VAT UPDATE
OCTOBER 2015

Covering material from July – September 2015

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1. INTRODUCTION

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

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

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

1.1 Appeals pending

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

The HMRC website section says that it will be updated "on a monthly basis", but it appears to be less frequent or regular than that. The latest update appeared on 18 May 2015 after a gap since 19 January.

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

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

1.1.1 UK appeals awaiting hearing or decision

- *Associated Newspapers Ltd*: HMRC are appealing to the UT against the FTT's interpretation of SI 1993/1507 on gifts of business services (hearing listed for 5 – 7 October 2015).
- *Bridport & West Dorset Golf Club*: the HMRC list notes that three follower cases are going to the FTT on the question of unjust enrichment, hearings listed for 22 – 26 June 2015.
- *British Film Institute*: HMRC have been granted leave to appeal to the Court of Appeal against the UT's confirmation of the FTT's decision that the Institute was entitled to rely on the cultural services exemption in the period 1990 – 1996 in support of a *Fleming* claim.
- *Brockenhurst College*: HMRC have been granted leave to appeal to the Court of Appeal against the UT's confirmation of the FTT's decision that supplies of meals to outsiders were an essential part of the education of the students who prepared and served the meals (appeal scheduled for 4 or 5 November 2015).

- *CCA Distribution Ltd*: HMRC have been granted leave to appeal in relation to 4 of 8 stated grounds against FTT's finding that fraud was not the only explanation of transactions in a MTIC case (hearing date set at 29 June – 1 July 2015).
- *Colaingrove Ltd*: HMRC's list includes separate entries for
    - TC02715 (removable contents/definition – UT allowed HMRC's appeal in part; taxpayer was granted leave to appeal to the CA, but has dropped the appeal).
    - TC02701 (removable contents/apportionment – appeal stayed pending decision in TC02715, neither party now pursuing the matter).
    - TC02534 (fuel – UT decision in favour of HMRC in last update; in April the CA started to hear the company's appeal against the UT's recent decision that it was not entitled to apply the lower rate to electricity supplied as part of a compound supply of "caravan with electricity"). This therefore appears to be the only remaining "live" issue.
    - TC02701 (verandas – UT decision in favour of taxpayer in last update – HMRC will not appeal: R&C Brief in this update).
- *Davis & Dann Ltd and Precis (1080) Ltd*: HMRC have received leave to appeal to the Court of Appeal against the Upper Tribunal's decision that the companies did not have the means of knowing that their transactions were connected with fraud (hearing listed for 24 November 2015).
- *DPAS Ltd*: Upper Tribunal heard HMRC's appeal against the FTT's acceptance that a VAT planning arrangement to circumvent the *AXA* judgment was effective and not abusive (hearing 6/8 May 2015, decision awaited).
- *Finance and Business Training Ltd v HMRC*: taxpayer is applying for leave to Court of Appeal against UT's upholding of FTT's decision that it was not an "eligible body" by being so closely connected with the University of Wales that it became a "college of the university" – oddly, the list says that "HMRC is appealing", even though the decisions below went against the taxpayer (hearing listed for October 2015).
- *GMAC UK plc v HMRC*: last update reported the reaffirmation of the UT decision in favour of the taxpayer on the basis of the CJEU decision (Case C-589/12). HMRC has been granted permission to appeal to the CA.
- *Investment Trust Companies (in Liquidation) v HMRC*: after the CA effectively reversed the High Court's decision in relation to the companies' direct claims for overpaid VAT, both parties are applying for leave to appeal to the Supreme Court.
- *Iveco Ltd*: HMRC have been granted leave to appeal to the Upper Tribunal against the FTT's ruling that a claim for repayment was not subject to the cap (hearing listed for 24 – 25 November 2015).

- *Longridge on the Thames*: HMRC have been granted leave to appeal against the UT's dismissal of their HMRC appeal against the FTT's ruling that a charity was not in business and could receive building services zero-rated (appeal scheduled to start in the Court of Appeal 19/20 April 2016).
- *Mercedes-Benz Financial Services UK Ltd v HMRC*: HMRC have been granted leave to appeal to the Court of Appeal against the decision that the Agility product involved a supply of services rather than goods (hearing commences 21/22 October 2015).
- *MG Rover Group Ltd*: HMRC have been granted leave to appeal against the FTT's decision about who is entitled to claim a refund where an overpayment was made on a group VAT return – case management decisions on this case and *Standard Chartered/Lloyds Banking Group* were issued in March 2015, hearing listed for July 2016.
- *Newey t/a Ocean Finance*: HMRC have been granted leave to appeal to the Court of Appeal against the UT's decision that the FTT was correct to find that the appellant's offshore business arrangements were not an abusive practice, hearing listed for July 2016.
- *Open University*: HMRC have been granted leave to appeal to the Court of Appeal against the UT's decision that the FTT was correct to find that supplies by the BBC to the OU qualified for exemption on the basis that the BBC was "another organisation defined by the UK as having similar objects", hearing listed for August 2016.
- *Pacific Computers Ltd*: the FTT found in favour of a MTIC appellant. HMRC are seeking leave to appeal to the UT.
- *Privin Corporation Ltd*: the FTT found in favour of a MTIC appellant. HMRC are seeking leave to appeal to the UT.
- *Shop Direct Group Ltd*: the company is continuing to appeal against the ruling that VAT repayments and interest are subject to corporation tax (Supreme Court hearing listed for 5 December 2015).
- *The "Spotting the Ball" Partnership & Others*: the taxpayers have been granted leave to appeal to the CA against the UT's overruling of the FTT decision in their favour in relation to the exemption of "spot the ball" competitions (hearing listed for November 2015).
- *Vodafone Group Services Ltd*: HMRC have been granted leave to appeal against the FTT's decision that the trader could replace the reasons for an in-time but disputed claim with the grounds for an accepted but out-of-time claim (UT hearing listed for December 2015).
- *Wakefield College*: HMRC have been granted leave to appeal against the FTT's decision (itself a finding on remittal from the UT) that the college's buildings were used for non-business purposes (hearing listed for 27 – 28 July 2015).

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:

- *AN Checker Heating & Service Engineers*: it was reported that the taxpayer will appeal to the UT against the FTT's decision that none of its supplies of boiler installation qualified for the lower rate as the installation of energy-saving materials. The hearing has apparently been stood over pending the UT's decision in the *Colaingrove* (fuel) case.
- *HMRC v Atlantic Electronics Ltd*: the Court of Appeal has reserved judgment in a dispute about the admissibility of evidence in a MTIC fraud case.
- *John Wilkins Ltd and others*: Supreme Court refused HMRC permission to appeal one aspect of the case, in which the Court of Appeal decided that motor dealers were entitled in principle to claim compound interest on VAT repayments. Substantive issue stayed pending the *Littlewoods* decision in the Court of Appeal (High Court applied the CJEU's judgment in Case C-591/10 in favour of the taxpayer, but HMRC have appealed).
- *Leeds City Council v HMRC*: taxpayer council's appeal to the Court of Appeal against the UT's decision that the three-year cap validly blocked a number of claims for repayment was heard in December 2014.
- *R (on the application of Rouse) v HMRC*: HMRC appealing against Upper Tribunal's decision that they were not entitled to set off a credit against money owing from the taxpayer under s.130 FA 2008.

1.1.3 Cases in the current update

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

- *Finmeccanica Group Services Spa*: HMRC have won their appeal to the UT against the FTT's decision that services were not subject to UK VAT.
- *Volkswagen Financial Services (UK) Ltd v HMRC*: CA has allowed taxpayer's appeal against the Upper Tribunal's decision in favour of HMRC, restoring the FTT's decision that the company's suggested partial exemption special method was more fair and reasonable than HMRC's.

2. OUTPUTS

2.1 Scope of VAT: linking supplies to consideration

2.1.1 Online sales

In an article in *Taxation*, Neil Warren considers the point at which someone selling goods on the internet may become liable for tax and VAT. The key tests are still those given in *Lord Fisher*. Where a person is already registered for VAT in respect of some other activity, it may be prudent to make online sales through a different "person" to avoid bringing them within the scope of the registered business.

Taxation, 3 September 2015

2.2 Disbursements

Nothing to report.

2.3 Exemptions

2.3.1 Warranties are insurance

The CJEU has considered the provision of mechanical breakdown warranties supplied by a third party company to customers of second hand car dealers. The question was whether this was in the nature of an insurance contract (exempt from VAT but subject to insurance premium tax) or was (as described by the taxpayers) the subcontracting by the dealers of some of their after-sales obligations, and therefore a taxable service.

It appeared that the customer entered into a direct contract with the third party company. There was no sub-contract. However, the appellant companies disputed this; the CJEU noted that there was insufficient evidence in the documents before the court to conclude on the issue. This did not make the reference inadmissible, but it would be left to the national court to determine the precise nature of the relationships between the parties.

What was clearer was that the dealer was not directly involved in implementing the warranty agreement – any required repairs did not have to be carried out by or on behalf of the dealer. The way in which the warranty operated was within the scope of CJEU precedents on insurance transactions.

The companies also argued that the warranty was an incidental part of the sale of the car, and therefore taxable for that reason. Because it was supplied by a different company, independent of the car dealer, that did not appear to be possible. Although any insurance transaction was necessarily closely linked to the item insured, that did not mean that it was in all cases "for the better enjoyment of" the item. The provision of a

breakdown warranty and the sale of the second-hand vehicle must, in principle, be considered to be distinct and independent supplies, to be treated separately from the point of view of VAT.

CJEU (Case C-584/13): *Directeur general des finances publiques v Mapfre asistencia compania internacional de seguros y reaseguros SA and Mapfre warranty SpA v Directeur general des finances publiques*

2.3.2 Bitcoin

Advocate-General Kokott has given an opinion that the service of providing a currency exchange between Bitcoins and Swedish legal tender is exempt. At present, the UK (together with Spain, Germany and Belgium) regards Bitcoins as a means of payment and therefore within the exemptions for financial services (see *R&C Brief 09/14*); Poland and Estonia regard Bitcoin exchanges as VATable. The Swedish authorities had also ruled against exemption, and the trader appealed.

The Advocate-General has considered two separate issues. First, it is her opinion that the exchange of Bitcoins for currency constitutes a supply for consideration, following the CJEU judgment in *First National Bank of Chicago*. Although Bitcoins are not legal tender, they are nevertheless intended to be used in the same way as means of payment, so the principle of fiscal neutrality should apply to give them the same VAT treatment.

The exemption for transactions involving means of payment should then apply (art.135(1)(e)). The separate exemptions for bank accounts ((1)(d)) and securities ((1)(f)) are not applicable because Bitcoins do not fall within the more specific definitions of their subject matter. Exemption of the means of payment would be consistent with the purpose of art.135(1)(e), because Bitcoins are used in the course of trade in the same way as legal tender currency.

The facts that Bitcoins are high risk and unregulated should make no difference to the VAT treatment. Even if an activity is illegal, it is still subject to VAT in the same way as a legal equivalent.

CJEU (A-G) (Cases C-264/14): *Skatteverket v David Hedqvist*

2.3.3 Gaming machines

The *Rank* case has reached its conclusion in the Supreme Court, and it is perhaps appropriate in a case about gambling that it is not one that many people had predicted. Here is a brief summary of the history of the dispute:

- Up to December 2005, the law required that income of a gaming machine was taxable if the 'element of chance' was provided 'by means of the machine' (s.23 VATA 1994, before amendments made with effect from 5 December 2005).
- Following the CJEU decision in *Linneweber*, many operators claimed refunds, arguing that their gaming machines did not meet this definition.
- The VAT Tribunal decided in 2008 that 'the machine' for this purpose could not apply to a random number generator (RNG) that was located somewhere else – so terminals attached to a central RNG would not be taxable gaming machines. Because Gaming Act

regulations limited the number of 'machines' that could be operated on the same premises, it was not possible to regard a single RNG with many terminals as one 'machine' – the terminal being played by the gambler was 'the machine', and the remote RNG was 'by means other than the machine'.

- Other claims were made by traders who opened the back of their machines and physically removed the RNG; still more by traders who argued that their machines provided a gaming experience that was identical to those machines, and they should therefore enjoy the exemption on the basis of fiscal neutrality.
- In 2009 the High Court upheld the VAT Tribunal's decision, and questions on the application of the principle of fiscal neutrality were answered by the CJEU in late 2011 (Case C-259/10).
- Following that decision, HMRC conceded that Rank had won in relation to its bingo claims and one ground of their appeal on slot machines. The Upper Tribunal remitted another ground of appeal on slots to the FTT for reconsideration (stayed pending the resolution of the current appeal).
- What remained was the issue of whether terminals with a remote RNG were properly regarded as exempt under the VAT law at the time; in fact, HMRC had so regarded them at the time, but had changed their view (as they were entitled to do).

In late 2013, the Court of Appeal decided unanimously that the only sensible way of interpreting the 1968 Gaming Act provisions was to regard the terminal and ancillary and connected equipment such as the RNG as 'a machine'. The RNG was essential for the game to be played. Even though the Gaming Act provisions were regulations the breach of which could constitute a criminal offence, it was not necessary to read them in a literal way; to do so would effectively make compliance (and VAT) voluntary. Anyone who sought to gain exemption from VAT by physically reconfiguring the machine did so 'with his eyes wide open' and, if he did not obtain clearance from HMRC, ran the risk that they would disagree – and win the argument in court.

The Supreme Court has dismissed the company's appeal, but for completely different reasons. The judgment is surprisingly brief (14 pages, 32 paragraphs), given the long and convoluted history of the dispute. Lord Carnwath gave the judgment and his four colleagues all simply agreed without further comment.

The decision reviews the history and identifies the major issues. The key question is how the element of chance is 'provided'. After some discussion of the concept of 'a machine', in which the judge acknowledges that there is some difficulty in identifying whether 'the terminal alone' or 'many terminals plus RNG' could be 'the machine', he declares that it is not necessary to resolve that issue. The courts below had concentrated too hard on the physical identity of the machine, rather than stepping back and identifying what it did. The game was played by pressing a button or pulling a lever to stop the constantly changing numbers in the RNG and so to produce a result. It was the pressing of the button at a particular moment that generated the element of chance. The

button or lever was part of the terminal, and that meant that the machine in front of the player provided the element of chance.

This is set out in one short paragraph, followed by the end of the affair: "Accordingly, albeit for somewhat different reasons, I agree with the conclusion reached by the Court of Appeal and I would dismiss the appeal."

Supreme Court: *HMRC v The Rank Group*

It remains to be seen what will happen to those *Rank* claimants who have received repayments over the years. HMRC's administration of such cases is not always successful. In theory:

- some claims will have been refused and stood over behind *Rank* – those will now simply fall away;
- some claims will have been paid, and HMRC ought to have raised a protective clawback assessment. Those assessments should now be enforced.

There will probably be some situations in which repayments were made and provisional assessments were not raised. HMRC will have to examine the time limits in order to determine whether they can now claw back the money. In general, a judicial decision is not considered a "new fact" that justifies the raising of an assessment – if HMRC were fighting the case, HMRC always considered that the eventual judicial decision would go in their favour.

2.3.4 Welfare services

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

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

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

The conclusion is that such a body could be regarded as exempt; it should be for the national court to decide whether it falls one side of the line or the other.

CJEU (A-G) (Case C-335/14): *Les Jardins de Jouvence SCRL v Belgian State*

2.3.5 Healthcare

A self-employed individual operated as a medical courier, transporting human organs and samples for hospitals and medical laboratories. She worked under the authority and supervision of a medical doctor. She claimed the benefit of the healthcare exemption for her services; the Belgian authorities ruled that they were taxable. Questions were referred to the CJEU.

The court considered the precedent cases and the difference between the exemption for "medical care and closely related goods and services" within hospitals (art.132(1)(b)) and "medical care" provided by medical professionals (art.132(1)(c)). In the context of this exemption, it was possible for a wide range of services to be regarded as having a therapeutic purpose.

However, the transportation service provided by an independent contractor could not qualify. She was not a "body governed by public law" or any of the other potentially qualifying entities for the purposes of art.132(1)(b), so she could not enjoy the exemption for "services closely linked to healthcare"; she was not herself providing services of a medical nature within art.132(1)(c).

An appeal to fiscal neutrality could not help. Where a laboratory or hospital provided its own in-house transport, that was a different situation and exemption could apply. The appellant was not providing a medical service with transport, but transport on its own.

CJEU (Case C-334/14): *Belgian State v Nathalie De Fruytier*

2.3.6 Health and welfare

A dentists' practice set up a company to provide dental services to the NHS. The practice continued to have the main contract with the NHS, but paid £30,000 per month for "dental services" to a company owned by the partners. HMRC carried out a direct tax enquiry and noted that the company was trading above the VAT registration threshold. They ruled that it should be charging VAT. The company appealed.

HMRC's argument was that the partnership provided dental services to the NHS, and the company only provided staff to the partnership. The company responded that the exemption did not require that an exempt medical service should be supplied direct to the patient: it depended on the nature of the service, not on the contractual relationship. The situation was different from that in *Sally Moher*, where the dental nurses came under the control of the practices that hired them – here, the dentists were themselves providing a medical service.

The Tribunal noted that exemptions should be construed restrictively. It made the following findings of fact:

(1) The contract between the partnership and the NHS Trust envisaged that clinical matters could be sub-contracted to a third party.

(2) The company and the partnership had complied with the requirement of that contract when setting up the arrangement for the partnership to sub-contract its obligations to the company.

(3) The day to day activities carried out by the two registered dentists who were the partners of the partnership and directors of the company were the same before and after the introduction of the company as a sub-contractor.

The Tribunal noted that HMRC were content for the partnership to be regarded as supplying medical services to patients even though its contract was with the NHS Trust. It was therefore not clear why the interposition of a second intermediary in the chain made a significant difference. HMRC feared that allowing this to succeed would "open the floodgates" for other multi-step chains, but the judge did not think that followed – it was still necessary for each intermediary in the chain to carry out a strictly medical function, which was the case here.

The judge concluded: "The difference between a supply of staff and a supply of services can be a fine one. HMRC made a number of arguments as to why this supply should be treated as a supply of staff but failed to properly explain the legal basis for their approach or provide evidence of the activities of CDP which would have supported their interpretation. On that basis we have concluded that the Appellant's approach comes closest to identifying the essential character of this supply, as a supply of exempt medical services. For that reason this appeal is allowed."

First-Tier Tribunal (TC04548): *City Fresh Services Ltd*

2.3.7 Sport and abuse

A partnership which operated a taxable golf club transferred its interests in the club to two companies which were supposed to be not-for-profit entities. HMRC assessed:

- two companies, on the basis that they did not qualify for exemption – they were in liquidation, and were not parties to the current appeal;
- two partnerships (first an unlimited partnership, then a LLP), on the basis that the transfer to the companies was an abusive transaction that ought to be disregarded.

Before the FTT (TC02787), the taxpayer's representative first claimed that there was no case to answer, on the basis that HMRC proposed to call no evidence. This depended on HMRC having the burden of proof. Judge Mosedale considered this question first, and concluded that the burden was, as is normal in the FTT, on the appellant. The only exception to this principle arose where the matter would have involved a criminal allegation if the FTT had been a criminal court; although the word "abuse" carried pejorative connotations, it was far short of an allegation of fraud.

The judge examined the history of the golf club and its organisational structure in detail. It appeared that the arrangements involving separate companies had been set up in accordance with VAT advice, and the intention was to obtain the advantage of exempting the charges to 'members' (annual season ticket holders) and 'visitors' (people who paid

to play for the day). Before considering whether the arrangement was abusive, the judge questioned whether HMRC were correct in denying the exemption to the companies; she concluded that the issues were very similar. The arrangement would be abusive if the companies were an artificial means of passing profits to the owners, and that would also deny the application of the exemption.

The taxpayer's representative argued that the concept of abuse required the taxpayer do have done 'something wrongful', and this was not the case here. The judge rejected this proposition: *Halifax* only required that there was an arrangement which obtained a tax advantage contrary to the purpose of the VAT legislation, and the obtaining of that tax advantage was an essential aim of the arrangement.

It is interesting to note that the company argued it had in fact been worse off during the currency of the arrangement, and its financial returns had increased after letting the site to a third party operator. The judge commented that this made no difference: the company was confusing financial advantage with tax advantage. If the tax arrangement led to financial problems, that was a commercial misjudgement, but it did not stop the reduction in tax being an advantage which could be abusive.

In deciding whether that was the case, the judge followed the precedent of *Lower Mill Estate*, in which the Upper Tribunal had suggested that it was necessary to compare the structure adopted with what would have been the case using a third party dealing at arm's length. Although the terms of trade between the LLP and the companies was examined in some detail, the overall conclusion was very clear: the rent paid was much higher than was later set at arm's length with the current third party operator, and it therefore appeared to be a covert way of extracting profit from the companies. It was therefore abusive.

The judge then had to consider whether this meant that the companies themselves failed to qualify for exemption. If that was the case, it was possible that only they should have been liable for the VAT; as they were in liquidation without sufficient assets, HMRC would not be able to collect it except by assessing the LLP. Relying on the precedent of the *Atrium Club*, the judge held that the interposition of the company was itself an abusive arrangement, and HMRC were therefore able to assess the LLP directly.

The decision ended with a note that the CJEU decision in *Newey* was published shortly after the hearing. Although the principles of *Newey* were not argued before the Tribunal, the judge considered that the conclusion – based on *Halifax* – was consistent with that decision, in that commercial reality required the recharacterisation of the supplies as being made by the partnership and LLP, not by the companies. Judge Mosedale also awarded costs against the appellants.

The taxpayers appealed both the decision and the award of costs to the Upper Tribunal. The hearing took place over 3 days in April. The *Pendragon* judgment of the Supreme Court was handed down on 10 June 2015, while the judges were preparing their decision. The taxpayers were invited to make additional submissions and did so, but HMRC declined the opportunity.

For the appellants, Keith Gordon argued that Judge Mosedale had erred in ruling that the taxpayer had the burden of proof, and reiterated that the appellants should have had no case to answer. The UT agreed that HMRC did have the burden of showing an abuse of law, but concluded that the FTT had wide powers to regulate its proceedings, and that the conclusion on abuse did not depend on who opened the proceedings.

The appellants further argued that the scheme did not succeed on technical grounds. As a result, the VAT should have been due from the subsidiaries, which had gone into insolvent liquidation. That fact did not justify an assessment on the owners on the basis of abuse of rights; as shown by the *BUPA Purchasing* decision in the CJEU, the doctrine only applies if the scheme "works". The UT did not agree with this proposition. The judges considered the precedent of *The Atrium Club* and found it indistinguishable. They agreed with the conclusion that the fact that a scheme does not work as the parties intended does not mean that no tax advantage accrued. HMRC were not obliged to collect the VAT from the subsidiaries; once a finding of abuse had been made, the transactions had to be recharacterised to decide who should be treated as liable for the tax.

Other criticisms of the FTT decision on points of law were likewise rejected. A number of arguments about Judge Mosedale's findings of fact failed to clear the high hurdle of the *Edwards v Bairstow* test.

The taxpayer applied to raise a new ground of appeal that had not been considered in the FTT – that the assessments had been raised out of time. The UT examined the principles that might allow, exceptionally, a new ground of appeal to be raised, and decided to refuse the application. The judges agreed with HMRC that the appeal would have proceeded differently in the FTT if the point had been argued there. The appeal on the substantive decision was dismissed.

On the award of costs, Keith Gordon argued that the appeal should be covered by the "Sheldon statement" from the 1970s, which assured taxpayers that Customs would not seek their costs in the VAT Tribunal except in limited circumstances. HMRC had added "tax avoidance cases" to the list of circumstances, which Mr Gordon argued they should not have done. HMRC responded that they had twice written to the taxpayer warning that they would seek their costs if they won. The UT considered the arguments and concluded that they could only overturn Judge Mosedale's decision if it was plainly unreasonable; in their opinion, it was not. The appeal against the award of costs was also dismissed.

Upper Tribunal: *Massey and another t/a Hilden Park Partnership v HMRC*

2.3.8 Bridge a sport?

In TC03321, the FTT ruled that bridge is not a "sport" for VAT purposes. Physical skill had to be a key element, as opposed to purely mental skill; the minimal physical activity involved in bridge was not the aim of participation in the game. The company, which had claimed exemption for competition entry fees, appealed to the Upper Tribunal.

The company's representative made the following points about the exemption in art.132(1)(m) PVD based on *Mesto* (Case C-18/12):

(a) the exemption constitutes an independent concept of European Union law the purpose of which is to avoid divergences in the application of the VAT system as between one member state and another;

(b) the exemption is intended to encourage certain activities in the public interest, but only those listed;

(c) the terms used to specify the exemption are to be interpreted strictly; however that does not mean that those terms should be construed in such a way as to deprive them of their intended effect;

(d) the term "sport" must be interpreted in the light of the context in which it is used and of the aims and the scheme of the Principal VAT Directive, having particular regard to the underlying purpose of the exemption in question;

(e) the provision is not intended to confer the benefit of the exemption under it only on certain types of sport; and

(f) the exemption seeks to encourage and promote participation in the relevant activities in the public interest by large sections of the population.

He argued that the FTT had been wrong to place reliance on the "normal English meaning" of the word "sport", when the underlying purpose of the exemption was to provide social and health benefits that could be mental or physical or both.

HMRC noted that the PVD juxtaposed "sport" and "physical education". It was clear from the context that the exemption was for physical, not purely mental, activities.

The Upper Tribunal decided that it could not resolve this dispute with absolute confidence. It would therefore be necessary to refer questions to the CJEU to determine the essential characteristics of an activity in order for it to be classified as a "sport" within art.132(1)(m), with particular reference to the question whether the activity must have a significant (or not insignificant) physical element which is material to its performance or outcome, or whether a game, such as contract or duplicate bridge, with a predominantly mental element of performance and outcome, falls within that meaning.

Upper Tribunal: *The English Bridge Union Ltd v HMRC*

2.4 Zero-rating

2.4.1 Verandas

HMRC have issued a Brief to comment on their defeat in the Upper Tribunal in the *Colaingrove* case about verandas supplied with caravans. They have accepted the decision, so verandas sold with static caravans can now be treated as part of a single zero-rated supply. Retrospective claims can be made subject to the normal rules on time limits and unjust enrichment.

R & C Brief 12/2015

2.5 Lower rate

2.5.1 Installation of energy-saving materials

HMRC have issued a Brief following the CJEU ruling against the UK's application of the lower rate to the installation of energy-saving materials in residential property. Any legislative changes will not be implemented until the FA 2016, and they will not be retrospective.

R & C Brief 13/2015

2.6 Computational matters

2.6.1 Adjustment of consideration

In January 2008, a company sold the Empire Stores trading name and some assets to Littlewoods. By a separate agreement, it sold Empire's book debts to the same purchaser. This included the transfer of a liability to pay commissions due to agents.

Up to that point, the company had accounted for output tax at the time of sale on the full catalogue price. Commission was only paid to the agent when the goods had been paid for. Agents then had to make a claim for commission, which was treated as reducing the sale value retrospectively and thereby leading to a reduction in output tax.

In the deal transferring the book debts, there was an agreed cap of £4,429,895 on the commission that Littlewoods would have to pay the agents. In the event, it paid more than that. The vendor claimed a reduction in output tax in respect of the extra amount that Littlewoods had paid. HMRC ruled that the company was only entitled to reduce turnover to the extent of the contractual commission payments in the sale of the debts. No evidence was presented as to the amount of the excess: this would only be required if the company succeeded in principle.

The trader argued that the whole of the deal for the sale of Empire had to be considered together. It was a complex deal, and several elements had led to disputes and claims for compensation. If Littlewoods had paid more than the stated reserve, it was doing so as part of the deal, and if a reduction was appropriate where the commission had been paid by Littlewoods, it should be available for the whole amount paid.

The judge did not agree with the company's representative that the situation was akin to that in *Elida Gibbs*. There, the VAT system was required to collect the proper proportion of the amount eventually paid by the final consumer; here, the final consumer was said to be the agent, and the amount eventually paid was net of the commission refunded by Littlewoods. But Elida Gibbs had made a supply in the chain; Littlewoods had not. To the extent that Littlewoods was acting as the vendor's agent in disbursing funds that the vendor had paid it (the commission reserve), the argument held, but where Littlewoods paid more than that, it did not. There was no explanation of Littlewoods' apparent willingness to pay amounts that it did not appear to be bound to pay, and

no evidence to support an assertion that the vendor had to reimburse Littlewoods for doing so.

The judge concluded that amounts in excess of the commission reserve, paid by Littlewoods to the agents, did not reduce the vendor's output tax. The appeal was dismissed.

First-Tier Tribunal (TC04558): *Redcat (Brands) Ltd*

2.7 Discounts, rebates and gifts

Nothing to report.

2.8 Compound and multiple

2.8.1 Multiple supply

A company ran a taxi business, providing a radio support service to a fleet of about 280 vehicles. Approximately 200 were owner drivers, the remainder being cars rented to the driver with the radio. The renting drivers were offered the option of taking third party insurance through the company. The company charged £120 per week for car plus radio, and an extra £45 for the insurance. HMRC ruled that the whole amount was taxable, and assessed for £66,859 of undeclared output tax in November 2011. The appeal reached the Tribunal in May 2015.

Both parties relied on *Card Protection Plan*, in which customers of CPP were brought within its "block policy". The company argued that it was doing the same thing; HMRC responded that the facts were different, because CPP's customers became "named insured", whereas the drivers' names were not added to the policy. The appellant company could not legally bind the insurer, and was therefore not an insurer, nor an intermediary, nor in the same position as CPP.

The director and the company's tax adviser both complained that HMRC had allowed exempt treatment to a trade rival, and the appellant was being unfairly "singled out". HMRC argued that the onus of proof was on the appellant to prove such a thing, which they denied. The Tribunal noted this part of the dispute, but did not consider it particularly relevant.

The Tribunal noted the broad interpretation of "insurance" by the CJEU in *CPP*:

"… art 13(b)(a) of the Sixth Directive is to be interpreted as meaning that a taxable person, not being an insurer, who, in the context of a block policy of which he is the holder, procures for his customers, who are the insured, insurance cover from an insurer who assumes the risk covered performs an insurance transaction within the meaning of that provision."

The Tribunal was satisfied that the optional extra payment by the drivers fell naturally within the extended sense of "insurance" set out by the CJEU in *CPP*. The judge was "unimpressed" by HMRC's attempts to

differentiate between the drivers "being insured" and "being given the benefit of an insurance policy". The policy operated to make sure that the drivers were protected against prosecution for driving without insurance.

The appeal against the assessment was allowed.

First-Tier Tribunal (TC04547): *Wheels Private Hire Ltd*

2.8.2 Direct marketing

Following on from the case on the subject reported in the last update (*The Marketing Lounge Partnership Ltd* (TC04411)), HMRC have issued a Brief to clarify their position in relation to supplies of "printed matter with other services". They consider that in many cases traders have incorrectly treated supplies of direct marketing incorrectly as zero-rated delivered goods, rather than standard rated services. They have accepted that guidance in Notice 700/24 was not clear, and have agreed transitional arrangements to take no action in respect of incorrectly zero-rated separate single supplies of either addressed or unaddressed mail made prior to 1 August 2015. Anti-forestalling applies to payments or invoices after 9 June 2015 for deliveries to take place after 31 July 2015. Suppliers wishing to adopt the transitional arrangements must notify HMRC by 30 November 2015.

Notice 700/24 has been updated to provide greater clarity, as has Notice 701/10 *Zero-rating of books and other forms of printed matter*.

In the view of HMRC, direct marketing via mail (addressed or unaddressed) or inserts in newspapers or magazines typically involves the production or acquisition of printed matter for distribution and any or all of the following services:

- posting or arranging the posting of customer mail such as publicity, advertising material or promotional goods to many recipients, including unaddressed mail (known as door drops);
- analysis or manipulation of data (either provided by the customer or sourced directly) for strategic or marketing reasons – for example, to target direct mail at specific groups based on geography, socio-economic factors or gender of recipients;
- purchase or rental of third party mailing lists, including for amalgamation with customer's own lists;
- analysis of own and customer data to produce reports on campaign results and advice on strategy.

The Brief sets out situations in which supplies of "addressed mail" and "unaddressed mail" which have been treated as zero-rated may remain uncorrected under the transitional arrangements. The transitional arrangements do not apply in cases where the arrangements are seen to be abusive or artificial. This includes forestalling, where a prepayment is made or an invoice issued after 9 June 2015 for deliveries to take place after 31 July 2015; the arrangements also only apply to businesses which had misunderstood the guidance in the former VAT Notice 700/24 *Postage and delivery charges* (1 April 2003). Businesses which correctly treated such supplies as standard rated cannot now claim a repayment.

R&C Brief 10/2015

2.9 Agency

Nothing to report.

2.10 Second hand goods

Nothing to report.

2.11 Charities and clubs

2.11.1 More business use

A pension scheme sold an opted property to a charity. The charity made a declaration of intended relevant charitable use to disapply the option. HMRC issued a ruling that the declaration was invalid and VAT was due. The charity appealed (as the contract for sale protected the vendor from the VAT liability in the event of such a ruling).

The charity had raised funds for the purchase of the property from supporter loans. The amount raised would cover the purchase on the basis that it was VAT exempt. However, it was necessary to carry out refurbishments and alterations, and in order to fund these, the charity rented out rooms in the premises. One of the trustees contacted HMRC to ask whether they would apply their guidance that a charity can rent out temporarily unused space without being regarded as "in business", and understood that this would not be a problem.

Following the sale in January/February 2013, HMRC issued an assessment to the seller in June 2013 for underdeclared output tax in its March return period of £133,333 (on the basis that the consideration of £800,000 should have been VAT-inclusive). HMRC had observed that two-thirds of the property was being rented out to tenants for exempt rent; that fees were charged to students for courses held in the rest of the property; and that the building probably contained the general administration function of the charity, which would not be eligible for a disapplication notice.

The Tribunal noted that the parties did not cite any authorities about "business activity". The judge therefore referred of his own motion to *Lord Fisher*, *Morrison's Academy Boarding Houses, Rompelman* and *Finland*. He summarised the issues as follows:

i. an activity whereby a supply is made for a price is not necessarily a business activity;

ii. that it is necessary to identify in objective terms what the activity is in order to determine whether it is an business activity;

iii. that to identify what that activity is, it is necessary to look, not at purpose or results, but at the entirety of what it is and the context in which it is carried out.

The judge accepted that several of the *Fisher* indicia were not met:

d) The Institute was not conducted on sound and recognised business principles in view of its reliance on volunteers and donations. No part of its fees was expended on the acquisition of capital assets.

e) The intrinsic nature and predominant purpose of its activity is providing courses and activities and to assist in defraying its operational costs, fees are received through its membership of the Cambridge Theological Federation.

f) The supplies it makes are in pursuance of its predominant objectives of promoting the Orthodox Church and its teachings and the courses it provides are probably unique and not of a kind commonly provided by others.

However, this did not mean that the charity could be regarded as not engaged in economic activity. The fees it received for teaching, while lower than they would have been without the charitable intention of the organisation, could not be anything other than consideration for the supply. The renting of rooms for students' living accommodation would also, once the refurbishment was completed, constitute economic activity. The temporary letting to companies and individuals wholly unconnected with the charity's objects also constituted "business". For all these reasons, the appeal was dismissed.

First-Tier Tribunal (TC04622): *Trustees of the Institute for Orthodox Christian Studies, Cambridge*

2.12 Other supply problems

2.12.1 Toolkit update

HMRC have updated their "toolkit" on output tax. As before, the toolkit identifies major risks of error in its specified area, and offers a checklist for agents to use when reviewing clients' systems to identify weaknesses.

The July 2015 includes information on the flat rate scheme, supplies and liability, exports and despatches, credit notes and bad debt relief, business gifts and deemed supplies, and record-keeping.

HMRC Toolkit (2015)

2.12.2 TOGC?

The Upper Tribunal has overturned a decision of the First-Tier Tribunal (TC03119) concerning the transfer of a "totality of assets" that was then used for making supplies within a VAT group registration.

Background

A company intended to enter into the electronic banking business. After encountering some difficulties with business development, its assets and undertaking were sold to part of the Virgin Money group. The business was described in the sale agreements as including:

(a) The Goodwill

(b) The Equipment

(c) The benefit of Transferring Contracts

(d) The Business Intellectual Property Rights

(e) The Information

(f) The Know-how

(g) The Records

(h) The benefit of the Claims.

The company proceeded on the basis that this was a VAT-free transfer of a going concern. However, HMRC considered that any banking processing activity of the vendor had ceased by the date of the transfer; if it had a business at all, it was IT consultancy, and that was not the same activity as that which the purchaser would carry on. It was really buying an IT platform, not a processing business.

First-Tier Tribunal

The Tribunal decision went through the history of a long and complex litigation in detail. It seems that the issues took some time for each side to clarify. The appellant company argued that HMRC had made various errors of fact and law, but if they were right that the UK law should be applied in this way, then it contravened various EU legal principles and the underlying purpose of the TOGC provisions as set out by the CJEU in *Zita Modes*.

The Tribunal rejected this contention. It agreed with the slightly different HMRC line, adopted by the time of the hearing, that the business carried on by the vendor was still carried on by the purchaser, but the supplies made in the course of that business were made within a VAT group registration. They were therefore "disregarded" for VAT purposes. As the business had therefore effectively ceased after the transfer, there could not be a TOGC, and output tax of £900,000 was properly due.

Upper Tribunal

The appeal took into account the CJEU decision in *Skandia* (Case C-7/13). This made it clear that the recipient of the transfer of the assets should be treated as "the group", not "the individual group company". The FTT had erred in law by considering the intra-group supplies made by the individual recipient company as "the business" that had to continue after the transfer, and by treating that business as ceasing because the intra-group supplies fell to be disregarded.

Under *Zita Modes*, what was necessary for a TOGC was a transfer of assets that were capable of operation as an independent business, in circumstances in which the transferee intended to use the assets rather than liquidating them. Those conditions were clearly satisfied here. The disregard of intra-group transactions did not change the fact that the group used the assets for its business, in the same kind of business as that formerly carried on by the taxpayer: the separate businesses of the individual companies within the group did not cease to exist or become a different amalgamated business.

There were other arguments about fiscal neutrality: if the transfer had been structured slightly differently, there would have been no question that it would have qualified as a TOGC, and there was no good reason for a different VAT treatment based only on the minor differences in corporate structure.

The appeal was allowed.

Upper Tribunal: *Intelligent Managed Services v HMRC*

In an article in *Taxation*, Peter Mason analyses the above decision, and comments that traders may consider making a reclaim if they have suffered sticking tax on a similar transfer of business assets in the last few years.

Taxation, 27 August 2015

A company appealed against a decision by HMRC to disallow £13,676 of input tax in relation to the purchase of assets. HMRC ruled that the purchase constituted a TOGC; the company argued that it had been a purchase in the ordinary course of the vendor's business, and it had not taken over all or any part of the vendor's trade.

The transfers were made over a period of two months in 16 separate transactions, all on sequentially numbered invoices, between two companies owned and directed by the same individual. The transferor went into liquidation not long afterwards. Five of its eight employees were also transferred.

The company argued that HMRC's ruling depended on hindsight. At the time of the transactions, the vendor had intended to carry on trading; it had been forced into compulsory liquidation. HMRC noted that if the vendor had accounted for the "VAT" shown on the invoices, HMRC would allow the purchaser to claim it – as it had not, this concession was not available.

The Tribunal was not convinced that the vendor could have been viable as a trade without the assets and employees that had been transferred. However, that was not the point: the Tribunal was satisfied that what had been transferred amounted to part of the business, capable of separate operation. It therefore met the conditions for being treated as a TOGC, and HMRC's assessment was justified.

First-Tier Tribunal (TC04542): *Amor Interiors Ltd*

2.12.3 Machinery transferred in legal dispute

A company manufactured and supplied optical components. In 2011 it had a legal dispute with a customer, at the end of which it agreed to pay compensation and costs, and to transfer an item of machinery to the customer. The company did not have enough money to pay the compensation in cash, so the machine was added to the settlement to make up the difference. No VAT was accounted for on the transfer of the machine, which had been imported from the USA in 2007. Following a VAT visit in 2013, an officer raised an assessment to output tax.

The company appealed, arguing that the transfer of the machine was "compensation" and therefore outside the scope of VAT (in accordance with HMRC guidance).

The judge pointed out the basic fallacy in this argument: it confused consideration with supply. The payment of compensation in cash is not consideration for a supply; however, the transfer of goods is always a supply, for whatever reason that transfer is made (unless it is disregarded under a statutory provision). The person receiving the compensation is not making a supply, but the person paying it in goods is doing so. The appeal was dismissed.

The valuation of the machine for the purposes of the supply had been agreed, if the Tribunal found for HMRC on principle. The basis of that valuation is not described in the decision – presumably it ought to be “the amount of cash compensation that the machine replaced”, in accordance with the principles of such cases as *Naturally Yours Cosmetics* and *Westmorland Motorway Services*.

First-Tier Tribunal (TC04631): *Phoenix Optical Technologies Ltd*

2.12.4 Vouchers

The FTT has heard a second appeal following the early 2014 decision in First-Tier Tribunal (TC03271): *S J Nagle & J Kemsley t/a Simon Templar Business Center*.

Background

A partnership traded in face value retailer vouchers. It bought them on issue by retailers, and sold them on at a profit, but still below face value. The partnership also supplied ‘accountancy and taxation advice’; however, it appears to have accepted the following misleading advice from HMRC without question:

Mr Nagle ... said that before commencing this trade he had telephoned HMRC to ascertain whether the Partnership should be registered for VAT and says he was told that the sale of vouchers was zero-rated but that fees for accountancy and taxation advice were standard-rated and that only if these standard-rated supplies exceeded the VAT registration threshold would registration for VAT be required.

HMRC raised an enquiry in December 2010 pointing out that it had received a self-assessment tax return disclosing turnover of £323,000, and wanting to know why there was no record of a VAT registration. The partner replied on 9 January 2011 to explain that the majority of the turnover related to ‘discounted food vouchers’ and that the firm had been advised that these could be disregarded. HMRC responded in a letter stating that ‘*it would be unusual for the sale of vouchers to be treated as zero rated other than vouchers sold by retailers for redemption in their own stores.*’

The partnership then registered with effect from 1 April 2011, accounting for output tax on the sale of vouchers where the partner was certain they were used for standard rated supplies (e.g. fuel vouchers). The first return, for the six months to 30 September 2011, claimed a repayment of £5,400 – input tax of £8,500 less output tax of £3,100.

Following investigation, HMRC amended the EDR to 6 December 2008, refused the claim to input tax, and ruled that all sales of vouchers were liable to output tax. The partnership appealed.

The Tribunal examined the underlying law in Sch.10A VATA 1994, and concluded that the intermediary sales of vouchers were chargeable to VAT. It was necessary to come to a just and reasonable apportionment where vouchers were used to obtain supplies chargeable at different rates (para.6(5) Sch.10A); the Tribunal invited the parties to negotiate the rate that would be appropriate and return to the Tribunal if they could not agree.

However, the input tax claim could not be allowed at all, because the issue of retailer vouchers is not chargeable to VAT.

The Tribunal noted that the firm claimed the letter which referred to the possible zero-rating of '*vouchers sold by retailers for redemption in their own stores*' created a legitimate expectation that it should not have to account for VAT on most of its sales. HMRC did not accept that this was a ruling of any sort, and the Tribunal confirmed that it did not have jurisdiction to consider the point – following *Noor*, that was a public law matter that was reserved to the Upper Tribunal or the High Court.

Notional VAT for intermediaries

No mention was made in that first decision of the practice of allowing 'notional VAT' to the first intermediary in the chain so that it is only effectively charged on the margin earned on its sales – in effect, it is given credit for the output tax that the retailer expects to account for when the vouchers are redeemed. If no credit is allowed at all, there is a double charge to VAT on what the customer pays. This concept is not mentioned anywhere in the decision. It is hinted at, but not explicitly described, in para.8.9 of Notice 700/7/12.

Example

A retailer issues a £100 face value voucher for £55 to an intermediary. The retailer expects to make sales which are 60% standard rated, 40% zero rated (based on gross selling prices) for its vouchers. It informs the intermediary of this split.

The intermediary (X) sells the vouchers on to another intermediary (Y) for £70 gross. Intermediary Y sells them to a member of the public for £95, VAT-inclusive.

Who should account for what VAT?

The 'just and reasonable proportion' approach suggests a VAT fraction of 10% should be applied to the gross price (1/6 x 60%).

The retailer accounts for VAT under the *Argos* principle – it treats the redemption of vouchers as chargeable to output tax according to the actual liability of products supplied, and using the £55 consideration received on issue instead of the £100 face value/selling price.

If the split is the expected 60/40 split, the retailer will account for output tax of 1/6 x 60% x £55 – £5.50.

Intermediary X accounts for output tax of 10% of £70 – £7. According to the decision, there is no deduction for input tax.

Intermediary Y accounts for output tax of 10% of £95 – £9.50. The £7 charged by X is deductible, so £2.50 is paid to HMRC.

HMRC have therefore collected VAT of £15.00. The retailer has supplied standard rated goods for which the consumer has paid 60% x £95 = £57. The 'proper' VAT charge should therefore be £9.50 (1/6 x £57).

The 'right answer' would be achieved if Intermediary X (in the position of the appellant in this case) is allowed to deduct the £5.50 to be accounted for by the retailer on redemption. It would then pay £1.50 to HMRC, and HMRC would collect in total £9.50.

Second decision

The parties negotiated over the "just and reasonable apportionment", but could not come to an agreement. HMRC offered to treat 50% of the turnover as effectively zero-rated, but the trader appeared to continue to argue for a deduction of input tax.

That could be explained by the very brief comment in the decision in the second appeal. The partner claimed not to have received the first decision, which had been sent to him by the Tribunal in January 2014, until it was sent to him by HMRC shortly before the second hearing in July 2015. He had not read it, and refused the offer of a short adjournment so he could do so. Instead, he attempted to argue again the same points that he had raised unsuccessfully in the first appeal. The judge pointed out that HMRC's figure of 50% was not "plucked from the air" but was based on its experience of the retailer concerned. In the absence of any evidence (or, it seems, relevant argument) from the taxpayer, the judge confirmed HMRC's ruling that 50% of the turnover would be standard rated.

First-Tier Tribunal (TC04572): *Simon Nagle & Julie Kemsley t/a Simon Templar Business Center*

2.12.5 Salary sacrifice

In an article in *Taxation*, Alastair Kendrick reviews the employment tax issues arising in salary sacrifice schemes. The VAT issues are mentioned (as highlighted in the *AstraZeneca* case), but they are not the focus of the article.

Taxation, 17 September 2015

2.12.6 Carrier bags

In line with similar statements when compulsory charges were introduced for single use carrier bags in Wales and in Northern Ireland, HMRC have issued a statement about their introduction in England in 5 October 2015. Although the charge is not itself a tax, any amount charged by a trader will be inclusive of VAT at the standard rate. If the business charges the minimum 5p, there will be VAT of 0.83p on a supply of 4.17p.

R & C Brief 14/2015

3. LAND AND PROPERTY

3.1 Exemption

3.1.1 Antiques fairs

The last update included the FTT decision in (TC04428): *Kati Zombory-Moldovan t/a Craft Carnival*, in which the Tribunal agreed with the taxpayer that she was making exempt supplies of "pitches" for vendors to sell their wares at craft fairs. HMRC have now won another case in respect of a similar business, and appear likely to appeal the first decision to the Upper Tribunal.

IACF organises and promotes antiques and collectors fairs at a number of locations in England – 30 fairs a year at 5 locations. HMRC ruled that VAT should be charged on booking fees charged to exhibitors for taking part in the fairs. This comprised about 76% of the company's income. It was agreed that other income streams (e.g. admission charges, hire of specific equipment to exhibitors) were standard rated.

For some years, the company had treated the booking fees as exempt. In 2012 it became aware that HMRC might take a different view: R&C Brief 22/2012 concerned the place of supply rules, but it implied that this sort of activity was not regarded by HMRC as an exempt supply of land. It contained the announcement "*However, where stand space is provided with accompanying services as a package, this package (stand and services) will no longer be seen as a supply of land with land related services but will be taxed under the general place of supply rule (customer location) when supplied to business customers.*"

Another similar business had received notice from HMRC that it should be charging VAT, so the company sought to clarify the position with HMRC. HMRC issued the disputed decision, and the company started to charge VAT to the exhibitors on a protective basis from November 2012.

HMRC argued that the company did not itself hold an interest in land sufficient to be able to make supplies of land to others in 3 of the 5 sites; alternatively, the nature of its supplies to the exhibitors was not a letting of immovable property. Both parties agreed that there was a single supply to the exhibitors, so it was either all taxable or all exempt.

The Tribunal started by examining the contracts between the owners of the showground locations and the company (relevant to the first argument), and the contracts between the company and the exhibitors (relevant to the second). Based on precedents in *Temco* (Case C-284/03) and *Willant Trust Ltd* (TC04172), HMRC argued that the rights of the company at the three sites were not consistent with it being able to let land. The site owners retained rights of access for all times and all purposes, and there was therefore no "exclusive occupation".

In relation to the second argument, HMRC argued that the supply was not a relatively passive supply of space related to the passage of time without the generation of any significant added value. The recent case of *Stade Luc Varenne* (Case C-55/14) confirmed that the provision of significant additional services suggested that the supply was "services using land" rather than "land with incidental services". HMRC cited a number of UK precedents that they considered analogous, including *Dazmonda*, *Byrom*

and *Sinclair Collis*. The land was of no use to the exhibitors without the services of organising and promoting the fair.

For the company, Penny Hamilton argued that the contracts constituted lettings of land within EU precedents. They were for a defined area for a specified period. The rights of access by the site owners had been identified in *Temco* as acceptable within the context of this kind of arrangement. For all practical purposes, the company had exclusive occupation and sublet a right of exclusive occupation to the exhibitors.

In respect of the second argument, she sought to distinguish the various cases put forward by HMRC. The company was much less involved with the supply of active services to individual exhibitors. Many of the services that HMRC relied on were general site services, supervisory and ancillary in nature. The company was more akin to the landlord of a shopping centre than to the organiser of wedding receptions in cases such as *Willant Trust* and *Drumtochty Castle*.

The Tribunal noted that it was necessary to consider the question of "letting of immovable property" in the context of EU law and precedent, not just in relation to UK law. The judge agreed that *Temco* contained a good statement of the principles. He agreed with Ms Hamilton that the company's contracts were sufficient to meet the *Temco* tests, and could be distinguished from the circumstances in *Willant Trust*. HMRC's first contention was rejected.

The judge noted that both parties relied on *Stade Luc Varenne* as refining the application of *Temco*. He considered it of little assistance, because the CJEU had referred in that case to a situation in which the extra services constituted some 80% of the value of the supply. It did not seem to be possible to provide such a figure here; approximately one third of the company's direct costs comprised ground rents paid to site owners, but that did not bring the case conclusively to one side or the other of the CJEU's decision.

The judge agreed with both parties that there was a single composite supply. As regards classifying that supply, he approved the approach of Warren J in the Upper Tribunal decision on *Finnamore (t/a Hanbridge Storage Services) v HMRC*. This included considering all the circumstances and assessing the matter from the perspective of a typical user. This would reflect the "economic and social reality". This led to a win for HMRC:

"*Our conclusion is that assessing the supply from the perspective of a typical Exhibitor, the economic and social reality is that the booking fees are payment for participation as a seller at one of the largest antiques fairs in Europe, attended by plentiful trade and public buyers. That is the opportunity provided by the Company and for which the Exhibitor pays the fees.*"

The judge went on to explain why he did not follow an old case that the company relied on (*Miller Freeman Worldwide*, in which HMRC had argued on similar facts that the supply was exempt), and also to comment on the company's complaints about the way in which HMRC's policy had been changed – effectively by issuing a R&C Brief on a different subject. The judge concluded "*We would just comment (in case it may be relevant, for example, to the matter of any potential penalties) that we do not think*

any blame can attach to the Company or its officers or advisers for not spotting earlier that there might be some VAT problem with continuing the previous long-standing arrangements after the publication of RCB 12/22." The appeal was dismissed.

First-Tier Tribunal (TC04538): *International Antiques and Collectors Fairs Ltd*

HMRC have apparently noted the following passage in para.55 of the *Craft Carnival* decision as particularly susceptible to criticism:

"*Accordingly, despite the force of Miss McCarthy's submissions in relation to the organisation of a fair, given the absence of any reference to this in the T&C, it must follow that the purpose, and therefore the effect and economic reality, of the arrangement between Mrs Zombory-Moldovan and a stallholder is that she grants the stallholder a licence to offer for sale specific types of goods at the craft and garden fairon the dates specified in the booking form.*"

HMRC are likely to argue that this is a finding of fact that is inconsistent with the eventual conclusion that the supply is an exempt licence to occupy land.

3.2 Option to tax

Nothing to report.

3.3 Developers and builders

3.3.1 Community building

A registered charity which operated a rugby club constructed a new clubhouse on the site it leased from Highland Council. HMRC ruled that it could not be zero-rated. This would add some £60,000 to the cost, of which £95,000 had been raised by the club through fundraising events, the balance coming from various grants.

The club's president gave evidence about the use of the clubhouse. It was used by a wide range of community groups. Although rugby took priority, so that others could not use it on a Saturday afternoon in the season, that did not undermine the fact that it was used in a similar way to a village hall.

HMRC relied on the funding application, which did not describe the level of outside use that it appeared had actually occurred. It was the intention at the time of construction that determined the liability, and it was for the club to show that zero-rating was justified. The person who completed the funding application was not available to give evidence, and HMRC said that "was the club's problem".

The Tribunal considered a number of precedents, and noted the following questions were suggested as crucial in *New Deer Community Association*:

(1) Were the facilities provided for the local community?

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

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

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

The funding application was important, but had to be considered in conjunction with all the other evidence. Given that the wide range of use had been present from the time of construction, that was an indication of an intention for such varied use. HMRC's different arguments were rejected in turn. The judge was satisfied that all the requirements of Group 5 Note 6(b) were met: the building was used, and intended to be used, by a charity for purposes similar to those of a village hall in that they benefited the local community. The appeal was allowed.

First-Tier Tribunal (TC04560): *Caithness Rugby Football Club*

3.3.2 Not a village hall

A bowls club was registered as a Community Amateur Sports Club, but not as a charity. It arranged for the construction of a new clubhouse, and obtained the support of the town council and local community groups. The total cost of the project was £273,039; the club issued a zero-rating certificate. HMRC ruled that zero-rating did not apply.

The main argument was that a CASC is not a charity. It enjoys a number of the tax benefits of charitable status, but it is not actually a charity, and the zero-rating of RCP buildings is restricted to "proper" charities. The Tribunal considered this proposition in detail and found for HMRC on the point. While not entirely agreeing with the way HMRC's representative presented the law, the CASC did not meet the conditions for being treated as a charity in the VAT Act.

For completeness, the Tribunal also considered whether the building was used for a relevant charitable purpose, if it should be found to be wrong on the question of status. The building was used for a business purpose, because the club charged for its use; it would therefore have to fall under the "village hall" provision. The Tribunal did not consider that it did so. The project was entirely managed by and for the club; there might be an incidental benefit to the wider community in that the facilities could be made available to other users, but that was not part of the driving intention behind the project.

The appeal was dismissed.

First-Tier Tribunal (TC04598): *Witney Town Bowls Club*

3.4 Input tax claims on land

Nothing to report.

3.5 Other land problems

Nothing to report.

4. INTERNATIONAL SUPPLIES

4.1 E-commerce

4.1.1 Consultation

The Commission has announced a consultation, to run for 12 weeks to 18 December 2015, on ways to improve the taxation of cross-border e-commerce transactions. It appears to represent a recognition that the MOSS system is too difficult for small businesses. The following statements are quoted in the press release:

"We promised to support companies, and especially smaller ones, to reduce burdens arising from different VAT regimes. Today we ask businesses and other stakeholders to help find the most effective and meaningful ways of delivering on this promise. In the Digital Single Market Strategy we have already put forward some measures we would like to take, such as a VAT threshold for start-ups."

"*This consultation presents a real opportunity to ensure that future VAT revenues from the digital economy are distributed fairly and effectively. At the same time, we want to make it as easy as possible to comply with the rules. We also have an interest in ensuring that future legislation reflects the reality for businesses across the EU.*"

In the context of the Digital Single Market, the Commission is working to minimise burdens attached to cross-border e-commerce arising from the different VAT regimes within the EU. It wants to provide a level playing field for EU companies, big or small, and ensure that VAT revenues flow to the country where the consumer is based.

The Commission will make a legislative proposal in 2016 to reduce the administrative burden on businesses arising from different VAT regimes. This consultation will feed into preparations for these proposed measures.

The Commission will propose simplification measures for small business including an appropriate threshold which can address the problems without causing further distortions to the single market or compliance challenges for tax administrations. Specifically, the Commission will propose reducing the administrative burden on businesses arising from different VAT regimes including:

- extending the current single electronic registration and payment mechanism to cover the sale of tangible goods;
- introducing a VAT threshold to help online start-ups and small businesses;
- allowing cross-border businesses to be audited only by their home country for VAT purposes;
- removing the VAT exemption for the import of small consignments from suppliers in third countries.

The press release states that more than EUR 3 billion VAT will be paid through MOSS in 2015, representing approximately EUR 18 billion in sales.

The Commission claims broad support for the new rules, but acknowledges that some very small businesses have faced difficulties. The Commission continues to hold that this is a particular problem in the UK where the registration threshold has entrenched an advantage that is taken away under MOSS. In its original proposal, the Commission had included a VAT threshold to exempt smaller businesses from the changes, but Member States rejected that option. The Commission would like to put that option forward again in order to support the EU's start up and smallest companies.

IP/15/5719; ec.europa.eu/eusurvey/runner/ModernisingVATcrossborderecommerce

4.2 Where is a supply of services?

4.2.1 Budget announcement

The July Budget included an announcement that, from 2016, the law will be changed so that VAT will be charged on services used and enjoyed in the UK. This appears to be a response to offshore-based avoidance schemes such as that found to be effective by the Upper Tribunal in the *Newey* case. It is not clear yet exactly how such changes are expected or intended to work.

Budget Report para.2.136

4.2.2 Place of supply and refund claim

An Italian company arranged an enclosure at the Farnborough Air Show to be made available to fellow Italian subsidiary companies. The subsidiaries invited customers, potential customers and the press to the enclosure. The arranging company incurred VAT on related costs and claimed it back from HMRC under the 8th Directive and the Refund Directive.

HMRC argued that the claimant company was making a supply in the UK – it was the service of organising an exhibition or a fair, which until 1 January 2011 was supplied where the exhibition took place. The company argued that it was supplying a marketing or advertising service, which would have been supplied in Italy where the supplier was established (up to 31 December 2009) or in Italy where the customers were established under the normal B2B rule (from 1 January 2010).

The FTT (TC03364) considered precedent cases including *Gillan Beach* and *Inter-Mark*. It concluded from the reasoning of the CJEU in those cases that the categories of art.9(2) 6th Directive were intended to be mutually exclusive: a supply could not fall under more than one heading. If something was "advertising", it could not also be regarded as "event organising". The judge went on to state that:

I have no doubt that the services which FGS supplied to its sister companies were: (1) designed and used for the purposes of the dissemination of messages intended to inform potential buyers of the existence or quality of the products offered by those companies with a

view to increasing the sales of such products, and (2) formed an inseparable part of the centrally coordinated advertising campaigns of the group companies by contributing to and conveying their marketing messages: the presence at the enclosure of employees of the group companies indicated that integration. As a result, because of the mutual exclusivity of the nature of the services described in the Article 9(2) provisions, the supply cannot fall within Art 9(2)(c) 'events'. Therefore the place of supply falls to be determined under the applicable general rule, and is Italy.

In case he was wrong about the mutual exclusivity of the art.9(2) categories, he went on to consider whether the supply could also fall within art.9(2)(c). He set out what he regarded as the main features of an art.9(2)(c) supply, which included a complex service organising an event which would be attended by a number of people, including many final consumers. He concluded that this was not a correct description of what this appellant did – it made a more limited supply to businesses within the context of an event organised by someone else.

The appellant failed to overturn a separate HMRC decision to disallow two claims for VAT on specific expenses. One was held to be an advertising service on which no UK VAT should have been charged to an Italian customer; the second was not supported by a VAT invoice, and the Tribunal declined to exercise a supervisory jurisdiction to override HMRC's decision to disallow. It could not be said to be an unreasonable decision.

HMRC appealed to the Upper Tribunal. The Upper Tribunal decided that the FTT erred in law in deciding that the categories in art.9(2) were mutually exclusive. Something that could be described as "advertising services" could also fall within the exception for fairs. The correct approach was to consider the precedent cases on fairs (*Dudda, Gillan Beach, Inter-Mark*) and conclude whether they indicated that this kind of activity was within them. In accordance with the CJEU decision in *Gillan Beach*, the airshow did not have to have a particular "theme" for the fairs exception in art.9(2)(c) to apply.

The FTT had been wrong to impose an additional criterion for the fairs exception to apply, over and above those contained in the *Gillan Beach* decision at paras.23 and 24. It was not essential for all of those receiving the company's services to be final consumers who bore the cost of the tax themselves. The crucial point was that the company was making supplies to people who received them at a particular location. It was easy to identify the place at which the supplies were made: the place of supply was where they were physically carried out within art.9(2)(c). The company was therefore making supplies in the UK, and was not eligible to claim a refund under the intra-community procedures.

Upper Tribunal: *HMRC v Finmeccanica Group Services SpA*

4.3 *International supplies of goods*

4.3.1 EU customs procedures

The European Commission has been working for several years on an overhaul of EU customs rules. It has now adopted a legal act which paves the way for a reform to take effect from 1 May 2016. The following benefits are foreseen:

- Simplifications of the customs procedure inward processing which allows the processing of non-Union goods without payment of import duty and other charges to support creation of added value in the EU;
- Clearer rules to ensure equal treatment of economic operators in the EU;
- Wide-ranging provisions which will allow customs decisions and authorisations to be valid across the EU in the future;
- Establishing common data requirements as the basis for new IT systems linking Member States' customs administrations to ensure a seamless exchange of information;
- Improvements in risk management to reinforce the fight against trade in illicit and prohibited goods, terrorism and other criminal activities.

http://europa.eu/rapid/press-release_IP-15-5445_en.htm

4.3.2 Zero-rating not allowed

A trader was assessed to £187,178 of output tax in relation to despatches of coal to customers in Ireland from 12/07 to 11/10. With the addition of interest, the total in dispute was £222,618. HMRC suspected that the supplies had been made to customers in Northern Ireland; in addition, the invoices did not meet the requirements of Notice 725, which has the force of law.

The representatives agreed that the main matter was the factual question of whether the goods were delivered to customers in Ireland. HMRC made no concession on the alternative ground relating to the adequacy of the invoices.

The Tribunal considered the evidence available from documents and the testimony of the investigating officer. The director of the company was not able to attend the Tribunal for medical reasons, so he could not be cross-examined. Several of the Irish customers recorded in the company’s books could not be found by Irish revenue officers.

The company’s tax adviser, a chartered accountant, gave evidence to the Tribunal, claiming that explanations existed for all the transactions and that he had shown the investigating officer adequate documentation on visits to his office during the course of the enquiry. Both sides had employed investigators to gather evidence about the customers south of the border, with conflicting results.

The Tribunal considered that the accountant’s evidence was credible. The officer appeared to have formed a view about the way in which the trade was carried on and had not made enough of an effort to understand the explanations that were provided. Although there were potentially

confusing factors such as invoicing in sterling but payment by cash in euros, sometimes directly to the appellant's suppliers, this could "with some diligence" have been verified.

However, the evidence of delivery to customers in Ireland was unsatisfactory. The trader had tried to obtain written confirmation from the customers that they had received the supplies; the fact that they refused to do so resulted in an allegation that they were cheating the Irish authorities. The Tribunal regarded this as "extraordinary". On the balance of probabilities, the goods had not been delivered as described; in the circumstances, it was perfectly proper for HMRC to rely on the strict application of Notice 725 in relation to the invoices.

The appeal was dismissed.

First-Tier Tribunal (TC04618): *MFS Fuel Supplies Ltd*

4.3.3 Intra-community goods

A self-employed German trader bought a car and transferred it to a Spanish car dealer. The authorities agreed that there was no evidence of tax evasion, but refused to allow exemption for the despatch because he did not provide a Spanish VRN. The following question has been referred by the German court to the CJEU:

Do Art.22(8), the first subparagraph of Art.28c(A)(a) and Art.28c(A)(d) [6th Directive] permit Member States to refuse to grant a tax exemption in respect of an intra-Community supply (in this instance, an intra-Community transfer) where, although the supplier has not taken all the measures that can reasonably be expected of him from the point of view of the formal requirements applicable to the recording of the [VAT] identification number, there is no specific evidence of tax evasion, the goods have been moved to another Member State and the other conditions of exemption from tax are also met?

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

4.3.4 Fuelling through intermediaries

The CJEU had to consider a situation in which fuel was supplied for ocean-going vessels (essentially an exempt-with-credit supply) through an EU-based intermediary. The court ruled that the exemption would not normally apply to the supply to an intermediary acting in its own name – it would incur VAT and have to claim the exemption itself in respect of the onward supply to the operators and owners of the vessels themselves. The court stated that the exemption would not apply even if "the ultimate use of the goods is known and duly established and evidence confirming this is submitted to the tax authority in accordance with the national legislation".

However, in this case the main supplier delivered the fuel directly into the tanks of the vessels. It therefore knew that the supply to the intermediary and by the intermediary must be made at the same moment – the invoicing was merely paperwork reflecting a physical transaction. The operators of the vessel were in a position to deal with the goods as owner at the same moment that the fuel company disposed of it. This meant that the intermediaries never acquired the right to dispose of the goods as owner,

and had therefore neither received nor made a supply of goods. In those circumstances (which the national court would have to confirm), the exemption should apply to the fuelling company's supply.

CJEU (Case C-526/13): *Fast Bunkering Klaipėda UAB v Valstybinė mokesčių inspekcija prie Lietuvos Respublikos finansų ministerijos*

4.3.5 Antiques

A jeweller imported some items from the USA. They were declared under a customs code for "antiques of an age exceeding 100 years". Customs argued that the code should be "articles of jewellery and parts thereof". The difference in the customs duty would be £24,015 and the VAT would be £144,965, which HMRC sought to collect by post clearance demand.

HMRC disputed the evidence. The director of the importing company regarded his own expertise as sufficient to judge the age of his purchases; the vendors stated on the invoices that the goods were over 100 years old. HMRC wanted more proof, as set out in Notice 362. They argued before the Tribunal that either there was insufficient proof, or it was a reasonable decision not to accept that there was sufficient proof.

The Tribunal was satisfied that, on the balance of probabilities and the available evidence, the items were over 100 years old as a matter of fact. This meant that a lower rate of VAT applied under s.21 VATA 1994.

However, the law was slightly different in respect of the customs duty. Here, the question was whether "the importer had satisfied the Commissioners that the items were over 100 years old". Clearly he had not; in the circumstances, this decision could not be said to be unreasonable. HMRC had a policy that they had applied consistently, and their decision could not be faulted.

The appeal was allowed in respect of the VAT, and dismissed in respect of the duty (which was slightly reduced to £20,010).

First-Tier Tribunal (TC04607): *G Music and Sons Ltd*

4.3.6 Intrastat General Guide

HMRC have issued an updated version of the *Intrastat General Guide*. The only listed change is a new way of obtaining advice from the Tariff Classification Service on the classification of goods to commodity codes. This follows closure of the Tariff Classification Helpline.

Notice 60

4.4 European rules

4.4.1 EU VAT gap static in 2013

The overall difference between expected VAT revenue and the amount actually collected remained static between 2012 and 2013 at approximately €168 billion. The Commission estimates that this constitutes a revenue loss of 15.2% to fraud and evasion, tax avoidance, bankruptcies, financial insolvencies and miscalculation across 26 Member States (Cyprus and Croatia are not included because of accounting delays).

The discrepancies range from 4% in Finland, the Netherlands and Sweden to 41% in Romania. According to the report, the UK's gap has fallen from 10.5% to 9.8%, making the UK 9th out of the 26 (position unchanged).

IP/15/5592

4.4.2 Rates in the EU

The Commission has published an updated list of VAT rates throughout the EU. This was last included in this update in April 2015 (with comparisons between January 2015 and 2011). The following table shows the standard rates in order of magnitude – there have been no changes since January 2015:

	Sep 15		*Sep 15*
Luxembourg	17	Lithuania	21
Malta	18	Latvia	21
Cyprus	19	Italy	22
Germany	19	Slovenia	22
France	20	Ireland	23
Austria	20	Greece	23
Bulgaria	20	Poland	23
Estonia	20	Portugal	23
Slovakia	20	Finland	24
UK	20	Romania	24
Spain	21	Croatia	25
Netherlands	21	Denmark	25
Czech Republic	21	Sweden	25
Belgium	21	Hungary	27

The table also includes references to the amount and scope of reduced rates, which are much more varied. They demonstrate that a common system is still a long way away.

http://ec.europa.eu/taxation_customs/resources/documents/taxation/vat/how_vat_works/rates/vat_rates_en.pdf

4.4.3 Holding companies

The full court judgment has now been issued in the joined cases of *Larentia + Minerva* and *Marenave*, essentially confirming the Advocate-General's opinion. There are several important issues:

- the extent to which VAT incurred on fees relating to the acquisition of subsidiaries is deductible – whether it can be attributed to non-business investment activities;
- whether a Member State can restrict VAT grouping to companies, or should allow partnerships and other taxable persons to join; and whether Germany was allowed to require that only a relationship of "control and subordination" should permit grouping.

The first issue was considered in the context of two different transactions:

- the acquisition of shares in the subsidiaries;
- the raising of finance in order to acquire shares in subsidiaries.

Advocate-General Mengozzi noted that the questions for reference asked about the specific method that ought to be used to calculate the recoverable VAT. Unusually, he chose to answer a slightly different question. According to cases such as *Securenta* (Case C-437/06) and *Portugal Telecom* (Case C-496/11), the PVD does not prescribe any method for apportioning input tax between business and non-business activities. It is for the Member State to choose a method that produces a fair result. It is therefore not within the jurisdiction of the CJEU to suggest a particular method.

The companies argued that the question should be rather whether they were purely economic operators within the principles of the *Cibo Participations* case (Case C-16/00). If so, all the VAT incurred should be attributed to their economic activities, and in the absence of exempt outputs, there was no reason to disallow any.

The Advocate-General agreed with this proposition, and the full court has followed the same line. The CJEU has in past cases distinguished between two types of holding company:

- those whose sole purpose is to hold and manage shares in other companies and which do not provide those companies with any services for remuneration and thus do not involve themselves directly or indirectly in the management of other undertakings, other than by exercising their rights as shareholders (*Polysar*);
- those which have direct or indirect involvement in the management of the companies in which the holding has been acquired, without prejudice to the rights held by the holding company as shareholder (*Cibo* and *Portugal Telecom*).

The first are regarded as merely acquiring and holding financial holdings, and are not engaged in economic activity. The second category, referred to as "management holding companies", are economic operators. There was no significant difference between the present cases and *Cibo* – and no reason to apportion any of the input tax incurred to the "*Polysar*-type" activity of merely holding shares.

The answers to the questions on apportionment of VAT on expenditure were:

- *the expenditure connected with the acquisition of shareholdings in subsidiaries incurred by a holding company which involves itself in their management and which, on that basis, carries out an economic activity must be regarded as belonging to its general expenditure and the VAT paid on that expenditure must, in principle, be deducted in full, unless certain output economic transactions are exempt from VAT under the Sixth Directive, in which case the right to deduct should have effect only in accordance with the procedures laid down in Article 17(5) of that directive;*
- *the expenditure connected with the acquisition of shareholdings in subsidiaries incurred by a holding company which involves itself in the management only of some of those subsidiaries and which, with regard to the others, does not, by contrast, carry out an economic activity must be regarded as only partially belonging to its general expenditure, so that the VAT paid on that expenditure may be deducted only in proportion to that which is inherent to the economic activity, according to the criteria for apportioning defined by the Member States, which when exercising that power, must have regard to the aims and broad logic of the Sixth Directive and, on that basis, provide for a method of calculation which objectively reflects the part of the input expenditure actually to be attributed, respectively, to economic and to non-economic activity, which it is for the national courts to establish.*

In relation to the rules on grouping, the A-G and the court noted that recent cases suggested that Member States had to either allow grouping or not allow it: they could not restrict grouping to particular types of company or sectors (*Commission v Sweden* Case C-480/10). The PVD provisions refer to allowing "persons" to be treated as a single taxable person; it does not refer to "legal persons" in this context, although it does so elsewhere (e.g. in some of the transitional provisions in art.28a and 28b 6th Directive). The court had held that such conditions could be lawful only if they were intended to prevent avoidance, evasion and abuse, and were proportional to that intention; in the Sweden case, no such intention could be discerned behind the legislation, so the provision was unlawful.

"Direct effect" only applies if an EU law provision is "unconditional where it sets forth an obligation which is not qualified by any condition, or subject, in its implementation or effects, to the taking of any measure either by the institutions of the European Union or by the Member States". The grouping provisions in the PVD were not mandatory, so they could not have direct effect in the same way as a mandatory provision. However, national courts should interpret their own legislation, as far as possible, in a manner that was consistent with the Directive and with general EU principles. The answers on this question were:

- *The second subparagraph of Article 4(4) of Sixth Directive 77/388, as amended by Directive 2006/69, must be interpreted as precluding national legislation which reserves the right to form a value added tax group, as provided for in those provisions, solely to entities with legal personality and linked to the controlling company of that group in a relationship of subordination, except where those two requirements*

constitute measures which are appropriate and necessary in order to achieve the objectives seeking to prevent abusive practices or behaviour or to combat tax evasion or tax avoidance, which it is for the referring court to determine.

- *Article 4(4) of Sixth Directive 77/388, as amended by Directive 2006/69, may not be considered to have direct effect allowing taxable persons to claim the benefit thereof against their Member State in the event that that State's legislation is not compatible with that provision and cannot be interpreted in a way compatible with it.*

CJEU (Case C-108/14): *Beteiligungsgesellschaft Larentia + Minerva mbH & Co. KG v Finanzamt Nordenham*; (C-109/14): *Finanzamt Hamburg-Mitte v Marenave Schiffahrts AG*

4.4.4 Fairness and certainty

Seven Romanian individuals entered into a partnership agreement to construct and sell four buildings. The partnership had no separate legal personality, and did not apply for VAT registration. Following an enquiry, the tax authority determined that a taxable economic activity was being undertaken, and demanded back tax. Two of the partners appealed.

The national court of appeal was not sure whether the traders might be protected by the principles of legal certainty and protection of legitimate expectations. The Romanian legislation laid down the provisions for implementing the rules governing the application of VAT to property transactions only as from 1 January 2010; the tax authority's practice, up to that date, had rather been not to make that type of transaction subject to VAT. Sufficient information had, according to the referring court, been available to that authority for it to conclude that the two appellants had had taxable person status since 2008. It might therefore be wrong to assess them for back tax in 2010.

The questions referred were long and detailed, as was the CJEU's examination of them. It determined that general legal principles did not preclude the tax authority from determining that the transactions in this case were VATable and demanding back tax and surcharges, provided that the decision was based on clear and precise rules and that the authority's practice had not been such as to give rise, in the mind of a prudent and well-informed trader, to a reasonable expectation that tax would not be levied on such transactions. That was a matter for the national court to determine. Any surcharges had to comply with the principle of proportionality.

On the other hand, it appeared that the tax authorities denied the deduction of input tax on the projects on the basis that the traders had not registered for VAT. The CJEU ruled that this was contrary to the PVD. Denial of the input tax while charging output tax contravened several principles of VAT, including proportionality.

CJEU (Case C-183/14): *Radu Florin Salomie, Nicolae Vasile Oltean v Direcția Generală a Finanțelor Publice Cluj*

Before Romania joined the EU, veterinary services were exempt from VAT. In January 2007, the law was changed to remove a specific reference to veterinary services from the law; it was not until 1 January 2010 that the law explicitly provided that such services were taxable.

In May 2011 the tax authorities assessed a veterinary practice for back tax. The practice appealed, and a number of issues were referred to the CJEU for clarification.

First, the trader argued that it had submitted tax returns for direct tax showing turnover above the VAT registration threshold. It was unfair, and contrary to the principle of protection of legitimate expectations, for the tax authority to be able to demand tax several years later. The question asked whether the tax authority of a member state was under an obligation to register "of its own motion" (i.e. without a request from the taxpayer) a person who exceeded the small business exemption limit in its state. The CJEU replied that it was not obligatory; that is, a person could be a taxable person even if not registered. The obligation to register falls on the trader, not on the authority.

The second issue was whether the tax authority was prevented by the principles of legal certainty and protection of legitimate expectations from deciding that veterinary services were subject to VAT in the circumstances of the case. The CJEU observed that these principles had to be protected by EU institutions; this meant that the application of rules had to be sufficiently clear for those people who were affected by them to know the financial consequences of their actions. In this case, the rule change in 2007 was clearly intended to make Romanian law consistent with EU law in this area. The EU law had been clarified by a case involving Italy (Case 122/87); even though that had not been published in a Romanian translation, the existence of case law should make the rule change clear and predictable. It was for the national court to determine whether that was so, but the CJEU clearly indicated that it was likely to be. The Romanian authorities had not given the traders positive reasons to believe that they were still exempt, and the absence of enforcement action should not be enough to create a legitimate expectation in the mind of a reasonably prudent economic operator.

CJEU (Case C-144/14): *Cabinet Medical Veterinar Dr. Tomoiagă Andrei v Direcția Generală Regională a Finanțelor Publice Cluj-Napoca prin Administrația Județeană a Finanțelor Publice Maramureș*

4.4.5 Subscription services

An agricultural company paid several subscriptions or retainers for consulting services to be provided over a period, and claimed input tax deductions. The Bulgarian authorities refused the claim, ruling that no services had been performed.

The four contracts related to corporate finance, commercial development, legal advice and information security. The four separate supplier companies were all owned and managed by the same individual, who would actually provide the services. The contracts ran from 1 August 2011 to 5 March 2012, and payments were made each week.

The agreements were relatively informal. The supplies were said to be carried out by telephone, at meetings and through e-mails for which no formal record was kept. The authorities disputed the deduction on the grounds that there was no proof as to the type, quantity and nature of the services actually provided. The referring court noted that the parties had not linked the consideration to the achievement of any particular result; also, the authorities had never suggested that the supplies were connected

with any fraud. The suppliers were said to have staff adequately qualified to provide the services for which they had contracted.

The Court agreed with the taxpayer. Provided that the services were "legitimate" (which it was for the national court to determine), the subscription contracts constituted taxable supplies. The chargeable event was the end of the period for which payment was to be made. In effect, the rules on continuous supplies of services applied.

CJEU (Case C-463/14): *Asparuhovo Lake Investment Company OOD v Direktor na Direktsia 'Obzhalvane i danachno-osiguritelna praktika' Varna pri Tsentralno Upravlenie na Natsionalnata Agentsia za Prihodite*

4.4.6 Italian leniency

The Italian law provides for the limitation period for prosecuting crimes to be extended only by a quarter following interruption of proceedings. As a result, crimes may become time-barred from prosecution even though the proceedings were brought in good time. The law was changed in 2005 with the effect of exempting many criminals from punishment. Questions about the acceptability of this rule were referred to the CJEU in relation to a VAT carousel fraud carried out between 2005 and 2009 – exempting the criminals effectively exempted the transactions from VAT as well.

The full court has now agreed with Advocate-General Kokott's opinion that the leniency of the Italian law is unacceptable. The CJEU has the right to rule on this because a share of Italian VAT is due to the EU as part of its own resources; failing to collect it is therefore a breach of Italy's obligations. The EU treaties require Member States to provide for effective, proportionate and dissuasive penalties for irregularities in matters of VAT; in cases of VAT fraud these penalties must, in serious cases at least, also include penalties involving deprivation of liberty. A limitation period which had in many cases the effect of exempting perpetrators from punishment is incompatible with EU law. The national court must therefore not apply such a limitation period in criminal proceedings in relation to VAT fraud. The CJEU was satisfied that this did not unacceptably infringe the rights of the accused. In particular, it could not lead to him being convicted of something that was not a criminal offence at the time that it was committed.

The questions referred raised several different possible ways in which the Italian law had breached EU law. The CJEU's conclusion was that that the main problem was with art.325(1) and (2) TFEU; other aspects, including the introduction of an unlawful State aid, were subsidiary to that. The cancellation of the limitation period in order to prosecute the crime did not need separate justification under other legal provisions.

CJEU (Case C-105/14): *Re Taricco and others*

4.4.7 Public bodies

The CJEU has given a ruling in a case concerning the VAT status of "local budget entities" that carry on public functions on behalf of local municipalities. Although they are not themselves public authorities, they are not "independently carrying on an economic activity".

The Polish tax authority had ruled that they were capable of being taxable persons; the CJEU agrees with the municipality involved in the case that they are not. The judgment is based on the exclusion of employees from the definition of taxable person by art.10 PVD: the court considers that the features necessary for independence include bearing the economic risk, the completion of an activity by an entity on its behalf and for its own account, the existence of its own assets, the free organisation of the implementing rules of work, staff resources and equipment, and the fact that the entity bears contractual liability and liability for damage caused to third parties. It is for the national court to apply these criteria to an individual case, but the implication is that the entity concerned in the appeal is not a taxable person.

CJEU (A-G) (Case C-276/14): *Gmina Wrocław v Minister Finansów*

4.4.8 Abusive practices

The Advocate-General has given an opinion (not made available in English) on the subject of abuse of rights in relation to international transactions and place of supply, a theme previously considered in the *Newey* case. A Hungarian individual created intellectual property (know-how relating to the provision of adult online content) through a Hungarian company. The Hungarian company licensed the content to a Portuguese company, while retaining the responsibility of "maintaining and developing" the content. Portuguese VAT rates (specifically, those applicable in Madeira) were lower than those in Hungary.

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

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

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

The A-G also considered whether the possibility that the individual exercised absolute control over the activities of the Portuguese company could be relevant. In his view this would not prevent the Portuguese company having a real presence in Portugal and carrying on a real economic activity there. The Portuguese government had confirmed that it regarded the company as having the appropriate human and technical resources to be treated as established there.

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

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

4.4.9 Cost sharing groups

The Latvian court has referred questions about cost-sharing groups and cross-border operations to the CJEU. The essence of the problem appears to be that different countries have enacted the cost-sharing exemption rules in art.132(1)(f) PVD with different conditions. It may therefore be the case that a cost-sharing group structure satisfies the conditions in one country but not in another. The questions ask the CJEU whether the exemption can validly be restricted in such circumstances – in effect, to clarify which country's rules should apply where transactions take place between the group entity in one country and a group member in another.

The questions also ask whether an "independent group of persons" has to have separate legal personality, whether uplifting recharges in accordance with direct tax rules on transfer pricing can be ignored, and whether the exemption can apply even across the EU boundary where a group has a member in a third country.

CJEU (Reference) (Case C-326/15): *DNB Banka'AS v Valsts ieņēmumu dienests*

4.5 Eighth Directive reclaims

Nothing to report.

5. INPUTS

5.1 Economic activity

Nothing to report.

5.2 Who receives the supply?

5.2.1 Minority report

A dispute arose among the shareholders of a family business. The company paid for legal services over a period of 18 months and claimed input tax of £22,024. After a visit, HMRC ruled that this was not deductible: the supplies had not been made to the company but to the shareholders, and the supplies had not been made for the purposes of the company's business.

The minority shareholder was a family member who had worked for the company up to 2005. He had left to set up in competition, but had remained a 25% shareholder. In 2011 he issued a petition under Companies Act rules that allow a minority shareholder to apply to the court for winding-up on the basis that the majority are acting in a way that is "unfairly prejudicial" to the minority. The company issued a counter-claim in respect of the ownership of intellectual property in some of the cutlery designs produced by the competitor during the time he worked for the company. The dispute was eventually settled by the company paying £900,000 for the minority shares (which were then cancelled) and £975,000 in respect of his legal costs.

The solicitors' invoices on which the company claimed input tax were addressed to the majority shareholders rather than to the company itself. Invoices from other professional advisers also referred to the individuals as the clients.

The Tribunal noted the approach of the Court of Appeal in *Airtours* (which is subject to appeal to the Supreme Court). This was to start with the contractual position, and then to decide whether this should be varied in light of the economic reality of the situation. In this case, although the engagement letters had not been provided in evidence, it appeared that the solicitors' contracts were with the individuals; this was consistent with the economic reality, as the individuals were the respondents in the legal proceedings and had an economic stake in the outcome of the case. Although the company and the majority shareholders had very similar interests, it could not be said that the company, rather than the shareholders, was the true recipient of supplies that had contractually been made to the shareholders.

For completeness, the Tribunal also considered the "purpose" test. There was a general benefit to the company in that resolving the disruption of the minority shareholder freed up management time and energy. The question was whether that was a link to the appellant company's economic activity as a whole, sufficient to justify treating the legal costs as an overhead. The Tribunal noted that the issue of new shares was held

to be linked in that way (*Kretztechnik*), but considered that the buy-back of existing shares was quite different – not least because the same result could have been achieved by the other shareholders making that purchase. The Tribunal therefore found against the company on the "purpose" test as well as the "to whom" test.

First-Tier Tribunal (TC04608): *Robert Welch Designs Ltd*

5.3 Partial exemption

5.3.1 Financial services: PESM restored

VW Financial Services are engaged in a long-running dispute with HMRC over the appropriate way to apportion and recover overhead input tax in a business providing hire purchase finance for cars. The problem is that a HP financier buys and sells the car, so it has substantial taxable turnover as well as exempt interest income; but HMRC regard it as essentially a financial business that should not recover input tax on overheads.

The FTT (TC01401) upheld the company's appeal against a refusal by HMRC to accept its proposed partial exemption special method. In late 2012, the Upper Tribunal overturned that decision. The Court of Appeal has now reversed it again, restoring the FTT's decision.

Background

There has been a long-running dispute between the leasing industry and HMRC about the proper attribution of overhead input tax. In R&C Brief 31/2007, they declared a new policy to be applied from 1 April 2007 onwards: HP finance was to be treated as a wholly exempt activity, even if legally there was a taxable supply of goods, and as a result the overhead input tax incurred by an HP financier was to be regarded as wholly attributable to making exempt supplies. The logic behind this approach was explained as follows:

"*In most HP transactions, the goods are resold at cost without any margin to cover overhead costs. As there is no margin on the HP goods, the cost of the overheads will normally be built into the price of the supply of credit. In this scenario, HMRC's view is that the overheads are purely cost components of the exempt supply. Otherwise the business would continually enjoy net VAT refunds despite:*

- *making no zero-rated or reduced rate supplies; and*
- *charging a total consideration under the HP agreement that fully recovers its costs and an element of profit.*"

This Brief was later reissued as RCB 82/2009.

VW Financial Services agreed a partial exemption special method with Customs in August 2000. It was based on a 1984 agreement between the Finance Leasing Association and Customs that restricted recoverable overhead input tax in a finance business to 15%. However, the FLA withdrew from the 1984 agreement during 2000. In 2007, VWFS returned to HMRC with a suggestion for a new PESM. By this time, the new policy was in operation, and the company's proposal could not be agreed

– they suggested that the overhead input tax in relation to retail business should be determined by the proportion which taxable transactions bore to total transactions. This transaction count was based on every HP agreement being two transactions (one taxable, one exempt), every leasing transaction being two transactions (both taxable) and every fixed price service and maintenance contract as one (taxable) transaction. On this basis, 50% of the residual input tax referable to HP transactions was recoverable.

For the four periods 10/07 to 07/08, the company applied its preferred PESM and received assessments against which it appealed. After that it operated HMRC's preferred method and made voluntary disclosures to claim more input tax, and appealed against HMRC's refusal to pay these. The total amount in issue before the Tribunal was about £500,000.

First-Tier Tribunal

The FTT examined the organisation of VWFS into eight departments and the way it did business. It also went through the PESM in detail. The company's approach was to apportion overhead input tax between the number of taxable and exempt transactions (i.e. payments received, rather than contracts entered into) in each period, without regard to their value. HMRC divided the input tax between the different classes of business, but then used a value-based apportionment in which no account was taken of the initial value of the taxable car. A small amount was still recoverable under HMRC's method because there were other taxable supplies such as settlement charges and option to purchase fees.

The FTT considered a number of precedents on the basis for deducting input tax on overheads, including *BLP Group plc*, *Abbey National plc*, *Midland Bank plc, Kretztechnik*, *Cibo Participations* and *AB SKF*. The FTT came to the conclusion that HMRC's approach was not logical: to attribute overheads entirely to the exempt part of a mixed transaction was inherently unfair and unreasonable. It was not necessary for the input tax to be passed on to the consumer in the form of a directly identifiable element of the price charged. The input tax was incurred in relation to both taxable and exempt transactions, and VWFS's approach was a reasonable one.

Upper Tribunal

The Upper Tribunal considered that it was necessary to characterise the trader's business. If it was truly engaged in taxable vehicle sales, the FTT decision would be reasonable; if, as HMRC argued, it was purely a financial business, then the overhead costs did not have a link to the taxed transactions, and a PESM which produced such a high recovery would not be reasonable.

HMRC submitted that the company made no profit on the taxable transactions, so it had to bear all of its costs out of its exempt income. HMRC's counsel argued that this meant its overheads were only a cost component of its exempt supplies and could never be recoverable. The Tribunal rejected this conclusion, holding that it was necessary to look at the facts of each case to determine whether there was a sufficient link to taxable activities to justify some recovery.

However, the Tribunal concluded on the basis of the facts of this case that VWFS is a financial business and its input tax recovery has to be viewed in that light. It takes no part in the sale of the cars, and cannot affect the price at which they are sold; those sales are not even shown in its statutory accounts. The judge commented:

We feel that the FTT may have been misdirected by looking at the matter purely through VAT-tinted spectacles. What is required is a focus on economic realities. It is true that VWFS's transactions will always involve a taxable transaction and an exempt transaction inextricably intertwined. But the finance transaction is, to put the matter colloquially, the 'main event' for VWFS. It is what VWFS is all about. Without it, VWFS would be a wholly unnecessary intervener.

The decision was that VWFS's PESM was not a fair and reasonable method. HMRC's assessment was based on a different PESM which excluded the value of the car itself, and as the UT has upheld the assessment, that implies approval of the imposition of that method.

Court of Appeal

The company appealed to the Court of Appeal. It argued that the UT was wrong to conclude that none of the overhead input tax of the company was incurred in making taxable supplies of motor vehicles. The CA agreed: the company was not a pure financial services business such as a bank. To make its supplies of HP finance, it had to make supplies of the cars as well. Neither part of the business could exist without the other. The FTT had therefore been entitled to conclude that the general overheads had been used to some extent in making taxable supplies.

HMRC maintained that they had put forward an alternative argument that a lesser apportionment than the PESM's 50% recovery was appropriate, if they were wrong that no recovery should be allowed. The CA did not accept that this had been part of the argument in the FTT. The challenge had been based on the view that no attribution to taxable supplies was permissible. As the FTT had rejected this point of principle, it had no alternative but to allow the company's proposed PESM instead. The CA was satisfied that the FTT's decision contained no error of law, and restored it, overturning the UT's decision.

Court of Appeal: *Volkswagen Financial Services (UK) Ltd v HMRC*

5.3.2 Attribution

A Masonic Lodge Social Club was registered for VAT as a non-profit organisation. It operated from premises that were owned by a Trustee Board, which leased them to a company that was responsible for the upkeep of the premises. The company collected dues from a number of Masonic clubs that used the centre, and also collected an annual fee from a catering company which operated under a franchise agreement. The appellant club had an informal agreement with the company under which it managed the premises from day to day.

In 2011 a new kitchen was purchased and input tax of £5,604 was claimed by the club. HMRC later ruled that there was no clear link between the expenditure and the club's taxable outputs, and disallowed the VAT. The club appealed.

The club referred to a number of old precedent Tribunal decisions about "nexus": *Hartridge t/a Hartridge Consultancy* (VTD 15,553), *Giffenbond Ltd* (VTD 13,481), *Myatt & Leason* (VTD 13,780) and *SRI International v HMRC* (UT 2011).

HMRC responded that the club's supplies consisted of managing the premises for the company for no consideration, and of taxable bar sales. There was no link between expenditure on a new kitchen, which mainly benefited the catering company, and the club's income. There was an indirect link in that the previous kitchen had been condemned by the local authority and it was therefore necessary to replace it, but that was very similar to the case of *Rosner*; the necessity of incurring the expenditure did not link it to the outputs. HMRC also relied on *BLP Group plc* as evidence that an indirect link was not enough to justify a deduction.

The Tribunal agreed with HMRC. Although there was a general benefit to the appellant, VAT is a transaction-based tax. Catering was no part of the club's taxable activities. The funding for the kitchen was provided by the management company, not by the club, and the main benefit accrued to the management company (which was not VAT-registered) and to the caterer. The expenditure was directly linked to the activity of managing the premises for no consideration, which was a non-business purpose, and the VAT therefore could not be claimed.

First-Tier Tribunal (TC04520): *Whiteabbey Masonic Club*

A golf club claimed £567 of input tax on maintenance and repair of a lift, refurbishment of chairs in the bar and lounge area of the clubhouse, and new curtains in the bar and lounge. The input tax was claimed in full on the basis that the costs were exclusively used in making taxable supplies of food and drink. HMRC ruled that the inputs were residual, which would lead to a reduction in the amount recoverable. The calculation of the residual recovery was not in dispute; the Tribunal was asked only to rule on the point of principle.

The same club had been involved in an earlier dispute about an earlier refurbishment in 2011. The club claimed four years' worth of the difference between 100% recovery and residual recovery in relation to the same kind of expenditure from June 2008 to December 2012. This was described as "a voluntary disclosure in its VAT return" – presumably an adjustment in the return under reg.34, accompanied by a letter to HMRC setting out the details because the club knew that HMRC would disagree with it. As a result, the Tribunal was considering an assessment rather than simply the refusal of a claim.

The club argued that the only reason that anyone would visit the upstairs areas was to consume food and drink. All the supplies made upstairs were taxable at the standard rate. There was no link between the upstairs and the playing of golf.

The club's representative explained that the club had tried to increase the income from its taxable sales in the clubhouse by introducing "social memberships" and attracting outside users, all of whom paid VAT. The income subsidised the exempt golfing activities.

The Tribunal considered a number of earlier decisions about golf clubs, including *Auchterarder Golf Club* (VTD 19,907) and *Bridgnorth Golf Club* (TC0094). In these cases, expenditure on the clubhouse was held to

be intrinsically linked to the supply of membership, because members enjoyed the facilities. The facilities of the clubhouse were among the benefits that the member received in return for a subscription. The Tribunal agreed with HMRC that there was a link between the subscriptions and use of the bar; the costs were not of a kind that could be exclusively linked to the sale of food and drink. The appeal was dismissed.

First-Tier Tribunal (TC04619): *Bedale Golf Club Ltd*

5.3.3 Toolkit update

HMRC have updated their "toolkit" on partial exemption. As before, the toolkit identifies major risks of error in its specified area, and offers a checklist for agents to use when reviewing clients' systems to identify weaknesses.

The July 2015 version includes information on attribution, apportionment, changes of intention, annual adjustments and the capital goods scheme.

VAT Partial Exemption (2015)

5.4 Cars

Nothing to report.

5.5 Business entertainment

Nothing to report.

5.6 Non-business use of supplies

Nothing to report.

5.7 Bad debt relief

Nothing to report.

5.8 Other input tax problems

5.8.1 Toolkit update

HMRC have updated their "toolkit" on input tax. As before, the toolkit identifies major risks of error in its specified area, and offers a checklist for agents to use when reviewing clients' systems to identify weaknesses.

The July 2015 version includes information on the following:

- preventing the application of the *Lennartz* approach to purchases of land, buildings, aircraft, ships, boats and other vessels made on or after 1 January 2011;

- extending the Capital Goods Scheme (CGS) to certain purchases of aircraft, ships, boats and other vessels made on or after 1 January 2011;
- extending the CGS to require input tax adjustments to reflect changes in the level of non-business use, including private use, of assets purchased on or after 1 January 2011;
- a number of technical changes in the operation of the CGS;
- extending the requirement to make 'payback' and 'clawback' adjustments when input tax is claimed or restricted on the basis of intended levels of business use, and that intention changes before use occurs;
- the treatment of input tax incurred in the course of entertaining overseas customers;
- the introduction of formalised special methods to apportion VAT incurred for business and non-business purposes and, where businesses are required to carry out partial exemption calculations, special methods incorporating both business/non-business and partial exemption calculations.

VAT Input Tax (2015)

5.8.2 Budget announcement

The July Budget included an announcement that the government will legislate so that eligible public bodies will be able to reclaim VAT refunds for specified shared services.

Budget Report para.2.137

5.8.3 Input tax deduction on vouchers

In TC03256 (early 2014), the FTT had to consider the application of SI 1993/1507 to a promotion by a newspaper publisher involving the purchase and distribution of retailer vouchers to customers. It concluded that in distributing vouchers the publisher was not "making them available for purposes other than a purpose of the business", because the whole purpose was to promote sales of newspapers. An appeal is due to be heard by the Upper Tribunal in October 2015.

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

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

(2) If the appellant does in fact incur input VAT on such purchases, whether it is entitled to set that input VAT (and the input VAT which

HMRC accept it has incurred on purchases of vouchers from the intermediary) against its output tax liabilities.

The problem was that the PVD does not currently contain any rules for vouchers. A comment by the Commission in May 2012 acknowledged that this created significant inconsistencies and problems. HMRC's representative claimed that "there was nothing in the existing UK legislation, when interpreted and supplemented by concession as HMRC did, that was inconsistent with the PVD and the case law." The company's representative responded that "there were certain crucial aspects of HMRC's interpretation and operation of the legislation which flew directly in the face of various fundamental principles of VAT and accordingly the UK legislation either needed to be re-interpreted to conform with those principles under the *Marleasing* approach or, if that were not possible, it needed to be overridden altogether by allowing the appellant to rely directly on the right to deduct input tax enshrined in the PVD."

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

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

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

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

The appeal was allowed in principle.

First-Tier Tribunal (TC04586): *Associated Newspapers Ltd*

5.8.4 Alternative evidence

Two companies (under common control) appealed against assessments of £56,636 and £47,489 representing disallowance of input tax on certain supplies between 11/06 and 02/09. The companies had been involved in groundwork maintenance (e.g. of NCP car parks) for 30 years. According to the director, HMRC had suddenly changed their approach and started to query invoices which referred to "services provided" and "various locations" when they had previously accepted them. The director said that he took warnings from HMRC about the VAT status of counterparties seriously: he checked the validity of VAT numbers, kept records of doing so, and stopped using firms if he received a "veto letter" stating that their VAT number was invalid.

The Tribunal heard evidence from the director, who explained that the descriptions on the invoice were adequate for him to know what was being provided. He kept records to control the companies' expenditure, and he would not pay a bill if it did not accord with his records. He accepted that some of the invoices had other faults, but the companies maintained their appeals in respect of most of the input tax.

The Tribunal also heard from an officer who took over the case after it started (the original officer had been very ill and had subsequently died) and from the reviewing officer. They explained HMRC's objections to the various invoices on the grounds of non-compliance with reg.14(g) and (h), and explained why HMRC did not consider it appropriate to exercise discretion under reg.29 on the basis of "alternative evidence". HMRC's counsel argued that the decision was reasonable and could therefore not be overturned by the Tribunal.

The appellants cited a number of precedents relevant to missing trader fraud. However, HMRC responded that they were not relying on *Kittel* – the absence of evidence was much more basic. The Tribunal explained that its approach had to be to consider each invoice and decide:

(1) Does a given disputed invoice satisfy reg.14? If we find that it does then we allow the appeal in respect of that particular invoice.

(2) If not, was HMRC's decision to refuse to exercise their discretion under reg.29 a reasonable one?

Jurisdiction under (1) was appellate, but under (2) was supervisory.

The Tribunal made the following comments about the application of the regulations:

How much detail must an invoice contain for it to satisfy reg.14 (g) & (h)? Without attempting to be definitive, our view is that it depends on the matters being invoiced. In relation to invoices for supplies of services, one example (one that was cited to us in evidence and in argument) is that of a professional firm (say, accountants) whose fee notes simply use a stock phrase such as "To professional services rendered in the period 1 March to 31 March 2015". That, it seems to us, must be adequate for the purposes of reg.14 (g) & (h). The services supplied can be identified (the professional services of a firm of accountants), as can their extent (those rendered in the month of March). Turning to invoicing of supplies of goods, one would, it seems to us, normally expect to see a narrative description of the goods that the customer could check and approve for

payment – that is what reg.14 (g) & (h) requires: a description to identify the goods and give the quantity of the goods. Often the goods invoice will recite the specification from the customer's purchase order (or if only part of the order is being satisfied, such part of it as relates to the particular goods being supplied). However, we accept Mr Deane's evidence that in the line of business of construction groundworks contractors it was common practice for less information to be provided, and we look at specifics later. Of course, it may be that on receipt of an invoice the customer wishes to check or query the invoice to ascertain that it covers all and only the supplies the customer believes he is liable to pay for. Where the customer approves and pays the invoice without challenge, that is some evidence that the invoice contains a sufficient identification (reg.14 (g)) and quantification (by quantity or extent) (reg.14 (h)) of the goods or services supplied; however, we do not accept that payment of the invoice is in itself conclusive that the invoice is reg.14 compliant. Part of the purpose of reg.14 is to ensure that invoices contain sufficient information to enable an independent observer (typically HMRC) to be satisfied as to the identification and quantification of the goods and services supplied.

The Tribunal applied this approach and concluded that a number of the invoices did not comply. For these, it had to consider the reasonableness of HMRC's decision. The judge noted that HMRC had explicitly stated that they were not alleging involvement in any fraud (to avoid taking on the burden of proof), and could not therefore ask the Tribunal to construe or infer a lack of good faith in the business dealings of the taxpayer. HMRC's pleading had to be consistent.

The Tribunal noted that the reviewing officer had spent considerable time and effort trying to tie together the disputed invoices and the supporting evidence provided by the companies, and had fully explained in his review decision letters why he had been unable to reconcile them. In the view of the Tribunal, the decision was entirely reasonable, and the appeal was therefore dismissed in respect of those invoices that the Tribunal found did not comply with the regulations.

The decision does not note the amounts of these invoices, so it is not clear how significant a (partial) success this was for the taxpayer.

First-Tier Tribunal (TC04610): *Deadoc Construction Ltd and Another*

5.8.5 Pre-registration VAT

An individual worked for a company that sold locks. The company was unable to trade on the internet so he started a business buying the locks from his employer and selling them online. He registered for VAT and claimed a deduction for VAT charged to him on goods he had bought before he registered. HMRC allowed only that proportion relating to goods held at the date of registration.

The trader appealed, arguing that the UK had not properly implemented the Directive. Transactions of a trader below the registration threshold were still, in UK law, taxable transactions; they therefore carried a Directive right of input tax deduction. The "small business exemption" in art.286/289 PVD had not been correctly implemented in the UK, because transactions of traders below the threshold were not described as exempt. The trader cited the case of *Nidera* (Case C-385/09) as authority for the

proposition that an administrative arrangement (such as the UK's threshold) could not deny a trader a Directive right of deduction.

The Tribunal agreed that the interpretation and interaction of arts.286/289 with UK law were not straightforward. However, the intention was clear: the goods on which the trader claimed a deduction had been sold without any liability to output tax, and had not been used in any way for his taxable transactions. There were clear statements in *Schemepanel* that supported the view that no deduction could be allowed. The situation was not similar to *Nidera*, which related to the accession of Lithuania to the EU.

The appeal was dismissed, and HMRC's decision not to allow the proportion of VAT relating to purchases that had been sold before registration was confirmed.

First-Tier Tribunal (TC04595): *Earl Redway t/a Loktonic*

5.8.6 Missing traders

A trader appealed against the FTT decision in TC03062 to confirm HMRC's decision to disallow about £1m of input tax claimed in the period 04/06. The FTT concluded that the director knew that the deals were "too good to be true" and therefore ought to have asked further questions, giving him the "means of knowledge". The FTT did not find that he actually knew about the fraud. The trader appealed, arguing that the FTT had applied the wrong test.

The appellant's representative argued that the FTT had found that the director was aware of the "risk of fraud", but that was not enough to show that the only reasonable explanation for the transactions was fraud. The UT examined the representative's criticisms of the FTT's decision in detail, and dismissed them. The FTT had identified the correct test and had applied it correctly. The decision could not be faulted.

Upper Tribunal: *Wireless Wizards Ltd v HMRC*

In an unusual MTIC case, the trader decided not to present any evidence, and to concede various points without argument. The judge considered the evidence presented by HMRC and concluded that the companies had the means of knowledge – indeed, must have known of the connection of its deals to fraudulent losses – on the basis of several of the points raised. The appeal was dismissed.

First-Tier Tribunal (TC04530): *Lakonia Ltd*

HMRC raised assessments on a company to disallow input tax claimed on supplies to it by an associated company that had not filed VAT returns for 31 periods. The assessments were based on *Kittel*, which required the losses to be connected to fraud. The Tribunal considered this to be a difficult question: the facts and the law were relatively straightforward, but the question of whether failing to file returns and pay the VAT due was actually fraudulent was less clear. The associated company had eventually been put into liquidation by HMRC owing very substantial amounts of PAYE, NIC and VAT; at the end of a long investigation, it appeared that HMRC had decided that an alternative approach to recover some of the VAT at least would be to assess it on the remaining trading company, which was solvent.

Much of the hearing was taken up with consideration of other arguments raised by HMRC, including a suggestion that there had in fact been no taxable supplies between the companies, whether they had been fully paid for, and whether the invoices were valid for VAT deduction. All these points were dropped on the final day of the hearing, which was decided only on the question of dishonesty.

The judge said that this had been a difficult decision, because there were numerous factors that suggested the director had made strenuous efforts to keep the business going and turn it around, and had never intended to defraud HMRC. It appeared that he had worked for no salary and had made significant personal losses. However, he had known that the appellant company was claiming input tax deductions for VAT that the other company had not paid, and this continued over an extended period.

It was also significant that in trying to negotiate a settlement of the other company's arrears, the director had misrepresented the true extent of the liabilities. By the time it was liquidated, its assets had progressively been transferred across to the appellant company, exacerbating HMRC's losses. The assessment for £230,000 was confirmed.

The judge concluded with some criticism of HMRC's handling of the case. It was apparent that they had failed to get to grips with the transactions and the missing returns over an extended period, and had concentrated on the PAYE liabilities while apparently not realising how serious the VAT situation was. The judge expressed the hope that HMRC would negotiate a settlement with the director that would enable him to keep the business afloat and settle his debts, which the judge considered he always intended to do.

First-Tier Tribunal (TC04583): *Medallion Europe Ltd*

A MTIC appeal started in 2014 (TC04097) but had to be adjourned because the appellant's representative (a director of the three companies concerned) was taken ill after presenting opening submissions but before any evidence was considered. The earlier Tribunal decided to proceed with the case on the basis of written submissions, given that the director might never be well enough to carry on presenting the case in person.

The total VAT in dispute was £12.7m. It related to alleged contra-trading by three companies in the periods 05/06 and 06/06. The Tribunal examined the evidence put forward by HMRC and the explanations put forward by the appellant, and came to the usual conclusion: the appeal should be dismissed, in this case because the director actually knew that all the transactions were connected with fraud.

First-Tier Tribunal (TC04614): *Westminster Trading Ltd and others*

A wholesaler of electrical goods appealed against HMRC's denial of input tax totalling £107,838 for monthly accounting periods 10/09 and 08/10 – 10/10, and against default surcharges totalling £1,537 in respect of five later VAT periods.

The disallowance related to alleged connection with missing trader fraud. Somewhat unusually, this related to only a small part of the company's trade, being specific transactions in televisions. The total turnover was much higher, most of it not in dispute.

The Tribunal examined the background to the trade, the due diligence carried out, and warnings given by HMRC about missing trader fraud. It concluded that, in relation to the deals on which HMRC sought to disallow input tax, the due diligence had been inadequate. A reasonably diligent trader would have asked more questions and would have concluded that the deals were not honest: this constituted “means of knowledge”, and the appeal against the disallowance was dismissed.

The trader’s excuses for the default surcharges were that it had an agreement with HMRC to offset the VAT in dispute against its current liabilities, or alternatively it was entitled to do so because of its belief that the VAT under appeal was not due. The Tribunal rejected both these arguments. The company had to have a reasonable excuse at the time the payment fell due: it could not choose not to pay because of a belief that it would win the case, but rather would be repaid the surcharge later if it did win. There was no evidence that HMRC had agreed to any offset (if anything, they had pointed out that no offset could be made). The surcharges were confirmed.

First-Tier Tribunal (TC04625): *AC (Wholesale) Ltd*

6. ADMINISTRATION AND PENALTIES

6.1 Group registration

6.1.1 Unreasonable decision?

In early 2013, the FTT (TC02605) ruled that HMRC should reconsider a refusal of a request to allow a company to validate its VAT returns by admitting two subsidiaries to a VAT group retrospectively. The 1979 High Court decision in *Save & Prosper Ltd* showed that HMRC have discretion to allow this, but it is their policy to allow it only in cases of HMRC error. As set out below, the FTT decided that the officers making and reviewing the decision had not even considered whether to exercise their discretion, which made their decisions unreasonable; they therefore were required to reconsider. Naturally, HMRC reconsidered and issued an identical decision, so the company appealed again to the FTT.

The first decision (Judge John Clark)

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

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

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

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

Retrospective grouping

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

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

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

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

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

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

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

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

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

The argument for the company was summed up as follows:

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

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

a "conscious process". The company had made mistakes, rather than deliberate decisions.

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

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

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

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

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

Can I backdate my application for more than 30 days?

Only in exceptional circumstances:

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

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

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

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

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

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

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

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

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

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

Belated notification

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

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

Overall conclusion

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

The second decision (Judge Howard Nowlan)

HMRC pointed out that all the judge could do was remit the matter to HMRC for further reconsideration – he could not force them to exercise their discretion in favour of the company. This was effectively an assurance that the company could not win, so the judge might as well dismiss the appeal. The judge accepted that a series of remittances back to HMRC could lead to an "embarrassing ping-pong".

Nevertheless, he clearly considered that the discretion ought to be exercised in favour of the company. After reviewing the history of the dispute, he observed that HMRC had made very minor changes to their policy on requests for retrospective grouping after the 2013 decision – they had changed "exceptional circumstances" to "most exceptional circumstances"; they had said these "include" HMRC errors, rather than implying that only HMRC errors could qualify; and they had changed the 30-day time limit to make it clear that backdating to a date before the end of the most recent return period for either the company concerned or the representative member was not possible.

The company argued, and the judge agreed, that HMRC had if anything made the conditions more restrictive. In his view, the word "include" was "window-dressing". It was still effectively impossible for a trader to benefit from a discretion that Parliament had intended to be freely available.

He considered the reasoning behind the change to the 30-day rule. It was clearly sensible to prevent a situation in which it would be necessary to revise returns that had already been filed. However, that was the opposite of the situation in the present case: exercising the discretion would remove the need to revise returns that had been filed.

It was also sensible to prevent companies rewriting history. Again, that did not appear to be the case here. It was clear that the group had always and consistently filed on the basis that the companies were part of the VAT group. It had not deferred taking a decision, or sought to change what it had done. All it was asking was for its administrative error to be ratified.

If the discretion was not exercised, the companies would suffer a VAT cost that was described as "incoherent" and contrary to the principles of fiscal neutrality. Traders should be relieved of the cost of VAT on their taxable transactions; this would create a sticking cost for no good reason.

The judge also commented on the way in which the error in the group had arisen and gone unnoticed for some time. The company had been in a period of "administrative turmoil", with different senior finance officers coming and going over an 18 month period. HMRC had sent lists of the VAT-grouped companies at least twice during the period, but once the

assumption had been made that the companies were in the group, it was understandable that no one would check the list for this particular error.

The judge allowed the appeal, remitting the matter back to the Commissioners for further reconsideration, with the following further comments about the factors HMRC should take into account in exercising their discretion:

- *The present applications had implicitly necessitated no remote change to any of the filings originally made by the group companies, and perversely it will have been the fact that the applications have been rejected twice that has occasioned the need to make several changes to the treatment, as originally filed.*
- *While the original filings were wrong, in that they were made on the basis of two erroneous assumptions made by the group, the treatment that the group is now requesting is, on any sensible approach, the fair and appropriate treatment in relation to input tax incurred by a housebuilding group.*
- *While HMRC may claim, without much support, that applications for retrospective inclusion in VAT groups are common, and that the present situation is no different from the run-of-the-mill retrospective applications, it must be the case that in most cases there will be little impact on net tax whether companies were or were not included in group registrations. In the present case, the significance of the dual error, and the feature that on 30 March 2007 the mistake made has occasioned a tax loss equal to about half the total economic loss made by the group on C28's housing development may, I suggest, make it very exceptional. The implicit suggestion that errors by HMRC are always "most exceptional" is highly doubtful at the very least. The summary by the Appellant's counsel was that HMRC could, at the stroke of a pen, have provided a fair solution, and one that was entirely consistent with the realistically intended treatment of this housebuilding group, had HMRC chosen to do so. That action would have involved no complication and no adjustment to past returns. As matters have emerged to date, the group has been involved in a long and expensive dispute, and still runs the risk of suffering tax treatment that might be strictly correct, but that is in common sense terms wholly unfair.*
- *HMRC should not give weight to the delays on the part of the Appellant in seeking retrospective inclusion into the VAT group, and to the fact of having failed to spot the group's errors when the Appellant was sent the list of companies believed to be in the VAT group unless these reasons were genuine reasons that led to the decisions. When there is every indication that, under the tightly-defined announced policy, precisely the same decisions would have been reached even disregarding these factors, those factors appear to have been inserted into the decision letter in relation to C28's application to seek to justify the decision, in fact made on other grounds. It is notable that these factors represented two out of the three points made in the summary paragraph, along with the unexplained, and wholly unconvincing suggestion, that there was nothing exceptional about the present circumstances.*

- *The final matter that I suggest that HMRC should consider is whether it is the proper function of HMRC to seek to retain tax charged solely because of incoherent and understandable errors made by the group and made during a period when the group has accepted that its finance administration was in some chaos, or whether it would be more appropriate to pay some regard to fairness and common sense.*

It remains to be seen whether HMRC will accept that they have been unreasonable in this case, or will change their published policy on discretion again.

First-Tier Tribunal (TC04582): *Copthorn Holdings Ltd*

6.2 Other registration rules

Nothing to report.

6.3 Payments and returns

6.3.1 Online filing

A barrister filed a paper return for the period 06/12. HMRC wrote to him requiring electronic returns; he continued to file on paper. HMRC imposed a penalty for failing to file electronically for 03/13. The trader's defence was that he did not mind filing electronically; however, he did object to the necessary preliminaries to that, which involved signing up to the 'Government Gateway' – that required him to tick a box stating that he had read HMRC's terms and conditions for online filing. He did not consider that a requirement that HMRC were entitled to impose on him. He did not object to any of the terms in detail (he had not read them); he considered that being required to read them would be burdensome (some 12.5 pages of closely printed A4).

This was, naturally, a case for Judge Mosedale. She examined the terms and conditions and found some of them questionable. She was not convinced that ticking the box created a binding contract that could be enforced against the taxpayer, but HMRC ought to have authority for imposing any duty on a taxpayer, particularly if failing to fulfil that duty necessarily led to the imposition of penalties. At the end of 155 paragraphs in which the jurisdiction of the Tribunal and questions of public law are considered in some detail (and Judge Mosedale rejects the authority of at least one "obiter" statement by a Court of Appeal judge), she concludes that the penalty is unlawful because HMRC's actions leading up to it were unlawful, and in addition he had a reasonable excuse for his failure to file online.

First-Tier Tribunal (TC04537): *Neil Garrod*

6.4 Repayment claims

6.4.1 Evidence for *Fleming* claim

The representative member of a group of car dealers made an "*Elida Gibbs/Fleming*" claim in respect of VAT accounted for on manufacturers' bonuses paid "outside a line of supply" between June 1973 and March 1997. HMRC refused the claim, ruling that the company had not shown that it had overpaid VAT. In September 2013, the FTT agreed that the company had failed to discharge the burden of proving on the balance of probabilities that it had done so, and dismissed its appeal. The company appealed to the Upper Tribunal.

The company had made an *Elida* claim in May 2000 for £143,000 in respect of VAT accounted for on manufacturers' bonuses from September 1997 to March 2000. HMRC had paid that claim. A further claim was made and settled for earlier periods using what was called the "Elida table" – a summary prepared by HMRC setting out the department's understanding of which manufacturers paid bonuses, and whether VAT was accounted for them, over the period from 1973 to 1997.

The company had argued that the Elida table was not exhaustive, and further overpayments had been made. Inferences should be drawn from the table: in periods for which there was no entry, it was probable that the company would have followed the same practice as it did in other periods (and would have accounted for VAT on bonuses); for manufacturers not covered by the table, it was also probable that the company would have accounted for VAT in the same way.

The FTT heard from an industry specialist within HMRC, and considered that he had direct knowledge of the practices in the motor business and of HMRC's treatment of them during the periods in question. It appeared that the manufacturers were not consistent in their application of the VAT treatment, either across the industry or even within the same manufacturer in different periods. The FTT accepted that this meant it was not possible to draw the inferences that the company argued for.

The company's representative acknowledged that the appeal depended on overturning findings of fact. He suggested that this was one of the rare occasions when the appellate Tribunal should consider that the findings of the First Tier were at odds with the only tenable conclusion that could be based on the evidence.

The UT noted that the Supreme Court's judgment in *Pendragon plc* was issued the day after the hearing in this case. As that included comments on the correct approach of the UT in considering a FTT decision, the UT asked for written submissions from the parties. In the event, these did not change the traditional principle: as there were no issues of primary fact in *Pendragon*, the case was not strictly relevant. It was still necessary for the company to succeed on the basis of *Edwards v Bairstow*: a finding of fact would only be an error of law if "no person acting judicially and properly instructed as to the relevant law could have come to the determination under appeal".

The taxpayer sought to rely on "the presumption of continuity" as set out in the case of *Jonas v Bamford*. The FTT had rejected this as not establishing a legal principle – it was not bound to conclude that

something that had happened in one year had happened in any other year. It preferred the evidence of HMRC's specialist that the industry had not been consistent.

The UT came to the same conclusion as the FTT: the fact that HMRC had accepted some claims did not in itself validate the others. The company had failed to discharge the burden of proof, and the appeal was dismissed again.

Upper Tribunal: *Why Pay More For Cars Ltd v HMRC*

6.5 Timing issues

Nothing to report.

6.6 Records

6.6.1 Updated Notice

HMRC have issued a revised (July 2015) edition of their Notice *How to correct VAT errors and make adjustments or claims*. The only change appears to be to the telephone number for contacting HMRC.

VAT Notice 700/45

6.7 Assessments

6.7.1 Out of time?

Assessments for periods 06/09 and 07/09 were raised on 26 October 2012. The trader argued that they were out of time under s.73(6)(b) VATA 1994, because – according to the company – HMRC had all the information required to make the assessment for more than a year before that date.

The assessment related to input tax on carbon credits, that were being refused on *Kittel* grounds. The officer had asked for certain due diligence information to be provided; this was received by her on 28 October 2011. She said that she could not make the assessment to best judgement before examining that material; the taxpayer argued that she could have raised an assessment before that, and it could then have been the subject of revision based on the extra information.

The Tribunal considered a number of precedents, and noted from *Pegasus Birds* that "that the tribunal must determine when the assessing officer received the last piece of evidence which in the officer's opinion was of sufficient weight to justify the making of the assessment. Therefore, if the further investigations produce nothing of material significance the result must be that the last such piece of evidence was received before the

officer asked for the further information... It is also clear, and this was common ground, that the focus of the tribunal's enquiry is on the assessment that the officer actually made, not one that could have been made."

The issues for the Tribunal were therefore twofold:

- whether the officer held the opinion that the last piece of evidence of sufficient weight to justify the assessment was all or any of the due diligence material she received on 28 October 2011; and
- if so, whether her opinion was perverse or wholly unreasonable.

After reviewing the history of the investigation that led to the assessment and hearing evidence from the officer, the Tribunal was satisfied that she did hold that opinion. It was not necessary to consider the question of whether there was a connection to fraud – that was for a substantive hearing – but it was necessary to consider whether the officer had a reasonable belief that she had not established such a connection before receiving the material in October 2011. The judge was satisfied that this was the case: part of the material related to the possibility of a change in the company's due diligence procedures after warnings were given by HMRC in July 2009. Such a change might have indicated that the company was serious about fraud prevention, rather than merely carrying out window-dressing. The information obtained in October 2011 enabled the officer to draw a conclusion on that point, and it was not unreasonable of her to regard the information as critical to that conclusion. The assessments were therefore not raised out of time.

First-Tier Tribunal (TC04550): *Carbondesk Group plc*

6.7.2 Best judgement

In an article in *Taxation*, Neil Warren considers the issue of "best judgement" in the context of the *Matthew Hodges* case (TC04419), in which HMRC had concluded that a one-man scaffolding business had understated his sales by £4m over a four year period. The article considers the case law precedent (*Pegasus Birds*) and HMRC internal guidance on how best judgement is to be exercised. In particular, VAEC1460 suggests that an officer should have at least two pieces of evidence to support the view that a trader is suppressing takings. The officer in *Hodges* only had one – a "street sweep" identifying the business's boards on residential jobs that were not recorded in the books. The Tribunal agreed with the taxpayer's representative that the numbers were not credible, and reduced the liability from £529,536 to £11,153 (with related penalties).

Taxation, 9 July 2015

6.8 Penalties and appeals

6.8.1 Default surcharge

The Upper Tribunal has considered the second surcharge (after *Enersys*) to have been held by the FTT to be "disproportionate". The FTT (Dr Khan) applied the Upper Tribunal's judgment in *Total Technology* and concluded that a penalty of £70,909 levied at 2% (for being one day late with the balancing payment for its 01/08 VAT quarter) on a net VAT payment of £3,545,324 was comparable to the £131,000 at 5% for Enersys Ltd's similar delay. The surcharge liability notice had been issued for a similar 1 day delay in making the balancing payment for the quarter to 06/07. These were the first such failures in Trinity Mirror's registration history, which dated back to 1986. The surcharge was originally higher, but reduced following a voluntary disclosure of an overpayment; and it was initially paid, but appealed following the *Enersys* decision.

The judge disagreed with HMRC's assertion that a finding in favour of the taxpayer would "make the surcharge system itself disproportionate". The judge also rejected an assertion by HMRC that they consider proportionality before imposing surcharges (and therefore make a decision which is in their power and cannot be overturned by the Tribunal); this appeared to be based on the waiver of £400 penalties at the 2% and 5% rates, which the judge considered was more to do with administrative convenience than any consideration of proportionality. There was no evidence that proportionality had been considered in relation to this particular penalty.

HMRC appealed to the Upper Tribunal, where the case came before Mrs Justice Rose and Judge Berner. They referred back to the *Enersys* and *Total Technology* decisions, noting an ECHR decision cited by Judge Bishopp in *Enersys* in which a fixed (but high) penalty was held to be "compatible with the principle of proportionality only in so far as it is made necessary by overriding requirements of enforcement and prevention, when the gravity of the offence is taken into account".

HMRC's appeal was based on the principal argument that there were a number of errors of law in the FTT decision, so the UT should set it aside and come to a new decision on the question of proportionality. There were six further grounds attacking some of the details of the decision.

The company's counsel argued that a number of the points at issue related to questions of fact, but the UT disagreed. There was little dispute about the facts, nor about the inferences to be drawn from the facts – the argument was about the legal test applied by the FTT in assessing the seriousness of the default, and whether the surcharge was disproportionate. These were questions of law.

The UT rejected the comparative arithmetical exercise carried out by the FTT – the decision that "£52,400 at 2% was equivalent to the 5% penalty of £131,000 in *Enersys*". This was too simplistic: there were a number of factors to be taken into account in deciding whether the penalty was appropriate. It was therefore an error of law.

Reliance on a passage in the *Total Technology* decision which referred to a flat rate penalty of £50,000 for a third default (or second within a surcharge period) as disproportionate was also based on a

misunderstanding. The UT had meant that a system that imposed such a flat rate penalty would be disproportionate, because it would plainly be inappropriate in a great number of cases; however, the DS system did not do so, because it related the penalty to the amount of VAT unpaid.

The UT also rejected an argument by HMRC that the absence of any reasonable excuse was relevant. If there had been a reasonable excuse, there would have been no reason to discuss proportionality. Absence of a reasonable excuse could not rule out a disproportionality defence.

Having decided that the FTT had erred in law, the UT went on to remake the decision, without considering HMRC's other detailed objections. The judge stated that: "The correct approach is to determine whether the penalty goes beyond what is strictly necessary for the objectives pursued by the default surcharge regime, as discussed in detail in *Total Technology* and whether the penalty is so disproportionate to the gravity of the infringement that it becomes an obstacle to the achievement of the underlying aim of the directive which, in this context, we have identified as that of fiscal neutrality. To those tests we would add that derived from *Roth* in the context of a challenge under the Convention to certain penalties, namely 'is the scheme not merely harsh but plainly unfair, so that, however effectively that unfairness may assist in achieving the social goal, it simply cannot be permitted?'"

The DS system as a whole was logical and sensible, but it could in exceptional cases produce an unfair result. The absence of a maximum limit was a problem, but judges should not attempt to set a level for what was acceptable – that would effectively become legislation. The judge declined to endorse a suggestion put forward by HMRC that the "spike" in VAT liability that led to the very high surcharge in *Enersys* was particularly relevant.

The eventual decision is quite brief: there were no exceptional circumstances in relation to the late paid liability; it was a modest percentage of the unpaid VAT; the company had paid late before, and had received a warning. The penalty was not disproportionate either in relation to the gravity of the offence nor to achieving the underlying aims of the Directive. The penalty might be considered harsh, but in the view of the judges it could not be regarded as plainly unfair.

HMRC's appeal was allowed.

Upper Tribunal: *HMRC v Trinity Mirror plc*

A company appealed against a 15% surcharge of £3,074 for the 11/13 period. The company had been in the surcharge regime since 11/08. The director had returned to work from the Christmas holiday on 8 January, realised that the VAT payment was due, and immediately made that payment. She argued that the penalty was unfair for being only a day late. The Tribunal noted that there had been 19 failures to pay VAT on time in the preceding 5 years, and did not regard the penalty as wholly disproportionate or plainly unfair. The appeal was dismissed.

First-Tier Tribunal (TC04506): *Euroguard Technical Services Ltd*

A company appealed against a 15% surcharge of £1,475 for its 03/13 period. The company had been in the surcharge regime since 12/07, with 12 defaults in that time giving rise to surcharge liability notices. The

director did not appear at the hearing, but in correspondence argued that the penalty was unfair when the payment was only a day late and the delay had probably been caused by the bank holiday. The Tribunal considered that the company had adequate warning that it needed to give instructions in proper time for the payment to be made, and dismissed the appeal.

First-Tier Tribunal (TC04527): *Cashmores Trade Supplies Ltd*

A company appealed against five surcharges for successive periods from 04/13 to 04/14 totalling £6,874. The company had received a "help letter" in response to late payment for 04/12, but had entered the surcharge regime after a further late payment for 07/12. The payments for 10/12 and 01/13 were also late, but the 2% and 5% surcharges were below £400. The company's accountants offered three "excuses": the itinerant nature of the director's work making it hard to access the internet; the risk of fraud making the company unwilling to make online payments; and frequent but unspecified late payments by customers causing cash flow difficulties. The judge considered these points in detail, together with an argument about fairness, and could find no defence against the penalties. The appeals were dismissed.

First-Tier Tribunal (TC04528): *Mabo Consulting Ltd*

A company appealed against a 15% surcharge of £1,928 for its 11/13 period. The return had been made electronically on time, and the payment was a day late. The company argued that the VAT liability for the period was much higher than it had been for the previous 3 quarters, and a payment from a large customer that would have enabled it to make the payment on time had arrived late. This might have been a reasonable excuse under *Steptoe*, but the trader should have contacted HMRC before the due date to agree Time To Pay. Although the trader claimed to have attempted to contact HMRC on 3 and 6 January, there was no evidence to support this. The appeal was dismissed.

First-Tier Tribunal (TC04529): *Woodfield Technologies Ltd*

A company appealed against surcharges totalling £6,009 for the periods 07/13 and 10/13. It had been in the surcharge regime since 04/08, these being the 13th and 14th defaults. At the time of the appeal, it had left the surcharge regime. During the first six months of 2013, HMRC had failed to update its records to reflect the Appellant's change of address, and had erroneously treated the Appellant as a "missing company". As a result, during that period HMRC had blocked the Appellant's normal access to enable returns to be filed online. HMRC had then agreed to the company filing for a 9-month period to 07/13 on 9 October 2013; this, and the return for 10/13, was filed on time, but the VAT was paid several months late.

The company argued that HMRC had said that "no surcharge would be pursued in respect of the 9-month period". HMRC replied that this related to the late payment for the earlier parts of that period, but that no such assurance had been given in respect of the total VAT for the extended period. There were also arguments about the offset of a corporation tax repayment, insufficiency of funds and non-receipt of a letter pursuing the surcharges. The judge considered all these points but could not find any reasonable excuse. Once again, the company could have applied for TTP

at the appropriate time – it had done so in the past – but failed to do so. The appeal was dismissed.

First-Tier Tribunal (TC04553): *HKR Architectural Services Ltd*

A company appealed against surcharges totalling over £7,000 for the periods 04/13 and 08/13. The company had been in the surcharge regime since 02/09. These were the 5th and 6th defaults, charged at 15%. The excuse offered was a conversation in January 2011 between the company's tax agent and a visiting HMRC officer which gave the agent to understand that online filing meant that the trader could pay on the 10th. Presumably the officer had given this as a benefit of paying by direct debit; the agent had failed to appreciate the extra requirement.

The Tribunal considered the case of *Dental IT Ltd* (TC01002), in which an employee had misunderstood telephone advice obtained from HMRC and concluded that the employee had acted in accordance with the standards expected of a reasonable businessperson. HMRC argued that there was no record of any compliance check at the time the accountant said he received the advice, and argued that the earlier case could be distinguished because there was clear evidence of the conversation and the advice given.

The Tribunal did not accept that it had been reasonable for the agent to give advice that was incorrect on the basis of the passing conversation with an HMRC, so long after the event, without carrying out the basic check that would have shown that the extension only applied to direct debits. Although the Tribunal found as a fact that the visiting officer had given incomplete advice to the agent, sufficient to be misleading, it was not an excuse for defaults taking place over two years later. The appeal was dismissed.

First-Tier Tribunal (TC04561): *Whiston Motor Factors Ltd*

A trader defaulted in 04/13, 07/13 and 07/14. Surcharges at 2% (£717) and 5% (£1,843) were assessed for the second and third periods. The trader argued that:

- the late payment for 04/13 arose because of extended verification being carried out on a repayment claim in respect of the period 01/13, so that should not have given rise to a SLN;
- the late payment for 07/13 should have given rise to a SLN but no liability;
- there was a reasonable excuse for 07/14, so the SLN would lapse at that point. A Faster Payment request had been made to the bank on Friday 5 September at 16.04, but HMRC had not received the money until Monday 8 September.

There is a long discussion in the decision about "defaults material to the surcharge". The Tribunal concluded that it could consider the period 04/13 because it affected the subsequent surcharges, even if the issue of the SLN had not been appealed at the time.

There then follows a long discussion of what constitutes a "reasonable excuse" in law, citing at length the decision of Judge Brannan in *Coales v HMRC* (TC02514). This is a 2012 case about late payment of income tax, but the judge in the present case clearly considered it to contain a very

good analysis of precedent on the question of reasonable excuse. This leads to the short statement that "The excuse must be objectively reasonable and that test must be applied to the facts of the individual case".

The Tribunal concluded that the trader's decision to offset the disputed repayment claim for 01/13 against the amount due for 04/13 was not a reasonable excuse for that late payment, even though the repayment was subsequently agreed by HMRC to be due. Information requested by HMRC to validate the claim had not been provided by the time the liability for 04/13 fell due. Apart from that, the defence for 04/13 amounted to "insufficiency of funds", which could not constitute an excuse.

Confusion of the bookkeeper did not constitute a reasonable excuse for 07/13, so the surcharge for that period was confirmed. However, there was information on HMRC's website suggesting that "Faster Payments" would normally arrive on the same day or the next day, including bank holidays or weekends. This meant that the trader did have a reasonable excuse for the 07/14 period, and that part of the appeal was allowed.

First-Tier Tribunal (TC04567): *Fifields Mechanical and Electrical Services*

A company appealed against a 2% surcharge of £16,237 for its 10/14 period. It argued disproportionality (which could not succeed), and also reasonable excuses both for the period in question and for the 01/14 period which had triggered the SLN.

The appellant's qualified accountant prepared its VAT returns. On the due date for the 10/14 return, he suffered a number of difficulties at home, with carers failing to turn up to look after his elderly mother. The Tribunal considered that this went beyond simple "reliance on another" by the company: it had been reasonable to rely on the accountant, and the accountant had a reasonable excuse in the circumstances. There had been a back-up plan, but the difficulties had arisen unexpectedly and too late for the back-up to be implemented.

The late payment for 01/14 was said to be due to a group company awaiting a VAT repayment from HMRC. The Tribunal briefly commented that this could not be a reasonable excuse; however, because there was an excuse for the 10/14 period, the appeal was allowed.

First-Tier Tribunal (TC04577): *Morrisroe UK Ltd*

A company appealed against surcharges at 2% for the period 06/11 (£543) and 5% for 03/12 (£2,089). The director had filed the returns electronically and paid cheques into his local bank with a pre-printed HMRC credit slip; he believed that this would result in HMRC being credited the same day. In each case, the payment was credited to HMRC on the second working day following, a day late. The Tribunal accepted that this was an honest belief, but did not regard it as a reasonable one, nor a reasonable excuse. Information from HMRC advised traders to allow three working days for payment to clear. The appeal was dismissed.

First-Tier Tribunal (TC04585): *Visual Verification Ltd*

A company appealed against surcharges at 2% for the period 05/13 (£666) and 5% for 08/13 (£13,165). The director claimed that the surcharge

liability notices had never been received. The Tribunal considered the history of the company and found it suffered from poor filing systems: it was more likely that the letters had been received and not actioned, than that they had not been received. The company had failed to establish a reasonable excuse, and the appeal was dismissed.

First-Tier Tribunal (TC04591): *Iboardtouch Ltd*

A company was surcharged for 8 successive periods from 07/11 to 04/13. The total amount was £71,868. The company argued that it had a reasonable excuse derived from difficult economic circumstances, exceptionally bad weather over two winters, difficulties in obtaining credit, and delayed repayments of Construction Industry Scheme deductions due from HMRC.

The Tribunal dismissed the first three points. It noted that HMRC had a discretion to offset the CIS repayments against other liabilities, but was not required to do so. However, there appeared to be no reasonable explanation for the delays by HMRC. If offset had been made on the effective dates that the amounts were due to be credited, there would still have been defaults, but the outstanding VAT on which the surcharges would be based would be much less. The Tribunal decided that the surcharges should be recalculated on this basis, and allowed the appeal to that extent.

First-Tier Tribunal (TC04592): *UPR Services Ltd*

A company appealed against a surcharge of £10,713 for its period 12/14. The VAT was paid one day late. A Faster Payments instruction had been given on Saturday 7 February 2015, but the money had not been credited to HMRC’s bank account until Sunday 8 February. The Tribunal concluded that the directors had taken the “high risk” approach of leaving payment until the last possible moment; if they had asked the bank at the time, it would have told them that payments instructed after 23.55pm on a Friday could not be guaranteed to arrive until the following Monday. The appeal was dismissed.

First-Tier Tribunal (TC04593): *Robert W Brownlie Motors Engineers Ltd*

A company appealed against surcharges and notices for 13 of the 14 periods from 04/11 to 07/14. Surcharges totalling over £64,000 had been charged. The company always filed its returns promptly, but was always late making the payment. During the preliminaries of the dispute, HMRC had removed some surcharges for earlier periods because there had been a Time to Pay agreement in force, and had as a result reduced the percentages applying to some of the periods still at issue.

The company argued that the effects of the recession were a reasonable excuse, following the decision of the Tribunal in *Scrimsign*. This Tribunal examined the management of funds in some detail and concluded that the circumstances were different. The company had taken the decision not to pay the VAT, knowing that the consequences would be a penalty. The unfairness of the penalty could not be sustained as a defence following *Total Technology*. The appeal was dismissed.

First-Tier Tribunal (TC04602): *TFD (Scotland) Ltd*

A firm appealed against surcharges for four periods totalling £2,051. The first was charged at 10% and the remainder at 15%; the trader had

received a help letter and two surcharges below the £400 level, so the 10% penalty was the first actually to be charged.

Some confusion had arisen because of a difference between the trader's accounting date and the VAT return periods. In the fourth of the periods under appeal, he had filed a one-month return to bring the dates into line. The trader also suffered from General Anxiety Disorder, which takes six months to diagnose; HMRC accepted that this provided a reasonable excuse for the third and fourth periods, but the delay in the first two had arisen simply because of error over the due dates, not illness.

The Tribunal agreed with HMRC. There was insufficient evidence, in a diagnosis made in March 2014, that there had been a reasonable excuse in 04/13 and 07/13. The appeal was formally allowed for 10/13 and 11/13, and dismissed for the first two periods.

First-Tier Tribunal (TC04605): *Talentmap HR*

A company appealed against a 2% surcharge of £8,043 for its 01/15 period. The only person able to prepare VAT returns fell ill and was absent from work on the Monday and Tuesday of the week in which the due date fell. He prepared the return in the evening of Thursday 5 March. The problem was that the VAT due was in excess of £100,000, and the company's usual modes of making electronic payments were capped at that level. The director believed that he could order a same-day transfer by 4.30pm on the Friday; however, this only applied to transfers to other HSBC accounts. For a transfer to another bank (as used by HMRC), the deadline was 3.30. The director who was required to countersign the transfer had to attend various business meetings, but returned to the office in time to authorise the payment at 4.28pm – unaware that this was in any case too late.

The Tribunal was satisfied that the combination of the first director's illness, the second director's business meetings and the honest but mistaken belief that the deadline was 4.30, constituted a reasonable excuse in all the circumstances. The appeal was allowed. A separate appeal on the grounds of disproportionality was rejected.

First-Tier Tribunal (TC04611): *Intrinsys Ltd*

A company sold beds online. It was advised by its accountant on 27 February 2015 that payment for the January quarter was not due until 12 March. Payment of the £92,228 VAT liability was made by two Faster Payments on 11 and 12 March. This triggered a 10% surcharge.

The Tribunal noted that "*the appellant had a bona fide reason to trust its accountant's statement that the VAT liability for the period 01/15 was not due until 12 March 2105, notwithstanding the fact that the appellant had been in business for two years by then and that its directors had had business experience for much longer than two years through their involvement in Joseph International prior to April 2013.*" That reliance might be "not unreasonable". However, it was subject to the statutory exclusion in s.71 VATA 1994, and could not be a reasonable excuse. The judge also commented "*If in this instance, the reliance on the accountant's advice has proved to be misplaced, and has resulted in financial harm in the form of a default surcharge imposed on the appellant, that is a matter between the appellant and its accountant, with remedy to be sought in contract or in tort. It is not equitable to request*

the public purse to provide the remedy by waiving the default surcharge that has been correctly imposed in accordance with the legislation."

A defence based on proportionality was also dismissed.

First-Tier Tribunal (TC04624): *Express Beds Ltd*

A firm appealed against a 15% surcharge of £5,042 on the grounds that it was only a day late. The history of the VAT returns showed that it had been 188 days late with its first default; 11 days late with its second, with a 2% surcharge below £400; 52 days late with the third, subject to TTP; 30 days late with the fourth, paying a 5% surcharge of £682; and 8 days late with the fifth, paying a 10% surcharge of £2,650. The business had negotiated TTP for some of the intervening periods as well.

HMRC had refused a further request for TTP because the appellant was paid in full at the point of sale, and funds had been deployed to buy stock and pay other debts. There was nothing exceptional about its cash flow difficulties that might make them into a reasonable excuse. Proportionality was also rejected as a defence. The appeal was dismissed.

First-Tier Tribunal (TC04623): *Affordable Cars*

A company appealed against a 10% surcharge of £12,800 for its period 12/14. It had last defaulted in 12/13, so if it had paid on time for 12/14, it would have left the surcharge system. The company appealed, claiming that it had not received the surcharge liability extension notice in relation to the 12/13 default, so the 12/14 period fell outside the surcharge period that had been notified to it.

This could not succeed: it had paid the surcharge for the 12/13 period, and the SLN extension is sent out with the demand for the surcharge. The Tribunal concluded that it must have received the notice.

The company also tried to blame a banking delay. The payment was made by CHAPS on the next working day after the due date. The company's director did not attend the hearing and the reasons given in correspondence were vague: it was not clear whether the deadline for initiating the transfer had been missed by the company. The director provided evidence for the preceding three timely transfers, but did not provide any evidence for the one that was late. The Tribunal concluded that there was no evidence that the company had given its instructions in time.

A further ground of appeal based on disproportionality had to be dismissed as well.

First-Tier Tribunal (TC04630): *V Group International Ltd*

6.8.2 Error penalties

A couple appealed against a penalty levied for misdeclaration in a DIY claim. HMRC's representative noted that there has been a recent policy decision to charge such penalties, resulting in one previous case (*Palau*) and this one. She suggested that HMRC officers would appreciate guidance from the Tribunal in relation to penalties in connection with this kind of claim, so the judge raised more points and issued a longer decision than might otherwise have been the case (particularly as the appellant did not attend and was not represented at the hearing).

The couple had carried out a DIY project on a building they claimed had been unoccupied for 10 years. However, it was difficult for them to prove this: because they had lived in a static caravan next to the property while it was being renovated, they appeared on the electoral roll at that address. HMRC did not accept photographic evidence of the state of the property as sufficient to show compliance with the 10-year rule. The couple decided that they could not provide the evidence required, so they withdrew the claim. HMRC then issued a penalty based on "careless behaviour" with the maximum mitigation for a prompted disclosure.

The claimants appealed against the penalty, arguing that:

(1) The claim was genuine and was only unsuccessful due to a failure to produce supporting evidence which was acceptable to HMRC.

(2) They abandoned the house as it was uninhabitable many years ago and never thought they would be required to prove this at a later date.

(3) They took reasonable care with the claim and provided all information. There was no intention to mislead.

(4) They could have reclaimed a proportion of the VAT in their farming business but were now out of date, and so HMRC would benefit financially.

(5) HMRC admitted the first penalty assessment was technically deficient. That was also careless, but has no consequence for HMRC, whereas the appellants have to pay a substantial penalty for their inability to prove non-habitation.

(6) The couple also offered some "exceptional circumstances" in relation to being unable to prove non-habitation (the fact that they lived in a caravan on the site).

The Tribunal went through the technical grounds for issuing a penalty in detail. The judge considered that HMRC's basis for an "inaccuracy" penalty was flawed: the failure to provide evidence acceptable to HMRC was not an "inaccuracy in a document". The precise logic of this is set out in detail in the decision, which notes that the appellants may find it long and tedious – so the judge starts by stating that he has found in their favour.

The judge also applied the same logic as in *Palau*: the form did not lead to any potential lost revenue. It enabled HMRC to question whether the claim was valid, and led to the claim being rejected. That did not fit the description in Sch.24 FA 2007.

Other details of the assessment were considered in the context of DIY claims and penalties – whether there had been a "disclosure", prompted or otherwise; the measurement of "potential lost revenue"; what the "tax period" was for the purpose of measuring PLR and raising an assessment; the time limits for assessment; exceptional circumstances in which HMRC might apply greater reductions to penalties than their standard maximum mitigations; grounds for suspension. All of these matters will presumably be considered in some detail by HMRC in reviewing their policy.

In conclusion, the judge comments that this case should never have reached the Tribunal. HMRC are entitled to police the DIY claims system and penalise fraudulent claims; however, it is difficult to see how such

penalties can be justified for "carelessness" where "to succeed in a claim requires navigating through a complex piece of legislation and a none too simple form and notes." HMRC's attempt to describe the inaccuracy was not sufficiently coherent to justify the penalty, and the appeal was upheld.

First-Tier Tribunal (TC04589): *M M & D A Howells*

A similar dispute arose in relation to a claim for £20,718, of which £9,106 was disallowed on the grounds that the goods had been supplied as part of a building service which should have been zero-rated. The claimant needed to recover the overcharged VAT from the supplier.

The claim had been prepared by the claimant's tax advisers. They wrote to HMRC to apologise for the incorrect claim, explaining that it had not been properly reviewed before submission because of staff holidays. HMRC issued a 15% penalty to the claimant, and refused to suspend it. The fact that the claimant was a director of a construction company led the reviewing officer to conclude that he ought to have questioned the claim.

In common with other cases on DIY claims, the Tribunal considered that the actions of the taxpayer did not constitute carelessness. In this case, it was the fact that he put the matter in the hands of his accountants that was held to be the action of a reasonable taxpayer. Although he was involved in the construction industry, his knowledge could not be expected to extend to DIY claims. His reliance on his advisers was reasonable. The penalty was cancelled.

First-Tier Tribunal (TC04628): *Simon Coates*

Following an investigation, HMRC assessed a trader to underdeclared VAT of £102,950 for periods from 1 February 2006 to 30 November 2010 and a dishonest evasion penalty of £67,565 for periods from 1 February 2006 to 28 February 2009. The trader appealed. After lengthy consideration of the evidence and some complaints of illegal practices by HMRC, the judge concluded that the assessments and penalty were all justified. The only question was whether they had been issued in time. Although a 20 year time limit applies to VAT losses arising from dishonesty (s.77(4A) VATA 1994), there is still an overriding time limit of "one year from evidence of facts sufficient to justify the making of the assessment". There was a possibility that this time limit had been exceeded. The parties were invited to make submissions on the issue.

First-Tier Tribunal (TC04536): *Shahzada Rasul*

A company was charged a misdeclaration penalty under s.63 VATA 1994 in respect of denied claims to input tax on missing trader grounds in its periods 03/06, 04/06 and 05/06. The penalty exceeded £3.2m. It also appealed against the refusal of a much smaller amount of input tax unconnected to the penalty.

The company had been denied input tax of £25m. Its appeal against that decision was struck out in 2012 because the company had failed to comply with directions of the Tribunal to produce evidence by a specified date. Applications to have that appeal reinstated were also refused.

Judge Mosedale commented that most of the particularised grounds of appeal against the penalty, filed in 16 pages the day before the hearing, amounted to no more than an attempt to relitigate the issues that would

have been considered at the MTIC hearing. As that liability was final, it was not possible to argue the points again.

There were four grounds that related solely to the penalty:

(1) The assessment was void because it gave the wrong company registration number for the appellant company;

(2) The assessment is out of time;

(3) The assessment is in the wrong amount;

(4) Even if the appellant ought to have known of fraud in its supply chain, HMRC were in breach of its public law duty to protect traders from such fraud and that amounts to a reasonable excuse.

HMRC argued that the appeal should be struck out for having no reasonable prospect of success, and for being an abuse of process. Judge Mosedale considered that the doctrine of "issue estoppels" did not apply to a VAT case – the fact that the question of connection to fraud had effectively been settled by determination of the MTIC appeal did not mean that the doctrine of res judicata prohibited the same question being raised in a different context. However, she did regard the attempt to reopen the question as an abuse of process. The trader's attempt to establish "special circumstances" did not succeed.

The new questions included whether a lack of actual knowledge of the connection to fraud could be a reasonable excuse for the misdeclaration – that is, the input tax could be denied under the "ought to have known" test, but there would be a different standard for assessing the penalty. Judge Mosedale analysed this as a distinction between an objective test for reasonable excuse (in which case the taxpayer would have to lose) and a subjective test (where an honest failure to ask the right questions could succeed). The judge noted that a 2013 FTT decision, under appeal to the UT, has held that the test is subjective – that a mistaken honest belief could be a reasonable excuse. She found this surprising, and did not agree with the application of the principle (if the UT upheld it) to the context of s.63. The test was not merely whether the taxpayer had acted honestly, but whether he had acted reasonably. She did not think he had a reasonable prospect of persuading a Tribunal of that.

The judge dismissed each of the trader's stated grounds of appeal. She then raised one of her own: that the penalty might be disproportionate. The unrepresented taxpayer had stated that the penalty was "very large"; Judge Mosedale considered that this might be turned into a viable argument that the penalty breached the principles of fairness. She mentioned *Enersys*, *Total Technology* and *Trinity Mirror*, all of which are cases on default surcharge rather than misdeclaration.

In conclusion, she directed that the trader should be allowed to appeal against the penalty on the limited grounds that it was disproportionate, but should not be allowed to abuse the litigation process by arguing again that there was no fraud or that he did not have actual knowledge of such a fraud.

First-Tier Tribunal (TC04587): *Foneshops Ltd*

6.8.3 Other penalties

The FTT published a full decision in a case about information notice penalties "in order to make known our views on one particular line of technical argument put forward by the appellant". The trader operated in the telecoms field and was therefore identified as at risk of involvement in MTIC fraud. An officer informally asked for some information on 28 April 2014 for risk assessment purposes. There was no reply, so after unsuccessful attempts to follow up the enquiry, the officer issued an information notice under FA 2008 Sch.36 para.1 on 21 May 2014.

There followed some correspondence between the trader and the officer about whether the Act required the information to be posted or e-mailed, or simply "provided for inspection at an agreed or reasonable place". The trader disputed the validity of the notice, referring to the HMRC Compliance Handbook at CH23260 which included the statement "The person does not have to send the document to you."

Further correspondence followed in which it continued to be difficult for the trader to provide the information requested. Eventually the officer issued a penalty notice for £300 on 21 July. The trader appealed, arguing first that the notice had been invalid, and second that the information had been made available at the accountant's office on 17 June but HMRC had failed to take advantage of that. The trader argued that he had complied with the notice. He also offered several "reasonable excuses", in case the Tribunal found that the notice was valid and he had not complied with it.

The FTT did not agree that the notice was invalid. It was open to HMRC to require mailing or e-mailing of documents; production for inspection was an alternative if the quantity of documents made sending them impractical. The FTT was also satisfied that a requirement to produce the original documents was "reasonably required" – simply asking for the names of counterparties would have been more convenient for the trader, but would not have served HMRC's purpose as well.

The Tribunal was satisfied that the trader had not complied with the notice, even allowing for the possibility that HMRC had informally allowed extensions of time. The excuses offered were likewise dismissed, even though the delay resulting was relatively short. The penalty assessment was upheld.

First-Tier Tribunal (TC04512): *Telng Ltd*

A trader was charged a penalty for failing to file an EC Sales List. The trader had been filing ECSLs for some time when the 12/12 list was missed. HMRC sent a warning letter, stating that further failures would lead to automatic penalties. The trader filed the return and was not charged a penalty. The return for the 03/13 period was also late (filed on 12 May), but HMRC charged no penalty, apparently allowing a period of grace.

No ECSL was filed for 06/13, but HMRC did not issue a penalty notice until 28 February 2014, when the amount was set at the maximum of 100 days at £5. It also failed to file for 09/13; the penalty notice for that period was also the maximum of £1,000. The 100-day period for 09/13 expired about a month before the issue of the penalty notice for 06/13. The review decisions for both these penalties referred also to non-filing or late filing for 12/13 and 03/14.

The trader claimed that he believed he must have sent in the ECSLs, as he always had done so at the same time as filing VAT returns. However, he could not produce any positive evidence, or even any positive recollection: he simply thought the forms would have turned up on his desk if he had not sent them in. The Tribunal could not find that, on the balance of probabilities, he had submitted the forms.

As there was no reasonable excuse, the appeal had to be dismissed. However, the Tribunal considered that it was important for HMRC immediately to address the issue of delaying sending out penalty notices until long after the failure to file. This had been criticised in the past in relation to late filing of PAYE returns; where a daily penalty was being charged, it amounted to unfairness. It was also harder for the trader to produce evidence of posting if there was no indication of non-receipt for seven months. The Tribunal urged HMRC to consider these points that had been "very fairly and sensibly advanced by the appellant".

First-Tier Tribunal (TC04511): *La Perle Blanche*

6.8.4 Appeal out of time

A trader sought to appeal against a number of assessments for periods in 2003 and 2004. The assessments were raised in 2006, and amended last in May 2008. The notice of appeal was received by the Tribunal on 17 February 2014. The Tribunal examined the history of the dispute. The trader's main ground for being allowed to appeal out of time was that he had believed that the matter was settled, and it was unfair not to allow him to dispute the liability now that he realised that it was not. The Tribunal agreed with HMRC that the trader and his representatives had been given a number of opportunities to appeal earlier in the process, and had missed them all. The balance of finality in the system required that the application to appeal 6 years out of time should be refused.

First-Tier Tribunal (TC04507): *Graham Dovey t/a The Goat*

A golf club made a "*Bridport*" claim on 10 March 2009, covering temporary green fees from 1974 to 31 December 2008 (split into four different claims). HMRC rejected the claim on 29 April 2009. The club did not appeal within the 30 day time limit for doing so – it only formally appealed on 10 March 2014. The club appealed out of time, claiming that it had misunderstood the process, and also had not received the rejection letter. HMRC applied for the appeal to be struck out.

The Tribunal reviewed the history of the dispute, which was confused by the existence of a separate rejected claim in respect of members' green fees, also under appeal. A VAT adviser was handling the club's claim along with those of about 20 other clubs: he argued that he was well aware of the procedure and, had he received notification of rejection, he would have submitted a standard letter appealing against it. In his view, HMRC were attempting to avoid repaying VAT that was legally due.

The FTT found as a fact that the rejection letter was sent to the club, but was not copied either to the VAT adviser or to the club's auditors. As an e-mail from the auditors to HMRC in August 2010 referred to the rejection of the claim, the letter must have been shown to the auditors by the club. A further letter was sent by HMRC to the club at this time; once again, it was not copied to the VAT adviser, but the FTT considered that it

was at that point the responsibility of the club and its auditors to make sure that it had understood the position properly. No action was taken for another three and a half years. Similarly, the VAT adviser should have been on notice that the claim might have been rejected, and should have investigated. It was not sufficient for the adviser to say that having not received a rejection letter, he assumed that this claim had been accepted, given the amount of the reclaims and their significance to the Appellant.

The judge concluded that the statutory deadline for making the appeal should not be extended, so the appeal against the refusal of the green fees claim was struck out. The appeal concerning membership fees remains open.

First-Tier Tribunal (TC04564): *Royal Liverpool Golf Club*

6.8.5 Procedure

A number of motor traders had made appeals in relation to what were known as "Italian Uplift claims". In early 2013 they withdrew those appeals on advice from their advisers. In November 2014 and February 2015 they applied to reinstate the appeals, claiming that the advice had been wrong (after changing advisers).

The applications to reinstate were made outside the 28-day time limit set by Tribunal rule 17(3). The judge (Jonathan Cannan) had to decide whether to exercise his discretion to hear the application out of time, and then whether to exercise his discretion to reinstate the appeals.

The normal criteria for deciding whether a time limit should be extended were considered. The judge noted that he was required to carry out a balancing exercise between the various factors:

- The reasons for the delay, that is to say, whether there is a good reason for it.
- Whether HMRC would be prejudiced by reinstatement.
- Loss to the appellant if reinstatement were refused.
- The issue of legal certainty and whether extending time would be prejudicial to the interests of good administration.
- Consideration of the merits of the proposed appeal so far as they can conveniently and proportionately be ascertained."

The judge considered the history of the "Italian Uplift" dispute. In early 2013, it appeared that these traders were advised that the chances of success were low and the costs of continuing would outweigh the likely benefit. However, in 2014 it appeared that HMRC were accepting some such claims, and a lead case had been designated for hearing in the Tribunal.

The judge concluded that the appellants had withdrawn their appeals based on professional advice. There was no evidence that the advice had been wrong at the time or negligently given. A different conclusion had now been drawn, but that was not a good enough reason to reinstate the appeals. The result of the required balancing exercise was that the judge decided not to allow reinstatement.

First-Tier Tribunal (TC04581): *Rolls Group & Others*

HMRC applied for several appeals to be consolidated and heard together. They related respectively to assessments for output tax in 10/12 to 03/13 on the basis that certain supplies of metals to a Belgian customer should not have been zero-rated, and denial of input tax credit for periods from 03/13 to 02/14.

The company objected to the application, arguing that it would be prejudiced by the risk that evidence in one of the appeals might appear to strengthen HMRC's case in the other, it was their right to conduct their appeals in any way that seemed advantageous to them, and HMRC's actions had caused a considerable procedural delay.

Judge Berner considered the factors to be weighed in deciding whether to consolidate appeals, and concluded that there would be no prejudice to the taxpayer in admitting evidence from one appeal into the other. The consolidated appeal should be heard at the earliest possible opportunity in order to counteract the disadvantage to the taxpayer of the delay. HMRC's application was granted.

First-Tier Tribunal (TC04584): *C F Booth Ltd*

6.9 Other administration issues

6.9.1 Penalties consultations

HMRC have issued a first summary of responses to the consultation on penalties that commenced in February 2015. The "emerging conclusions" include the following:

... the ultimate goal for the future is to charge fewer penalties, and for penalties to be well-targeted where we do charge them and to take account of the customer's compliance history across all of the taxes they are involved with.

Time based failures to file tax returns or pay by particular dates relate to high frequency, mechanical obligations. They tend to produce large volumes of low-value penalties with a high incidence of successful appeals and they generate significant levels of contact between customers and HMRC. Reform of these penalties will be our first priority.

This is clearly relevant to default surcharge, where numerous respondents raised concerns. Possibilities under review include:

- not charging a penalty where no tax is due and where the circumstances for not charging are appropriate;
- not charging a penalty where the period of lateness is very short;
- not charging a penalty for the first default;
- taking account of the customer's compliance history across all of the taxes they are involved with;
- increasing opportunities for and use of mitigation in recognition of the circumstances surrounding the default and HMRC's desire to encourage future good compliance; and

- using notifications to remind the customer that their return is due (before the due date is reached) and draw their attention to the default and its consequences for penalty purposes (after the due date has passed).

Not all of these are relevant to default surcharge; some relate only to other taxes, e.g. income tax where a late filing penalty was only recently introduced even where there was no tax to pay. There is no default surcharge on a nil or repayment VAT return.

In relation to error penalties, "non-financial options" are under consideration, including increasing the compliance burdens on non-compliant taxpayers by reducing the time available to meet future obligations.

Further consultation on separate individual areas will follow soon.

www.gov.uk/government/consultations/hmrc-penalties-a-discussion-document

6.9.2 Other consultations

HMRC are consulting until 14 October 2015 on a package of measures intended to improve tax compliance among large businesses, i.e. those with turnover/balance sheet of more than £200 million/£2 billion. These measures includes: a requirement for all large businesses to publish their tax strategy; a voluntary "Code of Practice on Taxation for Large Business"; and a "special measures" regime to tackle persistent and aggressive avoiders.

www.gov.uk/government/consultations/improving-large-business-tax-compliance

HMRC are consulting until 8 October 2015 on a new criminal offence for corporations that fail to take adequate steps to prevent their agents from facilitating tax evasion in relation to all taxes, subject to a due diligence defence.

www.gov.uk/government/consultations/tackling-offshore-evasion

HMRC are consulting until 14 October 2015 on detailed proposals for new measures against serial avoiders, including further reporting requirements, surcharges and public naming; a new POTAS threshold condition for serial promoters; and specific penalties where the GAAR applies. These proposals take account of responses to the initial consultation held between January and March 2015.

www.gov.uk/government/consultations/strengthening-sanctions-for-tax-avoidance-a-consultation-on-detailed-proposals

HMRC consulted until 2 September 2015 on draft regulations setting out the information deposit-takers will have to provide, on receipt of either an information notice or hold notice, to enable HMRC to determine whether direct recovery of a tax debt from a taxpayer's bank account is appropriate, under new powers contained in Sch.8 Summer FB 2015.

www.gov.uk/government/publications/draft-legislation-the-enforcement-by-deduction-from-accounts-information-regulations-2015

6.9.3 HMRC annual report and accounts

HMRC's annual report and accounts for the year ended 31 March 2015 have been published. HMRC identify the following matters as highlights:

- £517.7 billion tax revenue brought in – a record, and £11.9 billion more than the preceding year;
- £26.6 billion raised in compliance revenues – also a record;
- costs reduced by £210 million;
- 10.2 million Self Assessment returns submitted by midnight on 31 January 2015;
- a national "conversation" with staff at 1,404 events across 78 locations;
- 1 million employers claimed the new Employment Allowance – 85% of all eligible employers.

On the other hand, performance in dealing with post and telephone calls declined – 70% of post was answered within 15 working days (83% the previous year) and only 73% of call attempts were "handled" (down from 79%).

www.gov.uk/government/publications/hmrc-annual-report-and-accounts-2014-to-2015

6.9.4 OECD report on tax administrations

The OECD has published its sixth comparative survey of the performance of tax administrations in advanced and emerging economies. Costa Rica, Croatia, Morocco and Thailand are included for the first time. The survey identifies key elements of tax administration systems such as staffing, digitisation, e-services, measurement of the "tax gap", and collection of tax debt, and provides a range of comparative tables.

Some of the information is difficult to compare because monetary amounts are shown in local currency. However, trends over time can be compared.

The survey states that improvements in collection performance can generally be attributed to a range of the following factors:

- Strong management information systems;
- Well-developed analytics tools to guide use of extensive enforcement powers;
- Extensive use of tax withholding at source arrangements;
- Wide use of electronic payment methods; and
- Significant investment in information technology.

http://www.oecd.org/ctp/administration/tax-administration-23077727.htm

6.9.5 Summer Finance Bill

The second Finance Bill of 2015 was published in July. It contained 50 clauses, 8 schedules and ran to 212 pages. One of the main provisions relevant to VAT is the "tax lock", which is a commitment to set a ceiling

for the standard and reduced rates of VAT, and not to remove any items from the zero rate of VAT and the reduced rate of VAT for the duration of this Parliament.

www.gov.uk/government/publications/summer-finance-bill-2015-legislation-and-explanatory-notes; Budget Report para.2.53; www.gov.uk/government/publications/tax-lock-income-tax-national-insurance-contributions-and-vat

6.9.6 Tax Assurance Commissioner

The report of the Tax Assurance Commissioner, Edward Troup, has been published. It is entitled “How we resolve Tax Disputes” and reviews compliance of the department with the Litigation and Settlements Strategy and its codes of practice. It notes that a significant development in the last year has been the introduction of Accelerated Payment Notices and Follower Notices, and the next year will see the introduction of Direct Recovery of Debts.

www.gov.uk/government/publications/how-we-resolve-tax-disputes-2014-to-2015

6.9.7 Time to pay arrangements

HMRC have announced that taxpayers agreeing Time To Pay from 3 August 2015 will be required to settle their agreed instalments by direct debit. They say they are moving to direct debit by default because:

- It is more cost effective and more secure than other payment methods;
- It removes the chance that the customer will forget to make payment;
- Payments are more likely to be correctly allocated;
- Reduces the need for subsequent customer contact, saving time for the customer and HMRC;
- The Direct Debit scheme includes a guarantee to protect the customer.

https://taxagents.blog.gov.uk/2015/07/14/time-to-pay-arrangements-mandatory-direct-debit/

6.9.8 Exploitation of duty free arrangements

During the summer a number of newspapers have criticised retailers for “exploiting” the duty free arrangements at airports: if an airside retailer asks for a passenger’s boarding pass, and records the fact that the traveller is bound for a destination outside the EU, no VAT needs to be charged. However, the price is not usually adjusted downwards in favour of the customer. Some MPs have joined in the criticism, but there is no indication that anything will be done to change the rules or to restrict the practice.

Daily Telegraph, 13 August 2015

6.9.9 Security

A company appealed against a notice to require deposit of security. Its owner and director had been involved in two previous businesses that became insolvent owing significant amounts to HMRC. As usual, part of its grounds of appeal related to the company's difficulty in meeting the requirement, which only tended to demonstrate that HMRC's concerns were reasonable. Other factors that might have been more relevant, such as improvements in the way the business was being managed, were not enough to outweigh the good reasons HMRC had for making the decision. The appeal was dismissed.

First-Tier Tribunal (TC04588): *Upstage Scenery Ltd*