966,000 for its 03/06 period. It had been trading in mobile phones and other goods for a number of years, and had had previous run-ins with HMRC over claims that were alleged to be fraudulent. It was therefore clear that the director would have been well aware of the risks.

Once again, the history and the particular deals were examined, and the usual conclusion was reached: the director at the very least ought to have known of the connection to fraud, and very probably did know. The appeal was dismissed.

First-Tier Tribunal (TC04945): *Grade One Trading Ltd*

Two companies appealed against decisions to deny credit for £7.96m and £5.5m for periods 03/06, 04/06 and 05/06. The companies shared a director, who gave evidence on their behalf. This was a contra-trading case, involving 30 deals by one company and 22 by the other.

The Tribunal considered the following factors to be highly relevant in assessing the director's means of knowledge:

(1) the small number of counterparties,

(2) the profit margins,

(3) the lack of legal certainty of ownership,

(4) a lack of concern for physical location, state or identity of goods,

(5) a lack of valid insurance,

(6) the back to back trading pattern.

Each of these factors was discussed in detail in the context of the evidence. The director was experienced in the sector; the Tribunal concluded that someone in her position must have known that aspects of the deals could only mean that they were connected with fraud. The appeal was dismissed.

First-Tier Tribunal (TC04938): *Abbott International Trading Ltd and another*

The Upper Tribunal considered a point of principle in relation to two appeals before the FTT (TC04026 and TC04156). The appellants argued that an allegation of involvement in MTIC fraud constituted an allegation of dishonesty or wrongdoing, which if it is to be made must be pleaded with sufficient particularity and in accordance with the pleading rules of civil fraud litigation. HMRC contended that no such allegation of dishonesty was involved: the *Kittel* principle was well-established, and only involved an assertion that the appellant knew or ought to have known that its transactions were connected with fraud.

E Buyer is a large established online retailer which undertook 289 transactions during the period 06/10 to 09/11 that HMRC traced to VAT losses. According to HMRC, these involved both "standard" MTIC frauds and contra-trading. The FTT judge had rejected the company's request for a direction requiring further and better particulars of HMRC's pleaded case.

Citibank was assessed in relation to certain transactions in emissions allowances in 09/09. A similar application for further and better particulars was made, and Judge Mosedale in the FTT agreed with the taxpayer that HMRC's statement of case was seriously flawed. The Upper Tribunal was therefore considering one case as an appeal by HMRC, and the other as an appeal by the taxpayer.

The Upper Tribunal considered the history of case law relating to what might broadly be termed "wrongful" deduction of input tax – ranging from avoidance schemes such as that in *Halifax*, through *Optigen* to *Kittel*. None of these cases refer to "dishonesty". Given that *Kittel* covers those who did not know but should have done, that appeared to be wider than dishonesty as normally understood.

The question was whether a different standard would apply to a case brought by HMRC under the "first limb" of *Kittel* ("actually knew" rather than "should have known"). After considering the UK precedents on MTIC fraud at some length, the UT applied the principles to Judge Mosedale's decision in *Citibank*. Although HMRC's statement of case did not use the word "dishonesty", and appeared only to reflect the CJEU's composite "knew or ought to have known" formulation from *Kittel*, it was nevertheless clear that the case alleged that the appellant knew that its transactions formed part of a contrived scheme designed to defraud HMRC. That was equivalent to an allegation of dishonesty: Judge Mosedale was justified in requiring HMRC either to allege it explicitly or disclaim it explicitly, and HMRC's appeal against her decision was dismissed.

E Buyer's appeal was on two points: a request for disclosure according to the standard in civil fraud cases, where the prosecuting authority would have to disclose not only the evidence on which it sought to rely, but also anything else it had discovered in its enquiries that might undermine its case; and also further and better particulars of its case. The UT set aside the FTT's decision, and ordered that the disclosure application should be granted. It remitted the matter back to the FTT for reconsideration of the "further and better particulars" point in the light of the UT's findings.

Upper Tribunal: *E Buyer UK Ltd v HMRC; HMRC v Citibank NA*

5.8.6 Racehorses

HMRC have updated their Notice *Registration scheme for racehorse owners*. The steps involved in registering as a racehorse owner (section 2) have been amended, as well as "putting things right" and "how HMRC uses your information".

Notice 700/67

6. ADMINISTRATION AND PENALTIES

6.1 Group registration

6.1.1 Review of grouping

HMRC have issued a Brief announcing a consultation on proposals for changing the UK grouping rules following the *Larentia*, *Marenave* and *Skandia* decisions.

The government will take account of the CJEU judgment in *Larentia* and *Marenave*, which held that restricting grouping to "legal persons" (i.e. companies, as in the UK law) was only permitted under the Directive if those restrictions are appropriate and necessary in order to prevent, abuse, avoidance or evasion. The government therefore expects to extend VAT grouping to non-corporate bodies, and to identify new rules to determine the "close economic, financial and organisational links" that would be required, to replace the existing control test which is based on the company law definition of a subsidiary.

The consultation will start with meetings between HMRC and business representatives during January and February 2016 to explore and develop new ideas on grouping. The feedback from these meetings will be used to develop policy options, which will be the subject of the formal 12-week consultation during spring 2016. The results will be published in summer/autumn 2016, and presumably the changes will be included in Finance Bill 2017.

Revenue & Customs Brief 3/2016

6.2 Other registration rules

6.2.1 No exception in arrears

A doctor provided exempt medical services through a private practice, but also taxable supplies of medical legal reports as an expert witness. For 18 years from 1995, his taxable turnover was below the registration threshold. In October 2013, turnover for the preceding 12 months was £83,270, £4,270 over the threshold at the time.

Accounts were prepared for the 2012/13 tax year in January 2014, whereupon the problem was noticed (even though it would have been several months after the end of the period the accountants were directly concerned with). The doctor wrote to HMRC on 6 March 2014 to notify them that the threshold had been exceeded, and asked them to allow exception from registration on the basis that the projected turnover in the 12 months from 1 December 2013 would be about £65,000 (he planned to retire in August 2014).

HMRC stated that they would normally allow exception, but had concluded that his future turnover would only be below the threshold because he did not intend to trade for the full 12 months. After some correspondence about this point, they withdrew it as the reason, because that provision only applied to traders who were actually registered and wished to deregister.

Instead, they advanced the usual argument that they would have had to have been satisfied at the time that the doctor should have been registered; as he had not asked for exception at the right time, he could not qualify. There was further correspondence about what had actually happened after December 2013 – for a number of months, the cumulative turnover continued to be above the "backward look" threshold, but the total for the 12 months from December 2013 was indeed below the deregistration threshold. The Tribunal agreed with HMRC that this was irrelevant: the only information that HMRC could take into account was the information that had been available in October 2013. It was reasonable for HMRC to consider that a detailed forecast would have been required, given that the margin between the forecast turnover and the threshold was narrow. The decision to refuse exception was therefore also reasonable, and the appeal was dismissed.

First-Tier Tribunal (TC04815): *Geoffrey Lane*

6.2.2 Misdirection and registration

HMRC have published a Brief as a "reminder that the VAT misdirection class concession no longer exists". It also gives notice that HMRC will no longer routinely consider requests not to pursue the tax due, with effect from 1 August 2016.

Business Brief 28/04 explained Customs & Excise policy in relation to correction of errors where there had been a change of departmental policy about the liability of a supply. It referred to the "misdirection class concession". The Brief stated that where a business chose to register for VAT belatedly in respect of supplies that had previously been treated as exempt but should have been treated as taxable, Customs would not pursue tax under the misdirection class concession to the extent that it had not been passed on to the customers (net of input tax).

BB 28/04 item 2 was withdrawn by BB 24/11 with effect from 1 August 2011. HMRC still receive regular requests from traders who are registering late in which they specifically request HMRC not to pursue net tax due on supplies where VAT has not been passed on to customers.

HMRC say that they will no longer "routinely consider" such requests from 1 August 2016 onwards. Presumably it was always possible for them to consider and refuse, but now they will apparently not even bother to consider. Up to 31 July 2016, HMRC will only consider requests that include complete and accurate calculations of both output tax not charged on and the associated input tax and where the VAT return (covering all supplies whether or not VAT has been charged on) has been submitted. Claims should be sent to the "liable no longer liable team" in Grimsby.

R&C Brief 07/2016

6.2.3 Thresholds

The Budget included the usual announcement of increases to the registration and deregistration thresholds, which change from £82,000 and £80,000 to £83,000 and £81,000 with effect from 1 April 2016.

SI 2016/365

6.3 Payments and returns

6.3.1 Flat rate scheme

A trader operated the flat rate scheme from registration on 3 June 2009. On its registration application it described its trade as "consultant for advertising industry". However, it also described its business as "management consultancy activities (other than financial management)". In July 2009 its accountants applied for the FRS, and described the main business as "management consulting". The trader accounted for FRS VAT at 11% from the outset, the rate at the time for management consultancy, but failed to implement increases in 2010 and 2011 (to 12.5% and 14%). HMRC picked this up on an assurance visit in 2014 and issued an assessment for £18,060.

The trader appealed, arguing that it should have used the rates for advertising throughout (8.5%, 10% and 11%). It was therefore correct (by coincidence) in the periods since 2011, and had overpaid in 2009 and 2010. HMRC refused to allow "a retrospective change of category".

It seemed that the coincidental identity of the current rate for advertising with the 2009 rate for management consultancy had confused the trader and the accountants. They had failed to realise that they had applied for the FRS giving the wrong information, and therefore started their appeal on the wrong basis. By the time of the hearing, they had changed their grounds of appeal to argue that they had made a mistake on the original application. HMRC argued that the trader had intentionally selected the business category in 2009, and had correctly applied the appropriate percentage. It could not now change that.

The Tribunal noted that HMRC's representative suggested that it could only allow the appeal if it considered the HMRC decision to be unreasonable (s.84(4ZA)). It was not convinced that this was correct: HMRC did not appear to have a power to choose the trader's appropriate percentage. In any case, the Tribunal was satisfied that either on a full or a limited jurisdiction, the appeal had to be allowed. There was no doubt that the trader was involved in advertising, not in management consultancy. The officer raising the assessment had failed to take the actual nature of the trade into account, and had only focused on the description on the FRS application form.

The decision to refuse a retrospective change was also unreasonable. This was not such a change: it was the correction of a mistake. This would in theory give the trader the right to a repayment of tax for 2009 and 2010, but these years would be out of time.

The appeal was allowed.

First-Tier Tribunal (TC04808): *KDT Management Ltd*

A trader appealed against a refusal to admit him to the FRS with retrospective effect. He applied on 6 May 2014, but argued that he should be admitted with effect from 1 July 2012, when he first registered. That would lead to an overpayment of some £7,500; he applied at the same time for deferral of his VAT liability for the 02/14 period, which he was unable to pay because of cash flow difficulties, and clearly hoped that it could be cancelled because it was roughly the same amount as the "overpayment".

The appellant was a solicitor. His grounds of appeal were that "*The justification by HMRC of its decision not to agree to such a request is, it would seem, based on what I believe to be a quite misplaced decision that FRS may only be used 'to simplify your VAT'.*" This view was expanded over several paragraphs. The Tribunal rejected this analysis. Previous cases had considered and supported HMRC's view. Retrospection would only be considered in "exceptional circumstances", including possibly compassionate cases. No such circumstances had been put forward to HMRC in this case. HMRC appeared to have taken into account all the relevant factors, and no irrelevant factors, in refusing the appellant's request for retrospection. Their decision could not be said to be unreasonable.

The appeal was dismissed.

First-Tier Tribunal (TC04827): *Julian Anthony Goodman*

6.3.2 Article

In an article in *Taxation*, Neil Warren considers a number of cases in which HMRC have failed in an attempt to impose a FRS category on a taxpayer, and suggests that "enough is enough" – there should be a proper review of their policy in this area, and HMRC officers should be made to understand that their internal guidance is not the law.

Taxation, 3 March 2016

6.3.3 Payment by credit card

With effect from 1 April 2016, HMRC will no longer charge a single fee in relation to payments made by credit card, but will charge differing fees depending on whether the credit card is a personal or corporate credit card and the type of card used. The *Fees for Payment of Taxes, etc by Credit Card Regulations 2016* specify certain cards and the applicable rates.

SI 2016/333

6.4 Repayment claims

6.4.1 Substitute claim

HMRC have won two cases on "what constitutes a claim" for the purposes of applying the four-year time limit in s.80 VATA 1994. In both, the FTT had found in whole or part for the taxpayer, so the UT's decisions provide some reassurance to HMRC that their approach to this question is correct.

The *Vodafone* case concerned the extent to which a claim, validly made within the time limit, can be amended by the taxpayer to cover other matters. Judge Mosedale (TC03822) gave a decision in a preliminary hearing to consider the following question of principle:

In circumstances where the Appellant has submitted a claim for a sum of money in a VAT period, in accordance with the time limits set out in s.80 VATA 1994, (the "Claim"); can the Appellant maintain the quantum of the Claim, but vary the methodology by which the Claim is calculated (for

example by substituting a different reason for claiming an identical or lower amount) after the expiry of the time limits set out in s.80 but while the Claim remains unresolved?

The company had made a claim in January 2007 for a repayment of £4.17m of overpaid output tax from 01/04 to 01/06. It considered that this represented an overpayment when its participation in the Nectar loyalty points scheme was properly accounted for: at that time, it believed that it should have reduced its output tax in respect of the "value" of Nectar points awarded to customers when they were issued.

HMRC ruled that this was incorrect and refused the claim. That matter remains unresolved. However, it had been agreed that there were several other matters which did give rise to overpayments of output tax in the same period, including:

(1) non-EU line rental;

(2) non-EU SMS second leg;

(3) free minutes credited to customers;

(4) non-activated pre-paid top-ups;

(5) free top-ups.

The company made voluntary disclosures in respect of these issues in 2009 to 2011; as regards the periods in dispute, these claims were rejected because they were out of time.

HMRC were also in dispute with the company about the liability for sales of phonecards in Ireland in the periods 10/03 to 04/04. It raised an assessment, which was reduced by £1.1m in respect of the periods that overlapped the voluntary disclosure periods where a reclaim had been rejected – it seems that HMRC were willing to offset overpayments against underpayments, but not to make a repayment.

The net amount overpaid on the agreed matters (but refused as out of time) was considerably larger than the amount refused in respect of Nectar points.

The company argued that it had made an in-time voluntary disclosure in relation to certain periods totalling £4.17m. HMRC had accepted that it had overpaid that much output tax in those periods – indeed, that it had overpaid a great deal more – and should therefore repay it. The company would then not argue further about the proper treatment of Nectar points, and could not make any further claim in respect of the excess overpayments, because of the time limits. However, HMRC argued that they should not have to pay a voluntary disclosure that was made for the wrong reason.

S.80 requires that a "claim" shall be in such form as HMRC may prescribe by regulations. Reg.37 SI 1995/2518 states:

Any claim under s.80 shall be made in writing to the Commissioners and shall, by reference to such documentary evidence as is in the possession of the claimant, state the amount of the claim and the method by which that amount was calculated.

The company argued that a "claim" relates to the sum of money stated in it. As long as the claim is unresolved, it should be open to the company to

put forward any sustainable basis for the claim. Once an overpayment has been proved, it should be paid.

HMRC countered by arguing that the reason for a claim is fundamental to the claim. The substitution of new reasons constitutes the making of a new claim. If a claim is "amended", it must arise out of the same subject matter as the original claim, without extension to facts or circumstances that fall outside of the contemplation of the earlier claim.

Judge Mosedale agreed with the taxpayer that HMRC's interpretation required her to read into s.80 words that were not there. However, she needed also to consider whether allowing the company's interpretation was in accordance with the purpose of the legislation. She accepted HMRC's point that there might be a temptation to make spurious global s.80 claims just in case it subsequently turned out that there was an overpayment – however, this could be prevented by HMRC refusing the claim, which refusal would become final unless the company appealed (suffering the risk of strike-out and an award of costs for unreasonable behaviour). The judge did not accept that "the reasons" were fundamental to a claim made in accordance with s.80 and reg.37.

HMRC also relied on the Upper Tribunal's decision in *Reed Employment*. The judge agreed with the appellant's interpretation: Reed allowed a claim to be increased by amendment if it arose from exactly the same reasons and periods as the original claim, but denied an increase in amount if it arose from different reasons or periods. It had no relevance to a situation in which the taxpayer chose to sustain the same amount of an existing claim, without adding to it, by substituting different reasons.

After considering two other precedent cases (*Masterlease* and *BUPA*), the judge concluded that the preliminary issue should be decided in favour of the appellant. To do otherwise would allow HMRC an unjustified windfall.

She did not need then to go on to the taxpayer's third ground of appeal, which was the principle of equivalence, but she did so for completeness. The taxpayer argued that HMRC could substitute new reasons for an assessment, and the same should be allowed to taxpayers and claims. In *BUPA*, HMRC said that they would not do so; the judge commented that it would be hard for HMRC to resile from a concession of this sort made in the Court of Appeal and commented on by a CA judge. Judge Mosedale did not consider that the principle of equivalence assisted the taxpayer. However, as she had already found that the UK law was enough to sustain the appeal, that did not matter.

Upper Tribunal

HMRC appealed to the Upper Tribunal (Warren J and Judge Bishopp). HMRC accepted that the reasons for a claim could be amended to some extent after the claim had been made, but argued that the amended claim remained the same claim as that originally made only if it is supported by what is materially the same calculation and reasons: in other words, the underlying facts must be essentially the same. To allow a complete change of reasons offended against the principle of legal certainty.

The judges agreed with HMRC. The requirement in s.80 was to make a claim for an amount of tax that had been accounted for that was not due: that could not be viewed in the abstract, but related to the specific matters

on which the trader considered too much tax had been accounted for. In reg.37, there was a requirement to state the amount and the method by which it had been calculated: it would be surprising if the first was an absolute requirement, and the second could be changed at will. The overall conclusion was "essentially that reached by Roth J in *Reed Employment*. A claim must satisfy the mandatory requirements of writing, amount and method of calculation. The latter two identify its character – how much is claimed, and how that amount was determined. Errors and omissions may be corrected provided the correction does not enlarge the scope of the claim by adding elements not in contemplation when the claim was originally made."

The judges agreed with HMRC that what the company was trying to do was to abandon one claim and substitute a different one. This could not be done outside the time limit. This did not, as Judge Mosedale had stated, result in an unjustified windfall for HMRC; rather, it was simply the logical effect of the time limit.

HMRC's appeal against the FTT's preliminary decision was allowed. The case was remitted to the FTT to consider the validity of the Nectar claim itself, which will now be the only way to justify a repayment.

Upper Tribunal: *HMRC v Vodafone Group Services Ltd*

6.4.2 Validity of claim

A similar issue was considered in a case involving a vehicle rental and self-drive car hire company which argued that it made a *Fleming* claim in respect of the *Italian Republic* and *Elida Gibbs* issues on 30 March 2009. As with *Vodafone*, the FTT (TC03799) found in favour of the company, but the UT has allowed HMRC's appeal.

HMRC argued that the letter sent on the company's behalf by its solicitors did not meet the statutory requirements for a "claim" to have been made. The question put to the FTT was "whether the claims... are valid claims..."; Judge Berner pointed out that the validity of the claims was not the point at issue, but rather whether "what has been done amounts to a claim at all for the purposes of the relevant statutory provisions."

The solicitors' letter set out some details of the way in which a repayment would be calculated, but pointed out that the companies had been in administrative receivership, so much of the detailed information was not available. Accounts for the relevant years were being obtained from Companies House.

Judge Berner adopted a similar approach to Judge Mosedale: he examined the precedents and the statutory words, and concluded that the requirements of reg.37 were not as stringent as HMRC believed. In particular, HMRC's view appeared to be that a "claim" had to contain enough information for HMRC to be able to determine whether or not to accede to it; it was clearly the case that further enquiry and correspondence would normally follow the making of a claim, so that could not be right.

The judge set out his view of the requirements as follows:

(1) For there to be a "claim" it must constitute a demand for repayment of overpaid VAT.

(2) The requirements of reg.37 of the VAT Regulations are mandatory, in the sense that, even if there is a demand for repayment, such a demand that does not comply with reg.37 will not be a claim for the purpose of s.80 VATA.

(3) The requirements of reg.37 are, on the other hand, exhaustive. It is not a requirement that the claim must set out the prescribed accounting period or periods for which the claim is made. That is part of the enquiry as to whether HMRC are liable to credit or repay overpaid VAT, but is not a requirement in order that a claim may be made.

(4) Similarly, it is not a requirement that the claim must be such as to enable HMRC to determine the issue of overpayment, or that the claim should contain sufficient information as to enable a reasonably competent VAT officer to understand the way in which the amount claimed had been calculated. (That is likely to be the case in practice in most instances, but it is not a relevant test.)

(5) It is not sufficient to refer to a prospective claim, with a promise that details will be sent in due course. However, if the demand does constitute a claim within reg.37, the fact that such a claim does not include the full figures, or has been made at a time when the claimant has not gathered all the information required, but where further details are to be provided as soon as possible, will not prevent that demand from being a claim for s.80 purposes. The question then will be whether the provision of the further information relates to the same subject matter as the original claim, without extension to facts and circumstances outside the contemplation of the original claim, and is therefore an amendment of the original claim and not a new and separate claim.

His third conclusion meant that it was not possible to read in extra words that were not already in the regulation. On that basis, the *Elida Gibbs* claim made by the first appellant satisfied the law: it stated the amount (£1.29375m); it explained how that had been calculated; and it referred to the accounts of the company that would support the calculation. HMRC's only criticism of the letter was that it did not refer to prescribed accounting periods, but the judge did not agree that such a reference was a legal requirement.

The letter referred to an intention to make an *Italian Republic* claim, but did not give a figure. That did not satisfy the law, and any such claim made later would be a new claim and would be outside the *Fleming* time limit.

On the other hand, the *Elida Gibbs* claim could be extended by amendment to other years. The amount stated referred to one year, and the letter explained that the claim related to all the years from 1973 to April 2007, with details to be provided when the accounts had been retrieved from Companies House. Those further details would constitute amendments to an in-time claim, rather than new claims.

The second claimant had not stated any figure, and could therefore not satisfy reg.37. The appellant's representative had argued that it made no sense to refuse the claim simply because it did not contain a figure – if that was the case, it would be possible to enter a number arrived at by pure guesswork and so validate the claim. The judge disagreed: such a figure would not be "calculated", so it would not satisfy reg.37 either.

The preliminary issue was therefore found for the taxpayer in respect of one of the claims for one of the companies, but dismissed in respect of the other matters.

Upper Tribunal

Both parties appealed. The Upper Tribunal (Warren J and Judge Bishopp) agreed with the FTT that reg.37 was the "form and manner prescribed" for the purposes of s.80(6) VATA 1994: a claim could only be treated as such if the mandatory requirements of the regulation were met. The *Italian Republic* claims therefore failed for the same reason that the FTT had given.

With regard to the claim that the FTT had considered compliant with reg.37, the UT observed that the letter from the solicitors had not attempted to apportion the amount claimed for the year 1989 between the several accounting periods in that year. Although there is no reference to claims being made for accounting periods in reg.37, it is implicit in the wording of s.80(1). The judges considered that there were good reasons for the requirement to apportion a claim between periods: it would affect interest calculations, and could be relevant to determining whether time limits had been observed. The solicitors' letter therefore did not meet the statutory requirements. The UT therefore did not accept that a claim had been made in time, so it also could not be amended.

HMRC's appeal was allowed, and the companies' appeals were dismissed.

Upper Tribunal: *HMRC v Bratt Auto Contracts Ltd and another*

6.4.3 CT on VAT repayments

Early in 2012, the First Tier Tribunal rejected appeals by four companies which were each representative member of a group of retailers which had received large VAT repayments (£125m) together with statutory interest (£175m) under s.78 VATA 1994. The companies had all treated the receipts as outside the scope of corporation tax, and HMRC had raised assessments on the repayments as trading receipts and the interest as a "credit on a loan relationship".

The case was made more complicated by the fact that these included *Marks & Spencer* claims, and in the period between the original VAT payment and the repayment, some of the companies had been transferred from one group to another; all the trades that had given rise to the overpayments had been discontinued, and the claimant company was now dormant. The FTT therefore had to consider the mechanism by which groups account for VAT between themselves, and the consequences of transferring a member of a VAT group to another holding company. The FTT concluded that intra-group payments in respect of VAT recognised an obligation that existed within the group, even if that obligation was disregarded for the purposes of the VAT return.

The FTT rejected the argument that the accounting treatment was determinative of whether a receipt was a trading receipt or not. The fact that the VAT repayments had been credited to the companies' P&L accounts was suggestive but not conclusive. Once it had been determined whether they were trading receipts, the timing of any charge to CT would follow the accounting treatment.

The appellants' arguments on this issue were summarised as follows:

(1) Where there is a statutory right to a sum of money and money is received pursuant to that right, the source of the money is the statute and not something else.

(2) Whilst it is accepted that some receipts of a trader which are not directly derived from his basic trading activities may be regarded as trading receipts, in order for that to be so they must be paid to the trader for some specific trading purpose.

(3) Where a recovery is attributable to a trading activity in an earlier period, and the profits of that earlier period have been correctly computed, it is inherently unlikely that the recovery can be taxed in a later period as a receipt of a trade.

(4) Just because a sum is included in a company's accounts, it does not follow that it is liable to tax.

The FTT examined the arguments of the counsel for each side in relation to each of these propositions. In respect of the first, the FTT commented that the repayments were not attributable to a "statutory right" under s.80 VATA 1994 – that was merely the mechanism for obtaining the repayment. It was quite different from the cases cited to support the proposition, which related to a statutory right to compensation on termination of a lease. The underlying right to the money certainly derived from the trading activities of the companies.

In respect of the second, the FTT examined a number of precedent cases on the nature of "borderline" receipts, including voluntary payments, and concluded that there was no such principle – the circumstances of each receipt must be considered in its context, but there is no presumption that a specific trading purpose is necessary for a receipt to be chargeable as part of the trade.

Again, in respect of the third proposition, the FTT considered the precedents and rejected the appellants' argument. The starting point and the end point is the source of the profit, and there is no inherent likelihood or unlikelihood of the result that can be based on the fact that a recovery is attributable to a trading activity in an earlier period. The question is whether the actual receipt or accrual arose from the trade.

The fourth proposition was accepted.

The FTT concluded that the true purpose of the VAT repayments was to compensate for depletions in the trading results of the various companies whose supplies had given rise to the VAT overpayments, and in most cases the payments were directed to the companies that were carrying on those trades or had succeeded to them. They therefore had the nature of trading receipts.

Where the person who had originally carried on the trade had ceased to do so, the FTT was satisfied that a charge to CT still arose on "post-cessation receipts" in the hands of whoever was beneficially entitled to the repayments. However, this did not apply if a different person was now carrying on the trade as a successor – there appeared to be a gap in the post-cessation rules in that unusual circumstance (i.e. trader A has ceased to carry on the trade and transferred it to trader B, but person C receives the VAT repayment). This gap did not apply in any of the cases under

review, so all the repayments were correctly assessed either as trading receipts or as post-cessation receipts.

Turning to the statutory interest, the FTT concluded that the amounts had all the characteristics of interest on a money debt, even if there had not been an original "lending of money" on which the interest accrued. The existence of a money debt was enough to bring the interest within the corporation tax "loan relationship" rules, and it was therefore taxable. The appeals were dismissed on all counts.

Further appeals

The companies appealed to the Upper Tribunal, arguing that the FTT had erred in law in six respects, summed up by the judge as the concept that only the representative members of the VAT groups were entitled to the VAT repayments and interest; as the underlying trading transactions were not part of the trade of the representative members, the income was too remote from any trade.

The UT judge considered the facts, the precedents, and the decision of the FTT in great detail, and concluded that in all respects the FTT was entitled to come to the decisions it had made. There was no error of law, and the appeals were dismissed.

The companies appealed again to the Court of Appeal, arguing in particular that the specific statutory rules on taxation of post-cessation receipts could only charge a company which had carried on the trade that had now ceased. The judges disagreed: any recipient of a post-cessation receipt was taxable on it. This was consistent with the wording of the legislation and the intention underlying the law.

Furthermore, HMRC's obligation to pay was a money debt, and the interest charged on it therefore fell within the scope of the rules on loan relationships.

The appeal was dismissed on both counts.

At last, the appeal came before the Supreme Court, which confirmed it again. By this time, the only point at issue appeared to be the statutory treatment of post-cessation receipts. The judges were satisfied that the legislation did not offer any reason not to charge what were properly regarded as the fruits of trade.

Supreme Court: *Shop Direct Group v HMRC*

6.4.4 Interest

A company had accounted for output tax on supplies of herbal teas until 2014. Following the case of *Dr X Hua* (VTD 13,811) in 1995, HMRC had accepted that this type of supply qualified for zero-rating. The company made a successful repayment claim, capped at four years (but still £303,404), and applied for interest under s.78. HMRC denied that there had been an "official error" and the company appealed.

The company claimed to have tried to clarify the liability of its supplies several times with HMRC over the years, and to have received misleading advice. Specific questions were asked in correspondence in 1994, at a VAT visit in 2004, and on the telephone in 2008. The company claimed

that HMRC's guidance on its website was not updated after the 1995 case, and was confusing to taxpayers.

The Tribunal reviewed the precedents on what constitutes an "official error" for this purpose. It is normally for the trader to determine the correct amount of VAT, and HMRC do not have an obligation to carry out an in-depth investigation or offer advice. However, in this case the judge was satisfied that a specific question had been asked at the VAT visit: the visiting officer had been told how the teas were supplied, and had given the wrong answer. The phone call in 2008 was less conclusive, because it appeared that it related to "herbs sold as medicine". The advice given in 2004 was an error that had led to the overpayment, and it brought s.78 into play.

First-Tier Tribunal (TC04820): *Avicenna Centre for Chinese Medicine Ltd*

6.4.5 Questions on *Fleming* claims

The FTT has referred the following questions to the CJEU:

1. Does the UK's different treatment of output tax Fleming claims (which could be made for periods ending before 4 December 1996) and input tax Fleming claims (which could be made for periods ending before 1 May 1997 — i.e. later than output tax Fleming claims) result in:

a) a breach of the EU law principle of equal treatment; and/or

b) a breach of the EU law principle of fiscal neutrality; and/or

c) a breach of the EU law principle of effectiveness; and/or

d) a breach of any other relevant EU law principle?

2. If the answer to any of Question 1(a) to 1(d) is affirmative, how should output tax Fleming claims relating to the period from 4 December 1996 to 30 April 1997 be treated?

CJEU (Case C-38/16): *Compass Contract Services Ltd v HMRC*

6.4.6 Repayment supplement

A sole trader appealed against a refusal to pay repayment supplement following a delayed repayment. The 05/13 return had been submitted on 30 June, claiming a credit of £26,016. A computer check flagged it for checking on 1 July, and it was referred to a local compliance team for further verification on 5 July. A file note on 12 July stated that, following earlier information recorded about a change from standard rated to zero rated building work, the case would be selected for a visit. A letter was sent to the trader on 16 July, which arrived on 17 July; the officer chosen to make the visit prepared to do so, and it took place on 30 July. The officer wrote to the trader following the visit, stating that inaccuracies had been found (relating to claims for input tax on blocked materials) and the claim would be paid after a reduction of about £1,500. The payment was released by payable order on 8 August. After further correspondence, HMRC accepted that the disallowed input tax should be reinstated, and they paid it on 14 November. On 16 April 2014, the trader's accountant wrote to HMRC to request repayment supplement to be added to the whole amount.

HMRC responded that the time from receipt of return (30/6) to repayment (08/08) was 40 days, but the period from notifying the trader of the enquiry (16/07) to the date HMRC were satisfied (02/08) could be left out of account. That left only 18 days in the count. However, RS would be added to the repayment of the balance.

The accountant protested that the delay between notification of the enquiry and the visit was unacceptable. His client had been available earlier. The only purpose of the visit was to check the amounts that were initially disallowed and were subsequently found to have been properly claimed. HMRC had accepted that their delay in the repayment had been below their expected standards. HMRC were willing to take four days off the "reasonable enquiry" period to allow for this, but it was still enough to deny RS.

The judge (W Ruthven Gemmell) considered the precedents and decided that an "inquiry" for this purpose had to be "a question". The letter of 16 July was not an inquiry – it was a generic letter that only communicated to the trader that more information was required. In the judge's view, the inquiry was made and answered on 30 July, and that was the only day that could be left out of account. The "clock" therefore stood at 39 days, and RS was due.

First-Tier Tribunal (TC04966): *Shaun David Corrigan*

6.5 Timing issues

Nothing to report.

6.6 Records

Nothing to report.

6.7 Assessments

6.7.1 Income tax and VAT

An individual and a company under his control appealed against a range of assessments and penalties on a variety of income tax and VAT matters. The VAT issue was that the company had claimed input tax on various legal costs that were personal to the director, including the purchase of his house and his divorce. He tried to justify these in the Tribunal, but the judge said that his arguments were "quite wrong". The director also argued that a misdeclaration penalty could not be imposed before a Tribunal had confirmed that a misdeclaration had occurred. Again, this was quite wrong. There was no reason to vary the mitigation given, or to suspend the penalty. The amount of the penalty was reduced slightly because of a calculation error, but otherwise it was confirmed.

Two of the PAYE penalties had been withdrawn before the hearing, but the rest of the assessments and penalties were confirmed.

First-Tier Tribunal (TC04835): *Telematique Ltd and another*

6.7.2 No evidence

HMRC investigated a shopkeeper. It appeared that the "no sale" button had been used far more than seemed reasonable. The trader appealed, but did not offer any evidence to the Tribunal that might justify assessment of a different amount. The judge considered that the trader effectively admitted that his sales were understated. In the circumstances, there was no alternative for the Tribunal but to dismiss the appeal.

First-Tier Tribunal (TC04863): *Satpal Singh Laghmani*

6.7.3 Inputs and penalties

HMRC assessed an individual trader to recover all input tax claimed from 09/08 to 03/13 (£34,000), and levied a 70% penalty (£23,200) for deliberate behaviour for periods 03/09 to 03/13. The appellant did not attend, as he was ill, but the hearing proceeded as it was clear he had had notice of the date and had made no attempt to apply for an adjournment in advance or arrange for representation.

The Tribunal reviewed the history of the business and found that there was little evidence of business activity or valid input tax deduction. There was also little cooperation by the trader with HMRC, including inconsistencies in statements made during the enquiry. The Tribunal concluded that there was no evidence to support the input tax claims, so the assessment stood; the behaviour did appear to be deliberate, so the penalty was on the correct scale; but the trader had offered some limited cooperation in responding to HMRC enquiries, for which the penalty should be mitigated from 70% to 60%. In other respects, the appeal was dismissed.

First-Tier Tribunal (TC04986): *Group One (Arshad Mehmood)*

6.7.4 Article

In an article in *Taxation*, Neil Warren examines the decision in *Ernest O Bustard* (TC04703), drawing lessons both for HMRC (the difficulty of a mark-up exercise and the need for realistic figures) and for the taxpayer and advisers (the need for records good enough to prevent HMRC leaping to the wrong conclusions, as they did here).

Taxation, 4 February 2016

6.8 Penalties and appeals

6.8.1 Default surcharge

In (TC03769), a company which made payments on account suffered a default surcharge of £38,724 for its 9/11 period. The company operated through 18 KFC franchises, and its VAT liability for the period was £774,492. It had exceeded the payments on account threshold in the quarter to 3/11, and 9/11 was the first quarter within the POA regime. It had therefore moved from having to pay the whole quarter's tax 7 days and one month after the end of the period (7 November), to paying significant amounts on the last day of months 2 and 3 (31 August and 30 September) and the balance on the last day of the month following (31 October). As it had paid all its VAT taking the benefit of the 7 day extension in each month, it was all late.

The company had defaulted in 3/11 and 6/11. It claimed that this was due to difficulties arising from the illness of the group financial accountant, who then left immediately after returning from holiday in July 2011, leading to the further late payments in 9/11. The FTT considered that the problems were too long-running to constitute a reasonable excuse. The late payments were in August, September and October, and the directors should have taken steps to rectify the situation by then.

The problem was compounded by the fact that HMRC did not notify the company that its first two payments for the period were late. The directors argued that if they had been notified earlier, they would have taken action earlier and reduced the penalty by making the second and third payments on time. The FTT did not consider this unfair, nor treat it as a reasonable excuse. A company is expected to know its obligations, and HMRC are not required to remind it of them.

Although the company claimed that the penalty was disproportionate, no evidence was presented to the FTT about the impact of the penalty on the business. The fact that it was harsh was not enough to make it manifestly unfair. The appeal was dismissed.

The company appealed to the Upper Tribunal. Its first ground of appeal was to argue that it should not have been subject to POA. The threshold had been increased by a Statutory Instrument issued in January 2011; the March 2011 liability fell below the new threshold. The June 2011 liability was above the new threshold, but that would only trigger POA from the December 2011 quarter. Even though the company had accepted HMRC's direction to make POA, in fact the August and September payments had therefore been made early, not late.

The company further argued that it was unfair that it should not have the benefit of the 7 day extension; and argued that the FTT should not just have considered whether the accountant's departure was a reasonable excuse for the September quarter but also for the June quarter, which would have reduced the rate applicable.

The Upper Tribunal dismissed the appeal. The new threshold did not come into operation until 1 April 2011: the company had exceeded the old threshold in the year to 31 March 2011, and was therefore within the regime from the return period following that. It seems that HMRC missed the fact that POA were due for the June quarter (in the first quarter under

the regime, they normally only require the second of the two instalments to be paid, and the balance).

The 7-day threshold was available to traders who did not pay POA. They were in a different situation from those who did pay POA, so the principle of equal treatment was not infringed. A large trader who chose to settle the actual liability each month by submitting monthly returns would enjoy the extra 7 days to pay, but would have the burden of preparing 12 returns a year (and, in general, would pay VAT earlier because POA are only 1/24 of the previous year's liability).

The reasonable excuse point about the 6/11 period had not been raised before the FTT, and could not be raised for the first time in the UT. All the grounds of appeal therefore failed.

Upper Tribunal: *Marsdens Caterers of Sheffield v HMRC*

A company appealed against a surcharge for its 10/14 period. The decision starts with the following interesting statement:

Gaysha is a building and contracting company. Its turnover for 2013-2014 was £4.6 million, having grown from £1.5 million in 2012-13. At some point subsequent to the VAT accounting period to which the present appeal relates, it changed to the cash accounting basis for computing its liability to VAT.

As the threshold for cash accounting is £1.35m, it is hard to see how this could be permissible, but it does not seem to have been in point in the appeal.

The company was not permitted by its bank to make payments of more than £100,000 on any one day. On Friday 5 December it had made a series of payments that used up the limit. The finance manager came into the office early on Monday 8 December and processed four separate payments between 08.33 and 08.40 totalling the £88,764.30 that was due. A 10% surcharge was levied.

HMRC confirmed the surcharge on review, noting that the payments falling due on Friday 5 December were foreseeable, and the company could have taken steps to arrange the payment with its bank. It had the funds available, and was only prevented from paying by the daily limit.

The company's representative tried a number of arguments to bring the unfairness of the penalty within the jurisdiction of the FTT, including reference to Judge Mosedale's comments about public law matters in the *Neil Garrod* decision, and HMRC's own consultation about penalties in early 2015 in which it was accepted that default surcharge gave rise to too many problems.

The judge noted that it is generally possible to make Faster Payments over a weekend; the company had produced no evidence to explain why it did not try to do this on Saturday 6 or Sunday 7 December. It might have been impossible, but the possibility did not appear to have even been considered. The company had chosen to make the payments to the other people on the Friday, and that had put it in the position of not being able to pay HMRC. It did not constitute a reasonable excuse.

The company had also not produced any evidence about the disproportionality of the surcharge. To bring itself within the same

situation as *Enersys*, it needed to show the impact of the surcharge on its finances (in *Enersys*, the surcharge was 16% of its profits for the year). The FTT could in principle consider whether the surcharge was disproportionate, but could not conclude that it was without some evidence.

First-Tier Tribunal (TC04795): *Gaysha Ltd*

A company appealed against a surcharge of £1,562 for its 10/14 period. The company had transferred some vehicles to a related company during the period. That had caused its liability to be higher than it normally would be; it expected to receive a repayment of VAT to the sister company at the same time. However, HMRC removed the sister company from the cash accounting scheme under reg.64(1)(d) at that time (protection of the revenue), leading to the repayment being due some time later than expected.

The cash accounting scheme had been withdrawn because of the connection between the companies. HMRC explained this in a letter to the companies' accountants in December 2014: where one of two connected companies uses an invoice basis and the other uses cash accounting, there can be an unfair advantage "using public funds" where there are transactions between them. The cash accounting scheme was withdrawn until HMRC could be sure that the output tax had been accounted for.

The company had not asked for Time To Pay, in spite of being familiar with the system. It seemed to the judge that the company had taken a deliberate decision not to pay, based on the advice of the accountants, and then to argue that HMRC's actions had been unlawful. This did not constitute a reasonable excuse, and the appeal was dismissed.

First-Tier Tribunal (TC04814): *Ryefell Ltd t/a Hambledon Haulage*

A company appealed against a surcharge of £14,661 for its 10/14 period. It argued that it had a reasonable excuse, in that its overdraft facility had been reduced by £750,000 at a time when it was affected by a seasonal drop in business. It had asked for Time To Pay, and believed initially that this had been accepted, but discovered after the due date (i.e. too late) that it had been refused because of repeated requests for TTP in earlier periods. The company had defaulted twice before; its penalty was initially charged at 5%, but following the withdrawal of one of the earlier penalties, this was reduced to 2%.

The judge examined the history of late payments by the business and the actions taken by the directors to deal with its financial difficulties. Although the seasonal decline was foreseeable, the judge did not think that was the only measure to consider: the directors had acted late, but they had done all that they reasonably could to comply with their obligations. HMRC's refusal of TTP after the due date left them with no opportunity – however unlikely it might have been that they could have found one – to settle the VAT on time and avoid the surcharge.

The appeal was allowed on the basis of reasonable excuse arising from shortage of funds.

First-Tier Tribunal (TC04829): *Ripon Farm Services Ltd*

A company appealed against a surcharge of £2,300 for its period 04/14. It had paid the VAT 3 days late. The trader did not attend, and it appears that the only excuse that the Tribunal was able to consider was a claimed attempt to pay electronically on Saturday 7 June which "for some reason" did not work even though there were funds in the account. The judge noted that the "BillPay" system will normally take 3 days to clear, which the trader should have taken into account. There was no reasonable excuse.

First-Tier Tribunal (TC04830): *Spyshoponline.co.uk Ltd*

A company appealed against a surcharge of £277,185 arising on its first payment on account for the period 03/12. It had been late with a payment for the period 06/11, and then paid the first monthly instalment for 03/12 on 1 March instead of 29 February. The payment was £13,859,254. The sole ground of appeal was that the payment was only a day late.

After various other disputes and arguments had taken three years to resolve, the company sought at the FTT hearing to amend its grounds of appeal to include a claim that it had never received the original surcharge liability notice. The judge expressed surprise that this had never been raised before, and accepted HMRC's evidence that the notice had been sent to the correct address and had not been returned. The company had failed to show, on the balance of probabilities, that the notice had not arrived.

The judge went on to consider whether the penalty was disproportionate. The only ground offered was its absolute size; after some discussion of the principles established in earlier cases, in particular *Trinity Mirror*, the judge concluded that this was not the "wholly exceptional" circumstance referred to by the Upper Tribunal, and the appeal was dismissed.

First-Tier Tribunal (TC04841): *Blue Ocean Associates Ltd*

A company within the POA regime appealed against surcharges raised for five return periods from 02/14 to 02/15. In 2014 the FTT (TC04049) had allowed an appeal in part in relation to the preceding three periods on the grounds that the company had a reasonable belief that a Time To Pay agreement was in force.

The company argued that it was entitled to rely on a letter from HMRC from November 2013 that implied that timely payment of the balance in each quarter cancelled any surcharge liability. The judge agreed with HMRC, and the earlier decision, that this was not a reasonable excuse: the appellant should not have interpreted the letter in that way.

The company's shortages of funds were also rejected. They resulted from the normal hazards of trade, rather than from anything unexpected or exceptional.

The company had made proposals to HMRC for late payment when it was unable to meet a liability on time. In some quarters this had been explicitly refused, but in others it had not. The company argued that this constituted an agreement of Time To Pay that would suspend surcharges. The judge agreed with HMRC that there was no formal agreement in place, and the company could not rely on the absence of disagreement to have the same effect as TTP.

In respect of two of the late payments, the company had negotiated loans which it expected to arrive in time to meet the liability, but which arrived later than expected. The judge reviewed the chain of e-mails on each occasion and considered that in respect of one of these loans the company had a reasonable excuse. In respect of the other, the company had failed to give a clear enough instruction to its bank to make a same day payment, and did not have a reasonable excuse.

The appeal reduced the total of surcharges levied by £18,750 – however, the remaining amounts (not stated in the decision) must have been very substantial.

First-Tier Tribunal (TC04859): *Fogarty (Filled Products) Ltd*

A company appealed against a surcharge of £455 for its 06/15 period. The company had paid late in respect of 03/14, and had then agreed TTP for the 06/14 quarter. It had failed to comply with the agreement, and had protested at various "threatening letters" sent by HMRC over the following six months pursuing the payments.

The 09/14 payment was late, leading to the issue of a SLN. The 12/14 payment was also late, but the 2% surcharge was below the £400 limit. The 03/15 payment was also late, but the 5% surcharge was likewise not collected.

The appellant asserted that he had not received any warning that there would be a financial consequence to late payment. He claimed that he had intended to pay on time, but he and his wife had slipped up in their administration leading to accidental late payments. The judge considered the appellant's letters and claims in detail, and did not accept that he had established that, on the balance of probabilities, the SLN and SLNEs had not arrived. A claim that he did not know the due dates for payment of VAT was also rejected. If he still felt that he had been unfairly treated, he should complain to the Adjudicator, but the surcharge was confirmed.

First-Tier Tribunal (TC04918): *S K and J Creations Ltd*

A trader appealed against a surcharge of £732 for its 01/15 return period. The payment for the 7/14 quarter was received on Monday 8 September, leading to the issue of a SLN; the payment for 1/15 was due on Saturday 7 March, but was not received until the Monday again. The payment for the intervening period was on time.

The trader claimed that he had given the instructions to the bank in good time on each occasion, but the bank had not processed the late payments using Faster Payments. While investigating the reasons, he discovered that payments of over £15,000 would take 2 business days, while smaller payments would only take 2 hours. He offered this as a reasonable excuse.

HMRC argued that this was no more than the "genuine mistake" defence that was rejected by the Tribunal in *Garnmoss*. The Tribunal acknowledged that the bank's notifications, stating "payment successful", were misleading; however, the trader should have investigated the reasons when the SLN arrived. Having received that warning, to make the same mistake again was no longer reasonable. The appeal was dismissed.

First-Tier Tribunal (TC04928): *M P Burke Transport Ltd*

A company appealed against a 10% surcharge of £3,104 for its 09/15 period. On the day of the hearing the Tribunal was told that the managing director had realised on the previous day, on reading the bundle, that the appeal was unlikely to succeed so he had decided to withdraw. As the Tribunal did not have written confirmation of withdrawal, the hearing proceeded.

It appeared that the trader had attempted to make a "same day transfer" on Friday 6 November, but it had not been processed and the money had only arrived on the Monday. The trader had apparently had a similar problem before, leading to an earlier surcharge (although this was not one of those cases where all the payments were made late for a series of returns).

The Tribunal noted that no evidence was presented to explain the bank's delay; it appeared that the trader was aware of the need to pay on time, and should have taken all necessary steps to make sure this happened. The surcharge was confirmed.

First-Tier Tribunal (TC04931): *Mannor Construction Ltd*

A company appealed against a surcharge of £5,009 for its 08/15 return period. It had been late for the first time in 08/14 and then again in 11/14, leading to a surcharge of £604. There was a combination of factors leading to the late payment, including a misunderstanding between the director and the administrator, concerns about the relationship with the bank, and a late payment coming from a customer abroad – however, none of these amounted to a reasonable excuse, particularly as the company had received warnings and could have applied for Time To Pay. The Tribunal was sympathetic but could not allow the appeal.

First-Tier Tribunal (TC04937): *Bindery Machinery Services*

A company involved in managing student accommodation appealed against a 15% surcharge of £10,073 for its 12/14 period. The preparation of VAT returns had been subcontracted to external accountants while the in-house accountant was on maternity leave; they prepared and submitted the 12/14 return on time, but failed to communicate the payment due to the managing director. The in-house accountant returned from leave on 9 February and realised that the VAT had not been paid; she immediately arranged for it to be transferred, but it arrived 5 days late. The Tribunal agreed with HMRC that a "genuine mistake" could not constitute a reasonable excuse; it considered and dismissed an argument about disproportionality.

First-Tier Tribunal (TC04949): *Collegiate Accommodation Consulting Ltd*

A director gave what the judge described as an "excellent witness statement" setting out the background to a dispute that had started in 2010. The trader had a problem with late payment from a number of hospital trust clients. This might have been the basis for a *Steptoe* appeal, but the Tribunal decided that the trader had a far more obvious reasonable excuse – in 2010, he had been told by HMRC that cash accounting was not available, when it was. This would have solved all the problems, and as a result the trader was held to have a reasonable excuse for all the defaults. The judge noted that the trader might actually be owed VAT by HMRC, if the company could be allowed to make certain bad debt claims that might strictly be out of time. The implication was that the judge

thought HMRC were so badly at fault that they should accept these claims.

First-Tier Tribunal (TC04951): *Hospital Telecommunications Services Ltd*

A company appealed against a surcharge of £11,323 for its period 12/14. It also appealed against a surcharge for the following period, but by the time of the hearing, HMRC had withdrawn it. The company had commenced trading in 2010 and had grown rapidly, so that on 2 July 2013, HMRC wrote to direct it to make payments on account.

The appeal was based on the fact that the director who was responsible for the VAT returns had gone into hospital for an operation at the beginning of December 2014. She had arranged for the first payment on account to be made before she left; the operation led to complications and she did not return to work until mid-January, by which time the second payment had been missed.

The judge commented that this would have been a reasonable excuse had the business been a sole trade. However, the business had two directors and eleven staff, and arrangements should and could have been put in place to deal with the absence of the director on sick leave. The appeal was therefore dismissed.

First-Tier Tribunal (TC04965): *Boost Pay Ltd*

A company appealed against a 15% surcharge of £7,241 for the 10/14 quarter. The trader advanced a number of grounds of appeal, including the fact that he believed that a direct debit was in place, after consulting the bank statements for the previous year. The Tribunal noted that the last period for which a DD had been in force was 07/13. In view of the warnings issued, a more recent and careful check would have been prudent. None of the other defences constituted a reasonable excuse. The appeal was dismissed.

First-Tier Tribunal (TC04987): *G Siddons Ltd*

6.8.2 Penalties

Two companies appealed against penalties (£16,090 and £8,804) raised under para.2 Sch.41 FA 2008 for unauthorised issue of VAT invoices. They had issued invoices showing a charge to VAT before they had become registered. They claimed that they had acted in accordance with advice received from HMRC, so their conduct was not "deliberate" and should be excused. It was agreed between the parties that the Tribunal could not consider "misdirection", so the only defence was "reasonable excuse".

The companies both submitted VAT 1 forms on 30 July 2013. The registration process was completed on 10 October 2013: one was registered with effect from 1 April 2013, the other with effect from 1 July 2013.

During the registration process, HMRC asked to see sales invoices. Initially they were told that there were none, but subsequently some were produced for inspection, dated between 12 July 2013 and 3 October 2013. Most of the invoices were issued to other companies in the same corporate group (not a VAT group registration). The invoices showed "to be

confirmed" in place of a VAT registration number. One was issued to an external company with no reference to VAT.

A director stated that he had been advised at a meeting with an HMRC officer that companies within the corporate group starting to trade "could use the Group VAT registration as a temporary measure until the new VAT registration is issued". He had not heard of such a procedure before but assumed that it was correct as it was put forward by an officer.

The Tribunal stated that the correct procedure is: "*Having applied for a VAT registration number and whilst waiting for that number to be issued, a company should issue invoices for an amount grossed up to include VAT without showing the VAT as a separate amount and advise the customer that the invoice would be re-issued, showing the VAT as a separate amount, when the VAT registration number was received.*"

HMRC sought "deliberate conduct" penalties because of the inconsistent responses about the existence of sales invoices, and because the companies had not done even what they claimed to have understood the advice to have been. The officer who had met with the directors had left HMRC and was not contacted, but HMRC's records of her contacts with the company did not back up the company's contentions.

The Tribunal commented that "the term 'deliberate' should be interpreted as being an action taken consciously where there was an appreciation that there was a choice"; also "there is no requirement that a 'deliberate' action, within para.6B Sch.41 FA 2008, involve any intention to avoid tax or obtain a tax advantage." Applying these standards to the facts, the Tribunal was satisfied that the conduct was deliberate, and the appeals against the penalties were dismissed.

The Tribunal also considered the question of reasonable excuse, in case on appeal the decision on conduct was overturned. The question here was not whether what the directors actually believed was reasonable, but whether acting on it was reasonable. The directors had given evidence of what they believed, but their actions were not consistent with what they said. There could therefore be no reasonable excuse.

First-Tier Tribunal (TC04823): *Contractors 4 U Ltd and another*

A similar situation appears to have arisen in another case involving a company that supplies medical and other staff to commercial, NHS and local authority clients. The company originally registered for VAT in June 2008. This registration was cancelled in early 2009. However, between March 2011 and July 2013, it issued invoices showing VAT of £270,000. This started at the request of a client.

The director discussed the matter with the company's tax agent. It seems the agent considered the VAT position to be unclear: the supplies might be exempt and might be taxable. While this uncertainty persisted, the company paid the "VAT" it was collecting from clients into a ring-fenced account. HMRC assessed this as a debt due to the Crown in any case, regardless of uncertainty, because it was shown as VAT on something purporting to be a VAT invoice.

When HMRC discovered the matter, they levied a penalty on the "deliberate conduct" scale, giving the maximum possible mitigation for a

prompted disclosure – a 35% penalty amounted to £94,385. The company appealed.

The judge commented that submissions were invited on what "deliberate conduct" constituted. There were at least two possibilities:

(1) One possibility is that it is enough for the Company to issue an invoice referring to VAT deliberately. If it does so, and the Company is, as a matter of fact an "unauthorised person" at the time that invoice is issued then, whether or not the Company is aware of that fact, the Company would on that interpretation have "deliberately" made an unauthorised issue of an invoice showing VAT.

(2) Another possibility would be that the Company must intend to issue an invoice referring to VAT but also must have knowledge that it is an "unauthorised person".

At the hearing, the parties agreed that neither of these formulations was correct. They submitted that both of the following elements must be present for "deliberate conduct":

(1) the taxpayer must deliberately issue an unauthorised invoice that shows an amount of VAT or an amount attributable to VAT;

(2) the taxpayer must know that is wrong, but must carry on with the issue of the invoice regardless. The taxpayer need not know specifically that VAT legislation precluded "unauthorised persons" from issuing VAT invoices but had to know that in some sense what they were doing was wrong.

The judge considered the matter and concluded that the test should be as follows:

(1) the Company deliberately issued an invoice showing an amount as being VAT or as including an amount attributable to VAT; and

(2) at the time it issued that invoice, the Company was aware that it was an unauthorised person.

Beyond the matters set out in these two tests, no knowledge of "wrongdoing" was required.

The judge noted, and accepted, that the law concerning the liability of the company's supplies was complicated. However, the law prohibiting the unauthorised issue of VAT invoices by an unregistered person was not complicated. Even on the parties' formulation of the question, the conduct was "deliberate". The penalty was therefore assessed on the correct scale, and there could be no "reasonable excuse" defence. The judge was also satisfied that the disclosure was "prompted", because the initial enquiry about the registration status of the company came from HMRC.

The penalty was confirmed and the appeal dismissed.

First-Tier Tribunal (TC04964): *Kinesis Positive Recruitment Ltd*

A trust registered for VAT late, and was charged a penalty at 15%. It appealed, arguing that:

- *There was some technical complexity around the issue of whether the Trust was liable to register for VAT in relation to the letting of*

holiday accommodation, and expert advice had been taken. As soon as the correct position was realised, a voluntary notification of liability to register had been filed.

- *The penalty should be reduced to nil because the Trust had notified promptly on becoming aware of the liability. The penalty regime should be primarily directed at taxpayers who deliberately avoid their responsibilities, not for those such as the Trust who make a genuine mistake and voluntarily disclose their mistake to HMRC.*
- *Alternatively, the penalty should be reduced below the level assessed by HMRC because a reduction of only 15% (out of a maximum of 30%) had been allowed in relation to "telling", and a reduction of only 20% (out of a maximum of 40%) had been allowed in relation to "helping". The maximum reductions were not given because the information requested by HMRC had not been provided by the deadline. That failure was because the request had been placed in a bag of records for completion of the first VAT return and handed to the accountants who had not actioned it until preparing that return.*

HMRC responded that the disclosure was unprompted, but it occurred after the 12 months allowed for full mitigation. Different answers had been given by the trust in response to questions about the liability of the supplies, so it was not possible for HMRC to accept that the complexity constituted a reasonable excuse. The trust had not provided enough information to justify any further reductions in the penalty.

The Tribunal specifically disagreed with the earlier decision in *James Hillis* (TC02611), where the judge had adopted the view in the second ground stated above. Non-deliberate failures are explicitly within the penalty regime laid down by the law in Sch.41 FA 2008; deliberate ones are penalised more heavily.

The information provided by the trust in correspondence (no representative attended the hearing) was insufficient to show a reasonable excuse or special circumstances that might warrant cancellation or reduction of the penalty. The appeal was dismissed.

First-Tier Tribunal (TC04920): *The Green Bungalow Settlement*

An individual took over a takeaway food business on 6 April 2009 as a going concern. He did not register for VAT until 21 January 2013. HMRC imposed a penalty at 15%, adjusted for zero-rated sales and mitigated by 25% to leave £2,080 in charge. The trader appealed, stating that he had relied on his accountant, and had instructed him to register the business for VAT. The tax of £22,666 on which this was based was duly paid.

It seemed that the trader was well aware of his need to register for VAT, and was also aware that he had not paid any – but he relied on the assurances of his accountant that his tax affairs were in order. He had no formal records of correspondence with the accountant about this, having dealt with him "by word of mouth". The Tribunal had to rule this out as a reasonable excuse by reason of s.71 VATA 1994 "reliance on another". This was different from the situation in which it might be reasonable to suppose that the accountant had actually registered the business, as in the case of *KE Jenkinson*. The failure had continued over an extended period during which the trader was aware that he was not filing returns or making

payments. The penalty was confirmed, and the mitigation was considered reasonable.

First-Tier Tribunal (TC04900): *Roberto Pia*

A plant and equipment hire company appealed against inaccuracy penalties totalling £149,000 for the period from 1 December 2009 to 31 August 2013. The company accepted that penalties were due, but disputed the calculation of Potential Lost Revenue (PLR). The company argued that this should be computed under the different (and much more generous) arrangements for "delayed tax" under para.8 Sch.24 FA 2007.

At a VAT visit in December 2013, the company's external accountant provided a schedule of errors that had occurred over a number of years. In each quarter, the last day of input and outputs was omitted, and included instead in the following quarter – which would contain the same error. This appeared to result from the software "default date" for preparation of VAT returns being set to run from the last day of the previous quarter to the day before the last day of the current quarter, rather than the correct period. It seems that this was deliberately done to ease cash flow difficulties; presumably large numbers of rental payments were due to be received on the last day of a month, so exclusion of a single day had a disproportionately large impact on the figures.

It proved difficult to reprogram the computer. Even so, the company accepted that the penalty should be on the "deliberate, not concealed" scale for a prompted disclosure, with maximum mitigation for cooperation – a 35% penalty. HMRC aggregated the underpayments for the 15 quarters up to 11/13 (which was under preparation when the control visit happened, and was filed on the correct basis), and applied 35% to the total of £426,246.

Para.8 Sch.24 FA 2007 provides:

(1) Where an inaccuracy resulted in an amount of tax being declared later than it should have been ("the delayed tax"), the PLR is –

(a) 5% of the delayed tax for each year of the delay, or

(b) a percentage of the delayed tax, for each separate period of delay of less than a year, equating to 5% per year.

(2) This paragraph does not apply to a case to which paragraph 7 applies.

The effect of this would be to reduce the PLR to 3/12 x 5% x £426,246, and the penalty would become £1,865. The company wrote to HMRC in July 2015 suggesting that this was the correct approach in this case. HMRC responded:

Our guidance [CH82391] on delayed tax states that two conditions must be met for the delayed tax provisions to apply. These two conditions are:

Condition 1 – The nature of the inaccuracy is such that, when discovered, and without the person taking any action to correct it, the inaccuracy

- *has already been automatically reversed in one or more returns for a later period or periods, or*
- *would have been automatically reversed in one or more returns, but for HMRC intervention.*

Condition 2 – An amount of tax

- *is identified in the return for a later period that matches an amount which, but for the inaccuracy, would have been declared in the earlier period, or*
- *would have appeared in the return for a later period but for HMRC intervention.*

HMRC did not consider that Condition 1 was met. This was confirmed by a Review Officer, who based his confirmation of the decision on a reading of reg.34 SI 1995/2518. He considered that "when discovered" in Condition 1 referred to discovery by the taxpayer, leading to a deliberate correction: this had not happened. The officer stated that a deliberate error could not be "discovered" by the taxpayer – the taxpayer already knew it had been made. Only careless errors could be discovered and corrected within reg.34, so only careless errors could come within para.8.

On appeal, the taxpayer argued that HMRC's position was based on their internal guidance, not the law. Even then, there were examples in their guidance that seemed to fit the current situation. The "discovery" in Condition 1 surely referred to HMRC discovering an error after it had been corrected in the following period, which corresponded exactly to what had happened in this case.

The judge (Dr Heidi Poon) examined the legislation in detail, including the structure and purpose of Sch.24 and its relationship with late payment penalties (where VAT is still subject to the "old" default surcharge rules) and corrections under reg.34. Crucially, only "careless" errors can be corrected under reg.34; the judge concluded that this meant only "careless" errors could be subject to the "delayed tax" PLR calculation.

The judge went on to note that error penalties are generally more severe than late payment penalties. If the company had filed correct VAT returns, and had simply paid the VAT as shown on its incorrect returns, it would have been subject to default surcharges totalling £63,697.

The judge commented on the difficulties caused by the expression "automatically reversed" in HMRC's guidance. This certainly appeared to support the taxpayer's case; however, the deliberately misprogrammed computer system was in effect "not automatic" in reversing the error – the taxpayer was constantly taking action in the next period to reverse the error, applying reg.34 when it was not entitled to do so. The judge said that it would be clearer if the guidance said that an error could only meet Condition 1 if it was "careless, not deliberate".

It appears that HMRC were prepared to accept the para.8 treatment in respect of the last quarter (08/13), on the basis of their own description of the operation of para.8 in circumstances where an enquiry by HMRC prevented the "automatic reversal" of an error in the next period (set out in *R&C Brief 15/11*). The judge said she would not interfere with such a concession, but could see no legal basis for it. The appellant had rightly pointed out that allowing this approach for 08/13 but not for the other quarters was inconsistent; the judge agreed that it was illogical and, indeed, ultra vires. The argument therefore did not assist the appellant.

The appeal was dismissed and the penalty confirmed.

First-Tier Tribunal (TC04860): *M J Hickey Plant Hire and Contracts Ltd*

A company appealed against a "deliberate conduct" inaccuracy penalty charged at 40.25% of understated VAT for 06/11 to 06/13 amounting to £214,289 (penalty £86,251). The directors claimed to have been unaware of continual and substantial errors made by book-keepers.

HMRC argued that this was not credible, given the size of the errors in relation to the size of the business. The FTT agreed: the purchase figures were all correct, and all the errors were in favour of the business. The directors had been able to produce accurate returns from the point that HMRC started an enquiry. It seemed that the errors were more likely to be deliberate than careless.

A separate penalty for failing to apply fuel scale rates was suspended. However, a deliberate penalty cannot be suspended. HMRC's mitigation of the penalty by 85% of the maximum (the difference between 70% and 35% for a prompted disclosure) was appropriate. The appeal was dismissed.

First-Tier Tribunal (TC04963): *Gryson Air Conditioning Equipment Ltd*

6.8.3 Budget proposals on penalties

The government will consider clarifying in statute what constitutes "reasonable care" in avoidance penalty cases, to include making clear that avoiders cannot rely on generic, third party legal advice received via the promoter or other enabler of the scheme.

OOTLAR March 2016

As announced at Budget 2016, the government will consult on the idea of a new penalty for participating in VAT Fraud. The consultation document will be published in spring 2016. If, following consultation, the government decides to legislate, draft legislation will be published, for further consultation, with the intention of introducing final legislation in Finance Bill 2017.

OOTLAR March 2016

6.8.4 Barring HMRC from the proceedings

The *BPP* case has taken a further twist: the Court of Appeal has overturned the UT decision and restored the decision of Judge Mosedale in the FTT (TC03768).

First-Tier Tribunal

The taxpayer applied for HMRC to be barred from the proceedings for failing to follow Tribunal directions. The subject matter of the substantive appeal appears to be similar to that in *Kumon Educational UK Co Ltd and related appeal* (TC03249): a taxable education provider underwent a reorganisation, following which study material was supplied zero-rated by a different company (LM) from the standard rated education and training (Holdings).

On 29 November 2012 HMRC issued two alternative assessments on LM and Holdings of approximately £6 million for the period September 2008 to 18 July 2011 on the grounds that VAT should have been charged on the supply of the books on the bases either that there was a single composite supply, or that there was an abuse of rights. A further decision was issued

stating that the 2011 changes to the zero-rating of printed matter applied from 19 July 2011. The company accounted for VAT on sales of printed matter from that date, but nevertheless appealed against the decision.

The two assessments and the decision were appealed in time. The three appeals were joined and directions issued for a joined statement of case ("SOC") to be served on 2 October 2013. HMRC applied for a short extension of time when the joined SOC was served late on 21 October. The appellants did not consider that the SOC satisfactorily explained the factual and legal basis for the two assessments and decision. The appellants applied direct to HMRC for further and better particulars on 11 November 2013. There was some correspondence and calls between the parties in which the solicitor acting for HMRC appeared to accept in principle that HMRC ought to give the replies requested but would not (yet) commit HMRC to a time frame in which the replies would be provided.

The appellants then applied on 22 November 2013 to the Tribunal for an order that unless replies were provided within 14 days of the date of the order HMRC would be barred from proceedings. A hearing was convened for 9 January 2014. By the end of December the parties were agreed that the replies were to be provided by 31 January 2014. However, HMRC would not consent to the order proposed by the appellant as it was in the form of an "unless" order which stated that HMRC would be barred if the replies were not provided by the agreed date of 31 January 2014. The hearing of 9 January therefore went ahead, and Judge Hellier issued an "unless" direction – it was slightly different from that requested by the appellant (under rule 8(1) – mandatory strike-out for non-compliance), but had a similar effect (under rule 8(3)(a) – discretionary strike-out for non-compliance). The wording was:

If the Respondents fail to provide replies to each of the questions identified in the Appellants' Request for Further Information by 31 January 2014, the Respondents may be barred from taking further part in the proceedings...

HMRC sent a request for further information on 31 January. On 24 April they notified the appellant that they were withdrawing the assessments (probably realising after the *Kumon* decision that they were hopeless), but maintaining the decision about the post-July 2011 position.

The January directions also required both parties to carry out a further disclosure exercise by 30 April and file a disclosure statement and further list of documents on the other no later than that date. There was no suggestion that the appellants did not comply. HMRC did not comply until 8 May 2014. On that date a disclosure statement was served together with a list of documents, which included no new documents. HMRC did not apply was made for an extension of time until 5 June, when they stated that there were no further documents to disclose.

Judge Mosedale examined in detail what Judge Hellier's direction had required HMRC to do, and what they had done in response to it. Although pleadings in general do not require each party to identify every fact, matter and submission with the same degree of particularity as will be relied on at the hearing, nevertheless it is open to the Tribunal to direct more detailed pleadings than ordinarily required and in this particular case, in accordance with the parties' agreement, that is what the Tribunal

did. HMRC could have appealed against the direction or they could have sought to have it set aside; instead, they failed to comply with it. The direction required them to identify all the facts on which they sought to rely; their reply identified no facts at all.

The judge went on to consider the appropriate sanction. She agreed that the appellant was unable to appreciate HMRC's case or prepare to argue against it on the basis of the SOC and the reply to the direction. "Litigation should not be conducted by ambush." The judge could not understand why HMRC had failed to comply with the direction – in the absence of any clear reason, the failure could not be justified.

HMRC's representative pleaded that barring HMRC from the proceedings was a Draconian remedy that would allow the appellant to treat its supplies as zero-rated into the future, causing a distortion of competition. The case was supposed to be the first test of the operation of the 2011 legislation. None of these arguments held weight: HMRC could bring another test case, and they could issue a new decision from a current date that would have to be appealed again. There should be no special treatment of HMRC if they ignore the Tribunal's directions: "To say otherwise would mean HMRC (and perhaps appellants) have a licence to ignore Tribunal rules and directions where an HMRC decision in principle rather than an assessment or voluntary disclosure is the subject matter of the appeal."

The judge's decision was:

I have come to the conclusion that HMRC should be barred. There has been unnecessary delay and expense. Tribunal directions have been breached. There is clear prejudice to the appellant in having to wait 8 months for a proper statement of HMRC's case and not barring HMRC would leaves the appellant without a remedy for this prejudice. There was no good reason for the delay in stating its case, the failure lasted for a significant period of time, and HMRC were clearly on notice from the first that the appellant did not consider their SOC satisfactory, and clearly on notice from January that a failure to comply might lead to a barring order yet they did not correct the position for another 5 months. Barring is the appropriate sanction.

In theory, HMRC could maintain their decision, but they would not be able to appear or be represented at the hearing of the appeal. As they have still not put forward a cogent argument in support of their decision, this would be a substantial disadvantage. They are likely to concede this decision and issue a new one, and find another taxpayer to test the operation of the legislation.

HMRC then applied to a different FTT judge (Timothy Herrington) for the barring order to be lifted. The judge considered the basis of Judge Mosedale's decision and HMRC's criticisms of it, and concluded that it was only appropriate for the FTT to lift the barring order if:

(1) Factual circumstances have changed since Judge Mosedale's decision; or

(2) There was an obvious error of law in the decision.

The judge could find no such obvious error of law, and refused to lift the barring order (TC04031).

Upper Tribunal

HMRC appealed to the Upper Tribunal against the barring order. The Upper Tribunal judge (Colin Bishopp) agreed that Judge Herrington was correct not to lift the barring order: the proper place for a review of Judge Mosedale's decision was the UT, not the FTT.

HMRC's representative accepted that HMRC had failed to comply with Judge Hellier's original directions, and could not offer an explanation or an excuse for this. However, she claimed that there was no significant prejudice to BPP in the delay, which had been rectified before the hearing to consider the barring order. Such prejudice as there was could be remedied by an award of costs; the barring order had the effect of handing BPP an unwarranted windfall.

She went on to put forward five different criticisms of Judge Mosedale's decision. The first of these was that the judge had incorrectly applied the principles of the *Mitchell* case to the case before her. Judge Bishopp agreed that this was a material flaw in her reasoning – that was not her fault, because there were further developments in that line of case law after she had heard the application, and these showed that it was not applicable in the way that she had thought. In order to allow for the substantive appeal to proceed in the FTT in November, Judge Bishopp did not refer the matter back to the FTT, but instead "re-made" the decision in the UT.

He was highly critical of HMRC's failures in the case, but concluded that it was not appropriate to bar them from the proceedings. It was unsatisfactory that the FTT had so few sanctions to enforce its directions; but it should not necessarily impose the ultimate sanction for want of anything else. He did not make an order for costs at this time, but invited applications from the parties. He made the following comment in conclusion:

Miss Simor argued that I should instead make a direction for indemnity costs in HMRC's favour, since it should have been apparent to BPP, once the judgment in Denton and my own decision in Leeds City Council were released, that it should have agreed to the lifting of the bar. I do not think there is any merit in this argument. First, it does not seem to me that a party can be lightly criticised for defending a position in which it finds itself. Second, this was not a case of an inadvertent slip quickly corrected, or of an error, even if not quickly corrected, which was innocent and of little real consequence. It is a case in which there has been a prolonged failure to do what, as Judge Mosedale rightly said, it should have been obvious to any lawyer ought to be done. The prejudice to BPP of HMRC's conduct is not great, but it is real. It does not seem to me that BPP should be exposed to the costs of this application, and certainly not on the indemnity basis.

Court of Appeal

BPP appealed to the Court of Appeal. The issue before the appeal judges was the proper approach of the tax tribunals in the case of a breach of an order. It was established that:

- HMRC had not complied with the order;
- HMRC had not given any reason for their failure; and

- Prejudice had been caused to the taxpayer as 'litigation is not to be conducted by ambush' and HMRC's failure had caused significant delays.

BPP submitted that the UT could have given its own guidance to the FTT, rather than re-making the decision. The difference in wording of the Civil Procedures Rules and the Tribunals Rules did not suggest any difference of approach, and it had been the practice of the Tribunals for some years to consider the CPR for guidance; and the guidance in the *Mitchell* and *Denton* cases was as relevant to the Tribunals as it was to the courts. BPP contended that Judge Bishopp had been wrong to conclude that Judge Mosedale had given HMRC's non-compliance with the order too much weight in reaching her decision.

The appeal judges agreed. They noted that the UT is a superior court of record which can take its own view on interpretation and can develop its own precedent. There was no justification for a more relaxed approach to compliance with rules and directions in the Tribunals than in the courts. It was appropriate that compliance and the efficient conduct of litigation at a proportionate cost should be given the weight accorded to them by the FTT in this case.

Flexibility of process did not allow for a shoddy attitude to delay or compliance by any party. The correct approach for HMRC, if they were having difficulty with compliance, would be to discuss an alternative with the taxpayer, and make an application to the Tribunal for revised directions, explaining the reasons for non-compliance and the merits of the alternative proposal. In this case, HMRC had simply failed to do anything.

There was therefore no overriding policy argument that more leeway should be afforded to HMRC because of their special status. What was left was the question of whether Judge Mosedale had carried out the balancing exercise in an inappropriate manner. That was only subject to a test of "unreasonableness" on appeal. The Court was satisfied that the factors that weighed in BPP's favour had been properly assessed: not only had there been no good reason for non-compliance, there had been no reason at all; and prejudice had been occasioned as a consequence in the form of significant delay and expense. On the basis of those findings of fact, the balance was clear. Non-compliance had not been the only factor that had persuaded Judge Mosedale to grant the barring order. The lack of any reason for non-compliance and the finding of prejudice had also been relevant factors.

BPP's appeal was allowed, and the decision of the FTT was restored.

Court of Appeal: *BPP Holdings v HMRC*

6.8.5 Procedure

The Tribunal heard an application for directions concerning disclosure of documents. The appeal related to disallowance of input tax relating to purchase of emissions allowances. The decision was based on defects in the VAT invoices, and *Kittel* "knew or ought to have known" grounds.

The judge considered the various demands being made and suggested that both parties should moderate the generality of what they expected the other party to supply. He issued revised directions on this basis.

First-Tier Tribunal (TC04853): *Tower Bridge GP Ltd*

A company disputed HMRC decisions to disallow input tax over several periods. It submitted an appeal with non-specific grounds (simply claiming that "we are clearly entitled to make a reclaim"). HMRC served a statement of case on 2 February 2015 and a list of documents on 13 March. The Tribunal issued standard case management directions on 13 April. On 10 April HMRC wrote to the appellant, pointing out that it had not provided information and documents as previously requested.

On 16 April, HMRC wrote to the Tribunal asking for permission to change its statement of case: it had now decided that the taxpayer's option to tax would be disapplied under the anti-avoidance provisions in paras.12 – 17 Sch.10 VATA 1994. At this point the appellant appointed solicitors, who wrote to the Tribunal stating that the original statement of case had not been sent to the appellant, so it objected to an application to amend it. On 19 June the Tribunal issued a number of directions, including a requirement for HMRC to issue a draft amended statement of case and draft directions within 21 days.

HMRC then applied for this direction to be set aside, and for a new direction to require the appellant to file amended grounds of appeal. Further correspondence followed; this led to the Tribunal issuing a letter to HMRC on 1 September requiring them to comply with the direction of 19 June within 14 days. HMRC missed that deadline for the statement of case by one hour, and rather than filing draft amended directions, applied 3 weeks later (on 9 October) once again to have the directions set aside.

On 6 October 2015, the appellant had applied to have HMRC's statement of case struck out and the appeal allowed. Alternatively, a further unless order should be issued. On 11 January 2016, the appellant responded to HMRC's 9 October application.

The judge noted that he did not have the power to strike out HMRC's statement of case or simply to allow the appeal. However, it was clear from the appellant's application that it was seeking an order under rule 7(2)(c) and rule 8 to bar HMRC from taking any further part in the proceedings. The judge considered the UT decision in *BPP Holdings* (since overturned by the Court of Appeal) and decided that the conduct of HMRC, while unsatisfactory, had not cleared the high hurdle that would require a barring order.

In the alternative, the appellant wanted a limited barring order – restricting HMRC to the amended statement of case, which was not sufficiently specific in numerous aspects. The judge considered these applications unrealistic and unhelpful, and declined to grant them. He finished by issuing several directions on the future conduct of the case, exhorting the parties to proceed without further procedural wrangling. The Tribunal would not tolerate any further non-compliance with time limits or attempts to achieve a tactical advantage.

First-Tier Tribunal (TC04846): *PGPH Ltd*

6.8.6 Strike-out

A trader sold tiles, and also provided the service of planning their installation and fixing them. He was therefore under a disadvantage in comparison with other tile-fitters, who would generally be trading below the VAT registration threshold – because he also supplied the tiles, his turnover exceeded the limits.

He had spent some time trying to find a solution to this problem, including writing to his MP and asking for a special method of accounting for VAT that would allow him to deregister. HMRC refused, and the trader brought a threefold "appeal" to the Tribunal: he wanted to dispute a tax debt without offering any technical argument as to the inaccuracy of the amount; the refusal to deregister him; and some default surcharges that were long out of time to appeal against.

The Tribunal had some sympathy with the way in which the VAT rules operated against the taxpayer, but had no alternative but to strike out the appeal as, respectively, not being against an appealable decision; having no prospect of success; and being out of time.

Judge Nowlan took the highly unusual step of setting out in the decision a possible way in which the trader could arrange his business so that he did not supply both the tiles and the fixing services – in effect, providing the contact details for the fixing sub-contractors, but not supplying their services as principal. This seems to run the risk of a variety of challenges by HMRC, but if done correctly, could be a solution.

First-Tier Tribunal (TC04952): *Colin Thompson t/a CC Tiles*

A Tribunal had to consider a tangled dispute involving alleged supplies of sub-contract labour from one company, G, to the appellant, J. G had gone into liquidation owing HMRC a large VAT and PAYE debt; it was also in dispute with J about amounts owing, with J countering that it had claims for faulty workmanship. Questions then arose about whether G had in reality made supplies to J – if not, the output tax it owed to HMRC would be considerably reduced, and J's input tax claims would be invalid.

HMRC had discovered a handwritten note on one of the appellant's witness statements saying "Date needs to be changed otherwise they no [sic] we made story up." This led HMRC to doubt the credibility of all the evidence, and a hotly contested hearing about what was to be done about it all.

Judge Nowlan noted that HMRC appeared to have had the disputed document for four and a half years without making anything of it, but had decided to raise it as of fundamental importance only shortly before the hearing. Striking out an appeal, when the parties had been preparing for it for some five years, was an extreme course. It also appeared that the document was only of marginal relevance to the substantive issues.

The judge decided not to strike out the appeal, but to allow HMRC to amend their statement of case to take account of what they regarded were the changed underlying facts; and to allow the appellant time to consider this revised statement in order to prepare their revised response.

First-Tier Tribunal (TC04953): *JSM Construction Ltd*

6.8.7 Late appeals

HMRC issued a post-clearance demand notice to an import clearing agent in relation to alleged ineligible claims for Low Value Bulk Import arrangements. The demand was for £1.2m. The company asked for a review of the decision, which confirmed it. After some correspondence, the matter appeared to be dropped by both parties for 15 months. When HMRC took it up again, the company claimed that it had assumed HMRC were waiting for a decision in similar litigation involving Citipost Ltd. The company finally filed a notice of appeal with the Tribunal on 16 June 2015, in relation to a review decision of 4 November 2013 confirming an initial decision of 11 July 2013. HMRC objected to the appeal being allowed to proceed out of time.

There were possible arguments in favour of allowing the company's application. Some of the correspondence could have confused the appellant about whether an appeal had been made, and the correct course of action to follow. The consequences for the company of not allowing the appeal would be likely closure with the loss of four jobs. However, the correspondence did not mention the *Citipost* case or a stay of proceedings, and one letter made it clear that HMRC had not received notification from the Tribunal that an appeal had been made. With regret, the judge concluded the balancing exercise in favour of not allowing permission for an appeal out of time.

First-Tier Tribunal (TC04850): *Oceanair Express Logistics Ltd*

A second-hand car dealer applied to appeal out of time against assessments for 07/02 to 04/06, raised on 4 October 2010, and a civil evasion penalty assessed on 3 January 2011. Extended time limits applied because HMRC contended that dishonesty was involved. The decisions were confirmed on review on 14 June 2011; an appeal was not lodged until 12 March 2015.

The judge reviewed the history of the dispute. The taxpayer's accountant had submitted a Tribunal appeal form in July 2011, but it had been returned because it did not enclose a copy of the decision letter. It was resubmitted, still without the decision letter, and returned again. It was possible that the accountant was confused about whether the appeal had been lodged, but there was no excuse for his continued failure to follow up and clarify the situation. The taxpayer's reliance on the accountant also continued beyond the point where it was reasonable, given the various contacts by HMRC trying to enforce the debt and saying that they had no record of an appeal.

Although such a decision would clearly cause prejudice to the taxpayer, the Tribunal decided against allowing an appeal out of time. The judge commented that there might be a remedy against the accountant, but this had not been taken into account in coming to the decision.

First-Tier Tribunal (TC04889): *Benjamin Myles Marshall Hall*

A similar decision was reached in another case about a VAT assessment for the period 11/03 to 12/08 for nearly £100,000, together with income tax assessments for the corresponding tax years. The trader was a sub-contractor in the construction industry. It seemed that he had been advised by his accountant, when faced with an assessment of this size, "to do nothing". He only took action when HMRC tried to enforce the debt:

he appointed a different accountant, who made various attempts to file returns reducing the liability.

As in the previous case, the judge considered that there was a difference between relying on professional advice that was credible, and relying on advice that could not be right: "to do nothing" was surely wrong. The various factors were carefully weighed, but the Tribunal decided to refuse leave to appeal. Once again, there was a comment about a possible remedy against the former accountants.

First-Tier Tribunal (TC04970): *Baljit Singh*

6.8.8 Hardship

A company applied for its appeal to be heard without having to pay the £51,462 in dispute. The company had registered for VAT in 2010 and had appeared to be dormant for some time, but even so had reclaimed input tax. It then filed a number of VAT returns, mostly claiming a small net repayment. HMRC tried to carry out an enquiry but the trader was uncooperative; this led to the imposition of a penalty for failure to comply with an information notice, and an assessment to disallow all the input tax the company had ever claimed. This assessment was the subject of the appeal and the hardship application.

The Tribunal had to try to make sense of correspondence from the taxpayer that did not answer HMRC's questions while claiming to do so. The company's accountant gave oral evidence, but seemed unable to explain many aspects of the business or the accounts. The judge considered that the company had not provided enough evidence to justify a hardship application, and refused it.

First-Tier Tribunal (TC04892): *Luxur plc*

A company appealed against a refusal by HMRC to accept a "hardship application" in relation to an appeal about £771,430 of disputed input VAT. The company had had its authorisation as a customs warehousekeeper withdrawn in March 2015, after being assessed to claw back input tax in respect of 01/13 to 04/14 in January 2015.

The assessment was in respect of purchases of fizzy drinks that HMRC considered were connected to MTIC frauds. The company hotly denied that it knew or ought to have known of any such connection, and argued that the withdrawal of its approval involved it in considerable expense and loss of profitability. The company was not willing to approach its bankers for additional facilities because they might "pull the plug". Other lenders were approached, but it would still cause hardship to have to pay so much tax.

The Tribunal considered a number of precedents on hardship and noted that the purpose of the rule was to allow appeals to proceed without harming the business, where they were more than just a delaying tactic to put off "the evil day" when the tax would have to be paid. Although the judge had no material before him to decide whether this appeal had substantial merit, he did not consider that it was such a delaying tactic. He accepted the claims of the taxpayer that the company could not realistically borrow the money, or sell or charge fixed assets, without harming its business.

The appeal was allowed.

First-Tier Tribunal (TC04976): *Elbrook Cash & Carry Ltd*

6.8.9 Reinstatement

A company appealed on 7 August 2014 against an assessment for £14,966 and a penalty of £2,438. The notice applied for permission to appeal out of time and stated that the tax had not been paid, but no application for hardship had been made. The Tribunal acknowledged the form on 14 August, and notified the appellant that the appeal could not proceed without either payment or application for hardship.

On 4 September HMRC applied for the appeal to be struck out. This was notified to the appellant by the Tribunal on 2 October, with a request for a reply by 23 October. This was followed by a direction to reply by 19 February, failing which the proceedings might be struck out. There was still no reply, so on 7 May 2015 Judge Bishopp ordered the proceedings to be struck out.

On 3 June the appellant applied for the proceedings to be reinstated, claiming not to have received the Unless Direction. HMRC objected; eventually a hearing of this application was notified by the Tribunal on 17 December 2015, to take place on Monday 8 February 2016.

The appellant applied for a postponement on Friday 5 February at 4.16pm, claiming that HMRC's hearing bundle "was a mess". Judge Kempster refused this application for postponement on the Monday morning, and his decision was communicated to the parties by e-mail at 10.34am.

The judge proceeded to consider the reinstatement application in the absence of the appellant. He could see no good reason for the appellant's complete lack of engagement with the Tribunal. Although there might in some cases be a distinction to be drawn between penalty proceedings (where payment of the tax is not a prerequisite) and the tax appeal, in this case the Unless Order had related to the whole appeal, and Judge Bishopp had struck it all out. The judge noted that HMRC had set out the technical grounds for their ruling over five pages, but it would not be possible or appropriate to consider any of the technical merits of the case. Even though £17,000 was a substantial sum, in the interests of fairness the judge refused the application to reinstate.

First-Tier Tribunal (TC04869): *Midland Credit Ltd*

6.8.10 Costs

A chartered accountancy practice appealed against VAT assessments disallowing various claims to input tax, including on the purchase of a motorhome, and penalties relating to alleged dishonesty and deliberate behaviour. A settlement was negotiated in which the practice agreed to accept the VAT liabilities (which would be settled by a different partnership) and HMRC dropped the penalties. This agreement was determined by a "consent order" of the Tribunal. The trader had applied for costs of the proceedings before the settlement was reached, and pursued this application afterwards.

The trader was particularly aggrieved that HMRC had alleged dishonesty, a potentially ruinous accusation for a chartered accountant. This should

only have been done on the strongest possible evidence and with special care. HMRC had failed initially to find records of telephone conversations between the trader and their officers in which the basis of preparation of the returns had been agreed; had they done so earlier, substantial fees would not have been incurred in preparing for the hearing.

Judge Kempster (TC04207) stated that the question for him was whether "HMRC had unreasonably resisted the appeal before the First-tier Tribunal, or conducted themselves during the course of those proceedings in an unreasonable manner."

On that basis, the application had to be refused. The background to the dispute was relevant in considering the conduct of the appeal, but it appeared to the judge that once the proceedings had commenced, HMRC had acted reasonably. Tracing the phone calls was only possible after the officer had requested further specific information that the trader had not already supplied, and this enabled the officer to bring the matter to a conclusion.

It was noted that a separate complaint had been made about HMRC's conduct of the matter, and that would proceed (presumably to the Adjudicator) once the question of costs had been determined.

The trader appealed to the Upper Tribunal, with Judge Kempster's permission, on three grounds:

(a) The FTT erred in law in failing to review in depth the background to the proceedings.

(b) The FTT was mistaken in finding that HMRC did not act unreasonably after the appeal proceedings began.

(c) The FTT was mistaken in holding that section 83G VATA applied to preclude the bringing of an appeal against the Schedule 24 penalty until the "review" was concluded so that there were no "proceedings" in relation to that penalty.

The UT (Judges Berner and Thomas) examined the history of the dispute and the detailed wording of Judge Kempster's decision. They agreed with the third ground of appeal: because of an administrative mix-up (mainly of HMRC's making), the appeal had been made before the review was formally requested, which meant that a review could no longer be undertaken. However, that did not affect the correctness of the underlying decision: the UT judges were satisfied that the FTT had properly considered the correct questions on the reasonableness of HMRC's behaviour, and made a value judgement that it was entitled to come to on the basis of the evidence before it. The appeal was dismissed.

Upper Tribunal: *Marshall & Co v HMRC*

In TC04441, the FTT found that HMRC had incorrectly disallowed input tax on "entertaining expenditure" that the taxpayer was contractually obliged to provide as part of a composite onward supply, so it was not blocked. The appellant applied for costs on the basis that HMRC had acted unreasonably.

The criticism of HMRC mainly related to the refusal of a particular officer to accept or understand the way in which the business operated. In the end, the Tribunal accepted the explanation that had been given from the

outset, and the trader considered that HMRC should have given in much earlier. The judge considered this carefully and concluded that it was not until the hearing that HMRC could fully appreciate that their case was without merit. They had therefore not acted unreasonably in bringing or conducting the proceedings, so costs would not be awarded.

First-Tier Tribunal (TC04874): *Merlin Scientific LLP*

A trader was involved in over 20 separate appeals over the years up to 2011. An appeal in 2011 was finally settled by HMRC paying the disputed VAT in 2015 (the delay was partly due to the company having been struck off and having to be restored to the register before it could be paid). The director applied for costs and interest.

Judge Sinfield went through the tortuous history of the dispute in detail. He concluded that HMRC had not acted unreasonably, and declined to award costs. Had he done so, he would have accepted a list of invoices from the individual director (in the capacity of an accountancy business) to the appellant (his company) as external costs that could be claimed, subject to review by a costs judge.

The Tribunal did not have a general power to award interest. It could hear an appeal against a refusal to award interest under s.78, but it was not clear that this had happened. In the absence of an appealable decision – and possibly with some trepidation that this extended litigation would continue further – the judge declined to make any decision about interest.

First-Tier Tribunal (TC04910): *Enviroengineering Ltd*

6.9 Other administration issues

6.9.1 Court and Tribunal Fees

Between July and September 2015, the Ministry of Justice carried out a consultation on (among other things) the introduction of fees into the First-Tier and Upper Tribunal Tax Chambers. In response to the question "Do you agree with the proposed fee structures we are proposing in the First-tier Tribunal (Tax Chamber) and the Upper Tribunal (Tax and Chancery)?" the Ministry received a total of 73 responses. 54 disagreed with the proposal, 17 agreed and two further respondents agreed in part.

In spite of the strong opposition, the government has decided to proceed with the proposals anyway, broadly as set out in the consultation. Minor amendments have been made, for example to charge a lower fee of £20 for appeals relating to a fixed penalty notice of £100 or less. Those unable to afford to pay a fee will be able to apply for remission.

www.gov.uk/government/uploads/system/uploads/attachment_data/file/486536/further-fees-proposals-gov-response-consultation.pdf

6.9.2 HMRC's taxpayer charter

HMRC have updated their "taxpayer charter" which is intended to show what they expect from taxpayers, and what taxpayers can expect from them.

The summary lists the following:

Your rights – what you can expect from us:	Your obligations – what we expect from you:
Respect you and treat you as honest	Be honest and respect our staff
Provide a helpful, efficient and effective service	Work with us to get things right
Be professional and act with integrity	Find out what you need to do and keep us informed
Protect your information and respect your privacy	Keep accurate records and protect your information
Accept that someone else can represent you	Know what your representative does on your behalf
Deal with complaints quickly and fairly	Respond in good time
Tackle those who bend or break the rules	Take reasonable care to avoid mistakes

The rest of the document explains what these broad terms mean in more detail.

A new HMRC Board sub-committee has been recruited "that will hold us to account for our performance against our commitments in Your Charter and support us in improving our services." The 2014-2015 Charter Report

may be viewed at *www.gov.uk/government/publications/your-charter-annual-report-2014-to-2015*.

www.gov.uk/government/publications/your-charter

6.9.3 Budget measures

The government intends to consult over the summer on reform of the VAT Disclosure Regime (VADR) to expand coverage to other indirect taxes and align more closely with the Disclosure of Tax Avoidance Schemes (DOTAS) model which covers direct taxes.

OOTLAR March 2016

The government intends to explore new options to ensure that avoidance scheme promoters and other intermediaries who "enable" scheme sale and use face greater, direct consequences when one of their schemes fails.

OOTLAR March 2016

6.9.4 Due diligence scheme for UK fulfilment houses

HMRC are concerned about the evasion of VAT and customs duty by non-EU traders shipping goods to the UK for storage in local "fulfilment houses" prior to sale via online marketplaces. HMRC calculate that evasion linked to this particular type of business accounts for £1bn – £1.5bn of the VAT gap.

HMRC are consulting until 30 June 2016 on "fit and proper" standards for introduction of a registration scheme from 2018 for fulfilment houses that store and handle goods imported from outside the EU. The consultation is part of a package of measures, which will also include strengthening HMRC's powers to direct non-EU businesses to appoint a VAT representative and making online marketplaces jointly and severally liable for the unpaid VAT. It covers a wide range of issues, posing in total 66 questions.

www.gov.uk/government/consultations/fulfilment-house-due-diligence-scheme

These measures will be coupled with legislation in Finance Act 2016 to strengthen the existing rules in s.48 VATA 1994 that enable HMRC to direct overseas businesses selling goods in the UK to appoint a VAT representative with joint and several liability and/or provide security for the VAT that becomes due.

The new measures will allow HMRC to inform an online marketplace about non-compliant overseas sellers. If the marketplace takes no action to prevent the fraud, and evasion continues, the marketplace will become jointly and severally liable for the VAT that an overseas business selling goods via the online marketplace fails to account for.

A Tax Information and Impact Note was issued with the Budget.

OOTLAR March 2016; Red Book 1.218 – 1.220; www.gov.uk/government/publications/vat-overseas-businesses-and-joint-and-several-liability-for-online-marketplaces

6.9.5 Tax simplification

The Office of Tax Simplification has published recommendations for improving small company taxation. The main point relating to VAT is considering the possibility of an advance clearance facility. Others are:

- Improving VATMOSS system that seeks to simplify EU cross border VAT issues.
- Improving awareness among businesses of the VAT flat-rate and other simplifying schemes.

www.gov.uk/government/uploads/system/uploads/attachment_data/file/504850/small_company_taxation_review_final_03032016.pdf#page=26

6.9.6 Single Departmental Plan

HMRC, along with 16 other government departments, have published a "single departmental plan" setting out policy objectives for the 5 years to 2020. These include maximising revenues by continuing to clamp down on avoidance and evasion, introducing digital tax accounts, and making cost savings of £717m a year by the end of the period.

www.gov.uk/government/publications/hmrc-single-departmental-plan-2015-to-2020

6.9.7 Security

Traders can only win an appeal about a notice to require a deposit of security if the Tribunal is satisfied that HMRC have not acted reasonably in issuing the decision; the Tribunal also has to consider whether HMRC would inevitably have come to the same decision if they had approached the matter correctly. It is therefore vanishingly rare for the trader to succeed on an appeal, but there has been such a case in the last quarter.

A small incorporated general accountancy practice was seriously in arrears with its payments to HMRC at 6 February 2015: it had not paid £68,717 in VAT and £8,964 in default surcharges. Returns had been submitted, so the liability was not contested. The last payment received by HMRC was in December 2013 in respect of the October 2013 period, and payments for the 12 periods before that had been late by varying amounts, some extreme.

HMRC issued a notice requiring a deposit of security of £92,567 on 6 February 2015. The director asked for a review, pointing out that he was in negotiations with another firm of accountants to sell part or all of the business. This would potentially generate sufficient cash to pay off the arrears and move forward. If the security demand was enforced, the business would have to cease trading, which would undermine the prospects for the sale. The reviewer rejected this as a reason to cancel the security demand, stating that to allow it would give the taxpayer an unfair advantage over other traders.

The taxpayer's solicitor argued that this contained two errors of law. It was incorrect to ignore the potential sale of the business, because it was a relevant factor in deciding whether there was a risk to the revenue. The officer who made the original decision accepted in cross-examination that she would have considered it, although she did not know about it in

February. Secondly, any advantage over other taxpayers was irrelevant: the officer should only have considered whether there was a risk to the revenue. The reviewing officer – who was unwell and was therefore unable to attend the Tribunal and explain himself – had therefore carried out the task in an incorrect manner.

HMRC argued that the appeal was against the original notice, not against the review decision. The taxpayer's representative argued that the two were effectively a single thing for the purposes of an appeal.

The judge agreed with HMRC that the February notice satisfied the requirement for reasonableness. The decision therefore turned on two questions:

- whether the appeal could effectively be made against the review decision;
- and, if so, whether that decision was unreasonable.

The judge was satisfied that the review decision was subject to appeal. He noted:

39. We are fortified in this view by the following aspects of the review process:

(1) Once the review process is initiated, no appeal can be made to this tribunal until it has concluded.

(2) HMRC must give their reasoning when notifying the conclusions of the review.

(3) The review decision is a different decision from the decision originally taken, as HMRC are required, upon review, to "have regard to" and "take into account" matters which were not before the original decision-maker (see sub-sections 83F(3) and (4)). Furthermore, the nature and extent of the review are matters for HMRC's discretion (s83F(2)): in this case, it is clear to us that Mr Littlewood considered the matter afresh.

The judge went on to consider whether the review decision had been reasonable. He agreed with the taxpayer's representative that the supposed "unfairness to other taxpayers" was misconceived. The possibility of a sale that would generate enough money to pay off the debt was a new fact, and a new decision in the light of that fact would not be unfair to anyone – it would represent a reduction in the risk to the revenue. The decision was therefore flawed; it was not inevitable that HMRC would have come to the same decision if the officer had approached the review decision in the proper way, and the appeal was therefore allowed.

First-Tier Tribunal (TC04845): *Half Penny Accountants Ltd*