VAT UPDATE
JULY 2016

Covering material from April – June 2016

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1. INTRODUCTION

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

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

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

1.1 Appeals pending

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

The HMRC website section says that it will be updated "on a monthly basis", but it appears to be less frequent or regular than that. The latest update appeared on 19 April 2016, after a gap since November 2015.

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

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

1.1.1 UK appeals awaiting hearing or decision

- *Associated Newspapers Ltd*: HMRC have appealed to the CA against the UT's decision that SI 1993/1507 did not apply.
- *BPP Holdings*: HMRC have petitioned the Supreme Court for permission to appeal against the CA's ruling that the FTT was correct to bar HMRC from further participation in the proceedings.
- *HMRC v Bratt Auto Contracts Ltd and another*: taxpayer is applying for permission to appeal to the CA against the UT's ruling that its *Fleming* claims did not meet the statutory requirements for claims to be recognised, and therefore missed the 31 March 2009 deadline.
- *British Film Institute*: CA has decided to refer questions to CJEU about application of cultural services exemption in the early 1990s before UK implemented it properly.
- *Brockenhurst College*: CA has referred questions to CJEU about application of education exemption to meals supplied to third parties in order to train students in waiting and cooking.

- *Caithness Rugby Football Club*: HMRC have been granted leave to appeal to the Upper Tribunal against the FTT's decision that a new building was similar to a village hall.
- *CCA Distribution Ltd*: the UT remitted matters in dispute back to the FTT; an oral permission hearing for an appeal to the CA is listed for 18 October 2016.
- *The Chancellor, Masters & Scholars of the The University of Cambridge*: HMRC have been granted 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 that the lower rate did not apply because there was a compound supply of "caravan with electricity"); the company has been given permission to appeal to the CA, hearing set for February 2017. The cases about removable contents/definition, removable contents/apportionment and verandas are now resolved.
- *Copthorn Holdings Ltd*: HMRC were refused (by the FTT) leave to appeal against the FTT's decision that they should reconsider their refusal to allow retrospective grouping. They have decided not to apply to the UT for permission; it remains to be seen what will happen next, because the decision of the FTT required HMRC to consider again their original decision.
- *DPAS Ltd*: HMRC had a partial success in the UT, which stood over another point behind the CJEU decision in *NEC* and *Bookit*.
- *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, hearing listed for 28/29 June 2016.
- *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 appealed to the Supreme Court (hearing concluded 19 May 2016, judgment reserved).
- *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, hearing listed for 3 – 6 July 2017.
- *Longridge on the Thames*: HMRC have been granted leave to appeal against the UT's dismissal of their HMRC appeal against the FTT's

ruling that a charity was not in business and could receive building services zero-rated (appeal scheduled to start in the Court of Appeal 19/20 April 2016).

- *Mercedes-Benz Financial Services*: HMRC appealed the UT decision that the company's product was leasing rather than HP to the CA, which decided to refer questions to the CJEU.
- *Metropolitan International Schools*: HMRC have been granted leave to appeal to the UT against the FTT's decision that the taxpayer supplied predominantly printed matter with incidental services.
- *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 March 2017.
- *Pacific Computers Ltd*: the FTT found in favour of a MTIC appellant. HMRC have been given leave to appeal to the UT, hearing listed 21 – 22 June 2016.
- *Privin Corporation Ltd*: the FTT found in favour of a MTIC appellant. HMRC have been granted leave to appeal to the UT.
- *SAE Education Ltd*: the company will appeal to the CA in May 2017 against the UT's ruling (in this update) that the FTT was wrong to allow exemption to the taxpayer as a "college of a university".
- *Temple Finance Ltd and Temple Retail Ltd*: HMRC are seeking leave to appeal against the FTT's ruling that, in the main, Sch.6 para.1 directions were not possible and the standard method override did not apply.
- *United Grand Lodge of England v HMRC*: taxpayer will apply for leave to appeal to the CA (commencing 9 November 2016) against the UT's confirmation of the FTT's decision that it did not qualify as a body with philosophical, philanthropic or civic aims.
- *Victor Dunlop*: HMRC have been granted leave to appeal to the Upper Tribunal against the FTT's decision that part of a garage conversion qualified for a DIY claim.
- *Volkswagen Financial Services Ltd*: HMRC have been granted leave to appeal to the Supreme Court against the CA's ruling that VWFS's proposed special method was more fair and reasonable than HMRC's proposal.
- *Wakefield College v HMRC*: the college has applied for leave to appeal to the CA against the UT's ruling that it would use its building for a business purpose and therefore did not qualify for zero-rated construction.

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:

- *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 (now awaiting a Supreme Court ruling after the HC and CA both applied the CJEU's judgment in Case C-591/10 in favour of the taxpayer).
- *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).
- *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).

1.1.3 Cases in the current update

The current update includes the latest developments in the following cases from HMRC's list or previous outstanding lists in this update:

- *Airtours Holidays Transport Ltd v HMRC*: the Supreme Court dismissed the taxpayer's appeal against the CA ruling that it had not received the supply of professional services and could not deduct input tax charged.
- *Bookit Ltd, National Exhibition Centre*: CJEU has agreed with HMRC that "card handling charges" do not fall within the exemption for financial transactions.
- *Iveco Ltd*: HMRC won their appeal to the UT against the FTT's decision that the company's repayment claim succeeded.
- *SAE Education Ltd*: the UT allowed HMRC's appeal against the FTT finding that the company qualified for exemption as a "college of a university".
- *The "Spotting the Ball" Partnership & Others*: the CA upheld the taxpayer's appeal against the UT ruling that "spot the ball" was not a "game" and could therefore not be exempt.
- *University of Huddersfield Higher Education Corporation*: the CA has upheld the UT's decision that the university's 1995 VAT planning scheme was abusive.

2. OUTPUTS

2.1 Scope of VAT: linking supplies to consideration

2.1.1 Public services

A Netherlands municipality organised school transport for some pupils. It bought in the transport services from commercial companies, and collected contributions from parents, who had to apply to the authority to receive the school transport service. The authority regarded the contributions as VATable, entitling it to recover the VAT paid to the transport providers. The contributions were effectively nominal amounts, being only 3% of the costs, and the tax authorities considered that the local authority was not acting in the capacity of a taxable person. The contributions were collected in accordance with laws that provided for entitlement to free transport based on income, on distance from the school, and on special needs.

Questions were referred to the CJEU, asking whether this activity should be regarded as economic; subsidiary questions asked whether the activity should be considered as a whole, or whether each transport operation should be considered separately, and if separately, whether there was a difference in principle between journeys of between 6 and 20 kilometres and over 20 kilometres.

The Advocate-General (Kokott) gave an opinion that the collection of nominal contributions did not make this an economic activity. However, if the referring court found that there would be significant distortion of competition affecting more than a negligible number of transport services, the local authority would be acting as a taxable person to that extent.

The CJEU noted that the contribution paid by the parents was not linked to the costs of the services provided, and did not vary according to distance, price per journey or frequency of journeys. This did not stop it being “consideration”: the only question was whether there was a link between the payment and the thing done in return.

The huge disparity between the cost of the transport operation and the amounts collected suggested that the charge was more in the nature of a fee or levy (as in *Apple and Pear Development Council*) rather than consideration. The court also referred to the *Finland* case, which seems to be directly relevant because the amount of the contribution from parents appears to be linked to their income.

The court also noted that the local authority did not provide transport services to the general public. It was rather in the position of a final consumer of transport services, which were made available to parents as part of its public services activities.

Accordingly, the simple answer was that this was not an economic activity. The full judgment makes no reference to the possibility of distortion of competition: it appears that the court regarded that as so remote that it could be ignored.

CJEU (Case C-520/14): *Gemeente Borsele v Staatssecretaris van Financiën*

2.1.2 Consideration (1)

The Privy Council has heard an appeal in a case arising in Mauritius. Although this is not about EU VAT law, it considers a question that could be relevant to EU VAT, and the judgment may be regarded as informative about the relevant legal principles. It also appears to be related to the problems in the recent UK cases concerning fees charged by holding companies for management services.

The appellant company owned 51% of the share capital of a subsidiary. It had a contractual obligation to provide management services in return for a fee. In 2003, the directors resolved to waive the fee until the subsidiary was in a sustainable profit-making position. The agreement was not varied. Management services continued to be provided. In December 2007 and January 2008, the directors decided to reinstate the fee with effect from 1 July 2006, because the subsidiary had moved into profit.

No invoices were issued for the services provided between July 2003 to June 2006. The tax authorities assessed for output tax on the basis that the holding company had provided services during those periods; in the absence of tax invoices, if it had decided to forgo the payments, it was deemed to have received payment at each month end. The Supreme Court of Mauritius agreed with the tax authority.

The judges noted that the EU concept of consideration was different from consideration in English law, and the time of supply in the UK VAT law was different from that provided in the local legislation. It was therefore dangerous to use EU legal precedent, but it could cast light on the issues. In UK law, the provision of a service in accordance with a contract which required consideration could trigger a tax point; to avoid that in the circumstances of the current case, the waiver of the entitlement to remuneration would have had to have been formalised. However, Mauritian law only provided for time of supply to be based on the issue of an invoice or receipt of payment. As neither of these events had occurred, no tax point arose. The appeal was allowed.

Privy Council: *Shophold (Mauritius) Ltd v Assessment Review Committee and another*

2.1.3 Consideration (2)

A charity claimed input tax of £1,083,952 in relation to the training of street fundraisers. The issue was whether payments to the charity were consideration for a taxable supply of its publication “Earthmatters”, or were donations outside the scope of VAT.

The Tribunal examined the way in which the fundraisers behaved, the way in which the payments were described in promotional and other material, and the low likelihood that the fundraisers actually drew the attention of those they spoke to the benefits of the magazine, and concluded that the payments were in reality donations. It was unrealistic to regard them as either wholly or partly consideration for the magazine. The appeal was dismissed.

First-Tier Tribunal (TC05165): *Friends of the Earth Trust Ltd*

2.2 Disbursements

Nothing to report.

2.3 Exemptions

2.3.1 Spot the ball

In the case formerly known as *The "Spotting the Ball" Partnership and others*, the Upper Tribunal dismissed the taxpayers' claim that "spot the ball" (STB) was a game of chance and therefore exempt from VAT. The operators of the game had for years claimed that it was a game of skill, chargeable to VAT, in order to avoid being subject to gaming laws; they then submitted *Fleming* claims to recover output tax accounted for. The Upper Tribunal held that STB was not properly a "game" at all, and therefore could not be a "game of chance". The taxpayers appealed to the Court of Appeal.

The FTT had agreed with the taxpayers that the circumstances of STB made it a game of chance – the judgement of where the centre of the ball ought to be was not precise, so it was to at least some extent a matter of luck whether a close entry was declared the winner. The UT considered that a "game" required some degree of inter-player participation, and playing alone was not a game; this was an error of law on the FTT's part that enabled the UT to intervene.

The CA agreed with the taxpayers that there was no hard and fast rule or presumption that a "game" required inter-player participation. The FTT had considered the question and come to the correct conclusion. A game effectively played separately by many people at once, none of whom had any interaction with any of the others, was still a game. The finding that the game was a game of chance was also a finding of fact that could not be overturned.

The taxpayers' appeal was allowed, and a cross-appeal by HMRC (on the "game of chance" issue) was dismissed.

Court of Appeal: *IFX Investment Company Ltd and others v HMRC*

2.3.2 Notice update

HMRC have issued an updated version of their Notice *Betting, gaming and lotteries*, replacing the February 2013 edition. The "what has changed?" section states that the technical content remains the same, but minor changes have been made to a number of paragraphs.

Notice 701/29

2.3.3 Payment charges

The CJEU has held that the card handling charges levied by Bookit Ltd on customers buying tickets for the cinema are not within the financial services exemption. HMRC did not consider that the charges fell within the exemption for "transactions concerning payment".

The court noted that, during the period under consideration, Bookit provided card handling services for counter sales, but made no card handling charge for them. A charge of between 65p and 75p is charged on each transaction entered into online. The process is described as follows:

"…the debit card and credit card payments received by Bookit from customers buying tickets for the Odeon cinemas were processed by a bank known as the 'merchant acquirer', under a merchant services agreement. That agreement provided that the merchant acquirer should credit Bookit's account with the total sum of the transactions in respect of which the relevant card transaction data was presented to it. The agreement also provided that Bookit or, as applicable, Odeon was obliged, first, to obtain, from the merchant acquirer, an authorisation code – issued by the bank of the card holder, that bank being the 'card issuer', which signifies, in essence, that the card is valid and that there are funds in the account – before making any sale and, second, to ensure that that code was included in a file, known as 'the settlement file', which includes the card transaction data, and which has to be transmitted to the merchant acquirer at the end of the day with a view to completing the payments."

The stages in the sale of a ticket were listed, including the provision of information by the customer, the transmission of that information to the merchant acquirer and the return transmission of the authorisation code, followed by the completion of the transaction by the allocation of a seat to the customer and notification to the customer that the payment of the ticket price and the card handling charge will be debited to their card. At the end of the day, settlement files are transmitted to the various card issuers to trigger payments by the card issuers to the merchant acquirer, which in turn pays Bookit which pays Odeon.

HMRC argued that the financial transactions were carried out between the merchant acquirer and the card issuers. Bookit was not transferring funds on behalf of the customers, and could not therefore be within the exemption in relation to its charges.

The questions referred were:

1) With regard to the exemption in art.135 PVD as interpreted by the CJEU in *Sparekassernes Datacenter* (Case C-2/95), what are the relevant principles to be applied in determining whether or not a "debit and credit card handling service" (such as the service that is supplied in this case) has "the effect of transferring funds and entails changes in the legal and financial situation" within the meaning of para.66 of that judgment?

2) As a matter of principle, what factors distinguish (a) a service which consists in the provision of financial information without which a payment would not be made but which do not fall within the exemption [as in *Nordea Pankki Suomi* (C-350/10)], from (b) a data handling service which functionally has the effect of transferring funds and which the CJEU has identified as therefore being capable of falling within the exemption [as in *Sparekassernes Datacenter* as referred to above]?

3) In particular, and in the context of debit and credit card handling services:

(a) Does the exemption apply to such services which result in a transfer of funds but which do not include the task of making a debit to one account and a corresponding credit to another account?

(b) Does entitlement to the exemption depend on whether the service provider itself obtains authorisation codes directly from the cardholder's bank, or alternatively obtains those codes via its merchant acquirer bank?

The judgment starts by recalling the decision in *Everything Everywhere* (Case C-276/09) that extra charges by a service provider for paying by a particular method could not be exempt as they were not for a genuinely separate supply.

The question of whether there was a separate supply was for the referring court to determine. It is interesting that the court sets out what many people consider is the proper characterisation of the "card handling charge" as in reality being a booking fee: [whether it] "should be considered, for the purposes of the application of VAT, as a service that is ancillary to the sale of the cinema tickets concerned or as a service that is ancillary to another principal service that is supplied by Bookit to the purchasers of those tickets, which might be the remote reservation or purchase in advance of cinema tickets, and, consequently, as forming with that principal supply a single supply, with the result that that service should receive the same tax treatment as the principal supply." Having set out that proviso, the judgment goes on to consider whether the charge is exempt if it is in reality for a separate supply.

The key factor that distinguishes an exempt transaction is "whether the transaction under consideration causes the actual or potential transfer of ownership of the funds concerned, or fulfils in effect the specific, essential functions of such a transfer". Making account entries is likely to indicate that a transaction is exempt, but not making account entries does not rule out exemption.

However, the various stages in the collection and transmission of information and authorisation codes were regarded by the court as no more than technical and administrative assistance and provision of information that enable the company to make a sale and receive the corresponding funds – they did not, collectively or individually, constitute a financial transaction. There was no specific function essential to the transfer of ownership of the funds concerned.

The answer to the questions was therefore that exemption under art.135(1)(d) PVD did not apply to a card handling service, and HMRC have won a substantial victory.

CJEU (Case C-607/14): *Bookit Ltd v HMRC*

Similar issues and questions arose in the *NEC* case. NEC had accounted for output tax on booking fees charged in relation to tickets bought by credit or debit card; on 27 November 2002, it claimed a repayment of output tax for the period from 1 August 1999 to 30 April 2002, and the dispute continued in relation to later periods. The FTT held that the charges were exempt; the Upper Tribunal agreed with the contractual analysis (that NEC was genuinely making a supply of "card handling" to the customers that was separate from the supply of tickets and of selling services to the promoters of events), but was not sure whether that supply fell within the exemption under the Directive.

The analysis is effectively cut-and-pasted from the *Bookit* decision, and the result is the same: exemption does not apply.

CJEU (Case C-130/15): *HMRC v National Exhibition Centre Ltd*

2.3.4 Education

In TC03358, the FTT allowed an appeal by a commercial company which claimed the status of ‘eligible body’ by reason of its close links with Middlesex University. The FTT examined the principles established by the precedent cases of *HIBT* and *School of Finance & Management* (*SFM*), which succeeded in winning ‘eligible’ status in the courts, and the more recent decisions in *London College of Computing* and *Finance & Business Training*, both of which have been decided by the FTT and confirmed by the UT as not qualifying. The following principles were drawn from the precedents:

(1) The SFM factors may be helpful in determining whether a body is a college of a university, but that list of factors is not exhaustive and factors within that list may not always be relevant;

(2) It is necessary to consider the particular circumstances and specific facts of each individual case, which may involve considering factors other than those listed in SFM;

(3) In considering any particular factor, it must be determined whether that factor is compliant with EU law. If it is not, that factor must be put aside and not taken into account in reviewing the evidence;

(4) The “fundamental purpose” test does not replace the similar objects test, but has something in common with SFM factor (ix) (having a similar purpose to that of the university);

(5) There must be at least some degree of integration of the body with the university concerned;

(6) It is inappropriate to follow a “check list” or “tick box” approach. The cumulative effect of the relevant factors must be assessed to derive an overall impression, weighing the factors in the balance: some factors may carry more weight than others.

The ‘SFM factors’ are matters identified in that case which should be considered in determining whether the links between the bodies are close enough to regard the company as a college of the university. The Tribunal considered the evidence under headings (a) – (o) in detail, and concluded that the following carried the greatest weight:

(1) Status of Associated College, combined from September 2010 with status of Accredited Institution.

(2) Long-term links between SAE Institute and MU. Similar purposes to those of a university, namely the provision of higher education of a university standard.

(3) Courses leading to a degree from MU, such courses being supervised by MU, which regulated their quality standards.

(4) Conferment of degrees by MU, received by SAE students at MU degree ceremonies.

The appeal hearing took longer than the initial time estimates of the parties (three days). In spite of the FTT extending the hearing time each day and making available a fourth day, it was not possible to complete it; there was therefore an adjournment until further court time could be found, which meant that four months passed. After the second part of the

hearing, the Upper Tribunal gave its decision in *Finance & Business Training*, which led to further submissions being made to the FTT in this case. The FTT decided that that decision (which was binding on the FTT) did not mean that 100% of a company's activities had to be covered by the 'college of a university' umbrella; it had decided that 90% of this company's activities were so covered, and that was enough. The company's appeal was allowed, entitling it to a repayment of some £1.3m.

HMRC appealed to the Upper Tribunal, which examined the FTT's findings of fact and its reasoning based on those findings. HMRC's challenge to the FTT's decision was based on the assertion that there was insufficient integration between the college and Middlesex University to justify the FTT's finding. HMRC's counsel acknowledged that this amounted to an attack on the FTT's findings of fact, or on the conclusions it drew from those facts; but he argued that those findings were not supported by the evidence, or were based on an incorrect interpretation and application of some of the *SFM* factors. He cited the *Pendragon* decision in the Supreme Court as authority for the proposition that the UT should remake the FTT's unjustified decision.

The Upper Tribunal considered the arguments of both parties in detail. The Court of Appeal's ruling in *Finance & Business Training* has been handed down since the FTT decision in this case, and it provided a useful and binding explanation of the application of the EU law in this area. The UT should be very careful in overturning a decision of fact in a case about the application of an imprecise legal test: it would be necessary to be sure that there was an error in the FTT's approach.

The UT considered that it was necessary to adopt a multi-step evaluation of the relationship between the supposed "college" and the university:

- first, it would be necessary for both parties to have a common understanding of that relationship – both would have to regard the college as "of the university";
- second, that relationship would have to be of a college and university, rather than some other relationship such as partnership;
- third, the *SFM* factors would be relevant to consider whether the statutory test was met;
- fourth, it would be necessary to consider whether the body supplied education, which was accepted in this case.

The judges considered that the FTT had erred in failing to give proper consideration to the first and second of these tests, without which the *SFM* factors were irrelevant. HMRC's counsel's attack on the conclusions about the relationship between the bodies were well-founded: the status of "associate college" fell below the statutory requirement for a "college of a university". HMRC's appeal was allowed; submissions were invited on the possible consequences of the decision, in particular the action that the UT should take in relation to penalties.

Upper Tribunal: *HMRC v SAE Education Ltd*

2.3.5 Article

In an article in *Taxation*, Julie Butler considers recent cases on the exemption for private tuition, and in particular the condition that a subject must be "ordinarily taught". She states that HMRC have agreed exemption for some horse-riding lessons; the level of tuition, as well as the experience of the teacher and the pupil, may affect the question of whether it is "ordinary".

Taxation, 21 April 2016

2.3.6 Welfare?

A company registered for VAT with effect from 1 April 2010. It ran "holiday camps" at schools during the holidays. Initially it accounted for VAT on its income, but then claimed a repayment on the basis that it should always have been exempt and should be deregistered with effect from 1 April 2010 – it supplied "welfare" within VATA 1994 Sch.9 Group 7, in that its services were directly connected with the care or protection of children and young persons.

The company employed about 500 people. Many of its coaches were aged between 18 and 23 years. The company was required to meet certain standards in relation to child protection; parents were able to pay for its services with childcare vouchers.

The Tribunal accepted that this case was different from the earlier decision in *Slide & Seek Ltd*, because this company assumed responsibility for the care of children whose parents were absent. Several other similar precedents were considered. The judge accepted that the company did take responsibility for the care and protection of children and young people attending its camps, but concluded that the overall nature of the supply was the provision of the activities made available rather than welfare. This was based partly on what the company promised to deliver to parents in its promotional material, and partly on the qualities it looked for in its coaches in its recruitment procedures. The appeal was dismissed.

First-Tier Tribunal (TC05171): *Sport Academies Ltd*

2.3.7 Clawback on representative body

An association accounted for output tax on its subscriptions. In January 2008 it claimed back £100,141 in relation to the three years to 31 December 2007 on the basis that its income should have been exempt within VATA 1994 Sch.9 Group 9. HMRC accepted this and made the repayment. However, HMRC refused a *Fleming* claim for £501,798 submitted in February 2009 to cover the period from 1977 to 31 December 2004. HMRC had concluded that its subscriptions were not exempt, and an assessment was raised to claw back the earlier repayment. The association continued to account for output tax and periodically made claims for repayment, which were all subject to the present appeal.

HMRC submitted a late amendment to their statement of case, wishing to include "unjust enrichment" as an alternative ground for refusing the repayment claim (and therefore for clawing it back). The association could not repay the VAT to its members. The association argued that the

late introduction of this extra ground prejudiced it, as it could not properly assess the strength of the argument or respond to it at such short notice.

Judge Mosedale said that there would be a presumption that once proceedings were afoot, the case should be decided on a full consideration of all relevant law, and this weighed in favour of allowing HMRC to amend their statement of case. She decided that the present hearing would be a preliminary one: if the appellant made out its case in favour of exemption, HMRC would subsequently be able to argue the unjust enrichment point more fully.

The key legislation was Group 9 Item 1(d): "An association, the primary purpose of which is to make representations to the Government on legislation and other public matters which affect the business or professional interests of its members." The association represented members in the "inbound tourism industry", and its constitutional documents stated that 'the primary aim of the association is (sic) help our members manage successful, profitable businesses that are part of a vibrant and sustainable inbound tourism industry.' Slightly different words were used in different periods.

The judge considered evidence from past years, covering views of members as well as views of presidents and other officers. The question was whether the primary aim of the organisation was "political lobbying". She split the history into distinct periods, which she considered in turn. She concluded that political lobbying was not a main aim to which other aims were subsidiary; the main aim was the promotion of members' business interests, and political lobbying was one of the means by which that might be achieved. The appeal failed on those grounds.

This meant that it was not necessary to consider the technical issue of whether HMRC could enforce a clawback assessment under s.80(4A) on the grounds of unjust enrichment under s.80(3). Nevertheless, as it had been argued before her, Judge Mosedale gave an opinion. In her view, HMRC were entitled to raise such an assessment. The appellant therefore would have failed on that ground as well, if it had been relevant.

First-Tier Tribunal (TC05168): *UK Inbound Ltd*

2.3.8 Concert admission charges

The Halle Concerts Society is a membership organisation, constituted as a company limited by guarantee, which provides certain benefits to members in connection with concerts performed by the Halle Orchestra. These include the right to priority booking in advance of tickets going on sale to the general public.

A dispute had commenced in 1999 in relation to the exemption of the tickets themselves. That had been resolved, but the Society and HMRC could not agree on repayment claims for output tax accounted for on subscriptions amounting to £154,962 from 1 April 1973 to 31 May 1999 and £18,204 from 1 March 2001 to 30 November 2003.

The Society contended that the subscriptions were not consideration for a supply because they were subscriptions for membership of a company. Both parties agreed that if there was a supply, the Society made a single composite supply; the appellant argued that this was "membership" and was outside the scope, while HMRC responded that it was "the right to

priority booking" which would be VATable. Lastly, the appellant contended that if membership of the organisation was in itself a supply, it was exempt because the Society was a body with philanthropic aims, or provided cultural services.

The FTT considered the nature of the Society's activities, analysing what it did for its members over a considerable period. The judge considered in great detail the argument that the members' subscriptions were outside the scope as effectively to do with the rights of corporate membership of the company, and rejected it: it appeared that the benefits conferred on members by the Articles of Association were at the very least a significant aim of those who paid subscriptions, and if anything were the predominant aim. The subscriptions were therefore within the scope of VAT.

The judge went on to consider that the benefits provided, which varied over the period of the claim, were not in their intrinsic nature exempt, and constituted a single indivisible supply. The last consideration was whether the Society qualified as a "philanthropic body". Its representative claimed that it was "the epitome" of such a body; Judge Cannan considered the question to be more difficult, but nevertheless came to that conclusion. "Philanthropy" was wider in scope than "charity". The Society provided free and subsidised concerts in accordance with its aims, and that satisfied the statutory conditions. The supply of membership was exempt from 1977 onwards when the 6th Directive introduced that exemption.

First-Tier Tribunal (TC05067): *Hallé Concerts Society*

2.3.9 Updated Notice

HMRC have issued a revised version of their Notice *Sport*, replacing the August 2011 version. It has been updated to reflect the changes relating to membership with effect from 1 January 2015, which followed the *Bridport and West Dorset Golf Club* decision.

It is notable that under the heading "how has the exemption changed?" this version still refers to the changes introduced in 1 January 2000 to remove eligible body status from an entity that is subject to "commercial influence".

Notice 701/45

2.3.10 Sport?

The Upper Tribunal has referred the following questions to the CJEU in order to determine whether bridge can be described as a "sport" for VAT purposes and so qualify for exemption.

What are the essential characteristics which an activity must exhibit in order for it to be a "sport" within the meaning of art.132(1)(m) PVD?

In particular must an activity have a significant (or not insignificant) physical element which is material to its outcome or is it sufficient that it has a significant mental element which is material to its outcome? Is duplicate contract bridge a "sport" within art.132(1)(m) PVD?

CJEU (Reference) (Case C-90/16): *The English Bridge Union Limited v HMRC*

2.4 Zero-rating

2.4.1 Hot takeaways yet again

Four appellants claimed repayments of output tax charged on hot takeaways. Their original grounds of appeal raised the same issues of law as those decided by the Court of Appeal in the *Subway* case, and they therefore abandoned them. However, they applied to substitute different grounds. HMRC applied to the FTT (Judge Mosedale) for an order striking out the appeals on the ground that the reasons for the appeal could not be changed in this way. The judge considered this and accepted that the changes and delays would cause prejudice to HMRC, but were not sufficient in themselves to justify strike-out if there was an arguable point of law.

She went on to consider whether there was a reasonable prospect of success. The appellants' argument was based on the requirement in art.28 6th Directive for member states to consult the Commission before introducing "exemption with the right of deduction" (i.e. zero rates). The argument was that the tax on hot takeaways had been introduced in 1984 without such consultation, and was therefore ultra vires.

The judge examined this proposition and concluded that it stood no prospect of success, unless there was "an aberrant Tribunal decision". The requirement for consultation could not reasonably be supposed to apply to the partial, but not total, withdrawal of a zero-rate. She decided to refuse to allow the amendment of the grounds of appeal (because the alternative grounds were not properly arguable) and also to strike out on the basis that there was no reasonable prospect of success.

First-Tier Tribunal (TC04991): *Koon Chung and Yuk Fong Lam*

A company sold primarily takeaway food from sites in London, Sheffield and Bluewater. It accounted for output tax on various sales which it later decided should have been zero-rated, and in February 2013 made a claim for a refund of £681,000 covering the periods 12/08 to 03/12. It also ceased to account for output tax on these kinds of supply, and started to receive assessments. Appeals against the assessments and the refusal of the claim came before Judge Mosedale.

The company sold Mexican-style food. Judge Mosedale examined the way in which the various products were put together from a range of available ingredients. She considered arguments about the intentions of the seller, the intentions of the purchaser, advertising material, presentation and packaging, and food safety regulations, and concluded that it was more likely than not that there was a common intention that the food would be eaten "hot" – not in the normal everyday sense, but in the statutory sense of being above the ambient air temperature. It was therefore standard rated.

After 30 September 2012, the new statutory definition of "hot food" took effect, and covered any food that was kept hot after being heated. This meant that even "salads" were likely to be standard rated, as they generally included at least one of the various items that were kept hot, and those items would generally be a significant part of the selected product. If a salad was by definition "cold food", then the company was not selling salads; if they were salads, they were not "cold food". The appeal was

therefore also dismissed in relation to the periods after September 2012, with the minor caveat that, if the company could produce evidence to show that some customers selected only cold items for inclusion in their salads, those would be eligible for zero-rating. No evidence to this effect had been presented to the FTT.

First-Tier Tribunal (TC05071): *Mucho Mas Ltd t/a Chilango*

2.4.2 Caravans?

A company supplied "mobile timber structures and eco houses". It zero-rated some of these supplies as caravans. HMRC disputed this classification in relation to buildings constructed as temporary classrooms for schools, replacing portacabins.

HMRC stated that there was no definition of "caravan" for VAT purposes, but "the man in the street" would not recognise these structures as caravans, even if they could be moved from place to place. The purpose underlying the zero-rating provision was to give relief for residential caravans, which would not extend to the buildings in dispute in the case. It was clear from the planning permission that the company had been contracted to supply classrooms, not residential caravans. This was reflected in the design and adaptations required by the clients. The structures were therefore not caravans, and the appeal was dismissed.

First-Tier Tribunal (TC05013): *Thermo Timber Technology Ltd*

2.4.3 Designed for handicapped persons

VATA 1994 Sch.8 Group 12 item 2(g) provides zero-rating for equipment or appliances designed or adapted solely for use by handicapped persons. A company supplied mobile phones and tablets with specialised software installed to enable them to be used by handicapped persons. HMRC ruled that the supply was standard rated, and the company appealed. The Tribunal considered that it had jurisdiction to consider a ruling about future supplies under VATA 1994 s.83(1)(b) "the VAT chargeable on the supply of any goods or services", even though no supplies had been made yet.

The software reads text aloud and helps people with visual impairments and dyslexia in a number of reading and spelling tasks. It is only installed on mobile devices, not on laptops or desktop computers. The company argued that someone who was not disabled in this way would not buy a device with the software installed, partly because it changed various things about the way the device worked, but mainly because they would not pay extra for something that was of no use to them.

The Tribunal referred to the 2013 decision of the UT in *British Disabled Flying Association*. That case decided that the physical characteristics of the equipment had to be considered at the time of supply. An older decision, *Kirton Designs* (VTD 2,374), supported the view that an item could still be useful for and useable by able-bodied people and yet meet the definition.

On that basis, the Tribunal concluded that the supply of a mobile device with the software installed was zero-rated. HMRC's argument that the software itself was not zero-rated was irrelevant: the dispute was about the equipment, not the software.

There was a further dispute about the application of an ESC and the Tribunal's jurisdiction to consider that, but the Tribunal concluded that it had come to a decision on the basis of the legislation and the ESC was not necessary for the company to win.

First-Tier Tribunal (TC05126): *Iansyst Ltd*

2.4.4 Drugs

The Value Added Tax (Drugs, Medicines, Aids and Charities, etc) Order 2016 amends VATA 1994 Sch.8 Groups 12 and 15 to maintain the application or non-application of the zero-rate for supplies of certain medical and surgical goods, to take account of the restructuring of health service bodies in the UK and the Isle of Man. The regulations remove out-of-date references to superseded bodies. The amendments came into force on 28 June 2016.

SI 2016/620

2.5 Lower rate

2.5.1 Updated Notice

HMRC have updated their Notice *Fuel and power*, replacing the August 2012 version. Minor changes have been made to improve readability, and an obsolete section about the liability of connection charges before 2012 has been removed.

Notice 701/19

2.6 Computational matters

Nothing to report.

2.7 Discounts, rebates and gifts

Nothing to report.

2.8 Compound and multiple

2.8.1 Fish and fishing

A company operated a fishery business at a reservoir in Lancashire. It stocked the reservoir with trout, and sold two different kinds of ticket: one for pure sport angling (a "catch and return" ticket), and one that allowed the angler to keep 2, 3 or 5 fish (a "take" ticket). Different prices were charged for a half or a full day; for "catch and return" or "take"; and for 2, 3 or 5 fish.

The company had accounted for output tax on all tickets. It submitted a repayment claim on the basis that part of the consideration for "take" tickets should have been zero-rated as consideration for a supply of the fish. HMRC ruled that there was a single supply, and the dominant purpose was the right to fish. There had been similar cases in the 1980s, decided before *Card Protection Plan*, that had supported this view.

The Tribunal agreed with HMRC. When the customer purchased a "take" ticket, there was no guarantee that any fish would be caught. It was therefore not possible to characterise any of what was paid as being for a supply of fish. The experience of angling was quite different from the purchase of fish in a shop. There was no separate charge for fish taken away – there was a single charge for the opportunity to take fish away if they had been first caught. The Tribunal approved the conditions for zero-rating part of a fishing charge in Notice 742, and agreed that they were not satisfied.

There was a single supply of the right to catch fish, and the appeal was dismissed.

First-Tier Tribunal (TC04994): *Stocks Fly Fishery (a partnership)*

2.9 Agency

2.9.1 Employees

Two companies, A and I, jointly employed certain employees. A also supplied services to I under a service agreement. A and I treated the amounts paid by I to A in respect of remuneration of the employees as a disbursement outside the scope of VAT; HMRC disputed this, arguing that it was in fact part of the consideration A received from I for taxable services. Assessments totalling £644,000 were raised, covering 5 years. Under an indemnity clause in the service agreement, I paid these amounts, and was joined as a second appellant in the Tribunal appeal.

The employees concerned worked in a call centre known as the Patient Referral Centre (PRC). It was agreed that they were legally employed by both A and I. The judge cited the CJEU judgment in *Loyalty Management UK* that "consideration of economic realities" is crucial in applying the VAT law and in identifying the person to whom goods or services are supplied. The Supreme Court adopted a similar approach in *Secret Hotels2 Ltd*.

The judge commented that it was possible for either party to select parts of the service agreement to support their case. It was therefore necessary to analyse the facts in order to determine whether the services of the joint employees were provided to A, which in turn provided its services to I under the terms of the service agreement; or whether the joint employees provided their services to both I and A on the basis of a collaborative venture to deliver the services.

Senior personnel of I were involved in the recruitment, training, managing and supervision of the joint employees. Although it might be argued that they were mainly under the control of A, they were not working solely for A as a matter of economic reality.

The provision of the PRC to the NHS was a requirement of a contract entered into by I with the NHS. The evidence showed that the nature of the relationship between I and A was not a "classic outsourcing agreement where one party outsources to an external supplier and then disappears from the scene"; rather, I and A operated the PRC together. This was not apparent from the service agreement, but was once again the economic reality of the situation.

The conclusion was that the relationship between A and I could not be categorised, as HMRC contend, as the supply of services by A to I; rather it was a collaborative venture in which A provided the infrastructure and science of telephony and I the medical and diagnostic expertise allowing them to jointly select, employ, train and manage the joint employees with the costs of those joint employees being recharged by A to I as disbursements which, as is common ground, are not subject to VAT.

The appeal was allowed. The decision reproduces large extracts from the service agreement, which take up almost as many pages as the rest of the decision.

First-Tier Tribunal (TC05062): *Agilisys Contact Services Ltd and others*

2.10 Second hand goods

Nothing to report.

2.11 Charities and clubs

2.11.1 Community Amateur Sports Clubs

HMRC have updated their guidance notes on CASCs, with an extended Annex 1 giving information on VAT. It points out that a CASC is eligible for various tax reliefs but, unlike charities, there are no specific VAT reliefs for CASCs. They are not eligible for VAT relief on the construction of new buildings, for example clubhouses, pavilions, changing rooms etc. They are therefore not entitled to issue zero-rating certificates to builders on the construction of buildings, even for non-business purposes.

HMRC release 15 June 2016

2.12 Other supply problems

2.12.1 Tax point?

A company (J) agreed to sell a car to a corporate customer (A) for £7,200 in September 2013. The consideration was paid in two instalments in that month, but the car was returned in October because the customer was not satisfied with it. The consideration was not returned; instead, J agreed to replace the vehicle, once it had found a suitable replacement. This was done in September 2014. The issue before the Tribunal was whether the output tax on the £7,200 should have been included in the VAT return for October 2013, and whether a penalty was due for failing to do so.

The Tribunal examined the investigating officer's account of the discovery of the receipt, and the company's evidence. It accepted as facts that the company had agreed to take the car back and had recognised a liability to refund the proceeds in its October 2013 accounts; it had set off that liability against the sale value of the second car.

The Tribunal accepted that the sale had been cancelled. The output tax was therefore not due. There was a potential argument that the documentation produced to reflect this was not a valid credit note, but HMRC confirmed that it was not their policy to pursue penalties on a mere deficiency in paperwork where the return was correct. There were undisputed errors in relation to the operation of the second hand goods scheme, but the amounts were below the levels at which HMRC regard penalties as "de minimis" and not to be collected (as set out in paragraph 2.5 of Notice 700/42 *Misdeclaration penalty and repeated misdeclaration penalty,* a penalty of no more than £300 or potential lost revenue of £1,000). The judge said she expected HMRC to apply this policy in this case.

First-Tier Tribunal (TC05150): *Japan MPV Motors Ltd*

2.12.2 TOGCs

HMRC have issued a Brief revising their policy on TOGCs involving the transfer of a business to a company in a VAT group, following the Upper Tribunal decision in *Intelligent Managed Services*. The transfer of a business to a company in a VAT group can be a TOGC for VAT purposes, provided the company intends to operate the same kind of business in supplying services to other group members, who in turn make supplies outside of the group. The Upper Tribunal's view was that the disregarding of the intra-group supplies did not change the basic facts that the transferred business continued to be carried on by the transferee. It did not liquidate the transferred assets but used them in its economic activity.

HMRC has also revised its policy on TOGCs involving transfers out of a VAT group. Where, were it not for the VAT grouping rules, a business exists, the normal TOGC rules apply to transfers out of a VAT group. This supersedes guidance in section 4.3 of Public Notice 700/9, which will be amended in due course.

The Brief notes the rule on self-supply of assets where a partly exempt group acquires a TOGC. This rule was not considered at all in the *Intelligent Managed Services* case, even though it appeared to provide HMRC with another way to charge a similar amount of VAT.

Where SDLT has been paid on a VAT-inclusive value in the past that could now be regarded as a TOGC, HMRC invite businesses to request a repayment.

The Brief also discusses transfers of business to a person not established in the UK. For the TOGC rules to apply, the buyer has to be a taxable person, which means they must be registered or required to be registered at the time of the transaction. Where the buyer of a business is not established in the UK and not required to be registered, HMRC will take the view that a voluntary registration must be in place at the time of the transaction. If the purchaser expects to make a taxable supply in the UK in the 30 days following the TOGC, the absence of any registration threshold for non-established persons will make them compulsorily registrable at that time.

R&C Brief 11/2016

2.12.3 Local authority searches

HMRC had planned to require local authorities to charge output tax on CON29 and CON29O searches with effect from 4 July 2016. They have now deferred this to a date yet to be announced. The Law Society had questioned in May 2016 whether these searches were properly chargeable to VAT.

Law Society, 10 June 2016

3. LAND AND PROPERTY

3.1 Exemption

3.1.1 Wedding packages?

A hotel had a room that was licensed for carrying out civil wedding ceremonies. Customers could hire the room separately from the other facilities for wedding receptions supplied by the hotel. The hotel treated the hire of the ceremony room as exempt, while the rest of any services supplied were treated as standard rated catering. HMRC ruled that the whole supply was standard rated and assessed the hotel for £54,610 for periods from 09/09 to 12/12.

HMRC put forward two arguments: either the supply of the room was part of a single "wedding package", and it could not be given a separate liability; or else it was part of a composite supply of which the principal supply was the catering. They accepted that the hire of the ceremony room on its own was exempt, but wherever it was supplied to someone who also used the hotel for a wedding reception (which appears to be on most occasions), it would be standard rated.

The company argued that the facts differed from earlier cases on the subject of wedding facility hire. The room for the ceremony was supplied without any other facilities; it was not artificial to regard it as a separate supply. It was a genuine exempt licence to occupy land. If it was part of a composite supply, it was the predominant element: if there was no ceremony, there was no wedding.

The Tribunal considered that the elements of the package were closely linked to each other geographically, temporally, economically and from a marketing perspective. On the other hand, the wedding room was a legally separate supply, and people did buy the elements separately, or decide to buy them at different times. Separate prices were effectively charged, even though the total would be paid by the same people on the same invoice. The Tribunal did not consider that it would be artificial to treat the elements of the supply as separate, so they were not a single supply within *Levob*.

The Tribunal also considered the arguments about which was the principal supply. The significant differences in character between the supplies supported the conclusion that they were separate and distinct.

However, it was still necessary to consider whether the separate hire of the wedding room was an exempt supply. The Tribunal noted that HMRC had accepted this in situations where there was no supply of catering in addition, and seemed to doubt whether that was correct. Confining itself to the supplies which were under appeal, the Tribunal noted that the wedding regulations required that the public could not be excluded from a place where a legal wedding ceremony was being performed. That raised the question of whether it was truly a licence to occupy land. However, the key point was that the room was provided with the licence to carry out a lawful wedding: it was a facility or opportunity that went beyond the passive letting of land, similar to the opportunity to participate in a fair in *International Antiques & Collectors Fairs* (TC04538).

The appeal was dismissed.

First-Tier Tribunal (TC05078): *Blue Chip Hotels Ltd*

3.1.2 Article

In an article in *Taxation*, Neil Warren considers practical problems that may arise from transactions in property, giving examples of situations in which wrong advice led to problems for taxpayers.

Taxation, 14 April 2016

3.2 Option to tax

3.2.1 SIPP sale

In TC03770, the FTT held for HMRC in a dispute about belated notification of an option to tax. A couple purchased a property from a pension fund, which stated that it had opted to tax. The VAT on the consideration was placed in escrow while the purchasers appealed, as third parties affected by the decision, to the FTT. The price was stated in the contract to be "£650,000 plus VAT if applicable".

The property had been purchased by a self-invested pension plan (SIPP) on 30 March 2004. The members of the SIPP were a dentist and his wife; they were granted a 15 year lease to use the property for the business of a dental practice on 31 March 2004. Dr Patel died in September 2010, following which the sale of the property was contemplated. This was completed in December 2011.

On 12 July 2010, the SIPP trustees wrote to HMRC to make a belated notification of an option to tax, which they claimed should have taken effect from 14 April 2004. The letter stated that no exempt supplies had been made with the property up to that date. VAT had been charged to the dental practice from the outset. The practice had suffered irrecoverable VAT on the rent, but it appears that the dentist was aware of the cash flow benefit of being allowed to opt and recharge the VAT over the length of the lease.

Following correspondence, in which the possible problem of exempt supplies between 31 March and 14 April 2004 necessitating a "permission option" was considered, HMRC accepted the belated notification of an option which was to have effect from 31 March 2004.

As a preliminary issue, the Tribunal agreed at a late stage to an adjournment to consider several late arguments, and also to a late reassignment of the case to the "complex" category. This was unusual, but the Tribunal agreed that it would have been so classified if the point had been raised at the outset.

The appellants argued that the sale was exempt on a number of grounds. The first was that the SIPP trustees held the property as trustees for the dentist's widow, and therefore sold it on her behalf. She had not opted to tax the property. This appears to be the effect of Sch.10 para.40 VATA 1994.

The second ground was that HMRC's prior permission was required before an option could be exercised, and it had neither been sought nor validly given. The anti-avoidance provisions ought to have been applied to the lease to the dentist's practice, because it represented exempt use by someone who had financed the development. Because the SIPP trustees would have known that their future supplies would have been exempt, they should have asked for permission.

HMRC responded that para.40 did not apply to the present situation. The case of *Nell Gwynne House* had considered the predecessor provision, and held that it applied in a situation where the legal title was separated from the beneficial ownership. In this case the trustees were making the sale for the benefit of the widow, but not in the same sense: they would hold the proceeds on trust for her, but they were not "bare trustees" or mere nominees. There were arguments about the rule in *Saunders v Vautier* that a sole beneficiary of a trust can be treated as absolutely entitled to the trust property.

On the prior permission issue, HMRC argued that the original version of Sch.10 made it clear that permission was required if the intention was to make exempt supplies at a time before the option was to take effect. In this case, the exempt supplies would take place after the option, which would mean that prior permission would not be needed. It was clear that the trustees had never intended to make any exempt supplies – they had charged VAT on all the rent paid by the dentist's practice. The notification was late, but that did not mean that there had ever been an intention to make exempt supplies.

The FTT agreed with HMRC that para.40 applies to a bare trust, not to the situation in the present case. The trust law points were arguable, but the evidence did not support the view that the widow had acted as the beneficiary of a bare trust.

The FTT also decided to consider whether there was evidence that the trustees had taken a decision to opt from 30 March 2004 or from 14 April 2004. The FTT considered that the evidence was that they had; the initial attempt to apply for belated notification was misguided, in that it gave the wrong date, but it appeared that the intention had always been that all the supplies would have been taxable.

The FTT considered very briefly the possibility that the anti-avoidance provisions applied: "Although it was common ground that the property was a capital item and that Mrs Patel was connected with the Trustee for the purposes of Schedule 10, it is clear from the facts that the anti-avoidance provisions of paragraphs 12-17 were not applicable." This appears to be based on the view that Mrs Patel was not a "development financier" of the land.

As a result, the appeal was dismissed.

The disapplication provisions were held to apply to a SIPP in *Winterthur Life UK Ltd (No 2)* (VTD 15,785). The tenants of a commercial property were insurance brokers whose pension contributions had funded the purchase of the property. That was enough in that case to make them "development financiers" and trigger the disapplication rules. The case was not referred to in the FTT, so it is not clear whether it was raised in argument.

The taxpayers appealed to the Upper Tribunal. The UT noted that there had been three issues before the FTT – whether the trustees or Mrs Patel made the grant; whether the grantor had really opted to tax; and the question of prior permission. Only the third was argued in the UT; however, HMRC introduced a further argument which the appellants agreed should be determined, namely the question of whether HMRC had the power to give a dispensation for the option to be applied without permission having been asked for.

HMRC accepted that the disapplication rules could apply to the supplies by the SIPP to the Patels. However, they would not apply to a supply to an unconnected exempt business such as that operated by the purchasers of the property. The UT agreed: the FTT had erred in failing to appreciate that the anti-avoidance provisions applied. The question, then, was whether the exempt supplies arising after 30 March 2004 as a result of the disapplication meant that permission was required.

The judges considered that the effect of Sch.10 para.3(9) (as it was written at the time) was that prior permission was required if exempt supplies had been made before the option was intended to have effect. The option was intended to have effect from 30 March 2004; the exempt supplies to the Patels could only take place after that date, because the lease was granted to them on 31 March 2004. The construction placed on this provision by the appellant's counsel – that it referred to exempt supplies made or intended to be made, where the intention fell before the option but the exempt supplies might fall afterwards – was described as "strained". The UT therefore reached the same conclusion on this point as the FTT, but having properly considered the anti-avoidance rules.

The argument about the "dispensation" was dealt with briefly, because it was not strictly necessary after the permission issue had been decided for HMRC. The appellants argued that HMRC should not have effectively absolved the trustees from the consequences of a mistake (recovering input tax when they should not have done) where HMRC were out of time to correct it. Doing so offended against the principles of legal certainty and protection of legitimate expectations. The judges did not agree: at the time of the purchase, it appeared that the trustees and Mrs Patel considered that the sale would be taxable, and no representations to the contrary had been made to the purchasers by HMRC. There was therefore no legitimate expectation that the transaction would not be taxed.

The appeal was dismissed again.

Upper Tribunal: *Hills and another v HMRC*

The Upper Tribunal had a separate hearing to consider an application for costs by HMRC. There were several issues. Costs in the UT followed the result, so HMRC were in principle entitled to an award. They claimed £25,000, which the appellants disputed. The judge decided this should be assessed by the Senior Courts Costs Office.

The FTT had made a costs award on the basis that the case had been recategorised as "complex" at the beginning of the hearing. In a complex case, costs follow the result even at the FTT. The appellants had sent an e-mail to the FTT seeking to opt out of the costs regime, as they were entitled to do, but it had apparently not been given to the panel or to HMRC until much later. HMRC objected, because the categorisation as

complex had been requested by the appellants and they had at that time stated that they would not opt out of costs. The judge examined the rules and the conduct of the parties and concluded that the opt-out would give rise to an injustice. This meant that it was ineffective under the regulations, and the costs order was valid. If he was wrong on that point, he would have found the opt-out to be unreasonable behaviour, which would also trigger costs in the FTT. However, he did not consider the appellants' behaviour unreasonable in relation to the rest of the conduct of the appeal, even though they lost. So the costs in the FTT should be awarded on the standard basis from the date of the recategorisation as complex.

Upper Tribunal: *Hills and another v HMRC*

3.3 Developers and builders

3.3.1 Charitable certificate

A NHS Trust had constructed a secure mental health unit. HMRC ruled in July 2011 that it was to be used "as a hospital or similar institution" and was therefore not eligible for zero-rating as a relevant residential purpose. The Trust appealed, arguing that it satisfied paragraphs (b) and/or (g) of Note 4, and was therefore constructed for a RRP:

(b) a home or other institution providing residential accommodation with personal care for persons in need of personal care by reason of old age, disablement, past or present dependence on alcohol or drugs or past or present mental disorder;

(g) an institution which is the sole or main residence of at least 90 per cent of its residents,

except use as a hospital, a prison or similar institution or an hotel, inn or similar establishment.

HMRC clarified in their skeleton argument that the only problem was the "except use as a hospital" exclusion; if it were not for that, the Note would have been satisfied.

There is no statutory definition of the word "hospital" specifically for the purposes of VAT. Both counsel argued about the rules of construction relating to exemptions: they must be strictly construed, but not so as to deprive them of their effect. The judge stated that the following propositions were derived from the authorities cited by the parties (in particular *Customs v Fenwood Developments Ltd*):

(i) The starting point should be the ordinary usage of the English language;

(ii) In the absence of a statutory definition of "hospital or similar institution" other statutes do not assist;

(iii) Superficial similarities are not enough to bring the exception into play and care must be taken not to construe the provision so as to render the exemptions in Note 4 ineffective;

(iv) The relevant words must be construed in the appropriate context by application to the facts.

The key feature of a "hospital", according to precedent, is that its main aim is the treatment and medical care of patients. The main area of contention in this case was whether the care provided at the unit affected the residents' illnesses through treatment, rehabilitation and mental health nursing, so that it would fall within the meaning of a "hospital or similar institution".

The judge was satisfied that the unit was more engaged in helping residents to manage their illnesses over a usually extended period. It was not the case that the provision of any treatment at all would change a RRP building into a "hospital or similar" – the example was cited of a residential care home for the elderly where dementia medication might be administered. The level of mental health nursing at the unit constituted "personal care" in the context of these residents, and did not cross the line into medical treatment.

The appeal was allowed.

First-Tier Tribunal (TC04998): *Pennine Care NHS Trust*

3.3.2 Bedsits

A company purchased a commercial property with the intention of converting it to residential accommodation. It claimed £45,000 on the purchase. HMRC enquired into the repayment return and accepted the deduction on the basis of an intended supply under VATA 1994 Sch.8 Group 5 item 1(b).

In the event, the building was converted into a residential property with multiple occupancy (bedsits). HMRC ruled that the sale of this property was exempt, so there would be a clawback of the input tax claimed and the company would be deregistered. The company appealed against both parts of this decision.

The issue before the Tribunal was whether the building consisted of "self-contained living accommodation" (Group 5 Note 2(a)). The Tribunal noted a discussion of the question in HMRC's manuals at VCONST14120, where bedsits are not regarded as self-contained because they share facilities with other bedsits in the same building. Tribunal decisions on the issue included *Agudas Israel Housing Association* (VTD 18,798), *Oldrings Development Kingsclere Ltd* (VTD 17,769) and *SA Whiteley* (VTD 11,292).

The Tribunal considered that the question did not depend on a consideration of the individual bedsits, but rather on the building itself. "*The issue, therefore, is whether a property with multiple occupancy can be a dwelling within the zero-rating provisions of Item 1(b) Group 8 of schedule 8 VATA.*" Judge Brooks considered that there was nothing in Group 8 to exclude such a property. Although a zero-rating provision had to be interpreted strictly, it was in line with the purpose of the legislation to provide relief for the cost of new dwellings.

The appeal was allowed.

First-Tier Tribunal (TC05193): *Capital Focus Ltd*

3.3.3 Construction of dwelling

HMRC refused zero-rating on some construction work. The VAT at issue was £40,069. The Tribunal noted that the planning consent was not included in the appellant's bundle of evidence, and this might have counted against them; however, they were not tax experts, so they were directed to produce the documents after the hearing, which they did.

The project involved the demolition of a coach house. Two walls were retained as required by the council; the company argued that extra walls had been constructed inside these outer walls, so they ceased to be part of the building but rather were part of the perimeter. If they were part of the building, they were two facades required to be retained by planning consent.

The judge noted that no precedents were cited by either side. He said he had carried out his own researches and discovered the 2015 UT decision in *Astral Construction Ltd*, which he regarded as a relevant and binding precedent. He was surprised that HMRC's representative did not mention that there was such a relevant case. He also referred to the discussion of the purpose of Group 5 as discussed in *TGH (Commercial) Ltd* (TC04581). This would provide a useful "cross-check" of the decision.

The judge identified the key issue as whether there had been an "enlargement, extension or reconstruction" within Note 16, and if so, whether it fell within the "facade" rule of Note 18. HMRC did not argue for enlargement or extension, but considered that there had been a reconstruction. After examining the precedents of *Wimpey*, *Marchday*, *Penwith* and *Astral* in detail, and regarding the question as one of fact and degree, the Tribunal concluded that this was the construction of a new dwelling, not the reconstruction of an existing building.

The Tribunal went on to consider Note 18 in great detail, even though it was not strictly necessary as Note 16 was satisfied. The judge considered the history and purpose of the provision, and commented that the drafting was poor – if applied literally, it was hard to see how it could ever apply to a construction project. In this case, the judge accepted that what was retained constituted "facades" and the house was "a corner site", even though the side wall did not face a street (disagreeing with the recent Tribunal in TC04980 *Reeves*). However, the mere fact that the walls were shown as retained on the approved plans was not enough to make them required as a condition of planning consent (following *Boxmoor*).

The appeal was allowed on the basis of *Astral Construction* and Note 16.

First-Tier Tribunal (TC05087): *J3 Building Solutions Ltd*

3.3.4 Self-supply charge

Balhousie Holdings Ltd (BH) was the holding company of Faskally Care Home Ltd (F), the subject of a separate appeal about economic activity (TC05133, reported in section 5.1). BH operated some 25 care homes in the north-east of Scotland and was registered as a VAT group with subsidiaries that carried on related activities. The dispute related to a sale-and-leaseback arrangement in which a care home, constructed under the zero-rating provisions for RRP properties, was transferred to a Real Estate Investment Trust (REIT). HMRC considered that this triggered the self-supply charge on a change of use under VATA 1994 Sch.10 para.37.

The assessment was for over £800,000 of VAT, together with interest and an inaccuracy penalty – described as "potentially business ending" by the company's accountants.

BH argued that it did not fall within the legislation because it had not disposed of its "entire interest" in the property, as required by para.36(2). The sale of the property was inextricably linked to the leaseback. It was clear that BH would continue to use the building for residential purposes after the transactions, so the "mischief" that the legislation was aimed at had not occurred.

HMRC responded that the sale transaction was the "first grant of a major interest" by BH. It could not qualify for zero-rating because the grantee was not going to use it for a RRP; it was going to lease it back to BH. The transaction was therefore exempt, and that triggered the self-supply charge in Sch.10. It was necessary to look at each transaction separately, so it was not permissible to consider the sale and leaseback as part of a single whole.

There were references to numerous precedents from different taxes and legal contexts; to Notice 708, with each side putting a different slant on what the guidance meant and was supposed to mean; and to Hansard, with each side trying to discern the intention of Parliament when Sch.10 was rewritten in its current form.

The Tribunal considered that the taxpayer's arguments were stronger. The purpose of the legislation appeared to be to prevent tax avoidance where there was a change in the underlying use of the building, not where there was a funding arrangement such as a sale and leaseback. It was appropriate to interpret the legislation according to what appeared to be its purpose: that required the Tribunal to regard the sale-and-leaseback as a single indivisible whole. In that light, the company had not disposed of its entire interest, and the legislation did not bite. The appeal was allowed.

First-Tier Tribunal (TC05131): *Balhousie Holdings Ltd*

3.3.5 Protected building

A building company carried out various works to a protected building in periods 06/12, 09/12, 12/12 and 03/13. After initially accounting for output tax at the standard rate, it made a voluntary disclosure to recover some of this for the first two periods. HMRC subsequently issued clawback assessments in respect of these repayments, and assessments for underpaid output tax in the second two periods.

There were several issues:

- whether the supplies were "repairs and maintenance";
- whether they were carried out after 30 September 2012 and not eligible for transitional relief;
- whether there were supplies of insulating material that were eligible for the lower rate under Sch.7A Group 2;
- whether supplies in respect of an outbuilding qualified for zero-rating on the basis that it was not a "dwelling" in its own right.

The Tribunal examined the works and concluded that most, but not all, were repairs and maintenance. There was also no evidence of a contract

or planning consent before 21 March 2012, so the works should be time apportioned to apply zero-rating only to the pre-30 September 2012 portion (given that there was no better evidence capable of providing a more precise split).

At the hearing, HMRC conceded that the insulation supply qualified for the lower rate. Their earlier refusal to accept this had been based on a mis-reading of the legislation.

In accordance with the House of Lords decision in *Zielinski Baker*, the works to the outbuilding did not qualify. The planning consent in relation to that building stated that it could not be occupied or disposed of separately from the main building, so it was not a dwelling in its own right.

The appeal was allowed to a small extent.

First-Tier Tribunal (TC05127): *C Neary Ltd*

3.3.6 Conversions

HMRC have issued a Brief to clarify the conditions for zero-rating and lower rating where an individual takes advantage of "permitted development rights" (PDRs) to convert a non-residential building into a dwelling. The problem is that a DIY claim, or a lower rate charge by a builder on conversion services, relies on the claimant being able to prove that the development was lawful; in the past this has usually involved applying for a formal planning consent, but if that is no longer necessary in all circumstances, different conditions will have to be applied.

The Brief sets out the background to PDRs and explains that they may operated differently in different parts of the country, because they constitute a devolved matter.

HMRC will continue to require evidence to be produced that the work is lawful in order for the zero or reduced rate of VAT to apply or for a claim to be eligible under the DIY scheme. Where the builder, developer or DIY claimant establishes that the conversion is covered by a PDR and individual statutory planning consent is not required, they must be able to evidence it by at least one of the following:

a) Written notification from the local planning authority (LPA) advising of the grant of prior approval; or

b) Written notification from the LPA advising that prior approval is not required; or

c) Evidence of deemed consent (i.e. evidence that the claimant has written to the LPA and confirmation that no response has been received from them within 56 days, following which consent is deemed to have been given) and evidence that the development is a permitted development. This will include all of the following (where the documents have been created): plans of the development, evidence of the prior use of the property (e.g. evidenced by its classification for business rates purposes etc.), confirmation of which part of the planning legislation is relied upon for the development, and a lawful development certificate where one is already held.

Developments carried out under a PDR must still meet the appropriate building standards. Should any circumstances arise where building control is not required, evidence from the local authority confirming this should be provided.

Revenue & Customs Brief 9/2016

3.4 Input tax claims on land

3.4.1 DIY claim fails

An individual made a claim for £31,833 under the DIY scheme. HMRC refused it on the basis that the planning consent prohibited use as a sole or main residence, restricting use to short-term holiday accommodation. It appeared that the property would be rented out, constituting a business use for VAT, and therefore a DIY claim was not permitted.

The individual asked for a review and subsequently appealed, arguing that his intention had changed during the course of the project and the conditions had been removed. He now occupied the property as his family home. He had never actually used it for any business.

HMRC argued that the removal of the conditions was retrospective, and precedent cases showed that this was not enough: the consent had to be current at the time the work was done.

The Tribunal went through the conditions for a DIY claim, and agreed with HMRC. At the time of the claim, the conditions had not been removed, which meant that he could not satisfy the requirements of the law. The appeal was dismissed.

First-Tier Tribunal (TC05128): *Richard Akester*

3.5 Other land problems

Nothing to report.

4. INTERNATIONAL SUPPLIES

4.1 E-commerce

4.1.1 Updated guidance

HMRC have issued an updated version of their guidance *Register and use the VAT Mini one-stop-shop for digital supplies*. It contains the following additional information about VAT groups:

If your business is part of a VAT group the group can register for UK VAT MOSS if any member of the group qualifies for the scheme. The representative member must register using the group's UK VAT number.

If you're a VAT group's representative member, when you register for VAT MOSS you must:

- *state you're the representative member*
- *quote your group's UK VAT registration number*

Put 'no' when asked if there are any fixed establishments in other member states. Any ties with establishments outside the UK are considered to be broken for VAT MOSS purposes. As a result, a group registered for VAT MOSS in the UK can only use it to declare sales of digital services to consumers outside the UK that are made by the group's UK establishments and it should be used for all such sales, whether or not the group has fixed establishments outside the UK. A VAT group should not enter details of any fixed establishments outside the UK when registering for VAT MOSS.

If any of your group members have fixed establishments in, or are based in other member states, these should register for VAT MOSS in the member state where they are established.

If you need further information on VAT groups within VAT MOSS, please email HMRC for advice.

The document also deals as before with registration, returns, payments, corrections and audit.

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

The replies to the Commission's consultation on modernising VAT for cross-border e-commerce have been published in the form of an Excel spreadsheet. It is expected that a more narrative analysis will be published in due course.

http://ec.europa.eu/taxation_customs/common/consultations/tax/index_en.htm

4.1.2 Exchange rates

HMRC have issued the usual data about exchange rates to be used by MOSS-registered traders in the quarter to March 2016.

VAT Information Sheet 2/2016

4.1.3 Greek VAT rate

HMRC have announced that the standard VAT rate for Greece rose from 23% to 24% on 1 June 2016.

VAT Information Sheet 3/2016

4.2 Where is a supply of services?

4.2.1 Apportionment of telecoms

Under VATA 1994 Sch.4A para.8, telecommunications services that are "used and enjoyed outside the EU" are outside the scope of VAT. A telecoms company agreed a method of apportioning its charges with HMRC: the apportionment was based on values, taking the proportion of charges for extra services consumed in and out of the EU and applying that to the basic network access charge to remove some of it from the scope of VAT (referred to as "the revenue methodology"). This had been applied from 2008 to 2014 with HMRC's agreement.

In November 2014 HMRC issued a decision that the method was not fair and reasonable: because the charges for non-EU extra services were higher than for those services consumed in the EU, use of values distorted the proportion. HMRC ruled that a different method, based on actual use (e.g. minutes), should be used instead (referred to as "the usage methodology").

The company challenged the decision by way of judicial review in the Upper Tribunal, arguing that:

- the usage methodology was contrary to EU and domestic VAT legislation as VAT is a tax on consumption based on value and not usage;
- the decision constituted a breach of the company's legitimate expectation, based on a clear assurance given by HMRC in 2008 that it could continue using the revenue methodology until there was a material change in the law or in the company's business, which had not occurred;
- the decision had been taken without adequate consultation to enable the company to explain to HMRC the fundamental difficulties inherent in the adoption of the usage methodology.

The UT found that there was nothing contrary to the law in the usage methodology. It is noteworthy that the partial exemption law specifies values as the basis for the standard method, but there is no such specification in the rules on place of supply. Either method could comply with the law.

The UT also found that HMRC had not in correspondence given any unqualified assurance that the company could use the revenue methodology forever. The company had itself proposed minor changes to the methodology during the period it was in use, which suggested that the company did not regard it as fixed and immutable. There was therefore

no legitimate expectation that could prevent HMRC issuing a new decision.

The UT commented that it was well established that there was no general common law duty to consult persons who could be affected by a measure before it was adopted, but such a duty might exist where a promise or practice had created a legitimate expectation of consultation. Even where there was no such expectation, there could be a duty to consult where an abrupt change of policy would be so unfair as to amount to an abuse of power. The financial benefit arising from the revenue methodology (several million pounds a year) gave the company sufficient interest to create a legitimate expectation that HMRC would not require it to use another methodology, substantially reducing that benefit, without consultation. However, the UT considered that HMRC had consulted properly: they had raised concerns about the revenue methodology as early as July 2013, and there had been substantial discussion and correspondence throughout the period leading up to the decision. The company had had adequate opportunity to make representations and explain why they could not implement the usage methodology.

The application for judicial review was refused.

Upper Tribunal: *R (oao Telefonica Europe plc and another) v HMRC*

4.3 International supplies of goods

4.3.1 Despatch requirements

The A-G (Henrick Saugmandsgaard Oe) has given an opinion on the rights of Member States to refuse exemption for intra-EU transactions. In line with earlier decisions, the opinion is that exemption cannot be denied where it appears that all the substantive requirements for exemption are met (despatch to a taxable person in another Member State) and there is no indication of tax evasion (agreed in this case), even though some of the formal requirements (taxpayer ID in the destination state) are not met.

The A-G considers that denying exemption goes further than would be proportionate in the circumstances. However, the Member State could levy a fine or financial penalty for non-compliance with the formal requirements.

CJEU (A-G) (Case C-24/15): *Josef Plöckl v Finanzamt Schrobenhausen*

4.3.2 New means of transport

The Portuguese court has referred questions about the rules for taxation of new means of transport. It seems that the Portuguese authorities have sought to collect VAT from a supplier in Portugal who has been given documentation by a customer to suggest that the car will be taken to Spain and registered there. The court is concerned that the conditions of the Portuguese law for effectively zero-rating the sale may be more stringent than the PVD allows.

CJEU (Reference) (Case C-26/16): *Santogal M-Comércio e Reparação de Automóveis Lda v Autoridade Tributária e Aduaneira*

4.3.3 Imports

Low Value Consignment Relief (LVCR) means that goods can be imported by post free of VAT. The limit for LVCR was £18 until 31 October 2011, after which it reduced to £11. There is a separate LVCR threshold for customs duties, set at the equivalent of €150. This was originally set at £105 but was later changed to £135. Certain importers are granted "low value bulk imports approval" (LVBI) to allow them to list a number of separate negligible value packages on the same C88 form.

Citipost was granted LVBI approval on 17 July 2009. Its understanding was that it was permitted to list any number of packages to the same recipient on a C88 without attracting duty, as long as each individual package was below the threshold. HMRC took a different view. On 22 January 2013, they issued a penalty of £2,500, followed by post clearance demand notes for VAT of £911,000 and £24,000 in relation to consignments to the same recipient on the same manifest that exceeded the limits in total, rather than individually. The company appealed.

The Tribunal (Anne Redston) set out the issues as follows:

(1) whether Citipost had failed to comply with the LVBI; and if so

(2) whether that failure caused a liability to import VAT to arise by way of a customs debt;

(3) if there was a customs debt, whether Citipost was the debtor;

(4) if Citipost was the debtor, whether the Tribunal has the jurisdiction to consider whether the debt should have been waived under Article 220(2)(b) of the Community Customs Code ("the Code");

(5) if the Tribunal does have that jurisdiction, whether the debt should have been waived; and

(6) whether the penalty charged should be upheld, set aside or reduced.

The Tribunal examined in detail the history of the company's application for the LVBI approval and its operation of the system. Although the documentation was potentially confusing, the rule was clear: the limit had to be applied to the total value in one consignment to a single recipient, and the company had failed to comply.

However, after exhaustive examination of the law on small consignments, the Tribunal concluded that this did not in itself create a customs debt. There was a mandatory exemption for individual parcels, so the VAT was not payable. The LVBI approval was an administrative measure; for failing to comply with its terms, there could be a penalty, but it should be reduced from £2,500 to £500.

Having found for the company on issue (2), the Tribunal considered issues (3) to (5) because they had been fully argued and there might be an appeal. The judge concluded that had HMRC succeeded on point (2), they would also have succeeded on points (3) and (5): Citipost was the declarant and would owe the customs debt; the Tribunal had jurisdiction to consider whether it should be waived, but would not have exercised that jurisdiction in the company's favour on the facts.

First-Tier Tribunal (TC05057): *Citipost Mail Ltd*

4.3.4 Quotas

In a case about import quotas, the Italian authorities argued that a company had undertaken an abuse of rights in relation to garlic bought from Argentina. The garlic was imported at a preferential rate of duty within an import quota. However, the company that wanted to import the garlic no longer had licences to import at the preferential rate; it therefore established a chain of transactions involving other companies with the appropriate licences, the end result of which was the same as if it had imported the goods directly at the preferential rate.

The CJEU concluded that this was not abusive: the law did not preclude the "mechanism" that the taxpayer companies had used.

CJEU (Case C-131/14): *Cervati and another v Agenzia delle Dogane and another*

4.3.5 Import valuation

The Hungarian authorities investigated a customs declaration by an importer in relation to some goods arriving from China. The company said it had declared the amount it paid for the goods, but did not provide any other detailed evidence to support that valuation as a proper basis for import duties; although the authorities did not contradict the validity of the invoice or question the veracity of the bank transfer, they carried out a sampling exercise on the basis of the prices of similar imported goods, and concluded that the valuation of HUF 2.59m should be increased to HUF 3.02m. The company appealed, and questions were referred to the CJEU.

The court ruled that the Customs Implementing Regulation did not preclude such an action: that is, it is permissible for the authority to levy import duty and VAT on the price of similar goods rather than the actual transaction value, where the declared transaction value was considered to be unreasonably low in comparison with the statistical average of the purchase prices verified in the context of the importation of similar goods.

CJEU (Case C-291/15): *EURO 2004. Hungary Kft v Nemzeti Adó- és Vámhivatal Nyugat-dunántúli Regionális Vám- és Pénzügyori*

4.3.6 Paperwork deficiencies

The CJEU has considered two cases in which the German authorities imposed a customs debt for import VAT because paperwork was not completed at the right time. The first concerned goods that had been entered into a customs warehouse and then re-exported out of the EU. The removals were not entered into the records until 11 to 126 days after they took place, contrary to the rules. The second concerned an external transit procedure that had not been completed in the allowed time, triggering a customs debt.

In both cases, the CJEU was satisfied that the goods had left the EU and there was no risk of them re-entering the economic network. No import VAT was therefore due in either case.

CJEU (Case C-226/14): *Eurogate Distribution GmbH v Hauptzollamt Hamburg-Stadt* and CJEU (Case C-228/14): *DHL Hub Leipzig GmbH v Hauptzollamt Braunschweig*

4.3.7 Free zones

The German court has referred questions to the CJEU about the operation of free zones for customs duties and VAT. It appears that German law provides that a free zone is not part of the territory of Germany; the question is how this interacts with the charging provisions in art.156, art.61 and art.71 PVD.

CJEU (Reference) (Case C-340/15): *Wallenborn Transports SA v Hauptzollamt Gießen*

4.3.8 New Customs Code guidance

HMRC have issued guidance on UK implementation of the new Union Customs Code from 1 May 2016, setting out the main changes to import and export procedures.

Customs Information Paper on Union Customs Code 31 May 2016

HMRC issued a Notice *Customs special procedures for the Union Customs Code* in April 2016 and have already updated it with a new version. It replaces Notices 200, 221, 232, 235, 237, 306, 308 and 770, and explains the legal basis and generic requirements of the Customs Special Procedures under the Union Customs Code (UCC). Detailed information on each special procedure can be found in the annexes.

Notice 3001

HMRC's paper *Import valuation procedures under Union Customs Code* confirms the withdrawal of the earlier sale facility for customs valuations of imports from 1 May 2016, with transitional arrangements continuing until December 2017 for contracts in place on 18 January 2016. Pending a review of the European Commission's draft guidance, no changes are required to the way royalty fees are currently treated.

Customs Information Paper 34/2016

4.3.9 Updated Notices

HMRC have issued a new version of their Notice *Imports*, updated to reflect introduction of the new Union Customs Code (EU Regulation 952/2013) on 1 May 2016. Telephone and fax numbers for the Banking Operations Central Deferment Office have been amended.

Notice 702

HMRC have issued a new version of their Notice *Valuation of imported goods for customs purposes, VAT and trade statistics*. Amendments to the notice include advice on the Union Customs Code (UCC) changes for earlier sales, royalty fees, sales from warehouse and the withdrawal of form C109A which was used to make a valuation statement.

Notice 252

HMRC have issued a new version of their Notice *Simplified import VAT accounting*, replacing the April 2010 version. It has been updated to reflect the new Union Customs Code. A further update was issued in June, incorporating minor changes to reflect the Union Customs Code.

SIVA is a scheme that allows traders to reduce the level of financial guarantee required to operate a duty deferment account for VAT purposes.

The objective of this scheme is to provide compliance cost savings for legitimate businesses by reducing the level of financial security required to guarantee the payments of import VAT. The Notice sets out the operation of the scheme and the approval criteria.

Notice SIVA 1

HMRC have withdrawn their Notice *VAT import customs procedures*. The information is now contained in Notice 3001.

Notice 702/9

HMRC have replaced the January 2016 *Guide for international post users*. It has been updated to reflect the reduction in the threshold above which a formal customs declaration is required from £2,000 to £750 (or €1,000). The de minimis limit (£7) for waivers of customs debt has also been removed, as this has also been removed from the Union Customs Code.

Notice 143

Similar amendments have been made to the Notice *Trade imports by post – how to complete customs documents*.

Notice 144

HMRC have replaced the February 2013 version of their Notice *Customs freight simplified procedures*. The main change reflects the clearance time for supplementary declarations having changed from 24 hours to 10 minutes, corresponding with the timeout period for other import entries.

Notice 760

4.4 European rules

4.4.1 Action plan

The European Commission has presented its action plan for a modernised EU VAT system. The high-level plan, on which more detail is expected by the end of 2016 and during 2017, includes:

- a future single EU VAT area with more fraud-proof collection system;
- short-term measures for exchange of information related to fraud;
- two options for giving member states greater flexibility over reduced rates;
- simplified rules for e-commerce as part of the digital single market strategy;
- a VAT package for SMEs.

The objectives of the reboot are to make the VAT system simpler, more fraud-proof and business-friendly. The current VAT rules urgently need to be updated so they can better support the Single Market, facilitate cross-border trade and keep pace with today's digital and mobile economy. The “VAT gap”, which is the difference between the expected VAT

revenue and VAT actually collected in Member States, was almost €170 billion in 2013 (15.2% of revenue). Cross-border fraud itself is estimated to be responsible for a VAT revenue loss of around €50 billion a year in the European Union. At the same time, the current VAT system remains fragmented and creates significant administrative burdens, especially for SMEs and online companies.

Among the proposals is allowing digital publications to enjoy the same reliefs as physical publications. In 2017, the Commission will present a VAT simplification package designed to support the growth of SMEs and to make it easier for them to trade across borders.

europa.eu/rapid/press-release_IP-16-1022_en.htm

Further detailed proposals include:

- extending the current One Stop Shop concept to all cross-border e-commerce, including distance sales;
- introducing common EU-wide simplifications measures to help small start-up e-commerce businesses;
- streamlining audits in this sector (home country audits);
- removing the VAT exemption for the importation of small consignments from suppliers in third countries.

ec.europa.eu/taxation_customs/taxation/vat/action_plan/index_en.htm

The Council has welcomed the action plan and has made a number of comments about the way forward. The last item on its list is a call on the Commission to permit reduced or zero-rating for women's sanitary products at the earliest opportunity.

www.consilium.europa.eu/en/press/press-releases/2016/05/25-conclusions-vat-action-plan/

4.4.2 Minimum VAT rate

Art.97 PVD provided that the standard rate throughout the EU cannot be less than 15%. That provision applied from 1 January 2011 to 31 December 2015. At 1 January 2016, only four countries had standard rates below 20%: Luxembourg (17%), Malta (18%), Germany and Cyprus (19%). There is no official maximum – the highest is Hungary (27%).

Council Directive 2016/856 confirms that the minimum standard rate must be not lower than 15% from 1 January 2016 to 31 December 2017.

Official Journal of the European Union 31 May 2016

4.4.3 Vouchers

The Council has adopted an amendment to the PVD to regularise the treatment of vouchers throughout the Member States. It will have to be incorporated in national law and will apply to vouchers issued after 31 December 2018. It broadly provides for VAT to be accounted for at issue for single-purpose vouchers and at redemption for multi-purpose vouchers. It does not apply to discount vouchers.

www.consilium.europa.eu/en/press/press-releases/2016/06/27-agri-vat-rules/

4.4.4 Italian rules

The full court has agreed with the A-G's opinion, reported in the last update, that the Italian tax authorities were entitled to enter into a compromise with a VAT debtor and accept less than full payment, provided that this was authorised by a court and it could be shown that no less VAT would be collected than would be the case if the full amount was pursued in a liquidation. This is consistent with the Commission's recommendation that Member States should remove barriers to the effective restructuring of viable companies in financial difficulties.

CJEU (Case C-546/14): *Degano Trasporti S.a.s. di Ferruccio Degano & C., in liquidazione*

The Italian court has referred another question on what appears to be a similar issue. It asks whether extinguishing VAT debts as part of a bankruptcy discharge procedure is compatible with a country's obligations under the EU Treaty and the VAT Directive. It seems likely that the above judgment will be the basis for the court's answer in due course.

CJEU (Reference) (Case C-493/15): *Agenzia delle Entrate v Marco Identi*

4.4.5 Valuation of self-supply

In March 2004, a Netherlands company entered into a 20-year lease over a plot of land and a part-completed building. Under Netherlands law, the grantor's output tax was based on the capitalised present value of future rent. This was paid by the company to the grantor and deducted on its VAT return. The company then paid for completion of the building, again paying and deducting VAT; and paid the first annual ground rent. On 1 June 2004 the company granted leases over parts of the building, some of which were opted and some of which were not. As this involved partial exempt use of a building on which the company had deducted all its input tax, a self-supply charge arose on the "cost price" of the building, some of which would not be deductible.

The authorities took the view that the self-supply charge should be based on the full amount of the capitalised rent, plus the cost of completion. The company argued that it should only be the cost of completion plus the first year's rent that it had paid. The Netherlands courts did not agree on the point, and questions were referred to the CJEU.

The taxpayer argued that there would be double taxation. The CJEU rejected this: where VAT had been paid but had immediately been deducted in full, there would be no double taxation in including the same amount in the self-supply charge. There was nothing in the Directive to exclude the capitalised value of the future rent from the self-supply charge, because it had been deducted in full.

However, the value should be calculated at the time that the grant leading to the self-supply took place (i.e. 1 June 2004). The initial capitalised value had included the rental payment that had now been paid; presumably the judgment means that the value should be recalculated on the same basis as the original VAT charge, but excluding that payment and adjusting the period over which the value is worked out.

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

4.4.6 Infringement

The CJEU has ruled that the Netherlands rules on exemption for sporting supplies does not comply with the PVD, in particular in connection with water sports. It seems that exemption in the Netherlands depends on the organisation only using volunteers rather than paid employees, which goes beyond the requirement of the Directive for "non-profit bodies". On the other hand, the Netherlands extends exemption for letting of berths and moorings beyond what is provided for in the Directive. Infringement proceedings followed a reasoned opinion sent to the Netherlands by the Commission.

CJEU (Case C-22/15): *European Commission v Kingdom of the Netherlands*

4.4.7 Reverse charge rules

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

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

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

The full court agreed with the opinion. Art.198(2) did not define the type of material to which it applied except by reference to the gold content; these bars were considerably above the threshold stated in the article, so they were properly covered by it. If the law was more restrictively applied, it would not achieve its purpose in preventing fraud and evasion.

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

4.4.8 Public broadcaster

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, which the UK regards as outside the scope).

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. Note that the BBC is included in s.33 VATA 1994 as a public body eligible to recover VAT incurred on non-business activities.

The CJEU has agreed with the opinion in respect of the output tax side – the income is outside the scope of VAT. As the input tax side was not part of the question for reference, the conclusion to that argument has to be inferred from the outcome on output tax.

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

4.4.9 Sale below cost

A Netherlands local authority ordered the construction of two buildings, and deducted the VAT incurred on the cost. It then sold the buildings to a purchaser for 10% of the cost, the amount owing being converted to an interest-bearing loan. The purchaser was a Foundation which granted use of part of the buildings to special schools for no consideration, and granted leases to other tenants for consideration. The authority charged VAT on the sale proceeds.

The tax authority regarded the effect of the transactions between the local authority and the Foundation as a lease that ought to be treated as exempt, and sought to claw back the input tax claimed on the construction. Questions were referred to the CJEU.

It was accepted that the local authority was a taxable person. It had sold the building in an economic transaction, and the subsequent use by the Foundation could not affect the seller's right to deduct input tax under art.168. The CJEU has consistently held that selling at below cost does not lead to any restriction on input tax claims.

There is a reference in the decision to art.80 (the provision that allows outputs to be recalculated on market values to prevent avoidance and abuse), but the court does not appear to consider its possible application. There is an implication that the tax authorities might have had more success trying to collect more output tax rather than disallowing input tax, but the conditions for a direction in line with s.80 might not be met. The court did not consider the arrangement to constitute an abuse of rights.

CJEU (Case C-267/15): *Gemeente Woerden v Staatssecretaris van Financiën*

4.4.10 Charge on cessation

A Polish notary incurred VAT on the construction of a building that was used partly for private and partly for business purposes. He only claimed a deduction for the business element. The building was subject to the capital goods scheme. He asked for a ruling on whether the business element of the building would be subject to an output tax charge on the cessation of his economic activity, even though the CGS adjustment period for the building had expired. Questions were referred to the CJEU.

The opinion of Advocate-General Kokott is that the rules on taxation of private use and the rules on adjustment of input tax deduction have similar objectives, but they are independent of each other and are to be applied separately. If there was a risk of double taxation in the application of both rules, that should be taken into account in order to preserve fiscal neutrality; but the A-G did not consider that there was any double taxation in the present case. The rules on the cessation charge provided that there should be no output tax if there had been no input tax deduction; in this case, the input tax would have been deducted, so the charge on cessation was a single charge that would reflect private use after cessation.

CJEU (A-G) (Case C-229/15): *Minister Finansów v Jan Mateusiak*

4.4.11 Horse-racing

An individual ran a racehorse training stables. Her income was derived partly from prize money won by her own horses, and partly by fees charged to other owners for looking after their horses and preparing them for races. There were three points of dispute for the CJEU to resolve:

- whether she was entitled to full deduction of her input tax;
- whether her own prize-money income was subject to output tax;
- whether a lower rate of output tax could be applied to the stabling fees under point 14 Annex III PVD ("use of sporting facilities").

Advocate-General Wahl has given an opinion that the trainer is involved in economic activity and is therefore in principle entitled to full input tax deduction. The conclusion would be different if she entered her own horses in races merely as a hobby, but this did not appear to be the case.

This is related to the further opinion that prize money is a VATable output, even if it depends on factors that are not entirely within the control of the parties. The A-G considers that prize money is similar in nature to a competition entry fee or an appearance fee, and should therefore be taxed in the same way. He gives an example to illustrate the point: if someone instructs several estate agencies to try to sell a house, all will "enter" by advertising it, but generally only the one that succeeds in selling the house will get paid. That does not stop the payment from being consideration for a supply of services.

On the third issue, the A-G considered that point 14 of Annex III principally referred to the use of sporting facilities by individuals. The service supplied by the trainer was a complex supply that could not be broken down into constituent parts; it did not appear appropriate to characterise it as falling within point 14, because elements of the supply

that did not fit the description "use of sporting facilities" were too important as part of the whole.

CJEU (A-G) (Case C-432/15): *Odvolací finanční ředitelství v Pavlína Baštová*

4.4.12 Transfer to public authority

The Polish court has referred a question to the CJEU about the transfer of land by a taxable person to the State or to a local authority in settlement of arrears of tax. The question is whether it constitutes a "supply of goods for consideration"; presumably it is a supply, but there is doubt about whether "cancelling a tax debt" constitutes consideration, when paying tax is not consideration for any supply by the State or the local authority to the taxpayer.

CJEU (Reference) (Case C-36/16): *Minister Finansów v Posnania Investment SA*

4.4.13 Conditions for exemption

The Portuguese court has referred questions to the CJEU about the refusal of exemption for despatches. The Portuguese seller was aware that the customer was registered for VAT in the other member state, but was not included in the VIES database and was not subject to the local system of taxation for intra-community acquisitions. Nevertheless, the purchaser was registered for VAT and the formal and substantive conditions for exemption of a despatch appeared to be satisfied – the VRN was included on the invoice, ownership was transferred and the goods left Portugal. The seller claimed to be convinced that the purchaser would retroactively be registered as an intra-community operator. The Portuguese authorities have ruled that exemption does not apply.

CJEU (Reference) (Case C-21/16): *Euro Tyre BV v Autoridade Tributária e Aduaneira*

4.4.14 More electronic books

The Polish court has referred a question about fiscal neutrality and the exclusion of electronic books from lower rating. This seems to be a rerun of the case of *K Oy* (Case C-219/13), but it raises a procedural challenge to the legislation in that apparently the European Parliament was not consulted when point 6 of Annex III PVD was added in 2009.

CJEU (Reference) (Case C-390/15): *Rzecznik Praw Obywatelskich (RPO)*

4.4.15 Cost-sharing

The Polish court has referred a question about the exemption for "independent groups of persons" (cost sharing), asking about the conditions that ought to be included in national law to implement art.132(1)(f) PVD. It seems that Polish law does not have any conditions about distortion of competition. The questions ask also for guidance on applying the principle of distortion of competition, and on the relevance of cross-border transactions to the cost-sharing exemption.

CJEU (Reference) (Case C-605/15): *Minister Finansów v Aviva Towarzystwo Ubezpieczeń na Życie S.A. w Warszawie*

Meanwhile, the Commission has applied to the CJEU for a ruling that the German law on cost-sharing does not comply with the Directive. German law restricts the cost-sharing exemption to groups from the health and medical sector; the Commission argues that no such restriction is provided for in the PVD, so it is not allowed. A reasoned opinion was sent to Germany in April 2011, but no amendments were made to the German law.

CJEU (Application) (Case C-616/15): *European Commission v Federal Republic of Germany*

4.4.16 Loading and unloading

The Finnish court has referred questions about services supplied in relation to loading and unloading of cargo. This can qualify for exemption as an international service. It appears that the appellant in the case is a sub-contractor supplying a local business that makes an onward supply to the transporter, and the court is not sure whether this constitutes an "indirect export" that would have to be charged to VAT by the subcontractor, or is a service that "meets the direct needs" of the cargo or the vessel. The reference cites the case of *Elmeka* (Cases C-181/04 – C-183/04) as authority for the proposition that exemption cannot be extended to transactions earlier in the supply chain.

CJEU (Reference) (Case C-33/16): *A Oy*

4.4.17 Business splitting?

The Austrian court has referred questions to the CJEU about the status of an association of wine-growers with independent operations who trade under a common trade mark through a limited company whose shares are held by them. It appears that the business is operated by a family through several partnerships and a marketing company; the Austrian authorities want to regard them as a single taxable entity. The questions extend to whether the effect of a finding that the traders should be combined would be retrospective or for the future only.

CJEU (Reference) (Case C-340/15): *Christine Nigl and Others*

4.4.18 Blood and plasma

The German court has referred questions to the CJEU about the application of the exemption for supplies of human blood. The subject matter of the disputed transactions is blood plasma obtained from human blood; this may be used for therapeutic purposes, but may also be used to manufacture medicinal products. The questions are whether plasma is covered by the exemption at all, and if so, whether the intended use of the plasma makes a difference.

CJEU (Reference) (Case C-412/15): *TMD Gesellschaft für transfusionsmedizinische Dienste mbH v Finanzamt Kassel II — Hofgeismar*

4.4.19 Second-hand goods

The Danish court has referred questions to the CJEU to determine whether the sale of spare parts removed from scrapped vehicles can be included in the margin scheme for second-hand goods.

CJEU (Reference) (Case C-471/15): *Sjelle Autogenbrug I/S v Skatteministeriet*

4.4.20 Inactive supplier

The Romanian authorities published a list of "inactive suppliers" that had been deregistered for VAT purposes on its website. It denied the appellant the right to deduct input tax on an invoice issued by a company included on this list. Questions have been referred to the CJEU to find out if this is sufficient reason to disallow the VAT, or whether the authorities would need to do more, given that the appellant claimed not to be aware that the provider had been declared inactive.

CJEU (Reference) (Case C-101/16): *SC Paper Consult SRL v Direcția Regională a Finanțelor Publice Cluj-Napoca, Administrația Județeană a Finanțelor Publice Bistrița-Năsăud*

4.4.21 Reciprocal benefit

Bulgarian law restricts an input tax deduction where someone supplies improvements to a property in circumstances in which the owner of the property may enjoy some benefit from the improvements without charge. It appears that the case may involve "tenants' improvements", where the tenant is claiming input tax deduction on the basis that it uses the property in its business, even though technically the improvements belong to the owner of the property.

CJEU (Reference) (Case C-132/16): *Direktor na Direktsia 'Obzhalvane i danachno-osiguritelna praktika' — Sofia v Iberdrola Inmobiliaria Real Estate Investments EOOD*

4.5 Foreign refund reclaims

4.5.1 Updated Notice

HMRC have issued an updated version of their Notice *Refunds of VAT in the European Community for EC and non-EC businesses*. Changes include:

- the removal of a statement that deregistered applicants should submit applications for refund "as soon as possible, and not later than three months from the date of their deregistration";
- the addition of a requirement to include the country prefix in respect of invoices being claimed;
- a new telephone number for the UK VAT Overseas Repayment Unit (03000 545 316).

Notice 723A

4.5.2 Conditions for refund claims

The Romanian court has referred a question about the lawfulness of national law that imposes extra conditions on 8th Directive claims (and, possibly, on claims under the current electronic system under Directive 2008/9):

Are the Eighth Directive and the principle of fiscal neutrality to be interpreted as precluding/having precluded the legislation of a Member State which regulates/regulated, in the light of the principle that there should be certainty in tax matters, the conditions for eligibility for reimbursement of value added tax, such as, in the present case, the condition requiring proof of payment of the tax by suppliers?

If the Romanian authorities have some doubt as to whether the person to whom the claimant has paid VAT, has paid it over as output tax to the Romanian authorities, it seems likely that the *Kittel* principles would come into play. The law is likely to be unlawful if it imposes extra duties on non-residents that are not suffered by resident businesses, or if it makes the right excessively difficult or effectively impossible to claim.

CJEU (Reference) (Case C-): *Evo Bus GmbH v Direcția Generală Regională a Finanțelor Publice Ploiești — Administrația Județeană a Finanțelor Publice Argeș*

5. INPUTS

5.1 Economic activity

5.1.1 Holding company inputs

The Hungarian court has referred questions to the CJEU in relation to a holding company that supplies management services to its subsidiaries but does not charge them. This appears to reflect very closely the situation in the UK case of *Norseman Gold*.

CJEU (Reference) (Case C-28/16): *Magyar Villamos Művek Zrt. (MVM) v Nemzeti Adó- és Vámhivatal Fellebviteli Igazgatósága*

5.1.2 Abusive arrangements

Amazingly, the *University of Huddersfield* case continues to trouble the courts, more than 20 years after the instigation of the disputed VAT plan. The Court of Appeal has dismissed the taxpayer’s appeal against the Upper Tribunal’s reversal of the FTT’s decision (TC02823) that the arrangements entered into by the University of Huddersfield, which were considered by the CJEU (Case C-223/03) in a combined hearing with *Halifax plc* (Case C-255/02) and *BUPA Hospitals Ltd* (Case C-419/02), were not abusive. So HMRC are winning (at least for the moment).

It was clear from the CJEU decision that the court considered the *Halifax* scheme to be contrary to the purpose of the VAT Directive: an exempt financial institution should not be able to arrange its affairs so that it obtained full or nearly full relief for the VAT incurred on the construction of buildings. However, this was not so clear in relation to an educational organisation, as this case has shown.

The University was a mainly exempt trader providing education. In 1995, it decided to refurbish two leasehold buildings (W and E) for the general purposes of its business, and its accountants devised a scheme to improve the VAT recovery on the refurbishment work. The scheme operated as follows:

- on 27 November 1995, a discretionary trust was established by deed;
- on the same date, the University entered into another deed indemnifying the trustees against any liabilities arising;
- the University opted to tax building W and granted an underlease for 20 years to the trust, with provision that the lessor could break the lease on the 6th, 10th or 15th anniversary;
- the trust opted to tax and granted a subunderlease to the University for 20 years less three days;
- the rent on the first lease was £500,000 (trust to pay to University), and on the second was £520,000 (University to pay to trust);
- the idea was that all the VAT on the refurbishment work could be recovered in respect of the first VATable rentals paid to the University by the trust, but the lease and leaseback would be collapsed long before 20 years had passed, so the irrecoverable VAT on the £520,000 rentals would be much lower than the input tax recovery on the works.

The scheme for the other property was similar, except that the rents were nominal. A subsidiary of the University invoiced it for future construction services on this building in the quarter to January 1997, and input tax of £612,500 was recovered by the University at that time; the work was completed and the building was occupied on 7 September 1998.

The University asked Customs for a ruling that the later termination of the underlease under its cancellation terms would not give rise to any supply by either party. In response, Customs ruled that the whole arrangement was uncommercial and artificial, and on 26 January 2000, an assessment was issued to recover the £612,500 of input tax claimed in the January 1997 return.

In the original dispute, the appellant argued the following:

- the scheme was on all fours with the case of *Robert Gordon's College*, and Customs were trying to use the Tribunal's initial decision in *Halifax* to overrule a House of Lords precedent;
- the decision in *Halifax* had been overturned by the High Court and remitted to the Tribunal, which had referred it to the ECJ, so there was no precedent authority on which Customs could rely;
- the transactions were not "entered into solely or predominantly for the purpose of tax avoidance", and even if they were, that would only bring them within the ambit of any anti-avoidance legislation, of which there is none in the UK in this area.

The definition of tax avoidance is important. The appellant argued that it was merely involved in tax *deferral*, as the rents paid on W would give rise to irrecoverable VAT at a later date. Customs argued that there were three possibilities:

- the arrangements would be collapsed very quickly, leading to an immediate absolute VAT saving rather than merely a deferral;
- the arrangements would be collapsed later, so there was a deferral with the possibility of an absolute saving later;
- even deferral could be tax avoidance.

The VAT Tribunal agreed with Customs. The scheme involved features which were absent in *Robert Gordon's College* – the ability to collapse the arrangements meant that there was likely to be an absolute saving, and not merely a deferral. The transactions were entered into solely with the intention of creating a fiscal advantage, or the possibility of one, and this did not (in the Tribunal's opinion) constitute a business purpose.

The case so clearly depended on the view of the CJEU in *Halifax* that it was referred to the court and heard along with that case. However, the court's decision concentrated on *Halifax* (where it clearly regarded the arrangements as artificial and abusive) and *BUPA* (where the arrangements were ineffective). The court did accept that the Huddersfield transactions were 'economic activity' that would, in principle, give rise to the normal VAT consequences under the law, unless they were found to be abusive.

The University continued to dispute whether the outcome of its scheme was contrary to the purpose of the Directive. In the event, the leases had

not been collapsed at such an early stage that there was an overall saving: the net outcome had been more output tax payable to Customs than input tax recovery. The University argued that this tax deferral was acceptable and not abusive.

The same judge, David Demack, heard the case on its return to the FTT. It was not explained why this took place in February 2013, when the VAT Tribunal reference was made in July 2002 and the CJEU decision was handed down in February 2006.

Judge Demack considered the arguments put forward by HMRC and the University in detail. He noted that there had been several other decisions on abuse of rights since 2006, in particular *Weald Leasing Ltd* (Case C-103/09), in which the CJEU had circumscribed the concept of abuse. He agreed with the University's representative that there was an important distinction between a mere deferral of VAT and an attempt to obtain an absolute advantage; the CJEU in *Weald* had effectively affirmed the principle that traders were entitled to structure their operations in such a way that VAT could be recovered up front and paid back later by lease and leaseback transactions. The tax advantage obtained by the University was one that was entirely consistent with the domestic legislation, and the judge concluded that they were not abusive. The CJEU had remitted that point to the referring Tribunal; the appeal was therefore allowed.

HMRC argued that it was not possible to wait until the leases were collapsed in 2004 to raise an assessment: the mere possibility of an abusive absolute saving should have been enough to justify the raising of an assessment to disallow the input tax claimed as the work progressed. The judge disagreed: in his view, HMRC would be free to raise an assessment after the collapse of the leases, calculating the absolute VAT saving which could be shown to be contrary to the purpose of the legislation (being more than a mere deferral of VAT), and they would be entitled to raise an assessment at that time.

HMRC appealed to the Upper Tribunal, arguing that the FTT's approach to the tax saving scheme had been flawed. If they succeeded in persuading the UT that the scheme was abusive, it would also be necessary for the UT to consider how to recharacterise the transactions to cancel the tax advantage.

The UT disagreed with Judge Demack's interpretation of *Weald*. That decision was not a justification for a principle that the abusive nature of a scheme, or the extent of a tax advantage accruing, could only be determined after the event – in this case, once the leases had been collapsed. The CJEU in *Weald* had envisaged the possibility that a scheme could be cancelled with the refund of output tax and the clawback of input tax.

The FTT had also erred in regarding the collapse of the leases as somehow separate from the scheme as a whole. If the scheme had been created to generate a tax advantage, then the collapse of the leases was part of that tax advantage.

Overall, there were sufficient objective factors to show that the scheme had been designed to create a tax advantage. That was artificial in that the scheme had created a taxable supply that had no purpose other than to generate a deduction of input tax in circumstances when no deduction

would normally be allowed. That was contrary to the purposes of the 6th Directive.

The scheme should be recharacterised by removing the abusive transactions and regarding the refurbishment as carried out for the purposes of the general business of the taxpayer, rather than for the purpose of the lease. Input tax on the refurbishment would therefore be recoverable in line with the partial exemption method of the university in force at the time. No output tax was due on the lease, because it would be disregarded.

The Court of Appeal agreed with the Upper Tribunal. The abusive element was the ability to deduct all of the input tax, rather than simply spreading it as in *Weald*. The FTT had found as a fact that collapsing the leases, therefore making the saving permanent rather than merely a timing matter, was always the intention. The Court also agreed with the UT that the insertion of transactions and parties into the scheme had no purpose other than to facilitate the tax avoidance purpose, and the arrangements were therefore artificial. Those elements should be disregarded in recharacterising the transactions.

Court of Appeal: *The University of Huddersfield Higher Education Corporation v HMRC*

5.1.3 Refusal of registration

A company applied for registration in July 2014. HMRC asked for further information about the trade, but this was not provided. HMRC informed the company that it would not proceed with the registration without the information; the company requested a review, but did not provide all the information requested. HMRC met the sole director, who was Polish. The company did not appear to have a substantial UK presence, and the officers were not convinced by the evidence of an intending trade.

The taxpayer appealed against the refusal of registration. When it came before the Tribunal, it offered no evidence about the facts, and accepted that if HMRC were not "satisfied" that it was a taxable person, that was a matter within their discretion and it could not be argued with. The company claimed a direct right to register under art.9 PVD, and cited the case of *Valsts ienemumu dienests v Ablessio SIA* (Case C-527/11) as supporting a directly effective right to register.

HMRC's response was somewhat confused and had to be clarified by the Tribunal asking for further written submissions. Initially, HMRC sought to rely on art.284 PVD as allowing HMRC to treat small businesses as exempt. Their revised view was that art.286 gave HMRC authority to define taxable persons, and was the basis of both compulsory registration in Sch.1 para.1 and voluntary registration in Sch.1 para.9. The Tribunal agreed with this. The UK had a valid derogation and could impose conditions on voluntary registration. The *Valsts* case only supported the proposition that member states, refusing to register a business on the grounds of suspected fraud, would have to offer some evidence to support the suspicion. In this case, the Tribunal agreed that HMRC were entitled to refuse to register a company that had provided insufficient evidence of economic activity.

First-Tier Tribunal (TC05089): *Geotrading Europe Ltd*

5.1.4 Evidence of taxable outputs

A company (F) appealed against an assessment disallowing input tax of £173,000 in respect of periods from 12/10 to 09/13, together with a penalty of £31,000. The company was a subsidiary of Balhousie Holdings Ltd (BH), which was the subject of a separate appeal and decision (TC05131, considered in section 3.3).

F was not a member of a group registration with BH. Another group company, Balhousie Care Ltd (BC) operated care homes. F was used by the group to manage design and build of new homes and refurbishment of existing homes; this was done in order to achieve VAT recovery on expenditure, because BH and BC were partially exempt with low recovery rates.

The Tribunal heard evidence from the owner and principal director of BH, and examined documentary evidence provided by the taxpayer that it incurred the inputs and supplied them on to BH and BC. This evidence was "unsatisfactory". For example, F's statutory accounts for the year ending 30 April 2012 showed no trading turnover and no costs. It appeared that the structure had been established in order to achieve the recovery, but this had not been followed through in fact. The individuals best placed to explain the FC and BH relationships, being primarily the financial controller, did not give evidence. There were no formal documents supporting intra-group transactions that would show F carrying on a taxable activity. The Tribunal concluded that there was insufficient evidence that F was engaged in taxable activity and that it had incurred the claimed input tax in relation to taxable outputs, and dismissed the appeal.

First-Tier Tribunal (TC05133): *Faskally Care Home Ltd*

5.1.5 Non-profit companies

A non-profit company was created to construct and operate a water disposal system, a reservoir and a rainwater collection system on land belonging to members of the companies. It claimed a deduction for the VAT charged by the contractor who carried out the construction work. The Hungarian authorities disallowed the deduction, arguing that the activity was not economic. It consisted in fulfilling legal obligations, and the low fees charged to the members did not constitute consideration. The costs were subsidised by grants from the government.

The CJEU did not agree. The company proposed to carry on the activity, charging modest fees to the members, over a period of 8 years. That satisfied art.9(1) PVD – the realisation of income on a continuing basis. The grants and the legal obligations were not relevant to the issue, because economic activity was an objective concept. It was for the domestic court to decide whether the payments from the members were sufficiently closely linked to what they received to constitute "consideration" for the supply of services.

CJEU (Case C-263/15): *Lajvér Meliorációs Nonprofit Kft. and Lajvér Csapadékvízrendezési Nonprofit Kft. v Nemzeti Adó- és Vámhivatal Dél-dunántúli Regionális Adó Főigazgatósága*

5.2 *Who receives the supply?*

5.2.1 Professional services

A company was in financial difficulties and appointed an accountancy firm to liaise with its banks, bondholders and other creditors. It paid the fees and reclaimed input tax on them. HMRC assessed to disallow the tax, arguing that the firm's supplies were made to the creditors, not to the company.

The First Tier Tribunal examined the engagement letters, which appeared to support HMRC's position: they were addressed to the engaging institutions, and stated that the report was solely for the use of the engaging institutions. However, even HMRC accepted that the appellant was a party to the contracts – they were tripartite agreements. HMRC relied on the Tribunal decisions in *Telent plc* (VTD 19,967) and *Birmingham City Football Club* (VTD 20,151) to support the contention that the person who pays for services does not necessarily have the right to deduct the VAT.

The First Tier Tribunal quoted the *Redrow plc* decision of the House of Lords at length. It concluded that there was a supply made to the company as well as to the lenders; it was then obvious that the supply was used for the purposes of its business, and it was entitled to the deduction.

The Upper Tribunal reversed this decision on appeal. The judges did not consider that Airtours received any benefit for its business in the same way that Redrow did. It did not start by needing PwC's report to place before the institutions; the institutions started by wanting the report for themselves, as the agreement stated. The benefit to Airtours was that PwC's report might lead to continued finance from the institutions for which Airtours was willing (or was forced) to pay. In reality, the institutions were contracting with PwC for the provision of the services, and the involvement of the company in the agreement was only in order to make sure that it had to pay for those services.

The company appealed to the Court of Appeal. The hearing of the appeal was delayed pending the Supreme Court decisions in *Aimia* and *WHA Ltd*, which were considered likely to be relevant. In particular, the Supreme Court in *Aimia* confirmed that it still regarded *Redrow* as a correct decision, in spite of HMRC's view that the CJEU judgment in the case undermined it.

The company's appeal was based on the argument that the UT had overturned a finding of fact which the FTT had been entitled to reach on the basis of the evidence before it. The UT had therefore exceeded its authority. The Court of Appeal dismissed the appeal by a 2-1 majority.

The leading judgment found that the UT had applied the correct test, as refined by the Supreme Court in *Aimia*. It was necessary to consider the economic realities of the nature of the transaction and to consider what, if anything, the claimant received in return for the consideration paid. In this case, the contract clearly provided for PwC to provide services to and for the financial institutions, to be paid for by the claimant. The fact that the claimant "needed" or "wanted" these supplies to be carried out did not mean that it received them. That was a subjective matter that could not affect the outcome for VAT. The FTT's decision had been flawed in that

it had not asked the question clearly enough or considered it objectively; the UT had been right to consider the question anew, construing it in the correct manner and applying the correct test.

The taxpayer appealed to the Supreme Court, which dismissed the appeal by a 3-2 majority. The engagement letter did not require PwC to provide any services to Airtours. Airtours was only a party to the contract for the purpose of requiring it to pay the fees, to provide PwC with an indemnity, and to acknowledge a liability cap on PwC. It was clear from the terms of the letter that the engagement was with "the engaging institutions" who would receive and be the sole beneficiaries of the report. Lords Neuberger, Mance and Hodge agreed that the apparent satisfaction of the "*Redrow* tests" could not convert this contract into one in which PwC were supplying services to Airtours as well as to the institutions.

The starting point of the VAT analysis should be the contract. A different result might follow if the contract did not reflect the economic and commercial reality of the situation. In this case, however, the contract did reflect that reality. There was no reason to recharacterise anyone else as receiving the supply.

Lord Clarke and Lord Carnwath gave dissenting judgments, also referring to the dissenting judgment of Gloster LJ in the Court of Appeal. Lord Carnwath commented that it was unrealistic to suppose that Airtours had no enforceable rights against PwC, having paid a retainer and signed a contract that required PwC to produce a report to the lenders within a tight timetable. However, the minority views are now less important than the majority.

Supreme Court: *Airtours Holidays Transport Ltd v HMRC*

5.2.2 Helicopter

A company (EAH) sold US-manufactured helicopters and carried out specialist repairs and servicing. It claimed £50,310 of input tax in respect of the purchase of a helicopter. HMRC ruled that the input tax was not deductible: it was legally owned by a US trust, and EAH had not received the supply. In addition, there was doubt about the status of the supplier, and the VAT invoice did not show the supplier's name correctly.

The company argued that the helicopter was held by the trust in order to bring it within the less onerous US regulatory regime. If the sale had not been made by the company shown on the invoice, the invoice would be fraudulent, which HMRC would have had to have explicitly pleaded and they had not; and recent CJEU case law suggested that formal problems with documentation should not prevent a deduction where the substantive requirements were met.

The Tribunal noted that the key issue was really who was the supplier: HMRC considered that it was the US trust, which was not a taxable person, whereas the appellant considered it to be a company that had to charge output tax as it had used *Lennartz* accounting on importation of the helicopter into the UK. HMRC questioned whether this had been correct: they regarded the main director of the company as the owner, if anyone, and it had not been included as an asset in the filed accounts of the company. The Tribunal commented that the *SecretHotels2* case was the main precedent for the principles involved in identifying the supplier in a

transaction and the relevance of contractual documentation. The approach is:

(1) To characterise the relationship in the light of the contractual documentation.

(2) To consider whether the characterisation represents the economic reality of the relationship in the light of relevant facts.

According to the documentation, the seller was the US trust. The Tribunal considered all the available evidence about the ownership of the helicopter and concluded that it was more likely than not that there had been a taxable supply to the appellant. It was not absolutely clear who had received the proceeds, but that was not the crucial question.

HMRC objected to the invoice on the basis that the supplier company had changed its name before the date the invoice was issued. It therefore did not comply with reg.14. The Tribunal noted that HMRC had discretion to accept alternative evidence under reg.29, and made a clear recommendation that they should do so, given that the Tribunal had found as a fact that there was a taxable supply to the appellant as described in the invoice. The appeal was allowed to that extent.

First-Tier Tribunal (TC05050): *Eastern Atlantic Helicopters Ltd*

5.3 Partial exemption

5.3.1 PESM and grouping

A partially exempt trader agreed a floor area based special method of partial exemption with HMRC. On 1 May 2014 it joined a VAT group. HMRC's view was that it would have to agree a revised PESM as a result. The accountants proposed a new PESM that was substantially the same as the old one, and the company appealed against HMRC's refusal to accept that method.

Judge Bishopp asked HMRC's representative whether HMRC had ever issued a notice revoking the PESM under reg.102(3) SI 1995/2518. She said that this had not happened, and she was also unable to find any legislative provision that automatically cancelled a PESM when a company joined a VAT group.

As a result, the appeal had been brought on a false premise. The company was still obliged by reg.102 to continue to operate the old PESM until HMRC cancelled it; the decision was not a valid decision and could not be appealed against. The Tribunal made no adjudication between the various arguments, and expressed the hope that HMRC would now agree a new method with the company.

First-Tier Tribunal (TC05003): *Dynamic People Ltd*

5.3.2 Mixed use building

The CJEU has now given its ruling on a case referred from Germany about the way in which costs associated with a building should be apportioned between taxable and exempt use by the taxpayer.

The appellant constructed a building which contained residential accommodation, let out exempt, and commercial premises, which were let

out subject to VAT. The company applied a turnover-based method to determine the deduction of input tax on costs associated with the building in 2001 and 2002, and the tax authorities agreed these deductions.

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

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

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

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

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

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

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

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

The full court judgment appears to go against the A-G. It notes that the purpose of a special method (a “different allocation key”) is to produce a fairer result than the turnover-based method. It would be for the referring court to determine whether this was the result in a particular case, but the PVD did not preclude a change from one method to another during the CGS adjustment period, nor the adjustments being computed according to

different methods as a result of that change. Changing the method did not offend against the principle of protection of legitimate expectations.

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

5.3.3 Income outside the scope

A company had been registered since 1990 in relation to the operation of car parks. Until 2012, the majority of its income came from penalty charge notices. In March 2013, the CA decided that PCN income was outside the scope of VAT. On 6 June 2013, the company submitted its VAT return for 04/13, claiming a repayment of £78,077. The return excluded £363,059 of PCN income that previously would have been treated as taxable.

HMRC refused the claim, ruling that there had to be an income-based apportionment between income within and outside the scope of VAT. They recalculated the recovery and repaid an interim amount, treating 92% of the input tax as non-business.

The company argued on the basis of *Kretztechnik* and *Church of England Children's Society* that the existence of non-business income should not restrict input tax recovery when there were only economic activities. However, it was conceded that the claim included VAT that was incurred on expenses that only related to earning PCN income. The company accepted that this was non-deductible. However, this proportion was 31.2%, not 92%. If this attribution was not accepted as the appropriate basis, the company argued that the income-based apportionment was unfair, because costs were not incurred in proportion to the level of income. Other possibilities included time spent by employees on various activities, which would give a recovery of approximately 59%.

The judge noted a difference between the wording of VATA 1994 s.4 and the PVD. The VATA refers to a "taxable supply made by a taxable person in the course or furtherance of any business carried on by him", whereas the Directive refers to the supply of services, "effected for a consideration by a taxable person" and "taxable person" means a person who independently carries out any economic activity. The distinction is clearer in art.168, which only gives the right to deduct input tax on goods or services used for the purposes of the taxed transactions of a taxable person. The judge said that the UK law had to be interpreted in a manner consistent with the Directive.

In that light, he drew a distinction between:

(a) those costs which are attributable only to the generation of PCN income and which contribute nothing to VCS making taxable supplies and

(b) VCS's other inputs, comprising

(i) both those which are fully attributable to VCS's taxable supplies to its clients and

(ii) those, generally VCS's overheads, which are attributable both to the generation of PCN income and to making taxable supplies to clients.

The costs under (a) were not recoverable at all. Those under (b)(i) were recoverable in full but were relatively small. Those under (b)(ii) fell to be

apportioned. The judge considered that an income-based apportionment was easily undertaken and readily verifiable. With some minor refinements, the judge arrived at the 8% recovery figure that HMRC started with.

The appeal was dismissed.

First-Tier Tribunal (TC05196): *Vehicle Control Services Ltd*

5.3.4 Rounding of percentage

A German company calculated the deductible proportion of overhead input tax at 13.55% for 2009 and 13.18% for 2010. It rounded them up to 14%. The German authorities decided that it was incorrect to round up: as the company was using a special method, in accordance with the *Royal Bank of Scotland* decision (Case C-488/07), rounding was not required.

The CJEU agreed with the tax authorities. Rounding under art.175(1) was not required where the deductible proportion was calculated under one of the derogating methods in art.173(2); and rounding in capital goods scheme adjustments in art.184 and following was only required if the initial deduction had used round.

CJEU (Case C-186/15): *Kreissparkasse Wiedenbrück v Finanzamt Wiedenbrück*

5.3.5 Academic costs and commercial research

Imperial College made a *Fleming* claim for £626,757 on 31 March 2009. It covered part of the university's residual input tax for the years from April 1973 to July 1994. Three previous repayment claims had been submitted in 1993, 1994 and 1995, effectively claiming the same amount; these had been refused when the three-year cap was introduced in 1996. A fourth claim, made in 1997, was agreed by HMRC, but the effect of the cap meant that input tax was only repaid for the period from 1 August 1994 to 31 July 1997. When the *Fleming* claims window opened, the university argued that the only bar to its claims for the earlier periods had been removed, and they should simply be settled.

The basis for all the claims was that some of the academic overheads of the university should have been allocated to its commercial research activities, which involved making taxable supplies and should therefore have created an entitlement to input tax recovery. The university argued that HMRC's acceptance of the 1997 claim implied the approval of a partial exemption special method which would have had retrospective effect. This was because the 1997 claim was for the inclusion of a category of overheads that had not previously been included; if those overheads should be included as a matter of principle, the operation of the agreed PESM would generate a repayment.

HMRC argued that no such agreement was implied by the 1997 repayment. If the university's 2009 claims were treated as new claims, all earlier periods could be reopened by HMRC, with the most likely result being that no further input tax would be repaid to the taxpayer, because a "fair and reasonable" method would take further factors into account that would cancel the university's advantage (certain grant income that had previously been ignored would have to be included in the calculations as exempt). In HMRC's view, the earlier repayment had simply been an

adjustment to the operation of the "CVCP guidelines", rather than the agreement of a special method to operate retrospectively.

The FTT (TC04246) examined the history of the dispute and the correspondence. In the view of the judge, this was more consistent with the university's version of events. There were many references to agreeing "a method" and none to the guidelines. The earlier claims did not fit the framework provided by the guidelines. The evidence suggested that HMRC had, in early 1996, given positive approval for a non-CVCP special method to be operated retrospectively, and the only reason for not paying it was the cap. The judge rejected an argument that such an approval was ultra vires and therefore ineffective: the officer who gave approval appeared to think so, but he was wrong, and his opinion was not relevant.

The FTT decided all matters of principle in favour of the university. The approval of the method and the earlier claim meant that the only bar to the repayment was the cap, and that had been removed by the *Fleming* case. However, the evidence was not strong enough to support a repayment for the periods up to and including 1980/81. The appeal was therefore allowed in relation to the years after that.

HMRC appealed to the Upper Tribunal. An initial application was refused because it appeared to be an attempt to re-argue the finding of fact that there was an agreed PESM. A revised application was approved, even though the UT said it was "discursive and hard to follow". The essence of the appeal was that agreement of a combined method would have been ultra vires and therefore ineffective. The claims for each year would have been an agreed compromise between Customs and the taxpayer, rather than the mechanical operation of a method that had to be followed.

The UT considered the question as a matter of principle, examining a number of precedent cases on PESMs and also on HMRC's care and management powers. The judges concluded that HMRC did have the legal authority to agree a combined method, as a result of reg.102 and VATA 1994 Sch.11 para.1(1).

The UT went on to apply the principle to the method used in the present case, and agreed with the FTT that HMRC had the power to agree this method, and had done so. Although the split between business and non-business was not a partial exemption issue, HMRC had the power to include that split within a special method, and the college's agreed method had to be followed.

HMRC's appeal was dismissed.

Upper Tribunal: *HMRC v Imperial College of Science, Technology & Medicine*

5.4 Cars

Nothing to report.

5.5 Business entertainment

Nothing to report.

5.6 Non-business use of supplies

5.6.1 Article

In an article in *Taxation*, Julie Butler considers the difficulties for both direct tax and VAT where an activity is on the borderline between a business and a hobby. She examines yacht chartering as an example, and discusses the application of the *Lennartz* mechanism.

Taxation, 12 May 2016

5.7 Bad debt relief

Nothing to report.

5.8 Other input tax problems

5.8.1 Avoidance scheme

The Tribunal had to consider related corporation tax and VAT deductions in relation to the same company in its 31 October 2010 CT accounting period and its 01/11 VAT return period. It appeared that the advertising had been invoiced by a company connected with the taxpayer's accountant, and was probably a fictitious supply only recorded to obtain a deduction and not actually paid for.

The trader did not appear and was not represented. In the absence of the appellant, the Tribunal had to draw a number of inferences from the evidence. It appeared unlikely that the business would have paid as much as was shown on the invoice for the minimal advertising that was claimed to have been supplied. The judge concluded that the appellant had not shown that there was a supply received for the purposes of the business, and dismissed the appeal.

HMRC wanted to characterise a payment of £10,000 that was connected with the "supply" as a contrived loan made by the company to a director. Although she agreed that the nature of the payment was in doubt, the judge did not agree that HMRC had shown that it should be characterised as a loan. The appeal against the extra corporation tax that would result from such a finding was allowed.

First-Tier Tribunal (TC05097): *DTL Supplies Ltd*

5.8.2 No supply received

A company made two part-payments towards the purchase of wind turbines which were not delivered because the supplier went into liquidation. It was alleged that the supplier had carried out a fraud in obtaining the part payments, and had not ordered the goods from a supplier.

The taxpayer argued that “the taxpayer should not bear the burden of a fraud”, following *Kittel*. HMRC distinguished that case on the basis that no supply had taken place. Following a string of precedents, input tax could only be claimed where there was an actual supply.

The Tribunal agreed with HMRC. Only 70% of the price had been paid, which was not enough to secure transfer of title under the contract; even if the goods had existed or been delivered, they did not belong to the claimant yet. Although the result was harsh, it was inevitable. The appeal was dismissed.

First-Tier Tribunal (TC05195): *D & J Grant*

5.8.3 Missing traders

In TC04178, the FTT considered the refusal of a claim for £500,000 in respect of the 04/06 period. The hearing examined one issue on the basis of assumed facts, without hearing from witnesses or examining evidence to support those facts, to determine whether a line of defence could be effective in principle.

The trader argued that it had been defrauded by an agent to which it had subcontracted the due diligence work on purchases and sales of mobile phones. HMRC argued that the knowledge of an agent had to be imputed to the principal, so the defence was ineffective.

The principles of the defence are based in long-standing UK case law, not in VAT law. In general, a principal cannot hide behind an agent to deny wrongdoing – the principal has “constructive knowledge” of the agent’s activities; however, where the agent has deceived the principal, a “fraud exception” applies. This was considered in the context of MTIC fraud in 2012 by the Upper Tribunal in the *Greener Solutions* case. There, the FTT had concluded that the trader did not have “the means of knowledge”; but the Upper Tribunal reversed that decision, concluding that the exception did not apply.

The current appellant tried to distinguish *Greener Solutions* by pointing out that the agent had carried out a wider fraud than the agent in that case. It had not merely put the company in the position to claim fraudulent VAT credits and taken its share of that; it had raided the company’s bank account, leaving it with debts of £3m. HMRC argued that the two matters were not directly connected – the MTIC fraud was squarely within the principles of the *Greener Solutions* case, and if there had been a theft from the company’s bank account, that was a separate matter that would not assist the appellant.

The Tribunal interpreted *Greener Solutions* as restricting the fraud exception to circumstances in which the fraudulent acts of the agent have to be directly linked to the acts of which the principal is accused. On the basis of the assumed facts there was not a sufficient connection between

the alleged fraudulent acts of the agent and the disputed VAT transactions. The fraud on the bank account related to different transactions to the fraud that generated VAT repayments.

The appeal on the preliminary issue was dismissed by the FTT. The company appealed to the Upper Tribunal, again on the preliminary issue only, continuing to base the argument on assumed facts that might have to be tested later. The UT considered the legal basis of this line of appeal, and examined the Supreme Court's decision in *Bilta* (a case in which directors argued that they could not be sued by the liquidator of their company for participation in a fraud, because the company had been party to it as well). The UT concluded that "MSL is not able to rely upon the actions of [its agent] to claim that entitlement [to input tax] and, at the same time, to resist the attribution to it of the knowledge of [its agent] that the transactions were connected with fraud." The knowledge of the agent had to be attributed to the principal, and the appeal was dismissed again.

Upper Tribunal: *Mobile Sourcing Ltd v HMRC*

In a case management hearing in relation to a MTIC appeal, Judge Berner commented on what have become known as "Fairford directions" after the Upper Tribunal decision in *HMRC v Fairford Group plc (in liquidation)*. The point in that case was that HMRC wanted to strike out some of the company's grounds of appeal on the basis that they could not reasonably dispute substantial facts relating to fraudulent tax losses. The UT ruled that the FTT was correct not to strike out those elements of the case, but gave guidance on appropriate directions that could be issued to achieve a fair result.

After discussing the background law, the judge made a number of directions requiring the company to specify those areas of evidence that would be accepted without cross-examination.

First-Tier Tribunal (TC05036): *C F Booth Ltd*

A MTIC appeal was heard over 15 days in July and August 2014 in relation to the disallowance of £1.8m of input tax from periods 04/06 to 07/06. In one of the longer recent decisions (661 paragraphs) the Tribunal examined the trading in detail, and concluded that the transactions "simply screamed possible fraud". The *Kittel* test was satisfied throughout, and in respect of some deals actual knowledge was found "with no hesitation".

The last 50 or so paragraphs contain a discussion of procedural disputes on the admissibility of evidence.

First-Tier Tribunal (TC05160): *Aircall International Ltd and another*

5.8.4 Updated Notice

HMRC have updated to April 2016 their Notice *VAT refund scheme for certain charities* which explains the VAT rules that apply to charities eligible for refunds of VAT under s.33C and s.33D VATA 1994. The latest version includes a new postal address for refund claims by charities that are not registered for VAT.

Notice 1001

6. ADMINISTRATION AND PENALTIES

6.1 Group registration

Nothing to report.

6.2 Other registration rules

6.2.1 Exception from registration

An individual became self-employed in March 2012. His turnover for his first year's trading was £97,834. The breach of the registration threshold only came to light in January 2014, when he submitted his records to his accountants for submission of his self-assessment tax return. They reckoned he had exceeded the threshold at the end of February 2013, and therefore ought to be registered with effect from 1 April 2013. However, the accountants applied for exception from registration on the basis that the next year's turnover would be below the deregistration threshold. The trader wrote in support of this application, stating that the reason he had exceeded the threshold was a one-off contract that would not be repeated. The turnover for the following accounting year was only £74,168.

The Tribunal noted an "oddity": both parties appeared to agree that the date the threshold was breached was February 2013, when the analysis of the figures clearly showed it was January 2013. The trader's accounting year-end was 31 March, and the first month of trading to 31 March 2012 had simply been omitted from the calculations.

As usual, the Tribunal concluded that exception depended on what was foreseeable at the time the liability to register arose, and the actual outcome was irrelevant. The turnover for the year to 31 March 2014 was also irrelevant – it should be the year from February 2013 to January 2014, for which the turnover remained above the limit.

The judge (Dr Heidi Poon) appears to misunderstand the relationship between Sch.1 para.1(1)(a) and para.1(1)(b). She says: "By virtue of sub-para 1(1)(b), the appellant's liability to become registered arose in December 2012 when his cumulative taxable turnover stood at £69,690 and he would have 'reasonable grounds for believing' that the value of his taxable supplies in the next 30 days (ie: in January 2013) would exceed the registration threshold of £77,000 then in force." She therefore appears to be considering a "forward look to a backward look", rather than considering the next 30 days on their own. Although this is a serious error of law, it does not undermine the decision overall.

The Tribunal noted that no penalty for late notification was being sought. It does appear to have been an unprompted disclosure of a careless error within 12 months of the date VAT would have become payable, so it could in any case have been mitigated to nil.

First-Tier Tribunal (TC05021): *Ken Renforth t/a Facade Detailing Service*

Another trader was in the same position, arguing about exception and an assessment for nearly £15,000. The trader's accountant informed HMRC by letter of 19 September 2013 that the registration threshold had been exceeded in the year to November 2012. No material was placed in HMRC's hands at the time on which to base a decision about future turnover; the information retrospectively supplied once the liability had been notified disclosed that the business' historical turnover had exceeded the threshold in every month from September 2012 to December 2013. The assessment was based on a "liable not liable" period from 1 November 2012 to 31 January 2014.

By the end of the hearing, the appellant had accepted that he had no chance of success in claiming exception from registration. What remained was the amount of the assessment, where he considered that HMRC had offered him a binding settlement in a lower amount. HMRC said that this was not the subject matter of the appeal, and was part of a negotiation rather than an offer that would bind them.

The judge (J Gordon Reid) agreed that he could only dismiss the appeal, because as a matter of law it only related to the registration decision. However, he considered that HMRC's correspondence with the taxpayer did appear to offer him a settlement of £2,627, and the judge clearly considered the later issue of an assessment for a much higher figure to be unreasonable. He expressed the hope that HMRC would "give careful consideration to the question of enforcement of the assessment".

First-Tier Tribunal (TC05102): *Doogs Garden Services*

6.2.2 Cancellation of registration

An individual argued that she should not have been registered for VAT. She was represented by a chartered accountant, although neither of them attended the hearing. He raised a number of procedural arguments, all of which were rejected in preliminary findings by the Tribunal:

- HMRC's case should be struck out – this was impossible, because the only comparable action that the Tribunal could take would be to bar HMRC from taking any further part in the proceedings;
- a litigant in person would inevitably be at an unfair disadvantage through not being able to appoint tax counsel – the Tribunal considered that this was not within its jurisdiction, but it was obliged to make sure that any appeal was conducted fairly;
- HMRC's decision was "unconscionable" – this was a reference to income tax rules on "special relief", and had no relevance to a dispute about VAT registration;
- HMRC should pursue the appellant's former partner, and they were guilty of harassing the appellant with spurious demands – the Tribunal had no jurisdiction in relation to other taxpayers or the collection of tax.

The business had been registered in the name of a partnership, and the VAT2 showed the names of the appellant and her former partner. She accepted that she had signed the form, but alternatively argued that she did not know what she was signing, and that her signature was obtained by deception or duress. She had provided funding for the business and

had worked within it, but never received any money back. Her self-assessment returns for 2009/10 and 2010/11 both showed that she was a partner in the business and disclosed trading losses. Her former partner signed the VAT returns.

The Tribunal and HMRC's representative acknowledged that this was a sad case, but it appeared that the suggestion that there had not been a partnership at all only arose once it became apparent that she would be liable for tax. The Tribunal was satisfied that there had been a partnership, that she had been a partner in it, and that it was validly registered. Any alleged fraud perpetrated by her former partner could not change that. The appeal was dismissed.

First-Tier Tribunal (TC05008): *Suzanne Deutsch*

6.2.3 Date of registration

A company started a property development activity in April 2007. It applied for registration on 8 December 2011 and was registered with effect from 31 March 2011. The first return was completed for the period to February 2012, and input tax of £121,833 was claimed. This was investigated, and was found to include a great deal of VAT on services received more than 6 months before the EDR.

The company asked for its EDR to be backdated to 31 March 2008, which HMRC refused. There is no statutory basis for amending an EDR, but HMRC's policy is to do so in the circumstances set out in VATREG25400:

- *the EDR given must, at the time of registration, have been a backdated EDR. In other words, at the time of application, the trader voluntarily applied for an earlier EDR.*
- *the trader must demonstrate that there was a genuine misunderstanding or error in completing the application form. That does not include an error of judgement, for example, he thought he would be in repayment but found in fact he was a payment trader.*
- *the request must be made before the due date of the first VAT return (that is, one month after the end of the first period), which must not have been rendered.*
- *the trader must return the original VAT 4 certificate.*

You are not expected to work on the mechanistic basis that every business which does not meet all four of the change eligibility criteria must automatically have its change request refused. You should consider each trader's circumstances separately and think about how a First Tier Tribunal judge might regard those circumstances should the trader appeal against your decision to refuse the request.

The test of any decision is that it is reasonable and proportionate in all the circumstances of the case.

The Tribunal noted that its jurisdiction was only supervisory: it could only consider whether HMRC's refusal was unreasonable. The taxpayer argued that its accountant had failed to appreciate the difference between goods and services, and that was the basis of a misunderstanding that ought to be accepted as satisfying the conditions. The Tribunal found that

HMRC had not accepted that there had been a genuine misunderstanding, and this meant that they had failed to take into account something that should have been given weight. However, if they had taken the decision properly, it would inevitably have been the same, for the following reasons:

(1) there was a delay in making the application to backdate the EDR (which was not made until 5 September 2014 nearly three years after the application for registration was made);

(2) it is not disputed that the third condition (which requires the request to backdate the EDR to be made before the due date of the first VAT return) has not been satisfied; and

(3) the date, 31 March 2011, had been deliberately entered in form VAT1 (the only error or misunderstanding was as to its effect).

Accordingly, the appeal had to be dismissed.

First-Tier Tribunal (TC05063): *Max Investments Ltd*

6.2.4 Overassessment

A partnership operated a cafe. They failed to notify liability to register for VAT from 1 April 2009, and accepted that they were in default until 31 March 2013 when the business ceased to trade. They argued that they had relied on the advice of their accountant, who told them that their registration turnover did not include zero-rated food. HMRC assessed for a total of £23,988 and a belated notification penalty of £3,598.

HMRC pointed out that even if 20% of their turnover was excluded, the remaining 80% exceeded the registration threshold in 2009/10 and 2011/12. The judge agreed that reliance on the accountant was not a reasonable excuse, and an inability to pay could not be taken into account. However, he noted that the officer’s calculations did not appear to take zero-rated sales into account. He used the officer’s own best judgement estimate that 30% of sales would be zero-rated and recalculated the assessment to £15,965, and the penalty in consequence to £1,796. The appeal was allowed to that extent.

First-Tier Tribunal (TC05030): *Joshua Ready and Leanda Jones t/a The Open Kitchen Cafe*

6.2.5 Updated Notices

HMRC have updated the registration and deregistration thresholds in the April 2016 version of their Notice *Cancelling your registration*. It also provides more on how to cancel VAT registration using the online service.

Notice 700/11

HMRC have also updated their Notice *Should I be registered for VAT?* It reflects the introduction of the online registration system and the removal of the registration threshold for non-established taxable persons since the April 2010 version. The Statement of Practice about artificial separation of business activities has been moved to the list of statements of practice on the HMRC website.

Notice 700/1

6.3 Payments and returns

6.3.1 Religious objections

An individual entered into correspondence with HMRC after being notified that he would have to file his VAT returns electronically as part of "Tranche 2" from 1 April 2012. He referred to the exception for people with religious objections, but argued that HMRC were not qualified to comment on the nature of his religious beliefs. He considered that the law should not apply to him because it had been decided on by people who had sworn allegiance to the head of the Anglican church, which was not his choice of faith.

HMRC made several offers of the use of telephone filing, but the taxpayer was unwilling to "wait in for a phone call from HMRC". The Tribunal decided, with HMRC's agreement, to consider also whether he might be eligible for the exemption on grounds of "age, disability, remoteness of location or any other reason".

As the appellant had provided very little information about his religious beliefs, it was not possible for HMRC to be satisfied about them. In any case, the statutory exemption referred to membership of a religious society or order, and he did not belong to one. An argument that the requirement breached his human rights was dismissed. The Tribunal considered that he had no apparent religious beliefs that prevented him using a telephone, and that had been offered to him. His appeal was dismissed.

First-Tier Tribunal (TC05041): *Brian Harvey t/a Sun Ice Air Conditioning Services*

6.3.2 Updated Notices

HMRC have updated their Notice *Flat rate scheme for small businesses* to May 2016. It appears that they have taken on board some of the criticisms made of their decisions in recent Tribunal cases about categorisation for FRS purposes: the paragraph about choosing a category now refers to the regulation (55K) rather than only referring to HMRC guidance, and the paragraph about categorising many businesses as "management consultants" and "structural engineers" has been deleted.

A paragraph about associated businesses has also been deleted, but it is less clear why. Other minor amendments have been made throughout.

Notice 733

HMRC have updated their Notice *How to fill in and submit your VAT return*. It has been updated with new contact information for the Business Payment Support Service, and to show that it is no longer possible to pay VAT using the BillPay service. It has useful advice for those operating the various special accounting schemes.

Notice 700/12

6.4 Repayment claims

6.4.1 Amended or new claim?

A bingo firm made a *Fleming* claim in relation to overpaid output tax between 1980 and 1996 on 19 March 2009. The claim was for £158,459 and related to mechanised cash bingo (MCB) and gaming machines ("amusements with prizes" – AWP – and "jackpot machines" – JM). The amount claimed was itemised quarter by quarter and also broken down into annual amounts for each of MCB and AWP/JM. The claim stated explicitly that it was "in respect of mechanised cash bingo, AWP and Jackpot Machines as detailed in sections 14, 31 and 34 of the Gaming Act 1968".

The firm's advisors suggested later in 2009 that the claim could also extend to Main Stage Bingo (MSB). An "amendment" to the claim was submitted on 9 November 2009, covering the same periods as the original claim, and amounting to a further £92,167.

A further amendment was made in January 2010, adding the years 1973 to 1980 and a further £40,923. These had not been included in the original claim because of a lack of records. The January 2010 figures were based on annual accounts.

HMRC rejected the November 2009 and January 2010 claims on the basis that they were out of time. An appeal against this decision was stayed for a long time while waiting for the final outcome of the *Rank* litigation, and also the 2013 Upper Tribunal decision in *Reed Employment*, which concerned amendments to claims. The FTT dismissed the appeal in 2014 (TC03734).

The judge cited the *Reed* decision, and approved of the principle that amendments to a claim had to either be the correction of errors, or had to be envisaged in the original claim – for example, by stating that a particular matter or period was within the scope of the claim, but that further details of the amounts would be provided when available. Adding something that was not contemplated in the original claim would not be an amendment, but would be a new claim.

The taxpayer's representative argued that the November 2009 addition of MSB was a correction of a mistake: the initial claim had been prepared on the mistaken belief that MSB could not be included. The judge disagreed. It was very clear from the wording of both the original and the later claims that MSB was excluded from the first and added in the second; there had been a conscious decision to exclude the matter from the original claim, and the later addition was not the correction of an accidental error.

The fact that HMRC's published position at the time was incorrect, holding that MSB could not be included, could not assist the taxpayer. The taxpayer would have had to make the claim and argue about it; it was not possible to wait until later and then make a claim.

Similarly, the periods before 1980 were not included or contemplated in the original claim. The trader did not believe that he had the necessary documentation, and only made the claim when this accidentally came to light later. The judge reiterated that the original claim could have referred to these earlier periods and promised more accurate figures later: that

would have been valid. As it was, the addition of the earlier periods was a new claim, and it was out of time.

The appeal was rejected.

Upper Tribunal: *Grand Entertainments Company v HMRC*

6.4.2 Directly effective rights

A motor manufacturer made a *Fleming*-type claim in November 2011 for £78.68m in relation to manufacturers' rebates paid to buyers of commercial vehicles between 1 January 1978 and 31 December 1989. Following the CJEU's decision in *Grattan* (Case C-310/11), it dropped that part of its claim relating to the period up to 31 December 1977, i.e. before the implementation of the 6th Directive in the UK. This reduced the amount to £73.36m. HMRC resisted the claim on the basis of the time limits for making claims, and also on the question of whether this appellant (registered only from 31 December 1992) was entitled to make the claims, when different taxpayers had paid the VAT in the past.

In TC03141, the Tribunal considered the time limits and its jurisdiction as a preliminary issue.

The judge agreed with the taxpayer that the right on which the taxpayer relied, to adjust the consideration under Art.11C(1) 6th Directive, had not been properly implemented in the UK before 1990. As a result, there was nothing to determine how or when any adjustment to its VAT account should be made under UK law; until it made a claim for its directly effective EU rights, there was no "accounting for VAT that was not due". That meant that the claim was not made under s.80 VATA 1994, and the time limit in s.80(4) could not apply.

In order to give effect to the claim, the judge ruled that SI 1995/2518 reg.38 should be read as if reg.38(5) did not apply. This would be a "conforming construction" that allowed the company its EU rights. As the underlying Directive did not contain a time limit, an adjustment to the VAT account should be allowed at any time, without time limit.

HMRC argued that, if the claim was not made under s.80(4), the Tribunal did not have jurisdiction to hear an appeal. The part of s.83 most obviously applicable to repayment claims is s.83(1)(t): "a claim for the crediting or repayment of an amount under section 80." The conclusion on the time limit ruled that out. However, s.83(1)(b) allowed appeals to be heard in respect of "the VAT chargeable on the supply of any goods or services." The judge concluded that this was wide enough to encompass a dispute about the direct application of a VAT Directive in determining the chargeability of a taxable person to VAT in relation to a supply that had been made.

The preliminary issues were therefore decided in favour of the taxpayer.

The remaining issue was HMRC's argument that, as a matter of EU law, a directly-effective right under the Sixth VAT Directive had to be exercised within a reasonable time after the relevant price reduction leading to an overpayment. As a similar argument had been rejected by the Upper Tribunal in *GMAC UK v HMRC; British Telecommunications plc v HMRC* and was the subject of an appeal to the Court of Appeal, that issue was stood over to be considered after the CA had given its judgment.

Although BT lost in the CA, the FTT judge concluded that the CA agreed with the UT on this point: there is no principle of EU law that requires a claim based on adjustment of consideration to be brought within a particular time-frame.

As this was the only remaining issue, and the CA judgment was binding on the FTT, the judge allowed the taxpayer's appeal in TC03578.

HMRC appealed to the Upper Tribunal, which agreed with both parties to defer consideration of the question of whether EU law required a claim to be brought in a reasonable time until the CA has decided the *GMAC* appeal (hearing scheduled for late June 2016). HMRC had several other grounds, arguing that the FTT had erred:

- in holding that s.80 did not apply to the claim, or that if it did, the claim was made within the time limit;
- in seeking to interpret reg.38 to give effect to art.11C1(1);
- in concluding that it had jurisdiction to consider the preliminary issue.

The Upper Tribunal started with an interesting discussion about the interaction of reg.38 and s.80, commenting that the apparently mandatory corrective mechanism of reg.38 requires an adjustment through the VAT account of the current period. It is then not entirely clear from the legislation what should happen if the result is a negative entry in Box 1. There has not been an "overpayment" in the s.80 sense: when the original return was made, showing the original price charged, the VAT was properly due.

The company argued that this counted in its favour. There was no "overpayment" until it made a claim to adjust its VAT account using the directly effective rights under the PVD, so the time limits in s.80 could not apply. HMRC argued that the overpayment arose when the company made the adjustment to the price and could or should have adjusted its VAT account.

The Tribunal commented that it might be necessary to "mould" the legislation in order to interpret it in a manner compliant with the PVD, but it was not clear whether it would be reg.32, reg.38 or s.80 that had to be so "moulded". The UT's understanding of the *Marleasing* principle led it to the view that the company's claim should have been made under s.80: it had directly effective rights at the time the adjustment to consideration was made, and that would have led to a *Fleming* claim. It had missed the *Fleming* window, and it was now too late to claim.

The Tribunal also considered the law on restitutionary claims, and concluded that the company's claims based on price reductions occurring before the beginning of 1984 were time barred by 1 January 1990. This was because there was no UK regulation implementing art.11C(1) 6th Directive before reg.38 came into force on 1 January 1990; the time limit for making restitutionary claims, which would have been required to give direct effect to the company's EU rights, was six years.

The UT did agree with Judge Berner that the FTT had jurisdiction to consider a claim under a "moulded" reg.38. However, the claim should have fallen under s.80, and the FTT had therefore come to the wrong conclusion. HMRC's appeal was allowed: "Section 80 applies on the

basis that the reduction in the taxable amount and the consequent overpayment of VAT arose on the occasion of each price reduction. If that is wrong, all of Iveco's claims in relation to price reductions occurring before 1 January 1984 were time-barred prior to 1 January 1990. Section 80 does not apply in relation to such claims and does not revive them."

Upper Tribunal: *HMRC v Iveco Ltd*

6.4.3 Postal claim rejected

In 2014, the FTT (TC03773) dismissed an argument that a company should be entitled to input tax as the VAT fraction of money paid to Royal Mail in respect of supplies which were regarded by the UK law as exempt, but which were of a kind held by the CJEU not to qualify for exemption under EU law. The particular claim related to consideration paid of £120,000, but there are a number of other similar claims with a large amount of money riding on them. Judge Mosedale gave her decision acknowledging that it would surely be subject to appeal, and probably an eventual reference to the CJEU. She therefore set out the facts and her understanding of the law, and her reasoning for her decision, with the stated intention of making everything clear for those who would review the decision later.

First, she accepted the taxpayer's argument that the supplies concerned were taxable. It was necessary to apply a conforming construction of UK law where possible; although the UK law was understood at the time to mean that all supplies by the Post Office were exempt, it was possible to interpret the exemption as covering only those supplies that the CJEU held were included (the "universal service obligation", not individually negotiated contracts such as those at issue). The doctrine of direct effect would also entitle the appellant to claim against HMRC that the supplies were taxable, but the conforming construction of the UK law meant that this was not required.

The question was then whether the customer was entitled to deduct VAT. Under EU law, VAT is deductible if it is "due or paid". This has widely been interpreted as covering the situation where an amount of consideration has been paid by a customer to a supplier, and that consideration "included VAT" because the supply was taxable. HMRC argued that the claim would only succeed if the appellant now paid VAT to Royal Mail in addition to the agreed consideration, and Royal Mail issued a VAT invoice. This goes against the normal view of HMRC where VAT has not been accounted for on a taxable supply – if the contract does not mention VAT, the consideration includes it, and the supplier must account for it.

By contrast, Judge Mosedale carried out a detailed analysis of the law – one that appeared to go beyond what HMRC's representatives put to her – and concluded that the European law is really referring to VAT that is "due or paid [by the supplier]", i.e. has been or will be accounted for as output tax to the authorities. In this case, Royal Mail had not paid VAT on these supplies, and in the absence of an assessment being raised by HMRC, it would not do so. It was by no means clear that HMRC could raise such an assessment, given that the UK law and administrative practice was to treat such supplies as exempt.

The judge went on to consider whether HMRC should exercise their reg.29 discretion to allow a deduction for input tax without insisting on the normal condition that the claimant holds a tax invoice. The company argued that there was compelling evidence that the company had paid for a supply that ought to have been treated as taxable. However, the judge concluded that it was relevant to HMRC's decision that making the repayment would create a windfall for the appellant: it had not expected to receive that repayment at the time it entered into its contracts, and it would effectively receive a pure profit at the expense of other taxpayers. Although refusing the deduction would create a sticking cost in the chain of supply (because Royal Mail had passed on irrecoverable VAT in its own costs), that sticking cost was much smaller than the windfall. It could not be said that refusing to allow such a large windfall was an unreasonable decision, even if the result was a small windfall to HMRC.

These factors had not explicitly been considered by HMRC in making the decisions. That would make them "unreasonable" for the purposes of the Tribunal's supervisory jurisdiction. However, the judge was satisfied that the result would have inevitably have been the same if the proper factors had been taken into consideration.

This last point – the absence of a VAT invoice, and the reasonable exercise of discretion – was the ground for Judge Mosedale's decision that the appellant was not entitled to the claim. She recognised that all parts of her decision are likely to be reviewed on appeals, possibly by both parties, or by other appellants in other cases.

The company appealed to the Upper Tribunal. Mrs Justice Proudman rehearsed the legislative background to the claim in the PVD, the VAT Act and the regulations. She went on to state the two issues before her: whether VAT was "due or paid" within art.168(a) PVD; and whether, in the absence of invoices, HMRC should nevertheless exercise discretion in the company's favour. It was accepted by all sides that the UT had jurisdiction to consider the exercise of HMRC's discretion.

The judge noted a number of CJEU precedents, but in particular *PPUH Stehcemp sp. J. Florian Stefanek, Janina Stefanek, Jaroslow Stefanek v Dyrektor Izby Skarbowej w Łodzi* (Case C-277/14). The court had ruled that the right to deduction was based on VAT due or paid by the customer, not by whether it had been paid over to the authorities by the supplier. Both sides said that Judge Mosedale had gone off on a "frolic of her own" in reasoning otherwise. Proudman J declined to comment further, other than to follow the CJEU precedents.

The appellant's case was simple. Because VATA 1994 s.19(2) calculates VAT as a fraction of the consideration paid, then the customer must have "paid" VAT if the transaction was in principle taxable. HMRC's representative argued that s.19(2) was merely about calculation, and whether the consideration included VAT depended on the agreement between the parties: in his view, the customer could not now claim that it had paid VAT after years of not challenging invoices that stated the transaction was exempt. He relied on the opinion of the A-G in the *T-Mobile* case on the grant of telecommunications licences by Austria. The judge was not convinced that this was correct, but said that her view on the VAT invoice question rendered the point academic.

The judge noted that there was some uncertainty about the basis of the company's appeal in this area. It was explicitly not based on an alleged failure of HMRC to follow their own policy as set out in their statement of practice on *Input tax deduction without a valid VAT invoice*. However, that statement did appear to provide a reasonable explanation of how HMRC would and should exercise their discretion.

The judge also noted that there were three possible outcomes to a consideration of discretion:

- if the decision maker reached a decision that no reasonable decision maker could have reached, the appeal should be allowed and the appellant's claim for input tax should be upheld; but
- if HMRC's decision would inevitably have been the same had it been properly undertaken, then the appeal should be dismissed;
- in any other case HMRC should be required to reconsider their decision, taking into account such matters as they should take into account and leaving out of account those matters which they ought not to have taken into account.

The judge agreed with the reasoning of the FTT. Although the economic burden of the VAT was not relevant to the question of entitlement to recover, it was relevant to the decision to exercise discretion. Even though the officer had not considered the matter, it was clear to the judge that an officer would have inevitably rejected a claim that would lead to a repayment of 15% to 17.5% of the price on the basis that an economic cost of about 2.5% had been suffered (the amount of Royal Mail's irrecoverable input tax that led to higher prices).

As a result, the company's appeal failed on the matter of VAT invoices, regardless of the conclusion on "due or paid".

Upper Tribunal: *Zipvit Ltd v HMRC*

6.4.4 Sports club claims

HMRC have revised their Information Sheet on sports club claims following the Tribunal decision in *The Berkshire Golf Club and others*. There are a number of important points for clubs to bear in mind in making and pursuing claims, but in particular:

- Where a refund claim has been rejected and no appeal has been made against that rejection, HMRC will resist applications for late appeals. Any claim will be treated as a new claim subject to the 4-year time limit from a current date.
- In line with the *Berkshire* decision, course maintenance costs can be treated as overheads to be apportioned in accordance with a partial exemption method.

VAT Information Sheet 1/2015

HMRC have also issued a Brief to set out their new policy on unjust enrichment following the *Berkshire* decision, cancelling and replacing Briefs 25/14 and 19/15. It confirms that HMRC have decided not to appeal the decision and will be making refunds – although it does not explicitly say so, the clear implication is that it will apply the 10% restriction considered appropriate by the Tribunal. The Brief emphasises

that claims will only be considered if they are validly made in accordance with the principles of Information Sheet 1/2015 (as revised).

Revenue & Customs Brief 10/2016

6.4.5 Time barred

A barrister failed to submit returns on time for 05/09 to 02/10. When the returns were eventually filed on 29 July 2014, it appeared that the estimated assessments paid in 2009/10 exceeded the amount actually due by some £43,000. The barrister (anonymised) appealed against a refusal of repayment, arguing "exceptional circumstances" (ill-health), unfairness, and a possible breach of the Human Rights Act.

The Tribunal examined the history of the case and could find no possibility of granting any relief. The appeal was struck out as having no reasonable prospect of success.

First-Tier Tribunal (TC05157): *Mr XYZ*

6.5 Timing issues

Nothing to report.

6.6 Records

6.6.1 Updated Notice

HMRC have replaced the June 2015 version of their Notice *Keeping VAT records* with an update to April 2016. Although it says it has corrected paragraph 3.3 from referring to "30 March" as the end of a period, the online version still seems to do so; it also refers to updating the December 2007 version rather than June 2015.

Notice 700/21

6.7 Assessments

6.7.1 Problems with applicable period

HMRC assessed a company for underdeclared output tax of £110,360 plus interest for the period from 1 April 2008 to 31 December 2011. They also charged a penalty under FA 2007 Sch.24 of £18,717, and a s.63 misdeclaration penalty of £5,188 for the periods 06/08 and 09/08. In addition, HMRC issued a Sch.1 para.2 business splitting direction covering a number of businesses to take effect from 11 July 2013.

The company operated from premises that included four restaurants, cafes and bars, function rooms and apartments. Different entities operated

different business activities within the premises. The assessment was based on the presumption that many of the businesses were as a matter of fact operating in partnership – a business splitting direction would then not be necessary, because all the activities should have been reflected in the VAT returns of the one entity that was registered.

The Tribunal considered the history of the investigation into the business and the dispute over the assessment and penalties, which appeared to involve a number of procedural errors by HMRC. This included the surprising error that the Sch.24 penalty purported to cover a period before 1 April 2009. The Tribunal considered that this rendered it invalid in its entirety – it could not be partly valid. The appeal against the penalty was allowed on this basis. In case the decision on validity was wrong, the Tribunal considered the basis of the penalty and agreed with HMRC's calculation of the potential lost revenue, their assessment of the behaviour and the mitigation.

The assessment was based on evidence about the total sales made from the premises, with a number of adjustments and assumptions. Although there were possible criticisms of the officer's approach, it appeared to satisfy the "best judgement" rules and the trader's arguments were not sufficient to displace it. It was therefore confirmed.

The procedural problems included confusion over the timing of the issue of the misdeclaration penalty and the appeal against it. The Tribunal was satisfied that it had been validly issued. The trader's main ground of appeal was that it should be mitigated to nil using the same criteria as for a Sch.24 penalty; the Tribunal did not agree that the criteria were the same under s.70 VATA 1994, and decided that no mitigation was appropriate.

Turning to the direction notices, the Tribunal noted that its jurisdiction was only supervisory – it had to consider whether the decisions had been reasonably made. There was further confusion in the issuing of the directions, because earlier notices had been issued and withdrawn, then replaced with identical notices operating from a later date. The officer had identified financial, organisational and economic links between the entities named in the directions, and the Tribunal could not find anything unreasonable about that conclusion. The trader argued that "it was for HMRC to prove that the entities operated as a single business", but this was not correct: it was only for HMRC to conclude that the matters stated in Sch.1 para.2(2) were satisfied. It was then for the taxpayer to show that this was wrong, which they had failed to do. The appeal against the directions was dismissed.

First-Tier Tribunal (TC05064): *The Grand Folkestone Ltd and another*

6.7.2 Time limit

In TC04536, assessments and dishonesty penalties levied on a grocery and off-licence were upheld in principle, subject to submissions on whether the assessments had been raised in time. The question was whether the assessments had been raised within one year of HMRC having evidence of the facts "sufficient in the opinion of the Commissioners" to justify the making of the assessments.

The Tribunal referred to the CA judgment in *Pegasus Birds Ltd* as the leading authority on the issue. Aldous LJ set out the following principles:

1. The commissioners' opinion referred to in s 73(6) (b) is an opinion as to whether they have evidence of facts sufficient to justify making the assessment. Evidence is the means by which the facts are proved.

2. The evidence in question must be sufficient to justify the making of the assessment in question (see Customs and Excise Comrs v Post Office [1995] STC 749 at 754 per Potts J).

3. The knowledge referred to in s 73(6) (b) is actual, and not constructive knowledge (see Customs and Excise Comrs v Post Office [1995] STC 749 at 755). In this context, I understand constructive knowledge to mean knowledge of evidence which the commissioners do not in fact have, but which they could and would have if they had taken the necessary steps to acquire it.

4. The correct approach for a tribunal to adopt is (i) to decide what were the facts which, in the opinion of the officer making the assessment on behalf of the commissioners, justified the making of the assessment, and (ii) to determine when the last piece of evidence of these facts of sufficient weight to justify making the assessment was communicated to the commissioners. The period of one year runs from the date in (ii) (see Heyfordian Travel Ltd v Customs and Excise Comrs [1979] VATTR 139 at 151, and Classicmoor Ltd v Customs and Excise Comrs [1995] V&DR 1 at 10).

5. An officer's decision that the evidence of which he has knowledge is insufficient to justify making an assessment, and accordingly, his failure to make an earlier assessment, can only be challenged on Wednesbury principles, or principles analogous to Wednesbury (see Associated Provincial Picture Houses Ltd v Wednesbury Corp [1948] 1 KB 223) (see Classicmoor Ltd v Customs and Excise Comrs [1995] V&DR 1 at 10–11, and more generally John Dee Ltd v Customs and Excise Comrs [1995] STC 941 at 952 per Neill LJ).

6. The burden is on the taxpayer to show that the assessment was made outside the time limit specified in s 73(6) (b) of the 1994 Act.

The essential difference between the parties was this: the appellant considered that HMRC had had all the information that formed the basis of the assessment (business records etc.) after their last visit to the premises on 4 September 2009; HMRC regarded a 20 April 2010 PN160 meeting at their offices, involving the appellant and his tax agent, as significant to the raising of the assessments. The Tribunal considered the different points of view in some detail, and accepted the officer's view that he had received important information at the meeting, without which the assessment could not have been raised. The assessment and penalty were confirmed as raised in time, and the appeal was dismissed.

First-Tier Tribunal (TC05056): *Shahzada Rasul*

6.7.3 Accounts and returns

A company was visited by HMRC on 13 February 2013. The turnover in the accounts was compared to the figures on the VAT returns. Substantial differences were noted – in the year ended 31 July 2009, the accounts showed £944,000 while the VAT returns showed only £601,000. The company's accountants did not provide any explanations for these

differences. A "best judgement" assessment was therefore issued, taking account of the fact that the company made some zero-rated sales.

The company director gave evidence to the Tribunal by telephone. He said the company used a "one-man band" accountant for all of its book-keeping and accounting. Because of a personal tragedy befalling the accountant, certain documentary evidence was not available; as a result, it could not dispute these assessments, and had not been able to claim some £18,000 of input tax that ought to have been due to it when it left the flat rate scheme.

The judge expressed sympathy, but in the circumstances could only dismiss the appeal. The onus was on the company to displace the assessment, and it could not do so.

First-Tier Tribunal (TC05027): *Wholesale Clearance UK Ltd*

6.7.4 Assessments reduced

HMRC assessed a takeaway restaurant for periods 06/06 to 06/12 in the sum of £81,682. They then accepted that the assessment was out of time, so they replaced it with another for just £7,930 for periods 03/12 and 06/12.

The decision records an interesting account of an observation in a restaurant involving two teams coming to eat meals. They observed 55 customers buying meals, but later could only find 43 of these meals in the records. The shortfall was estimated at 22%. The decision goes on to examine a number of credibility checks used by HMRC, including the relationships between drinks and food, and even the cost of hot towels and napkins.

The judge examined the calculations and their bases in detail, and concluded that the assessments were in principle valid in that they were raised to best judgement. However, he considered that some of the bases were flawed, and he reduced the amount by 50% to reflect this. The appeal was allowed to that extent.

First-Tier Tribunal (TC05093): *Enfield Tandoori Ltd*

6.7.5 More restaurant understatement

Another restaurant was subject to an investigation and assessment on estimated 56% understatement of sales, plus a penalty. The Tribunal examined the methodology underlying the assessment and approved it, ruling that it was to the officers' best judgement.

In relation to the penalties, the Tribunal agreed that the correct scale (deliberate not concealed) had been used. However, the Tribunal increased the mitigation for "helping" and "giving" from 10% and 15% to 20% and 20%. The penalty was therefore reduced from 61.25% to 56%, saving the taxpayer about £3,000. The appeal was allowed to that small extent.

First-Tier Tribunal (TC05162): *Xuong Ngo*

6.8 Penalties and appeals

6.8.1 Default surcharge

A company appealed against a default surcharge of £35,060 for its 12/14 period. It had been late submitting by 3 days in 09/14, with the result that its direct debit was collected late, and this led to the issue of a SLN. The 12/14 return was not submitted until 4 March 2015, after the issue of an estimated assessment (and estimated surcharge).

The company appealed on the basis that it had had an accounting breakdown between 4 February and 13 February, following which it had had to investigate the files to make sure that they were not corrupted before filing the VAT return. The company did not send a representative to the appeal hearing; in the absence of further explanation about what alternative actions could have been taken to deal with the problem, and in particular in the absence of any contact between the company and HMRC while the problem was ongoing, the Tribunal did not consider that there was a reasonable excuse. The burden of proof was on the company, and it was not satisfied.

First-Tier Tribunal (TC04995): *Caligor RX Ltd*

A company within payments on account was 8 days late paying the final instalment for the period 05/14 and was charged a 5% surcharge of £32,460. Its POA were £119,862. It had entered the surcharge system after filing and paying late for the 08/13 period; it paid one of the POA 6 days late during the 02/14 period, and suffered a surcharge of £2,397; the 5% surcharge on the balancing payment for 05/14 of £649,206 was much larger.

The company's excuse was that staff had mislaid the HMRC letter setting out the payment deadlines and had looked up the required dates online. They had therefore assumed that they had to pay by 7 July, not by 30 June. The defence was that the penalty was disproportionate to the offence, and the system was discriminatory against POA traders.

The disproportionality defence was withdrawn at the hearing, following the UT decision in *Trinity Mirror*. The judge described the defence as "based on general unfairness". To have mislaid the letter from HMRC and relied on general guidance was not a reasonable excuse (the trader did not argue that it was); the Tribunal had no jurisdiction to allow an appeal on other grounds. The appeal was dismissed.

First-Tier Tribunal (TC04997): *Grosvenor Cleaning Services Ltd*

A company appealed against surcharges for 11/14 and 02/15 on the grounds of insufficiency of funds arising from circumstances beyond the company's control. The company dealt with large construction customers who regularly paid from 76 to 90 days, ignoring the company's 30-day terms. The company was also subject to deductions under the Construction Industry Scheme, which could be offset against PAYE and NI liabilities but not against VAT. It claimed that the deductions it had suffered were larger than its liabilities, so it was in effect paying some of its tax in advance while being penalised for not being able to settle its VAT. HMRC withdrew and reduced some surcharges, but maintained those in dispute.

The judge considered the *Steptoe* conditions in detail, describing the requirement as "could not be predicted with reasonable foresight". The situation in 11/14 was predictable, and the appeal was dismissed in respect of that period. However, there were exceptional circumstances in 02/15 which meant that there was a reasonable excuse.

The company had now moved to non-standard tax periods, which ought to improve its cash flow by matching the dates on which customers routinely paid with the dates on which the VAT fell due.

First-Tier Tribunal (TC05000): *SDI-Unistride (Southern) Ltd*

A married couple partnership running a restaurant appealed against a series of surcharges from 12/07 to 09/12 totalling £14,801. The appeal was based on reasonable excuse due to the ill-health and depression of the wife, who was also her mother's carer. HMRC had cancelled individual surcharges on this basis.

The Tribunal expressed sympathy with the appellant, who was regarded as an honest and straightforward witness to the facts, but did not consider that there were any exceptional circumstances relating to any of the other periods that would constitute a reasonable excuse. The appeal was dismissed.

First-Tier Tribunal (TC05001): *Kevin and Caroline Clarke*

A company on monthly returns appealed against surcharges for 13 periods between 10/12 and 04/14. The company was not represented; when contacted by telephone, an employee claimed that the company had not been notified of the hearing. The company had previously failed to comply with a number of Tribunal directions or provide more detailed reasons for its lateness. As the burden of proof was on the appellant to show a reasonable excuse, and it had not done so, its appeal had to be dismissed.

First-Tier Tribunal (TC05010): *Recruit Right Ltd*

Two connected companies appealed against surcharges of £9,524 and £8,620 for periods from 03/12 to 03/13. The companies claimed that they had reasonable excuses, and the payment was only a day late; it had also been accepted that some of their supplies were exempt, and the surcharges should not therefore be based on the unreduced amounts shown on their VAT returns.

The first two defences were dismissed after detailed consideration. In respect of the third, HMRC argued that the surcharge could only be reduced where the companies had made a successful claim for repayment of the output tax under s.80 VATA 1994. The companies had obtained a ruling in May 2013 that "transfer premiums" for residential property should have been treated as exempt, when they had always been treated as VATable. The companies could not practically return the VAT to the people who had paid it, so they could not make repayment arrangements or sign the related undertakings that would have made a s.80 claim possible.

The judge commented that he did not think this had ever been considered by a court before. The company argued that "outstanding VAT" for the purposes of s.59 ought to be "the VAT that ought to have been due" rather than the VAT that was actually shown on the return. After very detailed

examination of a range of legal principles, the judge concluded that it would be disproportionate to charge a penalty based on late payment of tax that was not, in fact, properly due. He considered that the Tribunal had the power under s.84(6) VATA 1994 to adjust a surcharge to the amount that was appropriate under s.59. The figures were not available to be sure of the appropriate reduction, but the judge directed that HMRC recalculate the surcharges on the basis of reduced amounts. The appeal was therefore allowed in part.

First-Tier Tribunal (TC05011): *Kingsdale Group Ltd and another*

A trader appealed against a 15% surcharge of £1,283 for the late payment of VAT for the period 10/14. The ground for the appeal was effectively disproportionality for a single day's delay, which could not succeed. However, the Tribunal took note of the trader's evidence about the reasons for earlier defaults, which arose after his wife's serious illness. The judge considered that this was a reasonable excuse for two earlier periods; reducing the 10% surcharge to 2% brought it below the de minimis £400, and a 5% surcharge for the 10/14 period would be less than the 10% surcharge already paid and now cancelled. The appeal was allowed in part, with a complete success for the trader.

First-Tier Tribunal (TC05038): *Fusion Care Solutions Ltd*

A trader appealed against surcharges for three successive periods. She had been in the system for some time, so these were charged at 10%, 15% and 15%, and amounted in total to nearly £6,000. The appellant did not appear, and there was nothing in her written submissions that could constitute a reasonable excuse. The appeal was dismissed.

First-Tier Tribunal (TC05055): *Nicola Kellett*

A trader appealed against a surcharge for its 11/14 period. The return was filed electronically on 6 January 2015, but payment was made by four cheques between 9 January and 17 February. The company claimed to have sent £35,000 of the money "in good time", but the cheque was dated 6 January – as cheque payments do not enjoy the 7-day extension, this could not possibly clear HMRC's bank account by the due date of 31 December. The appeal was dismissed.

First-Tier Tribunal (TC05066): *Falconwood Employment Agency*

A partnership appealed against surcharges totalling £74,941 covering periods from 06/09 to 12/11. The original appeal had been against a further 11 earlier periods, but that appeal was struck out at an earlier hearing. The business had cash flow problems that were exacerbated by being subject to Construction Industry Scheme deductions. There were also specific problems with bad debts as well as the general difficulties of trading in the manufacturing sector in the period concerned.

The partnership argued that HMRC's allocation of its payments to historic rather than current debts left it always unable to catch up. The Tribunal commented that it was possible for the partnership to insist on an allocation to current debts, which would have meant that it was not in default at all for several periods; but it had not done so. The defaults were therefore in most cases avoidable, which removed the reasonable excuse defence.

The judge allowed two specific factors – one customer going into administration, and the withdrawal of overdraft facilities by the bank – to constitute reasonable excuses for part of the late payment in the specific periods in which those events happened. To that very limited extent, the appeal was allowed; in all other respects, it was dismissed.

First-Tier Tribunal (TC05069): *GH Preston Partnership*

A brewery company appealed against surcharges totalling £7,267 over 18 periods. It was lossmaking from 2008 to 2011, before returning small profits in 2012 and 2013. The trader argued that its cash flow difficulties were beyond its control, and the surcharges were effectively "payday lending" interest.

The Tribunal commented that it saw no justification for HMRC's expressed view that only an unforeseeable event beyond the taxpayer's control could constitute a reasonable excuse. "The test is simply what is reasonable in all the circumstances." The CA judgment in *Steptoe* placed the burden on the taxpayer to show that there were specific reasons to show why foresight, diligence and regard to the due dates for payment would not have avoided the surcharge in each of the 18 periods. The taxpayer's arguments were not sufficiently specific to show this – they were general in nature, not surprisingly as they covered such a long period.

As regards disproportionality, the Tribunal could only quote the *Total Technology* decision of the Upper Tribunal and apply it. The appeal was dismissed.

First-Tier Tribunal (TC05072): *Lovibonds Brewery Ltd*

A company appealed against surcharges of £21,595 and penalties for incorrect returns of £18,923. The company bought scrap metal and exported it, mainly to India. It therefore made monthly returns and claimed repayments. In 2012 HMRC decided there was a risk of MTIC fraud, and subjected a return to extended verification. This created a severe cash flow problem for the trader, which depended on the VAT repayments. Some VAT was eventually released, but the dispute about the returns for 03/12, 04/12 and 05/12 continued into 2013. In June 2013 HMRC agreed to release the payments "without prejudice" while they continued to investigate, but by now the company was submitting returns late and in a payment position, so it was incurring surcharges.

When HMRC finally completed their investigation, they notified a number of overclaims for input tax and underdeclarations of output tax, some categorised as careless and some as deliberate; all had been discovered following prompted disclosure. Penalties of 18% and 35% respectively were added to the assessment of nearly £57,000 of overclaimed and underdeclared VAT.

The company argued in respect of the penalties that they should have been calculated taking into account the fact that HMRC owed repayments to the company, and also claimed that the disclosures were unprompted. The surcharges should have taken into account the repayments outstanding, with the result that the company was in credit with HMRC during the periods surcharged.

The judge (J Gordon Reid) commented that in the context of the size of the business (turnover of about £16m), the errors of £56,000 were almost de minimis. HMRC's initial reason for investigation (suspected MTIC fraud) had turned out not to be justified; the errors were different in nature, and had only come to light because of the continuous and considerable cooperation of the company's accountants. The judge therefore concluded that it would be too harsh to categorise the disclosure as prompted: the penalties should be calculated on the unprompted scale. The judge considered that the maximum mitigation should be given for cooperation, reducing the careless penalties to nil and the deliberate penalties to 20%.

The judge commented that he considered the levy of huge fines for minor delays in administrative matters unparalleled in any other area of law. However, he considered himself bound to follow the decisions in *Trinity Mirror* and *Total Technology*, and dismissed the appeals against the surcharges.

First-Tier Tribunal (TC05079): *JSJ Metal Recycling Ltd*

The England and Wales Cricket Board appealed against a surcharge of £106,602. Several grounds were included in the notice of appeal, but by the time of the hearing, the only issue in dispute was whether a surcharge liability notice had been received.

HMRC objected to the late arrival of a skeleton argument and list of authorities, which were served by the appellant by e-mail the day before the hearing and were only actually received on the day of the hearing itself. The judge noted that the Tribunal directions did not call for skeleton arguments, and surcharge appeals are normally "turn up and talk" hearings – the objection to the argument was therefore unfounded, but the start of the hearing was delayed by 45 minutes to allow HMRC's representative to read the documents. Late service of precedents was more serious, but HMRC had been aware of the cases earlier in the dispute, and therefore there was no prejudice to them.

The 1989 case of *Customs v Medway Draughting and Technical Services Ltd* was cited as authority for the proposition that a surcharge could not be levied if the notice had not been received.

The problem arose in respect of the 04/15 period, during which the Board was within the POA regime. It acknowledged that it had been 3 days late paying the balancing payment, and had no excuse for that. HMRC produced a copy of the SLN issued in respect of the 04/14 period. HMRC do not normally keep copy SLNs, but they do for POA regime taxpayers. The default in that period had been in respect of the first instalment payment: the return, the second instalment and the balance had all been on time.

The taxpayer's management accountant gave evidence about the post-receiving procedures. He said he had no record or recollection of the SLN being received; he also gave other examples of correspondence from HMRC that had never arrived. HMRC did not produce any evidence to contradict this; although they claimed that the entries in their computer records meant that the SLN must have been posted, and they said there was no record of it being returned by the Royal Mail, the accountant's

evidence was effectively undisputed. Based on the *Medway* precedent, the appeal therefore had to succeed.

First-Tier Tribunal (TC05107): *England and Wales Cricket Board Ltd*

A company appealed against a 2% surcharge of £867 for its 09/15 period. The payment was made on Thursday 5 November by a new staff member who did not realise that BACS payments would take extra time when a weekend intervened. The Tribunal considered that the trader should have ensured that the staff were properly trained or supervised, and there was no reasonable excuse. As usual, a separate complaint about the excessive size of the penalty was rejected.

First-Tier Tribunal (TC05124): *Ascot International Sports & Footwear Ltd*

A company appealed against a 15% surcharge of £737 for its 10/15 period. The payment was two weeks late. The trader wrote to appeal the penalty in February 2016 (although the letter was dated 5 February 2014); he explained that his online banking ID was locked out, and he had to visit the branch to sort the problem out. He also said "You can also check and verify that my company has never made a late payment in all previous years."

HMRC produced a schedule of defaults including periods 01/14, 04/14, 07/14, and 10/14. It appears that the trader then complied with the rules for 3 successive periods; if 10/15 had been on time, he would have escaped the surcharge system. The Tribunal noted that the trader seemed to be imprecise about dates; no evidence was produced of the banking problems; he could have discussed them with HMRC before the due date. There was no reasonable excuse, and the appeal was dismissed.

First-Tier Tribunal (TC05125): *Gamma Infinity Ltd*

A company appealed against a surcharge at 10%. This was a fourth default: the 2% penalty had been below the £400 limit, and no appeal was lodged against a £544 penalty at 5%. The liability had been paid by instalments; one of those, amounting to £12,000, had been paid one day late. The director did not object to the surcharge levied on the rest of the late payments, but considered that the £1,200 relating to this instalment was disproportionate.

The Tribunal judge, J Gordon Reid, commented that he might have agreed if he was not bound by authority. He "respectfully suggested" that the surcharge regime requires urgent consideration. However, he had no choice but to dismiss the appeal.

First-Tier Tribunal (TC05135): *Gastropub Hospitality Ltd*

A company appealed against a 2% surcharge of £540 for its 09/15 return period. The trader submitted the return on time, but HMRC's requested direct debit was returned unpaid because the funds in the account were insufficient. The company had been waiting for payment from a client that arrived a week late, and had also been waiting for a repayment of PAYE from HMRC amounting to £3,500 for about 12 months. The DD exceeded the amount in the account by £1,784.

The Tribunal considered that HMRC's delay in repaying the overpaid PAYE was "an unexpected or unusual event that is either unforeseeable or

beyond a person's control". HMRC's suggestion that "had we repaid the money the trader might have spent it on something else" was rejected as conjecture. At the time the DD was rejected, HMRC owed the company more than the amount by which the DD exceeded the funds available. That was a reasonable excuse, and the appeal was allowed.

First-Tier Tribunal (TC05140): *PR Powersaving Solutions Ltd*

A golf centre appealed against seven surcharges totalling £9,536 covering the periods 05/13 to 11/14. The appeal was brought out of time, but as the appellant had been in constant correspondence with HMRC and with the Adjudicator's Office, the judge considered that HMRC could have been in no doubt that he wished to challenge the penalties, and granted permission for the late appeal.

The trader had in the past agreed Time To Pay following the 2007 floods. When the last instalment was cleared, a visit revealed inaccuracies in accounting for VAT on catering, and an assessment followed. There were further problems in paying current and brought forward VAT, and surcharges followed. The decision records in detail the continuous efforts by the trader to settle the VAT and the continuous efforts by HMRC to enforce the debt over a long period.

The essence of the trader's appeal was that he had agreed a regular payment with an HMRC officer to continue while he tried to sell the business. In his view, he had followed this agreement. However, it was an oral agreement. HMRC provided a witness statement written by the officer, but did not make him available for the hearing. The judge described this as "remarkable", given that the whole point of the dispute was whether an oral agreement existed.

Nevertheless, the judge concluded that the officer could not have intended the TTP agreement to cover current and future VAT: from the facts, it appeared that it must only have covered the arrears. Some of the surcharges should be recalculated to give credit for some payments that appeared to have been made on time, but the appeal was dismissed in relation to the reasonable excuse/TTP argument.

First-Tier Tribunal (TC05159): *Sherdons Golf Ltd*

A company appealed against a 10% surcharge of £6,658 for the return period 09/15. Payment was three days late. The only basis of appeal was proportionality. The company operated TTP for its 12/15 return period. The judge (J Gordon Reid) made the same comment as in TC05135 above: if he had been free of binding authority, he might well have considered that the surcharge was disproportionate. However, he had no choice: "In the light of *Trinity Mirror*, its reasoning and the relatively brief discussion before us, we cannot hold that the imposition of a penalty of some £6000 for a minor administrative error enduring some three days, in circumstances in which there was no loss of or risk to the revenue was disproportionate and liable to be set aside."

First-Tier Tribunal (TC05174): *Highland Wood Energy Ltd*

A company appealed against a 15% surcharge of £24,447 for its 04/15 period. The company had applied for TTP before the due date; this was initially refused, but accepted after the due date. By that time, the surcharge had been imposed.

It appeared that TTP had been refused in a telephone call by an officer because the company had had several TTP agreements in the past. The company claimed that it had always complied with such agreements; the officer's note stated that non-compliance was a reason for refusal, but HMRC produced no evidence to show that there had been such non-compliance, and it did not appear to have been put to the director in the phone call.

When HMRC sent a winding-up warning to the trader on 6 July, he rang again and this time was allowed TTP for the 04/15 outstanding VAT. He submitted to the Tribunal that this satisfied the wording of FA 2009 s.108: he had applied for TTP before the due date for the VAT, and HMRC agreed to TTP. There was no statutory requirement that the agreement should be before the due date.

The judge (Anne Redston) examined this proposition in detail, and accepted it. HMRC's view that a TTP agreement was only valid to prevent the surcharge if HMRC had agreed to it by the due date would be without parallel in the tax system – reliefs are time-limited by when the taxpayer claims them, not by how long HMRC take to agree. On this basis, the appeal was allowed. Separate arguments about reasonable excuse and proportionality were rejected.

First-Tier Tribunal (TC05177): *BW Hills Southbank Ltd*

A company appealed against a 5% surcharge of £652 for its 02/15 period. The main ground was that one of the directors was on paternity leave (a copy of the child's birth certificate was produced in evidence). The Tribunal had some sympathy, but agreed with HMRC that in a business with two directors, procedures should have been in place to deal with the director's absence. The appeal was refused.

First-Tier Tribunal (TC05179): *AZ Automobiles Ltd*

A company appealed against a 15% surcharge of £2,318 for its 04/15 period. It appeared that the company had requested a bank transfer on a weekend, but this had only been actioned by the bank on the Monday, one day after the due date. The company argued that HMRC had a discretion to levy the surcharge or not, and should have exercised this discretion in the company's favour. It also argued that the penalty was disproportionate and unfair.

The judge accepted that VATA 1994 s.76 does include the word "may"; however, s.83 does not make this a matter appealable to the FTT. The surcharge was harsh, but not so harsh as to be manifestly unfair. The appeal was dismissed.

First-Tier Tribunal (TC05188): *Damson Consulting Ltd*

6.8.2 Dishonest conduct

In TC02762, the FTT held a director liable for a s.60 penalty in respect of VAT claims by his company which were supported by falsified invoices. The case included the unusual point that HMRC had to vacate the assessment to collect the tax in respect of one period, because they had initially raised it for the wrong period and were out of time to raise a new correct assessment; however, according to the precedent case of *Ali t/a Vakas Balti* (CA 2007), HMRC were still entitled to base a s.60 penalty

on the full amount of the tax which the trader had attempted to evade (successfully, in the end, because of HMRC's administrative error).

The director appealed to the Upper Tribunal. The FTT had not commented on the burden of proof, which lies with HMRC in a dishonesty case; rather, it had stated that it was "not convinced" by the director's explanations, which suggested that it had placed the burden on him. It was also questionable whether the director's actions in relation to the fabricated invoices were enough to constitute dishonesty – he had not been involved in fabricating them, but had simply submitted them to HMRC after obtaining what purported to be copies from the suppliers.

Mr Justice Newey held that it was not clear that the FTT had applied the law correctly. If it had done so, it should have explained the basis of its decision in much more detail to make it clear how the law was being applied. The appeal was allowed, and the case was remitted to the FTT for reconsideration.

Upper Tribunal: *Brookes v HMRC*

6.8.3 Error penalties

HMRC assessed a penalty on the "deliberate not concealed" scale for the period 09/14. The amount was £7,878. The problem arose from transactions with an associated company: the director and owner of the appellant had separated from her partner, and they now carried on business through separate companies. The other company had made part payments of an invoice from her new company, and she had excluded them from the records she provided to her accountants for preparation of the VAT return for the period. This was done by a junior staff member on the last available day for submission, and the exclusion was not picked up. It appeared that the other company was claiming the VAT back from HMRC, and could not afford to pay the full amount of the invoice until HMRC made the repayment; this was subjected to a verification visit, so there was a delay.

After investigation, HMRC decided that the error was "deliberate, not concealed", and allowed the maximum mitigation for an unprompted disclosure. The penalty was charged at 20%. HMRC's representative contended that the measure of behaviour for Sch.24 was that there was "conscious thought behind the taxpayer's actions". The taxpayer had made reference to a "cash flow issue" in correspondence about the penalty, which suggested that she had deliberately decided not to declare the part-payment receipts in an attempt to resolve that issue. A responsible taxpayer would have contacted HMRC to clarify the treatment.

The Tribunal stated: "*In our view, a deliberate inaccuracy occurs when a taxpayer knowingly provides HMRC with a document that contains an error with the intention that HMRC should rely upon it as an accurate document. This is a subjective test. The question is not whether a reasonable taxpayer might have made the same error or even whether this taxpayer failed to take all reasonable steps to ensure that the return was accurate. It is a question of the knowledge and intention of the particular taxpayer at the time.*"

The Tribunal accepted the director as a credible and honest witness, and accepted that her belief at the time of submission of the return that it was correct to treat the part-payments as relating to the non-VAT element; her reference to the "cash flow issue" was to the other company's inability to pay the invoice in full until it recovered the VAT from HMRC, at which point it would pay the VAT, enabling her company to pass it back to HMRC. This was clearly a misunderstanding of the VAT rules, but it was her belief.

The judge considered that this was an innocent mistake rather than an attempt to obtain an advantage, compounded by a mistake in the agent's processing of the figures on her behalf. It should be penalised on the "careless" scale, and as HMRC had accepted that disclosure was unprompted and the maximum mitigation should be given, it was reduced to nil. The appeal was allowed.

First-Tier Tribunal (TC05024): *Auxilium Project Management Ltd*

An individual was a sub-postmaster. He met "a man in the pub" who suggested he could make good money by incorporating a company, registering for VAT and dealing in airtime minutes. He did so, giving "telecommunications consultancy activities" as the company's business, and estimating its turnover in the first year at £80,000. The first two periods to 10/13 and 01/14 produced nil returns; the third period showed sales of £2,444,870 and purchases of £2,439,877, with reported input tax of £487,975.50.

HMRC visited the company's address and interviewed the individual. He could produce no documentation to support the existence of the trade or the contracts. He claimed that the transactions were carried out by a man called "James", who was uncontactable. HMRC subsequently deregistered the company, assessed to disallow the input tax claim, and assessed a penalty for a deliberate inaccuracy. The company was dissolved, but HMRC issued a personal liability notice to the individual for the full penalty of £281,205 (at 57.5%).

The basis of the appeal was that the individual had believed the penalty would go away if he dissolved the company. If he had known he could be made personally liable, he would have appealed against it. Now that the company no longer existed, that was not possible. There were alternative grounds of appeal that were somewhat desperate – the assessment was addressed to "Ltd" when the company's name was "Limited"; there was nothing in HMRC's pleadings to show that the penalty had not in fact been paid by the company; and if there was no input tax there should also have been no output tax, so the true liability was nil.

The Tribunal decided that it did have jurisdiction to hear an appeal about the underlying penalty, at least insofar as it related to the officer made liable for it. However, the objections to the company penalty were without any merit; it was also clear that there were deliberate inaccuracies in the returns, and they had been submitted by the sole director and shareholder. He was responsible. The appeal was dismissed.

First-Tier Tribunal (TC05068): *Jason Andrew*

In an article in *Taxation*, Richard Curtis examines this decision and the consequences of agreeing to something that sounded much too good to be true.

Taxation, 2 June 2016

HMRC issued information notices to a company asking for statutory records going back to 2009. The company had been registered for VAT from 1 April 2015 following a visit, and HMRC wanted to confirm whether it should in fact have been registered earlier. The company did not provide the information, and HMRC levied penalties under FA 2008 Sch.36 (fixed penalty of £300 and daily penalties of £900). Neither the company nor its representative attended an appeal hearing, but the HMRC representative explained the history of the matter.

The letter accompanying the information notice stated that there was no right of appeal against it, because it only asked for statutory records. However, the judge questioned whether all the records asked for were covered by this rule; in addition, there was a questionnaire that clearly asked for information, which went beyond statutory records, and was not covered by the "no appeal" rule.

There was a difficulty: HMRC justified the notice as requiring statutory records on the basis of SI 1995/2518 reg.31 – documents supporting the VAT account. However, this only applied to a "taxable person". Until the enquiry reached a conclusion, it was not possible to say whether the trader was a taxable person. However, the judge was satisfied that the information notice was validly issued.

The judge was also satisfied that the £300 fixed penalty had been assessed, and the assessment notified to the taxpayer. However, the records did not convince the judge that the daily penalty had been correctly raised. There was a combination of factors that the Tribunal considered constituted a reasonable excuse for failure to comply with the notice – including the fact that the trader had appointed an agent, took immediate action following the visit, had registered for VAT apparently giving much of the same information on the VAT 1 that had been requested on the information questionnaire, and the fact that the agent fell ill at around the crucial time.

The judge also criticised HMRC's "local" policy for setting daily penalties, and the officer concerned for taking into account irrelevant information in taking the decision of how much to assess. Had the Tribunal agreed that the daily penalty had been validly assessed, it would have varied it from £30 per day to £10 per day.

The appeal was allowed, cancelling both the fixed and daily penalties, for slightly different reasons. The judge went on to make general observations about the way in which HMRC had conducted the enquiry. The rules on review of and appeals against Sch.36 penalties were not the standard rules, and the officers concerned appeared to have misunderstood them and explained them incorrectly to the taxpayer. In the end, "no harm had been done", but unfairness and injustice could result.

First-Tier Tribunal (TC05081): *Mumbai Kitchen (Bromley) Ltd*

A firm was charged a penalty of £582 for failing to notify a change from sole trader to partnership. The penalty was for failing to notify liability to register, and was charged under FA 2008 Sch.41. The relevant period was 20 November 2012 to 15 July 2014. The partnership applied for registration on the latter date, but stated in its application that it had taken over another business as a going concern on the former date. The earlier business was a plumbing business carried on by a father, who had entered into partnership with his son. The father's VAT registration number was transferred to the partnership in September 2014.

The judge (J Gordon Reid) commented that the penalty was being charged on a mere technicality, an administrative hiccup which caused no inconvenience to HMRC and no loss of revenue, because the father had continued to account for VAT throughout. There were significant failings in how HMRC had dealt with the matter, including failing to respond to correspondence from an agent, and had therefore caused the taxpayer significant expense and inconvenience. Although there was a failure, a further reduction should be made, and the penalty was reduced to £100.97.

First-Tier Tribunal (TC05101): *J & W Brown*

An individual appealed against decisions from 2007 and 2008 to assess £70,000 and charge a belated notification penalty of £10,000. HMRC had concluded from self-assessment returns that the individual had been trading above the registration threshold (as a second hand car dealer) from at least 1999 to 2005. Further investigation led to a registration backdated to 6 April 1987. This was later amended to 6 April 1991.

The Tribunal carried out a detailed examination of the history of a dispute going back many years. There were changes of accountant and disputes between the taxpayer and the accountants as well as between the taxpayer and HMRC. After considering a substantial amount of evidence and argument, the judge concluded that the assessments were made to best judgement and the taxpayer had failed to discharge the burden of proof required to displace them. The appeals against assessment and penalty were dismissed.

First-Tier Tribunal (TC05094): *Susan Wilson*

A company engaged in what appeared to be contra-trading in relation to MTIC transactions. A number of assessments proceeded through the courts to a Court of Appeal hearing about a winding-up petition in the early part of 2015. Subsequently HMRC sought penalties against the director and the company for "deliberate and concealed inaccuracies", charged at 100% of the PLR with a 25% reduction for cooperation. The Tribunal examined the history, and although not accepting a number of factors in the director's defence, it concluded that the errors for two periods were not deliberate but careless, and for the later periods they were deliberate but not concealed. They should therefore be penalised at 30% and 70%, in each case with the same 25% reduction for cooperation, rather than at 100%.

First-Tier Tribunal (TC05153): *Changtel Solutions Ltd and another*

A company was found to have understated its output tax for periods 06/11 to 09/12 by £145,000. A penalty assessment was raised under Sch.24 FA 2007 for £50,576, i.e. 35% of the PLR – maximum mitigation for a prompted disclosure of a deliberate inaccuracy.

The circumstances of the case were unusual. The company installed solar power equipment in houses. Up to 2011, there was a very attractive government-sponsored regime to incentivise householders to do this. The regulations were changed comprehensively in early 2012, after an earlier attempt to make changes was ruled unlawful by a judge. The uncertainty that this created had a damaging effect on the company's business and cash flow.

It appeared that the director had manipulated the figures on the VAT returns to deal with the company's cash flow problems. He claimed that he thought he was entitled to do this as a form of "cash accounting", but the judge did not accept that this was a reasonable belief, and probably was not even his actual belief. The manipulation of the returns started even before the arguments over the regulatory changes. The judge was satisfied that the penalty was correctly assessed on the deliberate scale; although it might be considered harsh in the circumstances, it was not disproportionate. The appeal was dismissed.

First-Tier Tribunal (TC05154): *Solar Power PV Ltd*

A director was assessed to a penalty of £67,436 (reduced at the hearing to £65,660 on account of an arithmetical error) on account of deliberate inaccuracies in his company's VAT returns that were attributable to his dishonesty.

The case was unusual in that it featured operation of the flat rate scheme by a business that had turnover well in excess of the £150,000 limit for entering the scheme. At the time of applying to join the scheme, according to HMRC, the director must have known that the company would not be eligible to use it. The company also accounted for receipts from debt factoring on the net amount rather than the gross, understating its income. Some returns were not submitted at all.

The company had not appealed against the assessment to VAT of £101,466. HMRC contended that this had therefore to be taken as an accepted measure of the inaccuracy. The appellant was a qualified accountant who should therefore have a better understanding of the workings of the tax system than other taxpayers.

The Tribunal discussed the meaning of "deliberate conduct", and made the following comment: "*we consider that the term 'deliberate inaccuracy on a person's part'" can extend beyond this. Our view is that, depending on the precise circumstances, an inaccuracy may also be held to be deliberate where it is found that the person consciously or intentionally chose not to find out the correct position, in particular, where the circumstances are such that the person knew that he should do so. A person cannot simply escape liability by claiming complete ignorance where the person clearly knew that he should have taken steps to ascertain the position. We view the case where a person makes such a conscious choice not to take such steps with the result that an inaccuracy occurs, as no less of a 'deliberate inaccuracy' on that person's part than making the inaccuracy with full knowledge of the inaccuracy.*" On this basis, at the very least the appellant had failed to check the conditions for the FRS and had therefore "deliberately" filed inaccurate returns. The Tribunal was in any case satisfied that the deliberate conduct went further than this, and on the balance of probabilities knew that the conditions for the FRS were not satisfied.

The penalty was correctly calculated, 100% attributable to the individual, and not subject to any further mitigation. The appeal was dismissed.

First-Tier Tribunal (TC05123): *Anthony Clynes*

A company failed to submit returns for the periods 09/10 to 09/11, and paid estimated assessments. Following an investigation, the returns were submitted between 30 November 2011 and 15 March 2012, and showed that the actual liability exceeded the assessments by nearly £575,000. HMRC raised a penalty assessment under VATA 1994 s.60, allowing a 65% reduction for cooperation, and after the company went into liquidation, transferred the liability for half this amount (£100,496) to a director.

The decision refers to s.60 and s.61 VATA 1994, even though the dates are all after 1 April 2009: the penalty was for failure to submit returns, rather than accepting the underassessments, and this appears still to be within s.60. The Tribunal considered this point and confirmed that s.61 was the correct provision for charging the penalty to the individual.

HMRC's assessment of the director appeared to be based on a view of what a "hypothetical director" would know of the operation of the company, rather than on what this director actually knew. After examining the way in which the company operated and the history of the investigation, the Tribunal was satisfied that HMRC had not discharged the burden of proof that lay on them to show that the individual had acted dishonestly, and allowed his appeal.

First-Tier Tribunal (TC05187): *Colin Waller*

6.8.4 ECSL penalty

A company was issued with ESCL penalties totalling £13,000 for a succession of 10 periods from 06/11 to 09/13. All the penalties were calculated on the basis of the maximum 100 days' delay. The director had been in regular contact with HMRC during this period concerning time to pay and debt management, and said he had been unaware of these penalties building up. He claimed that he prepared the sales lists on paper after filing each quarter's VAT return online, and submitted them at that time.

The Tribunal noted that the onus of proof was on the taxpayer to show that the returns had been filed. No evidence of posting had been kept; HMRC said they had not received any of the returns until October 2014. The Tribunal held that, on the balance of probabilities, they had not been filed. The penalties were not disproportionate, and there was no reasonable excuse. The appeal was dismissed.

First-Tier Tribunal (TC04999): *Stereomatic Ltd*

6.8.5 Article

In an article in *Taxation*, Neil Warren examines the recent decision in *MJ Hickey Plant Hire and Contracts Ltd* and what appears to have been an ill-advised attempt to delay the payment of VAT to avoid default surcharge, resulting in an even larger error penalty.

Taxation, 5 May 2016

6.8.6 Appeal out of time

An individual sought leave to appeal out of time against decisions covering both income tax and VAT in relation to 2007/08 and five other years, following a closure notice at the conclusion of an enquiry. There were VAT assessments and a civil evasion penalty, as well as income tax charges. The deadline for appealing the income tax matters was 18 January 2013 and the VAT matters was 30 September 2013, but an appeal was not made to the Tribunal until 17 February 2014. This was as a result of debt management action being taken by HMRC.

The Tribunal considered the reasons for the late action by the taxpayer, which were mainly based on ill-health of himself and his partner (also his book-keeper), and non-receipt of certain correspondence from HMRC. The judge also considered the level of prejudice to both the taxpayer in refusing the application and to HMRC in allowing it. Although the prejudice was considerable, she considered that the taxpayer's delays were too great, and could not all be blamed on the ill-health that was put forward – for example, the partner suffered a stroke, but that was some time after the appeal was actually lodged. As a result, the assessments and penalties would stand.

First-Tier Tribunal (TC05083): *Anthony Lorimer*

6.8.7 Strike-out

An individual claimed a repayment of £7,045 in VAT paid on estimated assessments for the periods 02/08 to 11/09. A problem had arisen because he had traded as an individual but had also set up a company to which he considered transferring the business. For a while both were registered for VAT. He had thought he had ceased to trade as an individual, so he stopped making returns; that was the reason for the issue of estimated assessments, which he paid. He only finally made nil returns in September 2014.

The Tribunal agreed with HMRC. The effect was harsh but the Tribunal had no discretion. The nil returns were filed more than four years after the payments, and could not lead to a repayment. The appeal was struck out because there was no reasonable prospect of success.

First-Tier Tribunal (TC05047): *Peter Walls t/a Charlies Accessories Ltd*

6.8.8 Reinstatement

A Subway franchisee made an appeal that was one of the many stood over behind the lead case *Sub One Ltd t/a Subway*. Following the Court of Appeal's determination of that litigation, the Tribunal wrote to this appellant on 10 July 2015 to find out if it intended to pursue its appeal in spite of HMRC's success. As no reply was received, an "unless order" was issued, and as no reply was received to that, the appeal was automatically struck out on 14 August 2015.

In September 2015, the company became aware of a different line of argument being advanced on behalf of other Subway franchisees by a different firm of lawyers, and decided to apply for reinstatement. These new grounds have recently also been struck out by Judge Mosedale as having no real prospect of success (in *Lake Avenue and others*).

In any case, Judge Mosedale did not consider that there was a good reason for the delay in applying for reinstatement in this case. There was a public interest in finality of litigation. If a litigant could reinstate an appeal simply because more optimistic legal advice had been received, there would be no finality. The application was refused.

First-Tier Tribunal (TC05042): *Maltavini Ltd*

A company appealed in May 2014 against a refusal of input tax of £509,000 claimed in periods 06/11 to 09/12. Over the next 15 months, it failed to comply with numerous directions, and after an "unless" order in March 2015 demanding a response, reissued on 29 April 2015, the appeal was struck out on 3 September 2015. On 24 September 2015, the appellant's representative applied to have the appeal reinstated.

The judge noted the importance of the principles set out in the *Mitchell* and *Denton* cases when considering reinstatements and striking out for non-compliance: the need for litigation to be conducted efficiently and at proportionate cost, and to enforce compliance with rules, practice directions and orders.

The Tribunal listed the failures of the company to engage in the process, which were serious and continuous. The main reason for this was the appellant's difficulty in understanding the appeals process. Although the judge had some sympathy with his predicament, he felt that the appellant could have asked for help from the Tribunal or even from HMRC in dealing with the process. Instead, he ignored communications. In all the circumstances, it was not appropriate to reinstate the appeal.

HMRC applied for costs, not of the original appeal, but of the reinstatement application. The judge agreed that the seriousness of the breaches meant that the appellant's representatives ought to have concluded that the application was hopeless, and awarded costs of £6,333 to HMRC.

First-Tier Tribunal (TC05088): *Infocom IT (UK) Ltd*

6.8.9 Costs

A company was involved in a hearing over 17 days during 2008, and was required to pay 80% of HMRC's costs under the "old rules". Subsequently both sides appealed to the Upper Tribunal, which remitted the case to the FTT for further findings of fact. Following a further two day hearing, HMRC applied for their costs again. Judge Hellier considered a number of balancing factors and decided against awarding costs. The second hearing was so long after 1 April 2009 that it would have been reasonable for the parties to expect that the "new rules" would apply in the absence of a specific application or direction.

First-Tier Tribunal (TC05035): *S & I Electronics plc*

An individual made a DIY claim for £14,240, and appealed to the FTT against a refusal of that claim. The FTT found against him, on the basis that the planning consent linked the dwelling to other properties. He appealed to the Upper Tribunal on the grounds that he was applying for retrospective amendments to the planning consent. Leave to appeal was refused on the grounds that the UT had by then given a decision on retrospective permission in *Patel*. Similar decisions were later reached in

Shields and *Burton*. However, Judge Sinfield gave permission to appeal on the basis that there was a possibility that *Patel* might be distinguished. The basis of the appeal was very limited, but included the possible argument that the original planning restriction was invalid.

At the hearing, the judge warned the appellant that in the UT, he might be required to pay HMRC's costs if he lost. He was very concerned about this and asked for a ruling on whether this would happen. The judge gave an order in advance to this effect in September 2015. HMRC applied for this order to be set aside on the basis that it was beyond the UT's jurisdiction and should not have been made in this case.

Judge Sinfield considered the matter again and concluded that the UT did have the authority to make a "protective costs order". Although his original order should be set aside, he stated that the appellant could apply for a new order in the light of the more detailed analysis of the law in this decision, and HMRC would be able to make submissions in relation to that application.

Upper Tribunal: *Drummond v Revenue and Customs Comrs*

A charity appealed against a decision that construction work in relation to a day-care facility for children was standard rated. The FTT (TC03807) considered the precedent cases, including the two High Court *Cantrell* decisions and also *Macnamara* (VTD 16,039). It approved Sir Stephen Oliver's analysis of Group 5 Note 16:

- there are three exclusions from the zero-rating provisions, which are in descending order of their level of integration with the existing building;
- they are mutually exclusive;
- conversions, reconstructions and the alterations of existing building, the most closely integrated, are excluded first;
- enlargements of existing buildings are then excluded, the word 'enlargement' connoting structural work producing an overall increase in size or capacity;
- then come 'annexes' which, as a matter of principle, are also excluded – the term annexe connotes something that is adjoined but either not integrated with the existing building or of tenuous integration.

The Tribunal then considered in detail the design, construction and use of the new structure. It concluded that it was an extension rather than an annexe, and therefore could not qualify for zero-rating. If the Tribunal was wrong and it was in fact an annexe, it did not satisfy the conditions of Note 17(b)(i) (access to the annexe must not be through the main building). The appeal was dismissed.

The charity sought and was granted leave to appeal to the Upper Tribunal. It also sought a direction that it should be protected from a costs award if it lost. Judge Bishopp declined to give such a direction, whereupon the charity withdrew its appeal. HMRC then applied for costs of resisting the appeal to the Upper Tribunal, and Judge Bishopp had to consider their application. He could see no reason not to grant it, not least because the charity had not made any cogent argument but had asserted that HMRC

should apply their old practice of not asking for costs in the VAT and Duties Tribunal. On the other hand, he accepted that the charity might regard the amount claimed as excessive, and directed that the parties should negotiate over the amount. If there was no agreement, they could return to the Tribunal for a summary decision.

Upper Tribunal: *Gateshead Jewish Nursery v HMRC*

6.8.10 Stay of proceedings

An investment manager reclaimed over £5m of output tax charged to defined benefit pension schemes over the period from 1 April 2009 to 30 June 2012. HMRC refused the claim and the company appealed. It applied to the Tribunal for a direction to stay ("sist") proceedings behind the case of *United Biscuits (Pension Trustees) Ltd v HMRC* that is set for hearing in the High Court. UBPT are arguing a different line from that put forward (and rejected by the CJEU) in *Wheels Common Investment Fund* – that the UK allowed supplies of investment management to pension funds to be exempt if they were made by persons carrying on insurance business, but required them to be taxable if supplied by others. This, according to UBPT, contravened the EU principle of fiscal neutrality.

In its original appeal, the current appellant had advanced the same argument as *Wheels* (that the exemption for special investment fund management should apply), and this could not succeed. The company therefore sought leave to amend its grounds of appeal. Wheels has apparently also applied for a similar re-hearing of its appeal. The Supreme Court's judgment in *Investment Trust Companies* will also have a bearing on these disputes. For these reasons, the company applied to delay the substantive hearing of its own appeal until these other matters have been resolved.

Judge Gemmell considered that the issues in *Wheels*, *UBPT* and the current case were different from each other. In particular, HMRC had not objected to the current appellant's change of its grounds. The issues were simpler, and would not necessarily be determined by the other more complicated cases – not least, because the other cases were being heard by English judges rather than Scots courts. The direction to sist the appeal was refused.

First-Tier Tribunal (TC05108): *First State Investment Management (UK) Ltd*

6.8.11 Procedure

The Berkshire Golf Club and others (TC04774) was designated a "lead case" under rule 18 of the Tribunal Procedure Rules. Another club applied to the Tribunal for a direction that it need not be bound by the decision (that golf clubs would in general be unjustly enriched by full repayment of their *Bridport* claims, but only to the extent of 10%).

An officer of the club wrote to the Tribunal to explain why he did not consider the decision correctly applicable to his club. He argued that the concept of "enrichment" did not apply to a non-profit organisation; he also appeared to believe that the disallowance of input tax on expenditure through being partially exempt meant that there was a double

disadvantage: "To return to the pie-chart depictions in my letter, not only does the payment of the VAT leave a void in the income circle, but the expenditure circle is also enlarged by the entry of the "sticking" input tax. These are both financial burdens borne by the club." He did not attend the hearing to explain this further.

The judge considered the *Berkshire* decision and concluded that it properly took into account all the factors that the officer disputed. The decision was therefore on all fours with the appeal by this golf club, and the application was dismissed.

First-Tier Tribunal (TC05130): *Tadmarton Heath Golf Club Company Ltd*

6.9 Other administration issues

6.9.1 Brexit

The Chancellor made a statement on 27 June following the referendum vote. Not surprisingly, the detail of "what happens to the VAT rules" is completely absent. There will be a great deal of uncertainty, and work to do, while those details are worked out.

www.gov.uk/government/speeches/statement-by-the-chancellor-following-the-eu-referendum

6.9.2 Finance Bill

The Finance Bill 2016 has been delayed by the referendum. It may now only be given Royal Assent in the autumn.

The government tabled a large number of amendments to be considered on Monday 27 and Tuesday 28 June – days when the House was occupied with other matters. The main amendments that affect indirect tax relate to Schedule 18 on serial tax avoidance.

www.gov.uk/government/publications/finance-bill-2016-committee-of-the-whole-house

6.9.3 Tax strategy

The Finance Bill includes a requirement for all qualifying groups, companies, partnerships and permanent establishments to publish a tax strategy, in relation to UK taxation, on the internet. This is aimed at those businesses that are managed by the Large Business Office at HMRC and have Customer Relationship Managers, but others may also fall within its scope. Guidance has been published about the scope of the rules and how to comply with them. The first requirement to publish will be before the end of the first financial year commencing after Royal Assent to the FB 2016, e.g. by 31 December 2017 for a company with a December year end.

www.gov.uk/government/publications/large-business-publication-of-tax-strategy

The Finance Bill also includes measures to tackle the small number of large businesses who engage in aggressive tax planning, or who refuse to

engage with HMRC in an open and collaborative manner. A business will be put into a "12 month improvement period", at the end of which it will enter "special measures" if its behaviour has not improved. Guidance has been published to explain the triggers that will lead to special measures being imposed, the process, the sanctions and the way out of the system.

www.gov.uk/government/publications/large-business-special-measures/special-measures-guidance-introduction

6.9.4 Action on tax fraud

The latest Public Accounts Committee report states that HMRC is not doing enough to combat tax fraud amounting to some £16 billion each year. The PAC concluded that the department had only made "limited progress" in reducing the losses. Particular comments include:

- the level of tax fraud losses has remained relatively constant over the last five years, at around 3% of all tax liabilities;
- HMRC's strategy for tackling tax fraud is unclear, particularly their approach to prosecutions;
- HMRC needs to explain why the amount of tax they claim to have recovered from compliance work rises sharply each year whereas the size of the tax gap stays the same.

The report makes a number of recommendations, including increasing the number and the profile of prosecutions. The PAC is also particularly concerned about fraud in relation to internet transactions, both in electronic services and in goods bought over the internet.

www.publications.parliament.uk/pa/cm201516/cmselect/cmpubacc/674/674.pdf

At the March 2015 Budget the Chancellor said that the government would bring forward plans to introduce a criminal offence for corporations who fail to stop their staff facilitating tax evasion. For the first time, companies will be held criminally liable if they fail to stop their employees from facilitating tax evasion. Draft legislation and guidance for the new corporate criminal offence of failure to prevent the criminal facilitation of tax evasion has been published.

www.gov.uk/government/news/pm-companies-to-be-liable-for-employees-who-facilitate-tax-cheating; http://tinyurl.com/h5vflj7

The Queen's Speech 2016 included proposals for a Criminal Finances Bill that will tackle corruption, money laundering and tax evasion. It will strengthen the UK's enforcement provisions and allow the government to recover more criminal assets by reforming the laws on the proceeds of crime.

6.9.5 Disclosure regime changes

HMRC are consulting on proposals to make sure the VAT avoidance disclosure regime provides reasonable and timely information about avoidance. A consultation on reforms and extension of the regime, which also extends to Inheritance Tax schemes, closes on 13 July 2016.

Particular points to note include the possibility that the basis of the scheme might change. Direct tax schemes must be disclosed by promoters

of schemes, but VAT schemes are only disclosed by users. This difference might be removed in future, in order to give HMRC earlier and more comprehensive detail about schemes as they emerge.

www.gov.uk/government/consultations/strengthening-the-tax-avoidance-disclosure-regimes-for-indirect-taxes-and-inheritance-tax

6.9.6 Senior Accounting Officer guidance

HMRC have updated their guidance on the SAO rules, which require large companies to certify that their records are adequate to prepare reliable tax returns. The Brief covers a number of detailed amendments to the way the rules operate.

R&C Brief 12/2016

6.9.7 Articles

In an article in *Taxation*, Neil Warren examines four separate issues on which HMRC's views have been challenged or are developing over the past 12 months:

- Pre-registration input tax;
- Flat rate scheme categorisation;
- Delays in the option to tax unit over the processing of VAT 1614 forms;
- VAT liability of supplies following residential conversion of pubs.

Taxation, 2 June 2016

In an article in *Taxation*, Steve McIntyre examines the provisions in the Finance Bill 2016 about online sales of goods by overseas persons using "fulfilment houses" in the UK.

Taxation, 9 June 2016