VAT UPDATE
OCTOBER 2018

Covering material from July – September 2018

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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 which reports the progress of appeals originally said that it would be updated monthly, but it appears to be less frequent or regular than that. The list says "last updated 12 July 2018" after the previous update in February.

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

- *Fortyseven Park Street Ltd*: HMRC seeking leave to appeal against the UT decision that the company's supplies were exempt licences to occupy land not excluded as "similar to hotel accommodation".

- *Frank A Smart & Son Ltd v HMRC*: HMRC have applied to the Supreme Court for leave to appeal the CS decision in the taxpayer's favour on the deductibility of input tax on the cost of single farm payment entitlements. The CS refused leave to appeal; if the Supreme Court grants leave, HMRC will seek a reference to the CJEU.

- *Gala 1 Ltd v HMRC*: Court of Appeal due to hear taxpayer's appeal against refusal of claims for repayment of output tax on bingo – FTT/UT both ruled that only the representative member of the group could make the repayment claim (not on the HMRC list).

- *Hastings Insurance Services Ltd*: HMRC have applied for leave to appeal the FTT decision on place of establishment (and have hurried through counteracting legislation, covered in the current update).

- *Hotels4U.com Ltd*: HMRC's list states "no appeal lodged" – FTT decision mainly in favour of the taxpayer. A hearing is listed for November 2018 to decide whether to refer questions to the CJEU.
- *KE Entertainments Ltd*: HMRC have appealed to Court of Session against UT decision that change of calculation of bingo takings constituted an "adjustment of consideration" within reg.38, rather than leading to a time-capped repayment claim under s.80 (hearing listed for 25/26 September 2018).
- *LIFE Services Ltd*: partial win for HMRC in the Upper Tribunal; one point to be jointly decided in the Upper Tribunal with *The Learning Centre (Romford) Ltd* (hearing scheduled for December 2018).
- *Lowcostholidays and Lowcostbeds*: being heard with *Hotels4U.com Ltd* (CJEU reference to be considered in November 2018).
- *Metropolitan International Schools Ltd*: taxpayer is appealing to CA against UT decision that its supplies were compound supplies of taxable education rather than zero-rated printed matter (hearing date to be confirmed).
- *MG Rover Group Ltd*: taxpayer is appealing to CA against UT's ruling that its *Fleming* claim could not succeed as it should have been made by the representative member of the group (hearing listed for January 2019).
- *Pacific Computers Ltd*: MTIC case remitted by the UT to differently constituted FTT for rehearing (not on HMRC's list).
- *Praesto Consulting Ltd*: the UT overturned the FTT's decision in the taxpayer's favour about the deductibility of input tax on legal costs incurred in defending the shareholder/director from litigation. The company is appealing to the CA (hearing date to be confirmed).
- *Privin Corporation Ltd*: the FTT found in favour of a MTIC appellant. HMRC were granted leave to appeal to the UT, but it was agreed that the case would be remitted to a differently constituted FTT for rehearing (not on HMRC's list).
- *SAE Education Ltd*: company has been granted leave to appeal against CA's ruling that it did not qualify for exemption as a "college of a university" (Supreme Court hearing listed 30 October 2018).
- *Stoke by Nayland Golf and Leisure Ltd*: HMRC are appealing to the UT against the FTT's ruling that a members' club did not fall foul of anti-avoidance provisions and qualified for exemption (hearing date June 2018, decision awaited).
- *Tesco Freetime Ltd and Tesco plc*: HMRC are appealing to the UT against FTT finding in favour of taxpayer in relation to tax treatment of loyalty points scheme (hearing date to be confirmed, expected November 2018).
- *The Chancellor, Masters and Scholars of the University of Cambridge v HMRC*: CA has referred questions to CJEU on deductibility of investment management costs where an endowment fund supports the whole of the university's activities.

- *Volkswagen Financial Services (UK) Ltd v HMRC*: Supreme Court found for taxpayer on one issue but referred the main issue to the CJEU; A-G's opinion has been given, full court judgment awaited.

1.1.1 Decisions in this update

- *DPAS Ltd*: HMRC appealed points from FTT decision to Upper Tribunal, which decided to refer questions to CJEU after considering the judgments in *Bookit* and *NEC*; CJEU judgment effectively confirms HMRC's position.
- *Jigsaw Medical Services Ltd*: UT overturned FTT's decision in favour of taxpayer in case about whether provision of ambulances qualified for zero-rating as passenger transport – they were exempt.
- *Taylor Clark Leisure plc*: HMRC's appeal against the Court of Session's ruling that the company was entitled to a repayment based on a claim made by a former member of its VAT group registration succeeded in the Supreme Court.
- *Totel Ltd v HMRC*: Supreme Court refused taxpayer's appeal against the requirement to deposit the disputed VAT before an appeal can be entertained.

1.1.2 Other points on appeals

- *Dynamic People Ltd*: HMRC's list says that the appeal in TC05003/TC06345 (April 2018 update) concerning a special method "was allowed following a re-hearing – no further appeal so the decision is final".
- *Findmypast Ltd*: HMRC's list reports that the Supreme Court has refused HMRC leave to appeal against the CS ruling that "credits" did not trigger a tax point at the time they were purchased, so the decision is final.
- *Mercedes-Benz Financial Services Ltd*: HMRC list now reports that HMRC have withdrawn their appeal following the CJEU ruling on the interpretation of "in the normal course of events" in the context of hire purchase transactions.

2. OUTPUTS

2.1 Scope of VAT: linking supplies to consideration

Nothing to report.

2.2 Disbursements

Nothing to report.

2.3 Exemptions

2.3.1 Payment service not exempt

The CJEU has given its judgment in the *DPAS Ltd* case. It further restricts the scope of the exemption for payment processing services, but does not cast light (as was hoped) on the meaning of the expression "debt collection".

Background: UK Tribunals

A company operated a service whereby dental patients could spread the cost of dental treatment by making regular payments throughout the year. It collected money from patients and paid it over to the dentists, after deducting its own charges. HMRC regarded these as wholly taxable, relating either to "administration" or to "debt collection", in line with the *AXA (UK) plc* case (Case C-175/09). The company argued that it made separate supplies to the dentists (which would have to be taxable) and to the patients. The supply to the patients was exempt under the heading "payment services". HMRC further argued that, if the contracts were effective in creating a separate exempt supply to the patient, they constituted an abuse of rights.

The company had been registered for VAT from the commencement of its business in 1996. The proprietor realised in 2003 that its services were similar to those of *Sparekassernes Datacenter* (Case C-2/95), and he successfully applied to HMRC for deregistration at that time. Following the *AXA* judgment, HMRC ruled that the company should again be registered; however, as this was effectively a change of an agreed position, they would not pursue output tax arising before 1 January 2012 (a concession which was extended generally to businesses affected by *AXA*).

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

The documentation sent to dentists about the new arrangements explained that they arose from the consequences of the *AXA* judgment, and that they would make "no practical difference". It is therefore not surprising that

HMRC argued that they constituted an abuse of rights. However, the covering letter also claimed that the changes "reflect the nature of the reality of our services" – that, in fact, the company had always made payment service supplies to the patients, but these had not previously been recognised in the contracts.

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

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

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

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

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

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

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

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

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

HMRC appealed to the Upper Tribunal, challenging all five of the FTT's conclusions. First, HMRC's counsel argued that the FTT had been wrong to consider only the contractual arrangements after 1 January 2012. He relied on the *Debenhams* decision as authority for the proposition that the previous contractual arrangements were relevant and significant in interpreting the new contracts. The UT did not agree with this criticism.

The FTT had ruled that the old arrangements do not *necessarily* determine the new; the FTT had correctly taken the old arrangements into account as part of the context. The FTT judge had recognised, and had taken into account, that the purpose of the changes was to circumvent the CJEU ruling in *AXA*.

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

As regards those 30% of existing patients who signed the acceptance form, acknowledging the change of arrangements, the UT again agreed with the FTT that a new contract had been brought into existence. The position was less clear in respect of the other 70%, who were assumed to have consented by silence. The UT considered the competing arguments and concluded that it was not possible to infer a contract from the lack of a response. For those existing patients who did not sign a form, therefore, there was no supply between DPAS and the patient.

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

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

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

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

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

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

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

(3) the principle of fiscal neutrality which precludes treating similar goods and supplies of services, which are thus in competition with one another, differently for VAT purposes (see Joined Cases C-259/10 and C-260/10 *Rank Group plc v HMRC* at [32] – [36]).

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

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

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

The decision concluded by:

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

After the CJEU handed down its decisions in *NEC* and *Bookit*, DPAS and HMRC both made further submissions to the UT (Warren J and Judge Sinfield). The company argued that the CJEU in *AXA* had accepted that Denplan's services were within art.135(1)(d) and were only excluded from exemption because they were debt collection; as the FTT had decided as a fact that these services were not debt collection, these indistinguishable supplies must be exempt. HMRC responded that the services were covered by the same principles as the card processing services in *NEC* and *Bookit*.

The UT discussed the recent CJEU judgments and considered whether they determined the issues in the present case. The judges decided that

they did not: it was impossible to say for sure what the CJEU would decide on the key issues, both as regards debt collection and the scope of art.135(1)(d). They therefore decided to refer questions to the CJEU.

CJEU decision

The questions referred can be summarised briefly as follows:

- is this type of payment processing (calling for direct debits) within art.135(1)(d) at all, and therefore capable of being exempt?
- if it is, does it constitute debt collection if the debtor is paying for it?

DPAS placed reliance on the fact that its arrangements were effectively identical to those considered by the CJEU in *AXA*, the only difference of substance being that the debtor paid for them. The CJEU had not apparently even considered in that case that the services might fall outside art.135(1)(d). In the new decision, the court has ruled that these services do indeed fall outside art.135 and therefore cannot be exempt at all; the judges resolve the apparent inconsistency by commenting that the court had simply "focused its analysis on the question of whether that supply of services was covered by the concept of 'debt collection'". The court had not intended to broaden the scope of art.135(1)(d); it had simply found a different reason for the services to be taxable, and had therefore not considered the question.

The court described the difference between exempt services that fall within the provision and those that do not:

- a transfer or payment is a transaction consisting of the execution of an order for the transfer of a sum of money from one bank account to another. It is characterised in particular by the fact that it involves a change in the legal and financial situation existing, on the one hand, between the person giving the order and the recipient and, on the other, between those parties and their respective banks and, in some cases, between the banks. Moreover, the transaction which produces that change is solely the transfer of funds between accounts, irrespective of its cause.
- a transfer may be broken down into separate services, which then constitute 'transactions concerning transfers' within the meaning of that provision; the exemption provided for in that provision can, however, relate only to transactions which, viewed broadly, form a distinct whole, fulfilling in effect the specific, essential functions of such transfers, in so far as they have the effect of transferring funds and entail changes in the legal and financial situation resulting from that transfer. A transfer may be effected by an actual transfer of funds or by means of accounting entries.
- exempt services must also be distinguished from the supply of mere physical, technical or administrative services. To that end, it is relevant to examine, in particular, the extent of the liability of the supplier of the services in question and, inter alia, whether that liability is restricted to technical aspects or whether it extends to the specific, essential aspects characterising the transactions.

The fact that a service is "essential" for a transfer (as calling for the direct debits is) is not enough to make it exempt. The services in DPAS were

too similar to those in *Bookit* (Case C-607/14) and *NEC* (Case C-130/15), which the CJEU had held to be merely administrative (the transmission of information leading to a transfer, rather than effecting the transfer itself). The service was a step prior to the transfer, but was not itself covered by the exemption.

The court also noted that part of the purpose of the exemption for financial transactions is to deal with the difficulty in many cases involved in determining the taxable amount and any associated deductible VAT. There was no such difficulty in the present case, where there was a clearly identifiable payment for the service.

The answer to the first question referred was that the exemption did not apply to this type of service; in view of that answer, it was not necessary for the court to answer the second question about debt collection.

CJEU (Case C-5/17): *HMRC v DPAS Ltd*

2.3.2 Rank returns

The FTT has considered yet again the claim by The Rank Group in relation to supplies made using slot machines in the period 1 October 2002 to 5 December 2005. During that period, the UK law drew a distinction between exempt and taxable gaming machines based on definitions in the Gaming Act 1968. "Section 16/21" machines were exempt, and "section 31/34" machines were taxable. The claims were based on the assertion that the supplies were so similar that they must both be exempt, because different VAT treatment breached the principle of fiscal neutrality.

The case first went to the VAT Tribunal in 2008, with a further hearing in 2009 considering different questions in relation to fiscal neutrality. The 2008 hearing considered whether treating the machines differently for VAT breached the principle of fiscal neutrality, and the second considered in more detail whether the supplies made by the different type of machines were similar from the viewpoint of the typical consumer. The dispute was divided into two issues ("slots 1 and slots 2"). They were referred to the CJEU, which ruled on the application of fiscal neutrality in Cases C-259/10 and C-260/10. The "slots 2" appeal was remitted by the UT to the FTT for reconsideration, because the original decision contained errors of law; "slots 1" proceeded to the Supreme Court, which held in 2015 that supplies made using section 16/21 machines were taxable.

The FTT considered the precedent case law on fiscal neutrality, in particular the CJEU judgment in relation to *Rank* itself. The key paragraphs of that judgment cover the determination of whether supplies are sufficiently similar to engage the principle of fiscal neutrality:

43. In order to determine whether two supplies of services are similar within the meaning of the case-law cited in that paragraph, account must be taken of the point of view of a typical consumer … avoiding artificial distinctions based on insignificant differences …

44. Two supplies of services are therefore similar where they have similar characteristics and meet the same needs from the point of view of consumers, the test being whether their use is comparable, and where the

differences between them do not have a significant influence on the decision of the average consumer to use one such service or the other …

The CJEU also set out a number of factors that are irrelevant in considering whether two games of chance are similar for the purpose of the principle of fiscal neutrality. The factors that should not be taken into account are:

(1) the lawful or unlawful nature of the operation of a game of chance;

(2) the identity of the operators of the games and the legal form by means of which they exercise their activities;

(3) differences in the setting in which games of chance are made available and, in particular, accessibility in terms of location and opening times and atmosphere;

(4) differences in the application of other taxes;

(5) the legal regimes relating to control and regulation of the games; and

(6) differences in the details of the structure, the arrangements or the rules of games which fall within a single category of game, such as slot machines.

The UT had directed the FTT to consider again the evidence presented at the original hearing, rather than taking new evidence. Accordingly, the Tribunal examined the witness statements made by Rank employees and HMRC officers and other officials in 2009.

The Tribunal noted the error of law in the first decision: it had undertaken a comparison of the machines "at a high level of abstraction", which the CJEU disapproved. The FTT considered the elements identified by the CJEU as relevant, and came to the same decision as before – the differences between the machines were not liable to have a considerable or significant influence on the average consumer's decision to use one machine rather than another and all the machines met the same needs from the point of view of the typical customer. Accordingly, treating FOBTs, section 16/21 machines and section 31/34 machines differently for VAT purposes during the claim period breached the principle of fiscal neutrality. Rank's appeal was allowed.

First-Tier Tribunal (TC06607): *The Rank Group plc*

2.3.3 More gambling

Several appellants claimed exemption for supplies made through Fixed Odds Betting Terminals between 6 December 2005 and 31 January 2013. During this period, the provision of facilities for placing bets or playing games of chance was an exempt supply under item 1 Group 4 Sch.9 VATA 1994. In the same period, supplies made through FOBTs were subject to VAT at the standard rate because FOBTs were 'gaming machines' as defined by s.23 VATA 1994 and, as such, excluded from the exemption by Note (1)(d) to Group 4. Throughout the claim period, casino roulette, electronic roulette, online gaming, and over the counter bets on virtual games ('the comparator games') were exempt from VAT. The appellants accepted that the UK could lawfully limit the scope of the exemption of betting, lotteries and other forms of gambling but contended that was subject to the EU law principle of fiscal neutrality. The

appellants considered that the games supplied through FOBTs, which were taxable, were similar to the comparator games played in casinos and online which were exempt, and that the different treatment of the supplies for VAT purposes breached the principle of fiscal neutrality. Based on their view, the appellants made their claims for repayments of overpaid VAT. HMRC rejected the claims on the ground that the supplies were not sufficiently similar to engage the principle of fiscal neutrality. The appellants appealed to the FTT.

The amounts involved in the claims had not been agreed, and the FTT was asked to give a ruling in principle only. There were also other claims in relation to other types of machine that were much less significant (only 1% of the total value), which were left for separate consideration if required.

The same judges heard this appeal as *Rank* above. The section of the decision in which the principles of fiscal neutrality are considered is identical. In this case, HMRC submitted that the evidence showed that the average player of FOBT games was considerably influenced in their choice of whether to play a game on a FOBT or some other form of the game by the following differences between them:

(1) stakes and prizes;

(2) speed of play;

(3) return ratios (total prizes awarded as a percentage of total stakes);

(4) accessibility;

(5) the choice of events or games available;

(6) the ability of the player to influence the outcome of the game by their play; and

(7) the underlying nature of the game in question.

The Appellants contended that the following FOBT games and other games are comparable and similar for the purposes of the principle of fiscal neutrality:

(1) FOBT roulette and roulette played online, in a casino live at the table or electronically by reference to a live table or an automated table.

(2) FOBT slots (category B3) games and slots played online and on a "B3A" machine.

(3) FOBT virtual racing and virtual racing played over the counter in a licensed betting office or online.

(4) FOBT virtual card games, such as blackjack, and versions of the same card games played online.

(5) FOBT bingo and bingo played online and on a B3A machine.

(6) FOBT other games, such as Spoof, and versions of the same games played online and on a B3A machine

The FTT considered the evidence in each case and could find no material distinction between the different versions of the games. The appeals were allowed, apart from the category of "other games" where the appellants had provided limited evidence and no conclusion could be drawn in

relation to some of the category. The parties were left to discuss the amounts involved.

First-Tier Tribunal (TC06608): *Done Brothers (Cash Betting) Ltd and others*

2.3.4 Welfare

Four YMCAs (which are separate charities independently registered for VAT) appealed against HMRC decisions that they were making exempt supplies of welfare. They were in receipt of grants from government to support vulnerable people; they argued that they made two supplies, one to the local authority that delegated responsibility to them (VATable, enabling recovery of input tax) and one to the vulnerable people (for no consideration, funded by the grant). HMRC responded that the support services were made to the individuals for third party consideration from the local authority; that was the economic reality.

The judge considered:

- the nature of housing-related support (HRS) services;
- the identity of the recipient of the services;
- whether the services fell within "welfare";
- an argument about the reduced rate under Group 9 Sch.7A, which applies the reduced rate to "supplies of welfare advice or information by a charity".

The judge started with the contracts between the YMCAs and the local authorities. Some defined HRS services in detail; others had almost none (one referred to a definition in "schedule 1", but there was no schedule 1 in the document included in the bundle of evidence). The judge was able to make a number of findings of fact about the nature of HRS, which included a range of services provided on behalf of the local authorities. It was agreed that the YMCAs were not receiving a voluntary grant – they were receiving fees in return for providing the contracted services.

The appellants argued that the supplies could not fall within the exemption because the distressed person provided no consideration, and if the payments from the local authorities did constitute consideration, the local authority was not a distressed person. The judge did not agree that this was determinative. Both the EU and UK legislation only referred to the nature of the supply, not who paid for it or received it. According to the HL decision in *Redrow*, the YMCAs were supplying a service to the local authorities which was also for the benefit of the individuals. HMRC did not dispute that the local authorities would be entitled to reclaim any VAT charged under VATA 1994 s.33, but they disputed whether any VAT should be charged. The judge concluded that there was a supply of services for VAT purposes by YMCA to the local authority (regardless of the fact that the main beneficiaries of the HRS are the young residents), and the identity of the recipient does not affect whether the supply falls within Item 9.

The judge did not accept the YMCAs' arguments on the application of Item 9 Group 7. In his view, the recipients of the services were "distressed persons" by reason of actual or potential homelessness; the

services involved "instruction" in supporting them towards independent living; and the services were designed to promote their physical or mental welfare, taken in their context in line with the decision of Dr Avery Jones in *Watford & District Old People's Housing Association Ltd* (VTD 15,660). The local authorities determined that certain young people required supported housing and HRS. The HRS services might in a different context appear to be divorced from physical or mental welfare – for example, instructing someone how to hoover, or how to fill in a claim for housing benefit – but in the actual context of a distressed and vulnerable young person anxious to avoid repeat homelessness, the judge considered the HRS services were indeed designed to promote physical or mental welfare of the young recipient.

The judge noted the appellants' argument that HMRC's interpretation of "welfare" within Sch.9 appeared to leave nothing to be covered by "welfare advice or information" in Sch.7A. He disagreed: the reduced rate provisions specifically exclude "supplies of advice or information provided solely for the benefit of a particular individual or according to his personal circumstances" (Note 3(c)). There could be "advice or information" that is "provided solely for the benefit of a particular individual or according to his personal circumstances" but which does not amount to "instruction" in Item 9, and so does not constitute "welfare services" within Item 9.

There was also a question about the effect of the decisions. HMRC had indicated to three of the appellants in 2005 that HRS services were not exempt. They would therefore only apply the effect of the decisions (denying input tax deductions) from the date of the letters which communicated those decisions to the appellants. The fourth YMCA had not received any prior suggestion that its supplies might be taxable, so HMRC proposed to extend the effect of the decision back four years from the time it was made. The judge said that he had no jurisdiction to make any decision on this, but "completely obiter" he expressed the opinion that it was strange for one appellant to receive a less favourable treatment just because it had not had a control visit or a relevant discussion at the same time as the others.

The appeals were dismissed.

First-Tier Tribunal (TC06636): *YMCA Birmingham and others*

2.3.5 Fundraising

A number of university Students' Unions claimed exemption for social events on the basis that they ought to qualify for the fundraising exemption in VATA 1994 Sch.9 Group 12 by direct effect of PVD art.132(1)(o), because the requirement that the "primary purpose" had to be fundraising and the "15 events a year" restriction were not valid under EU law.

The appellants argued that, in effect, any activity that created a surplus was a "fundraising activity". The FTT rejected this, and also accepted HMRC's arguments that the limitations on the number of events and most of the other requirements of Group 12 were permitted restrictions that were intended to prevent distortion of competition. The judge decided that, on the evidence, all the events competed with other commercial

operations, and they were therefore not entitled to exemption under the UK law.

The argument relating to the PVD turned firstly on whether the appellants were "eligible bodies" under EU law (they clearly were under UK law). To qualify, they had to be "bodies recognised as being devoted to social wellbeing"; two of them also argued that they were non-profit making organisations supplying certain services closely linked to sport.

Judge Peter Kempster had considered this point before in relation to Loughborough Students' Union in 2017, and although he was not addressed on the subject, he came to the same conclusion as he did before: "From the evidence available to me I find that LSU's objects and activities are those of a student representative body promoting and supporting the general interests of its members; creating and promoting a good social, cultural and sporting life; and providing appropriate pastoral support for its members. I note that conclusion is consistent with what one would generally expect a good student union to be engaged in." He concluded that all four unions were eligible bodies under art.132(1)(o) by virtue of falling within art.132(1)(g).

The one requirement of Group 12 that the judge did not approve was the rule that any fundraising event has to be promoted as being primarily for the raising of money. He considered that the motive of the customers for attending an event should not determine the liability of the supplies, and it was therefore an unnecessary restriction. However, it was straightforward to "cure" the provision under the *Marleasing* principle – it remained coherent with the offending phrase in Item 1(c) simply struck out.

The appellants had not put forward a convincing argument for art.132(1)(o) being directly effective to override the UK provisions. None of the events qualified for exemption under the UK rules, so all the appeals were dismissed.

First-Tier Tribunal (TC06571): *Loughborough Students Union and others*

2.3.6 Cost-sharing exemption

From 15 August 2018, HMRC withdrew the 85% test for services to be regarded as 'directly necessary' for the exempt or non-business activities eligible for the cost-sharing exemption (CSE). In its place, HMRC added new guidance to the CSE manual, introducing a 'suitable apportionment calculation' for taxable or mixed use services regarded as 'directly necessary'. These changes follow HMRC's review of the exemption in response to recent CJEU judgments, as explained in R&C Brief 3/2018 and VAT Information Sheet 2/2018. Groups may continue to use the current tests until 31 December 2018, allowing them time to adjust to the new apportionment.

Apportionment of the recharge of costs by the CSG to its members will be allowed if the CSG can carry it out fairly and keep records necessary for HMRC to verify the calculation. Full details are in the updated VAT Cost Sharing Exemption manual pages CSE3850 to CSE 3895. HMRC reserve the right to refuse the exemption:

- if the records to justify the apportionment used have not been kept;
- in any case of avoidance or abuse.

CSGs that have correctly used the previous guidance can continue to use the previous tests for directly necessary services until 31 December 2018, to give them time to make sure the correct records are set up and kept.

The previous tests are set out in the VAT Cost Sharing Exemption manual pages CSE 3720 to CSE3840.

Revenue & Customs Brief 10/2018; www.gov.uk/hmrc-internal-manuals/vat-cost-sharing-exemption-manual/cse3700

2.3.7 Updated Notices

HMRC have updated their Notice *Health professionals and pharmaceutical products*. Physiotherapist independent prescribers and podiatrist independent prescribers have been added to the list of ‘relevant practitioners’ at paragraph 3.2.3.

Notice 701/57

HMRC have updated their Notice *Postage stamps and philatelic supplies*. It corrects the September 2017 version’s VAT calculation for imported collector’s items in paragraph 5.3 (based on the current 20% standard rate), which maintains an effective reduced rate of 5%.

Notice 701/8

2.3.8 Article

In an article in *Taxation*, Neil Warren examines the rules for exemption of fund-raising events for non-profit bodies. He suggests that some bodies that could benefit fail to take advantage of the exemption, and highlights the conditions that are required to qualify.

Taxation 23 August 2018

2.4 Zero-rating

2.4.1 Chocolate

A company zero-rated sales of an “allergen-free luxury dark chocolate bar” on the basis that it was cooking chocolate. HMRC decided it was confectionery and raised an assessment for £258,000 covering periods from 09/11 to 06/15.

Judge Anne Redston considered that the assessment of whether an item of food is zero rated or standard rated depended on how it was objectively “held out for sale”, which was a decision based on a multi-factorial assessment. Her conclusions were that:

(1) the Bar was held out for sale in supermarkets alongside other confectionery items and not alongside baking products;

(2) it was sometimes sold together with an Easter egg as a single item of confectionery;

(3) although the front of the wrapper included the words “delicious for cakes and desserts”, it contained no explicit statement that the Bar was “cooking chocolate” or “for cooking”;

(4) the back of the wrapper made no reference to cooking. It also stated that the portion size was one-quarter of a bar. Portion sizes are indicative of confectionery, not cooking chocolate;

(5) the company’s website positioned the Bar next to confectionery items, and did not say that it was cooking chocolate, or that it could be used for cooking;

(6) neither the wrapper nor the company’s website contained any recipes, or any indication of where recipes could be found;

(7) the company brand is known for its confectionery, not for its baking products. All other items sold by the company are confectionery, and the brand is reflected in the company’s name;

(8) the single advertisement provided as evidence positioned the Bar next to confectionery Items, and did not say that the Bar was “cooking chocolate”; instead it made the more limited statement that it was “ideal for cooking”; and

(9) consumers generally saw the Bar as eating chocolate which could also be used for cooking.

The appeal was dismissed.

First-Tier Tribunal (TC06548): *Kinnerton Confectionery Ltd*

2.4.2 Children’s clothes

A company held a numbers of licences to design, manufacture and sell products incorporating images of characters from popular movie, TV show, gaming and music brands. A dispute arose over the zero-rating of a particular type of product in two sizes, said to be suitable for 3 – 10 year olds and 10 – 13 year olds. HMRC raised assessments covering 08/13 to 03/16 totalling £157,579; originally penalties were assessed in addition, but these were dropped before the hearing.

The product was a rectangular piece of micro fibre with two sleeves. A competitor sold a similar item called a “slanket” (sleeved blanket); HMRC argued that it was not “clothing”. It had no fastening, but could be wrapped around the body. It was intended to be more convenient for a child than a simple blanket.

The parties accepted and adopted the approach of the FTT in *Snugglebundl Ltd* (TC04209) in deciding what is “designed as clothing”. An item has to be “worn” rather than simply covering the body (e.g. a blanket is not clothing); but the fact that something is worn does not of itself make it clothing (e.g. a brooch or a climbing harness).

The judge considered the application of these principles in some detail, and concluded that the product fulfilled the functions of clothing. “It keeps the user warm and can preserve the user’s modesty. Those are equally the functions of a blanket. However, unlike a blanket in my view it is natural to consider a child using the Product to be wearing it. It is appropriately shaped to fit the arms and can then be wrapped around the body, either with the opening at the front or the back.” The sleeves were

crucial: they enabled the product to be worn, and they were a fundamental part of the design. It was therefore designed as clothing.

The licensing agreements referred to the product as "fleece blankets", but that was not conclusive; it was simply because there was no other category in the agreements under which the items could fall, and there was no desire to change the agreements just to reflect these items.

The appeal was allowed. For some reason, the decision appears under two different reference numbers on the FTT website, but they appear to be identical.

First-Tier Tribunal (TC06619/TC06634): *Character World Ltd*

2.4.3 Bicarbonate of soda

HMRC have issued a Brief to confirm a change in policy on the liability of bicarbonate of soda following the FTT decision in *Phoenix Foods Ltd*. They explain the new approach as follows:

HMRC accepts that the product in question is zero-rated. In particular, it satisfies the conditions in paragraph 3.2 of Food products and VAT (VAT Notice 701/14) for zero rating, namely that it:

- *has some measurable nutritional content (sodium)*
- *is used solely or predominantly, in the particular form in which it is supplied, for baking (as evidenced by the way in which it was held out for sale)*
- *is not an excepted item*

In considering how a product is held out for sale, HMRC will consider a range of factors including the way in which a product is:

- *labelled;*
- *packaged;*
- *displayed;*
- *invoiced;*
- *advertised;*
- *marketed.*

Supplies of bicarbonate of soda that are similar to those made by Phoenix, where the bicarbonate of soda is in small tubs that are held out for sale as a baking ingredient, are zero-rated for VAT purposes.

Supplies of bicarbonate of soda that are sold in larger, industrial-sized quantities, or which are held out for non-culinary purposes, remain standard-rated.

HMRC will change the relevant guidance and Food products and VAT (Notice 701/14) to reflect this change in the VAT treatment of certain supplies of bicarbonate of soda.

Presumably these principles may have a wider application to other goods that have dual uses. The usual guidance is given about making claims and the concept of unjust enrichment.

Revenue & Customs Brief 8/2018

2.4.4 Emergency transport

A commercial company provided First Aid training, event medical cover and ambulance services. It had a contract to provide ambulance services to the NHS and purchased several vehicles for this purpose. It reclaimed the input tax on these vehicles on the basis that the supply could be zero-rated under Item 4, Group 8, Sch.8 as "transport". HMRC ruled that the supply was exempt under item 11, Group 7, Sch.9.

Note 4D of Group 8 Sch.8 provides that:

Item 4(a) includes the transport of passengers in a vehicle –

(a) Which is designed, or substantially and permanently adapted, for the safe carriage of a person in a wheelchair or two or more such persons, and

(b) Which, if it were not so designed or adapted, would be capable of carrying no less than 10 persons.

The ambulances were converted from base vehicles that were often converted for other users to carry at least 10 persons. The FTT (TC05986) decided that the meaning of the provision was "*to look at the vehicle itself and to determine whether or not that vehicle can, without complete rebuilding, be converted into a vehicle capable of carrying ten or more persons*". HMRC's argument, that it was necessary to consider only how many people could be carried if the wheelchair accommodation was removed, was rejected.

The judge was satisfied that the vehicles satisfied both Note 4D(a) and (b); it had been agreed that sick persons being transported were "passengers". The company could choose between zero-rating and exemption. The appeal was therefore allowed.

HMRC appealed to the Upper Tribunal. The judges noted that the facts were relatively uncontroversial; the question was how the law should be construed. They considered that the proper starting point was item 4(a) and not Note 4D. Note 4D does not, of itself, determine zero-rating, but rather is a mandatory interpretative provision, requiring item 4(a) to be read in a certain way.

Accordingly, it is necessary to begin with Item 4(a), and to ask whether the vehicle in question is designed or adapted to carry not less than ten passengers. This test must be applied at the time the supplies in question were rendered; and (where variable numbers of passengers are capable of being carried) requires consideration of the actual and anticipated ways in which the vehicle is being used. Clearly, on this basis, the supplies fell outside the ambit of Item 4(a).

The judges considered that the proper application of Note 4D was to consider a vehicle that had actually been adapted to carry a wheelchair by removing seats. It was not permissible to consider hypothetical adaptations that might have been ordered to add seats, which was the effect of the FTT decision. These vehicles had never been capable of carrying more than ten passengers. They could have been, had the specification been different, but they were not. The judges noted that the FTT's construction of the law could lead to absurd results, in which a luxury van with very comfortable seating for fewer than 10 people could become zero-rated merely by adding wheelchair restraints to engage Note

4D (on the basis that it would be capable of taking more than 10 people if the luxury seating were replaced by more basic and more numerous seats).

A narrow construction was required in applying an exception to the basic rule that supplies should be standard rated. Although in this case the choice was between exemption and zero rating, the judges commented that the same principles would apply in other circumstances where the choice was between exemption and standard rating. This strengthened the conclusion that the relief was not available.

HMRC's appeal was allowed.

Upper Tribunal: *HMRC v Jigsaw Medical Services Ltd*

2.5 Lower rate

2.5.1 Energy saving materials

A business installed central heating systems in houses. It accounted for lower rated VAT on certain components, and an apportioned amount of labour charges, on the basis that they qualified to be treated as 'energy saving materials' under s.29A VATA 1994. The company carried out the calculation using a software program called 'the VAT optimiser'. After carrying out a VAT inspection, HMRC disputed this and raised an assessment for the difference between the lower rate and the standard rated VAT.

HMRC accepted that the components might qualify for the lower rate if installed on their own, but not if they were part of a larger installation. In their view, there would be a single supply of 'installation of a central heating system' which would not fall within the narrow definition of 'installation of energy-saving materials'.

The FTT heard the case in 2013 (TC02895). It had to consider whether there was a single supply or mixed supplies, and if there was a single supply, whether it could qualify for the lower rate. The chairman considered various arguments put forward on the basis of precedents, including *Card Protection Plan*, the French undertakers case and *Talacre Beach Caravan Sales*. He was satisfied that, on *CPP* principles, there was a single supply.

The taxpayer's counsel argued that the undertakers case and *Talacre* supported the idea that a single supply could be apportioned. The chairman did not agree that they were relevant: they dealt with situations in which the national law provided for a lower rate to be applied, and the dispute was about whether it was possible to apply mixed rates to a single supply. In the present case, he was satisfied that the national law did not provide for the lower rate: the single supply was not 'of a description' included in Sch.7A.

The appeal was dismissed, and the company appealed to the Upper Tribunal. The judges noted that this was a lead case to determine whether, as a matter of fact or law, the supplies of installing energy saving materials together with installing boilers or other central heating products is:

- a single supply subject to a single rate of VAT, or
- a single supply subject to two or more different rates of VAT, or
- two or more separate supplies subject to different rates of VAT.

The appeal to the UT was stayed by the *Colaingrove* appeal on energy supplied with caravans, which went to the UT in 2015 and the CA in 2017. The judge noted that, since the FTT decision, there have also been other relevant CJEU and UT cases – *Stadion Amsterdam* (Case C-463/16), *HMRC v Pinevale Ltd* (UT 2014) and *HMRC v Wetheralds Construction Ltd* (UT 2018). These had all found that the lower rate would only apply to a part of a single supply if the national legislation explicitly provided for this.

By the end of the hearing, the appellant had accepted that it was not sufficient simply for the court to find that the supply of hot water controls is a concrete and specific part of an overall "*CPP*" supply of a hot water system in order for the reduced rate derogation to be applied – it would depend instead on whether the UK has in fact exercised its discretion to apply the reduced rate to a concrete and specific element of a complex single supply. That in turn depended on whether, as a matter of statutory construction, Parliament had legislated that the supply of controls should benefit from the reduced rate even where they were supplied as part of a larger composite supply. It was also agreed that, on the facts of the present case, there was a single *CPP* supply, and fiscal neutrality was not relevant.

The taxpayer's counsel argued that this case could be distinguished from cases on other groups of Sch.7A because Group 2 gave a list of items that, by definition, are supplied as part of a larger whole. That supported his contention that Parliament had intended to apply a reduced rate to components of a wider *CPP* supply.

The UT disagreed. The statutory focus is on the description of the supply in question as referred to by s.29A(1) VATA 1994. It is no part of the statutory test to ask whether the thing that is installed forms part of a wider product, and the wider supply does not fall within the descriptions in Group 2. It is possible for the items listed in Group 2 to be supplied separately – it is not inevitable that they are part of a larger supply.

After detailed examination of the precedents and counsel's arguments, the judges rejected the company's appeal. It was possible that the trader could have arranged the business differently, for example by arranging for a different entity to make supplies of the items qualifying for the reduced rate; but that was true of any *CPP* supply, and did not mean that this supply had to be treated other than as the law provided.

Upper Tribunal: *AN Checker Heating and Service Engineers v HMRC*

2.5.2 Private Member's Bill

Christopher Chope MP has introduced a Private Member's Bill "to reduce VAT on domestic energy bills, and for connected purposes". As such bills rarely get anywhere near becoming legislation, they are not printed for publication at the outset, so it is difficult to find out what is being proposed.

Domestic Energy (Value Added Tax) Bill

2.6 Computational matters

2.6.1 Motor dealer deposit contributions

HMRC have published a Brief to clarify the treatment of situations in which a motor dealer promotes sales by "making a payment to the finance company on behalf of the customer" (known as "DDC" or "dealer deposit contributions"). Some dealers have apparently continued to account for output tax on the "headline price" of the car, treating the "payment" as third party consideration for the sale. HMRC confirm that it should be treated as a discount on the price, reducing the output tax.

The Brief also refers to "MDC" or "manufacturer deposit contributions", which are accounted for in accordance with the principles of the *Elida Gibbs* case.

The Brief explains the operation of a DDC as follows:

For example a finance company may require a deposit from the customer of £8,000 on a £28,000 car. Under a DDC promotion the dealer is said to contribute (say) £2,000 towards the deposit. The effect being that the customer only has to pay £26,000 for the vehicle (plus finance charges).

Some dealers and finance companies account for VAT based on the headline price (£28,000) with the DDC then deducted from the payment due. By deducting the DDC after the VAT has been calculated and by bearing the burden of the DDC (£2,000) dealers are overpaying VAT as they account for more VAT than the customer pays.

Some dealers have tried to correct this by making an adjustment to their VAT account based on Regulation 38ZA of the VAT Regulations, SI 1995/2518.

HMRC views DDCs as a discount on the headline price charged by the dealer. The DDC is shown on the finance and sales documentation and is agreed by all the parties to the transactions before these take place. There is no retrospective adjustment to the amount the customer will pay, nor the amount the finance company will pay the dealer.

VAT is therefore due on the discounted amount actually charged to the finance company and the customer.

For example, the headline price of a car is stated as £28,000, this is shown as being funded by £20,000 finance, a deposit (including part exchange) of £6,000 from the customer and a DDC of £2,000. HMRC views the selling price from which VAT is due as £26,000 (£28,000 headline price less the £2,000 discount/contribution from the dealer).

The appropriate way to correct the accounting is by making a claim under s.80 or, if the amounts are within the appropriate limits, adjusting the VAT account under SI 1995/2518 reg.34. It is not appropriate to use the procedure for "adjustments in the course of business", because there has been no adjustment – the treatment was clear from the outset. The particular treatment in reg.38ZA applies to retrospective discounts made by the manufacturer or 'first supplier' in the UK (a UK VAT registered business that starts the supply chain in the UK, such as an importer). It does not apply to discounts agreed at the point of sale by the dealer.

A dealer who has made a correction using the wrong procedure should check whether it falls under the reg.34 limits. If in doubt, they should contact HMRC for further advice. Finance houses would have a matching adjustment to output tax and input tax, and therefore do not need to make any correction.

A business that has bought a vehicle with a DDC and is able to claim input tax on it may also have to make a correction, as it is not entitled to the VAT incorrectly calculated on the headline price.

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2.7 Discounts, rebates and gifts

Nothing to report.

2.8 Compound and multiple

2.8.1 Books and courses

This is the text of an article I have written for *Taxation* magazine summarising the history and current developments in the *BPP* case.

I have to declare a special interest in BPP's long-running argument with HMRC over the VAT treatment of study material sold in connection with courses. In another lifetime, before I knew very much about VAT, I was a partner in an accountancy college. We sold courses and printed matter to resit students (consumers, not businesses), and the VAT we had to charge made a big difference. In those days (the 1980s), HMRC would have accepted that there were separate supplies – standard-rated commercial education and zero-rated printed matter – but we were concerned that they might argue about our apportionment of fees between the two. We made sure that there was plenty of evidence to support our pricing structure: we sold courses without printed matter, and we sold printed matter without courses, so we could justify an arm's length price for each. When we sold both together, we were satisfied that the value of the standard rated element could be justified.

History lesson

HMRC reconsidered the treatment of mixed supplies, particularly those involving services and printed matter, following the CJEU judgment in *Card Protection Plan* (Case C-349/96). In the educational field, this led to the House of Lords decision in *College of Estate Management* (HL [2005] STC 1597 – '*CEM*'): study material used on exempt courses was part of a single supply of education, and could not be treated as zero-rated. The college was denied recovery of input tax on the costs of production.

In the same year, the Court of Appeal held in *Telewest Communications* (CA [2005] STC 481) that supplies made by separate companies could not be compounded together by HMRC. Although the CJEU ruled in *Part Service Srl* (Case C-425/06) that such supplies could be treated as a single

transaction in cases of abuse, the UK courts have upheld the *Telewest* principle in a number of decisions. For example, *Kumon Educational UK Co Ltd* (TC03249) restructured its business so that study materials were supplied by a different company from the franchisor of the educational method; in 2013 the FTT dismissed assessments raised by HMRC on the consideration received for the sale of study materials.

In 2011 HMRC tried to overturn the effect of *Telewest* at least in relation to supplies of printed matter. New Notes 2 and 3 were inserted in VATA 1994 Sch 8 Group 3 (Books, etc) to deny zero-rating of goods, that would otherwise qualify, where the supply of the goods is connected with a supply of services, made by a different supplier, in circumstances where *CEM* would have applied – if the supplies had been made by the same person, they would have been treated as a single supply of services that was either standard rated or exempt. The new rule applied to supplies made on or after 19 July 2011; in the *Kumon* decision, it is noted that the companies concerned accepted that it defeated their arrangements from that date onwards.

Enter BPP

In 2006 BPP carried out a reorganisation with a similar outcome to that in *Kumon* (although it is not stated anywhere that this was the purpose of that reorganisation): afterwards, standard rated education was supplied by BPP University College of Professional Studies Ltd ('PE'), and study material was supplied by BPP Learning Media Ltd ('LM'). In November 2012, HMRC raised assessments on books sold from 2006 onwards. The assessments were based on the same arguments that HMRC later put before the FTT in *Kumon*: either BPP's analysis of the supply chain was wrong and *CEM* applied anyway, or *Telewest* had been overturned by *Part Service*, or there was an abuse of rights.

Presumably the assessments related to periods before 19 July 2011, because BPP requested a formal decision in relation to supplies from that date in order to be able to appeal against it. That is one of the key points of interest in the dispute: there were originally separate arguments about the periods before and after the change of the law. On 24 April 2014, after considerable correspondence, HMRC withdrew the assessments, so that part of BPP's appeal was allowed. By that time, *Kumon* had been decided and HMRC must have concluded that they were unlikely to persuade the FTT to come to a different decision on similar facts.

However, unlike *Kumon*, BPP did not accept that Group 3 Notes 2 and 3 applied to exclude their supplies of printed matter from zero-rating after July 2011. They proposed to maintain the appeal against that decision.

Justice delayed

I suspect that anyone who has ever had an argument with HMRC has experienced the frustration of waiting for the officer, or the reviewer, or the technical department to which the issue has been referred, to set out clearly what HMRC's argument is. If HMRC are not clear about their case, it is very difficult to produce a defence – do they dispute the facts, or the application of the law to the facts, or both? In the dispute I wrote about in *In memoriam* (*Taxation*, 4 March 2009) I only realised that HMRC were entirely relying on a disagreement over underlying facts when listening to the officer addressing the General Commissioners at the

hearing. I had tried to pin him down on this many times over the preceding two years, but could never get a clear answer. I had a convincing witness who confirmed that the facts were as I had set them out two years before; HMRC had nothing at all. Not surprisingly, the appeal was allowed.

It is, of course, wrong to extrapolate from a single example. However, even in my limited practice I come across this problem too frequently, and I read about it in Tribunal reports all the time. In BPP's case, it was extreme. The facts are set out in the Supreme Court decision of 26 July 2017 (*BPP Holdings Ltd and others v HMRC* [2017] UKSC 55). I have summarised them here, removing references to the appeals against the assessments, which HMRC dropped.

May 2013: BPP raised appeals to the FTT.

21 October 2013: following directions from the Tribunal, HMRC served a statement of case (SOC), 14 days late, and applied for an extension of time (not opposed by BPP).

11 November 2013: BPP requested further and better particulars of HMRC's case.

22 November 2013: BPP applied to the FTT for a direction requiring HMRC to provide these particulars.

9 January 2014: Judge Hellier heard BPP's application and issued an 'unless order' – requiring HMRC to 'provide replies to each of the questions identified in the appellants' request by 31 January 2014', failing which 'the respondents may be barred from taking further part in the proceedings'. The order also included directions for the future conduct of the appeals including an order for the filing of disclosure statements and lists of documents by 30 April, and a provision for a seven day hearing.

31 January 2014: HMRC served a response to the request.

14 March 2014: BPP served a response to HMRC's SOC and applied for a barring order on the grounds that HMRC's response did not meet the terms of the 9 January order.

8 May 2014: HMRC supplied a 'defective disclosure statement and list of documents' (as described by Lord Neuberger), 8 days late, and did not apply for an extension of time in that connection until four weeks later.

23 June 2014: BPP's application for a barring order came before the FTT.

First FTT

Judge Barbara Mosedale has issued some striking decisions over the years, but TC03768 is what I would describe as 'an absolute belter'. She examined in detail what Judge Hellier's direction had required HMRC to do, and what they had done in response to it. Although pleadings in general do not require each party to identify every fact, matter and submission with the same degree of particularity as will be relied on at the hearing, nevertheless it is open to the Tribunal to direct more detailed pleadings than ordinarily required and in this particular case, in accordance with the parties' agreement, that is what the Tribunal did. HMRC could have appealed against the direction or they could have sought to have it set aside; instead, they failed to comply with it. The

direction required them to identify all the facts on which they sought to rely; their reply identified no facts at all.

She went on to consider the appropriate sanction. She agreed that the appellant was unable to appreciate HMRC's case or prepare to argue against it on the basis of the SOC and the reply to the direction. She stated that 'litigation should not be conducted by ambush.' HMRC had not even offered an explanation for their failure to comply with the direction – in the absence of any clear reason, that failure could not be justified. The judge was reluctant to impose the severe sanction of barring HMRC from taking any further part in the proceedings, but she considered that, in the absence of any excuse and the clear breach of Tribunal directions, she had no choice.

Onward and upward

Not surprisingly, HMRC were deeply unhappy at the prospect of a penalty shoot-out in which they would not be allowed a goalkeeper. They applied to a different FTT judge for an order setting aside the decision; he refused. They appealed to the Upper Tribunal, where Judge Bishopp, while still highly critical of HMRC's conduct, held that barring was too harsh. An award of costs might suffice to compensate BPP for the delays.

BPP appealed to the Court of Appeal, which restored Judge Mosedale's order; HMRC appealed to the Supreme Court, where the judges unanimously held that it was a decision she was entirely justified in making. She had taken a number of factors into account and carried out an appropriate balancing exercise. HMRC's representative argued that barring HMRC could lead to the public interest being harmed in that VAT which should be paid may not be recovered. Lord Neuberger considered that it would set a dangerous precedent if that point were accepted, as it would discourage public bodies from living up to the standards expected of individuals and private bodies in the conduct of litigation. It seemed to him that there was at least as strong an argument for saying that the courts should expect higher standards from public bodies than from private bodies or individuals.

Three cheers from all of us who have ever had to chase HMRC to make them explain their case. Sadly, not all of us are willing and able to go to the Supreme Court. Indeed, if HMRC have not issued a formal decision, we cannot even go to the FTT. There can be a deeply inconvenient and potentially expensive delay waiting to find out if HMRC will say that there is a problem at all.

Belter #2

TC06632 is, if anything, more fascinating than the first decision. The first point is procedural: given that HMRC could not take part, should Judge Mosedale summarily allow the remaining appeal? BPP asked her not to do that, but to give a fully reasoned decision.

Most importantly – and this is another key problem with HMRC's delays – BPP had accounted for VAT on sales of books in accordance with HMRC's decision, taking the prudent line that it was better to collect and pay over the money, risking commercial disadvantage, than to gamble on winning the case and build up a massive contingent liability (see, for example, the decision in *Metropolitan International Schools* UT 2017). If the books were properly zero-rated, BPP would be entitled to a substantial

repayment in respect of some 7 years' worth of sales. They were concerned that, if the appeal was allowed on merely procedural grounds, HMRC might refuse to repay the voluntary disclosure.

Judge Mosedale considered whether it was proper for her even to consider material submitted by HMRC before the barring order. HMRC had put forward a statement of case and some further information, even though the judge noted that they were 'found by me in 2014 to be inadequate to set out HMRC's case'. She decided that she had discretion to take this into account, and BPP raised no objection. There had been a statement of agreed facts, and BPP did not consider it necessary to call any further evidence to make their case. HMRC could not cross-examine or dispute any of the factual basis.

The judge went on to set out the principles relating to single, compound and mixed supplies, noting the subtle difference between supplies where there is an ancillary part that takes on the liability of the principal element (as in *Card Protection Plan*) and those where the minor part has lost its identity altogether and there is in reality a single supply (as in *CEM*). As is usual in one of Judge Mosedale's decisions, she analysed a wide range of precedents and considered their relevance to the facts. For anyone having an argument about mixed supplies, the reasoning is worth reading in full.

I will summarise it much more briefly: I found it particularly heartening that she settled on the point that my college considered crucial way back in the 1980s when I would not have known a *CEM* from a *CPP*. 'Looked at from the point of view of a typical consumer, a significant number of LM's customers buy the printed material *without* buying tuition from PE... It is clear that so far as the transactions between LM and the typical consumer is concerned, for a significant number of them the printed material is an end in itself. This factor is a major distinction with *CEM* where the printed material was found not to be an end in itself but always purchased with the view to obtaining the qualification offered by *CEM*.' The supply of tuition and the supply of the printed materials were independent of each other; a student could buy one without the other, either way around.

As a result, even if the supplies had been made by the same person, they would not have been regarded as a single supply of services. The Notes to Group 3 did not apply, and the appeal against the liability decision was allowed.

Where now?

It appears from this that the FA 2011 changes to Group 3 did not achieve what HMRC thought they did. To put it in the terms of my complaint set out above, I think they reckoned it made 'books and courses' a single supply as a matter of principle, particularly where they are supplied by different but connected persons; this decision holds (at least for the moment) that it remains a question that has to be determined on the facts. I wonder if the delays in setting out the argument in 2013/14 arose from HMRC's confusion over the distinction between a question of fact and a question of principle or law.

For that reason, HMRC will surely not be happy to let the matter rest. However, as discussed in the last few paragraphs of Judge Mosedale's

decision, it is not at all clear what they can do about it. 'Barred from taking further part in the proceedings' could extend to rights of appeal against the outcome of the proceedings. The judge speculates that HMRC could even be barred from making representations to her about their rights of appeal against her decision. She ordered that, if HMRC do wish to appeal, they must address that question when they do so, and BPP will be given the opportunity to object. Who knows – there could be another trip to the Supreme Court in a few years' time.

In the meantime, I hope that the history of this case will encourage at least some HMRC officers to address themselves more urgently to determining exactly what they wish to argue in a dispute with a taxpayer, and to communicate that clearly and promptly. I have a couple in my 'pending' tray.

First-Tier Tribunal (TC06632): *BPP University College of Professional Studies Ltd*

2.9 Agency

2.9.1 Tripartite arrangements

A recruitment company (AUK) made a voluntary disclosure to claim back VAT charged on receipts from clients who employed temporary staff. The company argued that the decision in *Reed Employment* meant that it should only have accounted for output tax on its margins. A number of other claims were made by companies that were now in the same VAT group registration, but had not been at the time that the claimed overpayments had been made. There was therefore a separate issue about the identity of the appropriate claimant, but the FTT (TC04743) was not asked to rule on that.

First-Tier Tribunal

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

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

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

Judge Mosedale summarised the issues as follows:

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

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

The judge concluded that the company was liable to pay the temp the agreed payment for its services in undertaking the assignment for the client. The client had no contractual obligation with either the temp or AUK to pay the temp for its work in undertaking the assignment. The client's only obligation to pay for the work was an obligation to pay AUK the agreed fee. The appellant's interpretation of the contract was inconsistent with the company's standard temp contract and inconsistent with the lack of legal obligation between the temp and the client. Looking at the contract in its context, HMRC's interpretation was clearly to be preferred.

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

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

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

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

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

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

Judge Mosedale did not agree with this conclusion. It was perfectly possible for a supply to involve the following: "*If A agrees with B, in return for money, to do what C tells it to do, that is doing something in return for consideration and there is no reason in logic why that cannot be a VAT supply by A to B, even though at no time does A agree to work under B's direction. Yet the conclusion in Reed Employment seems to have been that A can't supply its work to B if what A agrees to do for B is to work at C's direction. I simply can't agree.*"

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

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

It was more difficult to reconcile the decision in *Redrow* with that in *WHA*, where the Supreme Court had come to the opposite conclusion – the person who paid for the supply (the insurance company) did not receive it, but rather the garage made its supply to the owner of the car. It was difficult for a Tribunal judge to know which Supreme Court

precedent to apply. She summed up the principle she derived from these cases as follows:

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

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

Finally, she concluded "*I take from consideration of all these cases that a VAT supply, ordinarily at least, requires a legal relationship between the supplier and recipient under which the supplier is obliged to make the supply and the recipient is liable to pay for it, whether or not that liability arises under an enforceable contract (Tolsma, Redrow, Town & County Factors). Nevertheless, where the economic reality of the legal relationship is such that it results in final consumption of goods or services by a consumer in circumstances where in effect there is no VAT charge on that consumption then this normal rule is overridden because the ultimate purpose of the Principal VAT Directive is to tax final consumption...*

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

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

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

As a postscript (at paragraph 313), Judge Mosedale noted that her decision was consistent with fiscal neutrality: there was little difference

from the client's point of view between the supply of an employed temp and the supply of a non-employed temp, so it would be surprising if there was a fundamental difference between the VAT treatments of those supplies.

Upper Tribunal

The companies appealed against the decision to the UT. The judges noted that the issue (who received the supply from the temps) was similar to that in *Airtours*, where the FTT did not have the benefit of the Supreme Court's judgment. The UT had to construe the contracts, and then consider whether they represented economic and commercial reality.

The UT was clear that there were contracts between the temps and the appellant, and between the appellant and the clients, but no contracts between the temps and the clients. That was strongly suggestive that the temps were being supplied by the appellant to the clients. The appellant argued that the commercial and economic reality was that the temps did their work only for the clients, and could not therefore "be supplied" by the appellant, but the UT did not consider that to be a correct statement of VAT principle. It was clear from the terms of the contract that it was not a mere introduction; if it had been, there would have been no need for provisions about the appellant's obligations if the temp failed to turn up through sickness or unauthorised absence. The UT also agreed that the position of the employed and non-employed temps was so similar that they should be treated in the same way for VAT.

The UT noted that Judge Mosedale had expressed the hope that there would be guidance from a higher court to clarify what she considered to be the incorrect decision in *Reed Employment*. As that case was not the subject of an appeal before them, the UT judges declined to make any such comment, and emphasised that the present decision related to the particular facts of the case, its own contracts and economic reality.

The appeal was dismissed.

Court of Appeal

The company appealed again to the CA, where it came before Lord Justices Patten, David Richards and Newey. Newey LJ gave the leading judgment. He reviewed the facts, the contracts and the decisions below before setting out what he considered to be the main propositions to be derived from the precedents:

- the concept of a "supply" is "an autonomous concept of the EU-wide VAT system;
- a supply of goods or services "for consideration" within the meaning of the PVD presupposes the existence of a direct link between the goods or services provided and the consideration received;
- a supply of services is "effected for consideration" within the meaning of the PVD only if there is a legal relationship between the provider of the service and the recipient pursuant to which there is reciprocal performance, the remuneration received by the provider of the service constituting the value actually given in return for the service supplied;

- all or part of the consideration can, however, potentially come from someone other than the recipient of the supply;
- consideration of economic realities is a fundamental criterion for the application of VAT.

The company's counsel argued that the UT did not look beyond the contractual provisions, failed to take account of the FTT's findings as to how things worked in practice, overlooked the regulatory context and ignored aspects of the contracts that favoured the appellant's case. She set out a number of features of the "economic reality" that she considered indicated that Adecco only arranged a contract that was performed by the temps for the clients.

However, the judge agreed with HMRC. The starting point was the contracts: there were no contracts between the temps and the clients, so based only on the contractual analysis, the FTT and UT decisions had to be correct. The contracts referred to the temp undertaking an assignment "for a client", but it also referred to this taking place "through Adecco". The contracts were enforceable only by Adecco, which conferred control over the temps on their clients by contractual provisions. Adecco continued to be involved after the introduction: it was responsible for paying the temp, and it would terminate the contract with the temp if the work was unsatisfactory. The fees were not split between "what belonged to Adecco" and "what belonged to the temp": the charge was a single sum. There was no suggestion that the contractual provisions were a sham or were vitiated for any other reasons. In all the circumstances, it seemed that Adecco did more than supply introductory and ancillary services, but both contractually and as a matter of commercial and economic reality, it supplied the workers' services.

The judge commented that the contractual provisions in *Reed* would not have been identical, but he still considered the decision could not have been correct. The other judges agreed, and the company's appeal was dismissed again.

Court of Appeal: *Adecco UK Ltd and others v HMRC*

2.9.2 Catering and food

A company supplied catering services to the University of Aberdeen. It claimed a repayment of VAT for 09/11 to 09/12 on the basis that it had charged output tax; HMRC refused the claim, and also raised an assessment for underdeclared output tax for 09/10 to 06/12. The total amount at issue was £233,614, comprising £171,951 on the assessment, £23,176 in respect of VAT charged on supplies of food and £38,484 in relation to charges for staff costs.

The key question was whether supplies of food and staff by the company to the university comprised a single supply of catering, or the main supply was food and the supply of staff could be treated separately under a staff wages concession. The judge (Heidi Poon) noted that the factual matrix was not identical throughout the period, but certain issues remained constant throughout:

(1) Whether the food and labour supplied by the company was a single and composite supply in the course of catering;

(2) Whether the food supplied by the company under the wholesale arrangement was a separate supply of food;

(3) Whether the staff wages concession applied to the periods in question.

The judge reviewed the history of the relationship between the university and the company, which began when the university had closed its central refectory. The company contracted in 2005 to provide catering services; there were changes to the way in which the food itself was sourced, because prior to the involvement of a private sector company, the university benefited from membership of two buying consortia. This ended six months after the appellant became involved because the consortia were not happy with the idea of the greatly reduced supplier prices being shared with the private sector.

In 2008, the company made an earlier voluntary disclosure, claiming back output tax charged on food. HMRC refused the claim, ruling that the company supplied catering services and the whole supply was standard rated. A new contract was entered into in 2009 which stated "the contractor will purchase all agreed food provisions on behalf of the university". The Contract had an annual value of £463,258, made up by four components:

(1) Net Food Costs at £126,453;

(2) Labour Charges at £235,031;

(3) Management Fee at £39,274; and

(4) Expected Profit Margin at £52,500.

Some of the supplies under this new contract were treated as zero-rated. HMRC carried out a visit in 2013 and queried why this was so, given that there had been an unappealed ruling that all the supplies were standard rated. This led in due course to assessments. New advisers were appointed; they argued that no appealable decision had been given in 2008, and they sought to reopen the argument. They extended it to cover items that the company had standard rated.

The company's grounds of appeal were:

(1) Although the supplies were the subject of a single, framework contract, it is clear that they were in reality separate supplies.

(2) Food was supplied to UOA at premises other than those at which it was to be served to consumers (students and staff). It was not supplied ready to be served, and required to be prepared before serving to consumers.

(3) The staff supplied were involved in preparation from premises other than to those to which food was delivered, and using equipment provided by UOA and worked under supervision of UOA staff. They did not prepare all the food that the appellant delivered to UOA; neither was all the food delivered by the appellant prepared by the staff so supplied.

(4) The charges for food and staff were calculated and invoiced separately.

HMRC responded that the contract provided for a single indivisible economic supply, and under the principles of *Card Protection Plan* and

Levob, it could not be “cherry-picked” by the appellant into different elements with more advantageous treatments.

The appellant’s counsel argued that the contracts were “shams” and should be ignored. The judge noted that sham contracts usually reduced the tax payable; these had the opposite effect, by including the food within the supply when it would probably have been possible to exclude it. He considered a range of precedents on construing contracts, including *Newey* and *SecretHotels2*, and concluded that the contracts were not shams. They provided the framework for the parties to carry out their respective obligations. There was no incongruity between the contracts and the conduct of the parties in any material sense.

In that light, the judge held that the involvement of the appellant’s staff in the regeneration of cook chill food was an integral part of the supply, which was therefore far more than the mere provision of food. If the regeneration of the cook chill food had been carried out by UOA in-house staff instead of the appellant’s staff, then the supply of cook chill food, of itself, would not have been a supply in the course of catering. It would have been the ‘small modification of the facts’ that led to a different conclusion. However, the commercial and economic reality required that the appellant’s staff carried out the regeneration of the cook chill food, and that is the crucial factor which turned the supply of the food for the university’s “hub” eating area into a supply in the course of catering. Similar conclusions followed in relation to supplies in the halls of residence and in relation to functions.

However, part of the contract was for the supply of food under a wholesale arrangement. Here, there was a separate activity that was not incidental to the catering services; indeed, the value considerably exceeded the catering contract. The food bought under this procurement arrangement was not changed by the appellant. The situation was similar to that in *Compass Contract Catering*; under the principle of fiscal neutrality, food that was eligible for zero-rating from the wholesalers to the appellant should also be eligible for the same relief when supplied by the appellant to the university and by the university to consumers.

The judge examined arguments based on the catering staff wages concession in the HMRC manual at VTAXPER64200: “Some clients wish to maintain control over the catering facility, without necessarily being involved in the day-to-day operation. As a result a catering contractor may be appointed to provide the catering on behalf of the client. In such circumstances it is common for the agreement or invitation to tender to talk of the client “inviting the contractor on to the premises”, or asking the contractor to “manage and administer the facilities” on their behalf.”

The judge considered the argument put forward by the appellant to be self-contradictory: it was arguing on the one hand that there was no catering contract, but was also arguing on the other that a concession relevant to catering contracts applied. She was not convinced that the concession as stated applied to the facts, but in any case it was well-established that an appeal to the FTT could not succeed in forcing HMRC to apply a concession.

There was also an argument about whether the appellant was acting as agent for the university and was therefore capable of supplying exempt catering when it was incidental to supplies of education to the students.

The judge commented that she saw nothing inconsistent in regarding the supplies of food under the procurement arrangement as being a principal supply, while the supplies of catering were an agency supply. The VAT treatment of the appellant's supplies under the wholesale arrangement was not reliant on the university's status as an exempt education provider.

The appeal against the assessment was allowed, while the appeal against the refusal of the reclaim was dismissed.

First-Tier Tribunal (TC06595): *Olive Garden Catering Company Ltd*

2.10 Second hand goods

2.10.1 Scope of the second-hand schemes

A company operated a pawn shop. It regularly sold unredeemed pledges, which included items that incorporated precious metal and stones. It acquired them from non-taxable people, but it sold them to other traders. It applied a margin scheme to the sales. The tax authority ruled that the margin scheme did not apply, because the goods were being sold for their scrap value rather than as second-hand goods.

PVD art.311(1)(1) defines "second-hand goods" as movable tangible property that is suitable for further use as it is or after repair, other than works of art, collectors' items or antiques and other than precious metals or precious stones as defined by the Member States. The company argued that it was unreasonable for the VAT treatment to depend on whether the seller knew what the purchaser would use the items for (resale or processing).

The CJEU noted that the definition excludes works of art, collectors' items and antiques, but these can be subject to a margin scheme – they are defined in detail in Annex IX and covered by art.313 and 314. However, precious metals and precious stones are excluded from the definition and not then referred to again. As the margin scheme is an exception to the normal rules of VAT and must therefore be interpreted strictly, it must be assumed that the margin scheme does not apply to such items.

The CJEU noted that the Commission had originally considered including a more detailed definition when designing the predecessor legislation in 1994. In the end, the definition had been left to the Member States; but that power would have to be exercised in accordance with EU legal principles. In this case, the CJEU concluded that in order for an object composed of precious metals or precious stones to be capable of falling within the category of 'second-hand goods', within the meaning of PVD art.311(1)(1), which are eligible for the special margin scheme, and not that of 'precious metals or precious stones', which are excluded from that scheme, it must have had a functionality other than that which is inherent in the materials of which it is composed, have retained that functionality and be suitable for further use, as it is or after repair.

By contrast, where an object has no functionality other than that inherent in its component materials, or is not capable of fulfilling any other function, the object in question does not qualify for the special margin

scheme since it is no longer in the same economic cycle and will be useful only for the purposes of being transformed into a new object, which will have a new economic cycle, with the result that the risk of double taxation, which is the basis for the establishment of the margin scheme, disappears.

The decision on whether the goods were to be used for a new purpose or were second-hand goods should be based on all relevant objective factors, including for example how they were presented for sale and how the price was calculated (e.g. in bulk and sold by weight, or per item).

The conclusion was that it was for the national court to determine whether the goods had ceased to be capable of performing their original function and were only being sold for the value inherent in their constituent precious stones and metals. If they were, they had to be excluded from the margin scheme.

CJEU (Case C-154/17): *SIA 'E LATS' v Valsts ienemumu dienests*

2.11 Charities and clubs

Nothing to report.

2.12 Other supply problems

2.12.1 Goods or services?

To understand the *Marcandi* case, it is necessary to understand the underlying business model. It is described as follows on Wikipedia (slightly more clearly than in the CJEU judgment):

The pay-to-bid auction process employed by MadBid [the trading name of Marcandi Ltd] *is based on users buying "credits" which allow them to place bids in auctions. Users must purchase these credits before participating. Credits are sold in different bulk amounts and cost between 10p and 12.5p. However the effective credit value is significantly lower due to offers and to won credits and credits purchased in "Buy Now". The number of credits to place a bid on each auction varies; smaller auctions require two credits for every bid placed, while larger and more popular auctions can use up to fifteen credits.*

Every bid placed raises the auction price of an item by 1p and at the same time extends the closing time of the auction by up to 60 seconds. The auction closes when time runs out, and the last bid wins the right to buy the item for the final auction price plus any processing and shipping costs.

The net result is those who did not win paid for a number of bids and receive nothing (though the amount paid does count towards the "earned discount"), the winning bidder has paid for their bids and will still need to pay the final auction price plus p&p. In one example for a television with an RRP of £450, which cost four credits per bid, the winner spent

£217.60 on bids plus the winning price and P&P, all other bidders paid and did not win the item, the highest of those paying £211.60, the other bidders paid much smaller amounts. In total Madbid received £612 for the item. In a more recent example, for a circa £600 laptop, MadBid could have received around £14,000 in bids assuming the cost of bids was equal for all participants.

The company therefore received payments from customers for "the right to bid", and also for "goods sold" – either to successful bidders or to customers who bought in the online shop. The "buy now" and "earned discount" features were means of transferring the value of unsuccessful bids to a purchase in the online shop.

HMRC ruled that the "right to bid" receipts were consideration for a supply of services that were separate from the consideration for the supply of goods. The company argued that the sale of rights to bid was a "preliminary transaction" before a supply of goods, similar to the sale of points in *MacDonald Resorts* (Case C-270/09), and was therefore not taxable as a separate supply. The consequence of this is not spelled out in the CJEU judgment: presumably, it would mean that credits used up in unsuccessful bids would not be subject to VAT at all, because there would be no supply of goods to the unsuccessful bidders. The value of credits issued to the successful bidder might be included in the value of the supply of goods, but it would be taxed later than on HMRC's analysis.

It is also worth noting, although not mentioned in the decision, that the distinction could affect the place of supply. The *Welmory* case about fixed establishments was concerned with a similar business model. It would be possible for the "rights to bid" to be taxable in a different Member State from the supply of goods (unless they are covered by MOSS, in which case they would probably both be taxed where the consumer belonged).

The dispute went to the First-Tier Tribunal, which noted that the German tax authority had concluded that the sale of bid credits was neither a supply of goods nor a supply of services, and the consideration for credits should be added to the taxable amount for a subsequent supply of goods. One of the questions referred to the CJEU concerned the need of a national court to take into account the views of other jurisdictions, in order to prevent double taxation or non-taxation.

The CJEU considered the way the auctions worked and concluded that the "rights to bid" served a function that was wholly separate from the supply of goods. The value of credits was not set against the price of the auctioned item; if the successful purchaser cancelled the order, only the auction price was refunded, not the value of the credits. Even where there was some limited overlap, in the case of "buy now" and "earned discount", the two transactions were still separate. Nor was the supply of "bid rights" ancillary to the sale of goods. The consideration for one transaction could not also be the consideration for another transaction, nor could its nature be changed after the event.

Accordingly, the sale of "bid rights" or "credits" was a separate supply of services, and was taxable as such. It was not part of the sale of goods, which was an independent supply for the auction price, irrespective of the amount paid for credits used in that auction.

Where a national court identified a possible conflict with the views of a different tax jurisdiction, it would have the power, and possibly the obligation, of making a reference to the CJEU to determine the matter. This answer to the third question effectively points out that it is for the CJEU to resolve differences in treatment between Member States; it is not for a national court to try to anticipate the answer that the CJEU might give.

CJEU (Case C-644/16): *Marcandi Ltd (t/a Madbid) v HMRC*

2.12.2 Delivery charges

A company appealed against the refusal of a reclaim under s.80 VATA 1994 for £740,287. The company supplied goods on mail order; where a customer returned the order, the company would refund the price of the goods, but not the price of delivery that had been charged to the customer on the original order.

The argument was that the supply was a single supply of "delivered goods"; when the customer returned the goods, the supply was cancelled, so the VAT was discharged under art.90 PVD. The amount retained was analogous to the forfeited deposit in *Eugenie-les-Bains*.

HMRC argued that the delivery element of the single supply "delivered goods" did not cease to exist if the goods were returned. It had been supplied and could not be cancelled. Although it was subsumed in a single supply in the normal situation, it remained a distinct and separate supply that had been made for consideration, and that was not changed by the return of the goods.

The FTT accepted HMRC's argument. As a matter of contract (and as a matter of economic and commercial reality) the appellant agreed to sell and deliver, and sold and delivered, goods to the customer. The customer paid the appellant the contract price for the goods and paid a separate delivery charge for the special delivery of the goods. That original contract was not rescinded (or otherwise avoided) ab initio for some extraneous vitiating factor (e.g. misrepresentation); and the parties have not been purportedly restored to the position as if the contract had never been made. The basic position remained that the customer has furnished (monetary) consideration to the Appellant in return for something done by the Appellant.

As a matter of VAT analysis:

(a) ASOS made a single, composite taxable supply for VAT purposes, comprising the sale of goods and the special delivery of those goods, for a monetary consideration comprising the price of the goods and the delivery charge. One of the features was the right to return the goods after the supply was completed.

(b) That single, composite taxable supply was properly characterised for VAT as a supply of goods.

(c) The taxable amount for which the appellant was required to account on that taxable supply was the full monetary consideration comprising the price of the goods and the delivery charge.

(d) Subsequently, the transaction was (arguably) "cancelled" – in part, but not in full (and any "cancellation" was in those circumstances prospective

rather than retroactive): see Case C-404/16 *Lombard* – and the consideration for the single composite supply was reduced after the supply took place.

(e) However analysed, the appellant had received and retained the delivery charge paid by the customer. Accordingly, the taxable amount fell to be "reduced accordingly" under art.90 PVD.

(f) Having regard to all the circumstances, the reduction in the taxable amount was represented by the price of the goods refunded, and not the retained delivery charge, since the total consideration received for the single composite supply was reduced only by the amount of the refund.

Judge Rupert Jones considered the appellant's arguments in some detail, but could find no merit in them. The appeal against refusal of the reclaim was dismissed.

First-Tier Tribunal (TC06567): *Asos plc*

2.12.3 Salary sacrifice

A company appealed against assessments covering periods 07/09 to 07/14 totalling over £715,000, with more assessments standing behind the appeals. The dispute related to the operation by the company of a scheme for the provision of travel and subsistence expenses to employees known as a "Mobile Advantage Plan" or "MAP".

The Tribunal set out the issues to be decided as follows:

(1) whether or not the operation of MAP involved a supply of services for VAT purposes by Pertemps to participating employees;

(2) if so, whether or not the supply was an exempt supply falling within item 1 Group 5 Sch.9 to VATA 1994;

(3) if Pertemps made a taxable supply, whether HMRC was entitled to collect the tax or whether it was precluded from doing so by the issue of Business Brief 28/11 for periods to which it applied as a result of application of its powers of collection and management. HMRC argued that the FTT did not have jurisdiction to find for the company on this ground.

The workers involved in the appeal were "flexible employees" who were guaranteed a minimum number of hours of temp work, typically 336 hours a year or 7 hours a week. They were given the option to participate in a MAP, which involved a reduction in the wages earned and a payment to the employee in respect of travel and subsistence expenses. The amount of the reduction applied to the employee's wages was equal to the amount of the expenses payment plus a fixed amount (50p or £1 per shift, the "MAP adjustment"). This was not separately identifiable in the company's accounts, but was simply reflected in the lower cost of providing workers to clients and therefore in higher profit.

The reduction in gross pay was therefore greater than the payment for travel and subsistence, but because these workers were assigned to temporary work away from their permanent workplace, the travel and subsistence payments were not taxable. The net pay was therefore greater. Steps were taken to ensure that employees for whom MAP was not suitable – for example, those for whom a reduction in wages would

breach the national minimum wage requirements – did not participate in MAP or were unable to do so. HMRC had confirmed that the income tax and NIC side of the arrangement was effective.

The main benefits from the operation of the MAP scheme accrued to the employer: the cash amounts paid to flexible employees were reduced by the MAP adjustment; the employer did not have to account for employer's national insurance contributions on the MAP payment; and the employer was not required to include the MAP payment in its returns of benefits provided to employees.

The salary sacrifice arrangement had first been introduced in 2004 and had been discussed in detail with HMRC several times in the years up to 2011. That was one of the original grounds of appeal, that HMRC should not be able to question the treatment in arrears when they had effectively approved it. That ground was withdrawn before the hearing.

HMRC raised the VAT treatment of MAP at a meeting with the company on 17 October 2011. HMRC's position, as reflected in a letter dated 16 December 2011, was that, while the VAT issues had been raised and, perhaps, not followed through as promptly as might have been desirable, the question of the VAT treatment of MAP remained open. HMRC did, however, acknowledge in that letter that any disagreement over the VAT treatment was a technical one and that penalties would not be applied if any VAT was found to be chargeable as part of the review. On 17 April 2013, the relevant HMRC officer wrote to the company, setting out her conclusion that the MAP adjustment was consideration for a supply made by the company to flexible employees for VAT purposes. The decision was confirmed on review and the company appealed to the Tribunal.

The company distinguished its circumstances from those of *AstraZeneca*, which supplied an identifiable item (a voucher) to employees in return for salary sacrifice. Here, there was nothing supplied by the company to the workers. There was also no consideration given by the workers for such a supply, even if it existed. The salary sacrifice was an adjustment to the contracts between the parties; the MAP adjustment was an element in the calculation that resulted, but it was not consideration for anything.

An alternative argument was based on the decision in *Wakefield College*: the arrangement was not made "for the purposes of obtaining income", and was therefore not an economic activity.

HMRC argued that the nature of the supply was the administration of the MAP scheme, which provided a real benefit to the employees in saving them the bother of making claims for expenses through the self-assessment system. HMRC's counsel countered the various points raised by the company based on *Wakefield*. Overall, the MAP scheme was an activity that was pursued on a large scale over a long period and resulted in a significant profit. It was therefore an economic activity.

Judge Ashley Greenbank summarised the arguments in terms of the PVD:

(1) First, it is necessary to show that the operation of MAP involves a supply of services for a consideration for the purposes of art.2(c) PVD. He referred to this issue as the "article 2 question". In the UK legislation, this wording is reflected in s.5(2) VATA.

(2) Second, the supply must be made by a "taxable person acting as such" (also in art.2(c)). A taxable person is a person who carries out an "economic activity" within art.9 PVD. He referred to this issue as the "article 9 question". The equivalent phrase in the UK legislation is "in the course or furtherance of the business" in s.4(1) VATA.

The CA gave its judgement in *Wakefield College* after the end of the hearing, and both parties made submissions based on it. The judge relied heavily on it, because the CA analysed several of the other cases on which the parties had based their arguments – *Finland*, *Gemeente Borsele* and *Longridge on the Thames*.

The first key question was whether there was a supply of goods or services for a consideration for the purposes of art.2. This test requires a legal relationship between the supplier and the recipient, pursuant to which there is reciprocal performance whereby the goods or services are supplied in return for the consideration provided by the recipient. There is no requirement for the consideration to be equivalent to the value of the supply.

The second question is whether or not the supply constitutes an economic activity within art.9. As described by David Richards LJ in *Wakefield College* this is a broad enquiry which has to take into account all of the circumstances in which the goods or services are supplied. The essential test is whether the supply is made for the purpose of obtaining income on a continuing basis.

The judge also referred to *AstraZeneca*, in which employees gave up some of their salary in return for retailer vouchers. The CJEU held that there was a supply of services, and the amount of salary forgone was monetary consideration for that supply. He noted that this was essentially concerned with the "article 2 question" rather than the "article 9 question".

The judge considered that the criteria in the case law for a supply within art.2 were met. He summarised his reasons as follows:

(1) There is a legal relationship between Pertemps and the flexible employee expressed in the contract of employment incorporating relevant terms of the Flexible Employee Handbook.

(2) Pursuant to that legal relationship, the employee exchanges a right to receive a payment of salary for a right to receive a payment of expenses for a consideration. This is clear from the contractual position that I have described above. The two payments (salary and expenses) have different characteristics for tax and national insurance purposes. That exchange potentially involves the supply of a service.

(3) Pursuant to that relationship, the employee provides an identifiable consideration, the MAP adjustment. It is expressed in monetary terms. It does not matter that the employee does not become entitled to the payment (and so no income tax charge arises in relation to that amount). This is clear from the AstraZeneca case. It is sufficient that the employee forgoes part of what could be his or her remuneration as part of a bargain in exchange for the service.

(4) There is reciprocal performance. The consideration is directly referable to the supply: it is only incurred by those employees who make

claims under the MAP scheme; and the amount of the charge is proportionate to the number of claims that are made.

The judge did not agree with HMRC's counsel that the supply was "the operation of the scheme". Rather, the employee agreed to forgo an element of salary in exchange for the tax-free payment of expenses. The operation of the scheme was part of the internal administration of the company.

The judge determined the article 9 question in favour of the company for the following reasons:

(1) The operation of MAP does not provide an income stream to Pertemps. It reduces the cost to Pertemps of employing its workers and accordingly increases the profits which Pertemps makes from its business of providing those workers to its clients.

(2) MAP is not a service that could be provided by a third party supplier. The MAP scheme relies upon the issue of the dispensation by HMRC to the employer. It can only be operated by a person who is the employer. It is not "an activity likely to be carried on by a private undertaking on a market, organized within a professional framework generally performed in the interest of generating profit" (Banque Bruxelles Lambert SA v Belgium, per Advocate General Poiares Maduro at [10]).

(3) In a similar vein, this is a supply that is being made pursuant to the employment relationship. The principal supply that is being made in the context of that relationship is the supply by the employees of their labour in consideration for the remuneration and benefits provided by Pertemps. The same was, of course, true in the AstraZeneca case. But this supply is, in my view, too ancillary to the fundamental elements of the employment relationship. This is not a case – as in AstraZeneca – where the employer also makes available to the employee goods or a separate service (the voucher in the AstraZeneca case) which could have been provided by a third person outside the obligations normally performed by the employer as part of the employment relationship.

(4) This is also not a case in which it is necessary to impose a charge to VAT in order to ensure that the coherence of the VAT system is maintained or to ensure that a level playing field is maintained between participants in a market. This was a factor in the AstraZeneca case. It is not so here.

The judge considered the second ground of appeal more briefly, but concluded that, if he was wrong about there being no economic activity, the supply was exempt within item 1 Group 5 Sch.9 as a "dealing in money". The transaction involved a change in the legal and financial position between the parties as required by the CJEU case law.

Because he had allowed the appeal on other grounds, the judge declined to make any findings in relation to the contentious jurisdictional issue relating to BB 28/11. That could be considered as a question of law by a higher court on appeal without him having made any findings, so he did not need to determine it.

First-Tier Tribunal (TC06583): *Pertemps Ltd*

2.12.4 Vouchers legislation

The government has published draft legislation for Finance Bill 2019 containing provisions to transpose the EU vouchers directive into UK law from 1 January 2019. The change will mean that the use of multi-purpose vouchers will give rise to a single supply of the underlying goods or services, rather than treating the voucher as a separate supply of services. The government acknowledges possible issues around the likelihood that many businesses will change their business model from a buy/sell arrangement to an agency arrangement, and difficulties in tracking vouchers issued before and after 1 January 2019. HMRC say they will take a 'pragmatic approach' to difficulties experienced by businesses during the transition.

www.gov.uk/government/consultations/vat-and-vouchers

The following notes present a summary of the changes. A new Sch.10B will be inserted in VATA 1994 to apply to vouchers issued on or after 1 January 2019. Vouchers are defined as follows:

In this Schedule "voucher" means an instrument (in physical or electronic form) in relation to which the following conditions are met.

(2) The first condition is that one or more persons are under an obligation to accept the instrument as consideration for the provision of goods or services.

(3) The second condition is that either or both of:

(a) the goods and services for the provision of which the instrument may be accepted as consideration, and

(b) the persons who are under the obligation to accept the instrument as consideration for the provision of goods or services, are limited and are stated on or recorded in the instrument or the terms and conditions governing the use of the instrument.

(4) The third condition is that the instrument is transferable by gift (whether or not it is transferable for consideration).

(5) The following are not vouchers:

(a) an instrument entitling a person to a reduction in the consideration for the provision of goods or services;

(b) an instrument functioning as a ticket, for example for travel or for admission to a venue or event;

(c) postage stamps.

Single purpose vouchers (SPVs) are defined as vouchers where, at the time the voucher is issued, the following are known:

(a) the place of supply of the relevant goods or services, and

(b) that any supply of relevant goods or services falls into a single supply category (and what that supply category is).

Multi-purpose vouchers (MPVs) are vouchers that are not SPVs.

The current rules (VATA 1994 Sch.10A, which will not apply to vouchers issued on or after 1 January 2019) are these:

- Intermediate sales in a chain of supply of both SPVs and MPVs are taxed as SR supplies of services (the vouchers) based on the actual consideration (but see below for the fudge on MPV tax rate);
- The issue of SPVs is taxed and the redemption is not;
- The issue of MPVs is not taxed but the redemption is;
- On redemption, the amount taxed on a MPV is the amount originally received for the issue, not the face value.

This leads to some problems. Suppose M issues a voucher to N, who pays £10; N sells it to O for £16; O sells it to P for £25; P exchanges it for goods at the face value of £30 from M.

Under the current rules (all figures gross)...

If the voucher is a SPV:

- M accounts for output tax on £10 on issue
- N has input tax on £10 and output tax on £16
- O has input tax on £16 and output tax on £25
- M has bought some goods with selling price £30 but has paid £25

That's all as it should be – SPVs are not such a problem.

If the voucher is a MPV:

- M accounts for no output tax on issue
- N has output tax on £16, but strictly no input tax – HMRC have allowed a sort of margin scheme as a fudge, but not consistently
- O has output tax on £25 and input tax on £16
- P has bought some goods with selling price £30 but has paid £25 – but M now accounts for output tax on £10 at whatever VAT rate is applicable to whatever is supplied

Because it's a MPV, the liability of the supply could be different. HMRC allow an estimated rate to be used for the output tax calculated by N and O – M will tell them "half our vouchers are used for ZR supplies and half for SR, so use a VAT rate of 1/12 rather than 1/6".

Because N may have to account for output tax with no input tax, the overall tax take could be too much – but if the voucher is never redeemed, M never accounts for output tax.

Under the new rules (all figures gross)...

SPV – the consequences do not change, except that the intermediate supplies are treated as "the goods or services" rather than "the voucher".

MPV:

- M accounts for no output tax on issue
- N and O account for no output tax or input tax on sales – if they separately charge for promotional services (as in the example on your slide) rather than making a profit on buying and selling, then those promotional services are separate and taxable in the normal way

- P has bought some goods with selling price £30 but has paid £25 – if M somehow knows that P paid £25 for the voucher, M accounts for output tax on £25; if M doesn't know that, M accounts for output tax on £30.

The last point – the relevance of the face value – is a key change. It remains the case that, if P loses the voucher, no VAT is ever payable.

2.12.5 Fuel scale rates

The UK's derogation to operate fuel scale rate charges expires on 31 December 2018. In April the UK applied to extend the derogation to the end of 2020. The Commission has published a proposal for the Council to authorise the extension. The derogation is required because the use of scale rates is a simplification measure; such measures are not supposed to make a significant difference to the overall VAT collected. The "winners and losers" through claiming all VAT on road fuel and accounting for fixed outputs to reflect private use, rather than working out the business percentage exactly, are supposed to even out.

3. LAND AND PROPERTY

3.1 Exemption

3.1.1 Immovable property?

In TC05253, a company supplied modular temporary classroom accommodation. HMRC ruled that it was making exempt supplies of land – immovable property – and therefore could not recover input tax on its costs. The FTT considered the *Maierhofer* precedent (Case C-315/00) in which the CJEU had ruled that the difficulty of putting up, taking down and moving a prefabricated structure was relevant in deciding whether it was "immovable". The UK Upper Tribunal had applied that decision in *UK Storage Company (SW) Ltd*. Both parties were in agreement that the length of the lease, the fact that the units had previously been used on a different site and were subsequently used elsewhere and that it was conceded that the units were not "inseverably fixed to or in the ground" were not relevant and that the Tribunal had to look at the objective characteristics of the structure.

HMRC pointed out that this was a two-storey structure requiring planning permission. It contained 19 classrooms, staff and office accommodation, toilets, stores and ancillary accommodation, an internal lift and lift shaft, and internal staircases. It had required foundations to be set in the ground, and had taken the appellant 48 days to deliver it, construct it and fit it out, and it took 14 individuals 7 days to dismantle and remove it.

The appellant argued that the units were not fixed to the ground and dismantling them was a straightforward exercise. The number of units involved did not make any difference, and the requirement for planning permission was nothing to do with VAT law.

The FTT examined the installation and removal process in some detail. The judge noted that there was a conflict between the arguments of the parties: HMRC wanted to consider the combination of 66 prefabricated units into one substantial building, while the appellant argued that the proper test was to consider each component individually. The FTT concluded that the proper *Maierhofer* test was nearer the appellant's position: it was necessary to consider whether each unit was fixed to the ground.

The connections to the ground were in three possible forms: foundation trenches, levelling beams and friction clamps; mains services; and two external staircases. The judge did not consider that any of these were so fundamental as to establish that the units were fixed.

The length of time taken to dismantle and remove the units arose mainly from the number of them, rather than the difficulty of the exercise. They were within the same bounds as *UK Storage* and *Maierhofer*. The units were movable property, and the appeal was allowed.

HMRC appealed to the Upper Tribunal, which reversed the decision. The issue was in relation to the UK law ("grant of any interest in or right over land or of any licence to occupy land"), to be construed in accordance with the EU law ("letting of immovable property", defined as "a building fixed to or in the ground").

The UT derived a number of principles from the precedents:

- exemption would follow if there was a letting of something immovable, which meant fixed to or in the ground, and there was no exhaustive definition of how that should be interpreted – rather, it should be interpreted after an objective consideration of how the structure related to the site;
- the two main precedents, *Maierhofer* and *Leichenich* (Case C-532/11), did not support the consideration of individual components in the overall structure, nor a sequential approach considering each step in the process of construction and dismantling separately. Rather, all aspects of the structure should be considered together.

The UT concluded that the FTT had misdirected itself as to the law, and failed to apply the law properly to the facts. It had arrived at conclusions that no reasonable FTT could properly reach. The building had substantial foundations set in the ground. It was fixed to the ground not only by the connection to utilities and the fire escapes, but also by its own very substantial weight. Moving it involved dismantling the structure, which would effectively make it no longer a structure – it could not be "moved" without changing it fundamentally.

The UT allowed HMRC's appeal and remade the decision, holding that the original ruling for exemption was correct.

The company appealed to the Court of Session, which considered that the question of immovability was not the only issue. It was, rather, whether the appellant's supply of the accommodation constituted a grant of an interest in or right over land within Group 1 Sch.9 VATA 1994. That was a matter of law, and there could only be one correct answer. In a case such as the present where there were features beyond the mere passive leasing of land or a building, the purpose of the exemption should be borne in mind: it was not intended to exempt transactions with active elements such as design, construction, transportation, hire and removal, which is what the appellant did for its customer.

Another factor, although not a determinative one, was whether any interest in the land (i.e. the undoubtedly immovable property) was conveyed or leased, or already belonged to, the person receiving the supply. In this case, the land was not, nor could it have been, leased by the appellant to the school. At the start of the contract, and at all times thereafter, the property which the appellants supplied, i.e. their units, were movable property. It was always intended that the structure was temporary and would be removed at the end of the hire.

The UT had been correct to identify a number of errors in the FTT's approach. However, the determinative issue was whether, applying a holistic approach, the design, provision and removal of the temporary school accommodation amounted to a lease of immovable property. That was a wider question than the more restricted one of whether the building was fixed to or in the ground. The FTT had reached the correct conclusion: the structure was one that was "inherently movable", and its conclusion should therefore be reinstated.

The taxpayer's appeal was allowed.

Court of Session: *SiBCAS Ltd v HMRC*

3.1.2 Domestic service charges

HMRC have published a Brief and an Information Sheet to publicise a change in policy on service charges levied by property management companies. From 1 November 2018, HMRC will require all property management companies to account for VAT at the standard rate on fees they charge landlords for providing common services to the occupants of residential property. Management companies cannot use ESC 3.18, under which landlords who provide such services directly may treat mandatory service charges paid by the occupants as exempt from VAT.

The concession came into effect on 1 April 1994. Landlords who are contractually obliged to provide services to all occupants of a common estate may choose to use the concession to treat these supplies, when made to a freeholder, as exempt from VAT. Leaseholders and tenants are exempt from paying VAT on these charges as the charge is directly linked to an exempt supply of an interest in land. Freeholders do not have this link, so for them, these charges are normally taxable at the standard rate of VAT.

The services covered by the concession are the:

- upkeep of the common areas of the estate, dwellings or blocks of flats where the occupants live and where these charges are mandatory for all the occupants;
- provision of a warden, superintendent, caretaker or those performing a similar function connected with the day-to-day running of that estate, dwelling or blocks of flats, for those occupants;
- general maintenance of the exterior of a block of flats or individual dwelling - where the residents cannot refuse this.

This concession does not apply to any management fees charged by a management company, or similar, for its services.

HMRC know of a number of property management and similar service companies who provide goods and services to landlords of residential buildings, but are not correctly accounting for VAT. These companies cannot use the concession to:

- treat their supplies as if made to the occupant rather than the landlord;
- recharge costs borne on behalf of the landlord, back to the landlord;
- recharge staff or personnel costs to the landlord.

VAT Information Sheet 07/18 provides guidance on:

- applying ESC 3.18 on or after 1 November 2018;
- the direction of a supply made by the various parties and the relevant liability of that supply;
- common scenarios that arise when applying ESC 3.18 incorrectly:

(a) Property management companies, or similar treating their supply as being to the occupant, rather than the landlord

As outlined in sections 3 and 4, if you're a management company, or similar, providing services to the landlord so that their contractual

obligations to the occupants are met, then this supply is from you to the landlord and is taxable at the standard rate of VAT.

You cannot treat your supplies as VAT exempt supplies, made to the occupant. So ESC 3.18 does not apply.

This type of error usually arises because management companies wrongly assume that as they're collecting periodic payments directly from the occupant, they must be making their supply to the occupant and not the landlord. However, the monies collected are contractual payments due to the landlord for their supply.

Any collected monies kept by management companies, or similar, and not used to meet the contractual obligations of the landlord, will be payment for the services provided by the management company, for acting on behalf of the landlord. These services are taxable at the standard rate of VAT.

(b) Not recharging costs borne on behalf of the landlord back to the landlord

As outlined in section 4(b), If you're a management company, or similar, and bear the initial cost of the goods or services acquired on behalf of the landlord, you can recover these costs from the landlord.

Some management companies however, are recovering input tax on bought-in supplies and then recharging them directly to the occupant exempt from VAT. They have been relying on ESC 3.18 to do so and this has led to their fees also being incorrectly treated as exempt.

(c) Supply of staff

As outlined at section 5, the recharge of staff or personnel costs by a management company, or similar, is a taxable supply to the landlord. In some cases, management companies have wrongly relied on ESC 3.18 to recharge staff or personnel costs direct to the occupant, exempt from VAT.

Revenue and Customs Brief 6/2018, VAT Information Sheet 7/2018

3.2 Option to tax

3.2.1 Disapplication

HMRC ruled that the sale of a property covered by an option to tax was taxable because the disapplication conditions of para.12 Sch.10 VATA 1994 were not met. The trader appealed. The facts were not in dispute: the property had been purchased for £1.14m in May 2001, and had opted to tax after the purchase. VAT had been paid to the vendor, who had also opted to tax, and it was reclaimed on the VAT return for the quarter to 06/2001.

The property was then leased to an optician's business that was connected to the owner. VAT was accounted for on the rentals; in 2007 following a VAT visit the owner became aware that the rentals should have been

exempt, and HMRC appear to have allowed repayment of the previous three years' worth of output tax without revisiting the original recovery.

In September 2014, the owner sold the property to an unconnected person, subject to the lease to the optician. The price on sale was £1.149m. The purchaser was not VAT registered and did not notify HMRC of an option to tax.

The judge pointed out that there is a potential circularity in the legislation: if the asset is no longer a capital item for the vendor, the OTT is not disapplied so the sale becomes taxable; but it then creates a capital item for the purchaser, which may affect the treatment of the sale. This is noted in Scammell on VAT on Construction, Land and Property as a long-standing anomaly on which there is no consensus of the correct approach.

The judge also noted that the purpose of the law is hard to discern or apply. HMRC's internal guidance states that it is an anti-avoidance provision, but its operation is mechanistic. The relevant law in para.12 states:

A supply is not, as a result of an option to tax, a taxable supply if:

a) the grant giving rise to the supply was made by a person ('the grantor') who was a developer of the land, and

b) the exempt land test is met.

"Developer" does not carry its usual everyday meaning and can include someone who has merely purchased the building. Para.13 defines a developer for the purposes of para.12 and the test is in fact whether the property is or will be a capital item in the hands of the grantor or of a person to whom the property is to be transferred.

This leads to the circularity. For the vendor, the CGS period had expired, so it was no longer a capital item. That would mean that the option would not be disapplied, and the transaction would be taxable. However, that would mean that a capital item would be created for the purchaser, which would potentially disapply the option again.

Judge Anne Scott analysed the legislation in line with the recent Tribunal decision in *PGPH Ltd*. She concluded that the "intention or expectation that the property will become a capital item in relation to any relevant transferee" was a subjective test, as to what would be a genuine or real, not a hypothetical, intention or expectation as at the time of the grant.

The taxpayer's counsel argued that the circularity could be avoided by "stopping" after considering the disapplication rules up to the point of the transaction. According to the words of the legislation, the trader knew that the property would be occupied for exempt purposes and would be a capital item in the hands of the purchaser. Therefore the option to tax should be disapplied.

The judge followed the circularity to its "logical" conclusion: "As a matter of fact, we find that at the date of the grant the appellant knew that the supply would not be, and could not be, taxable. Accordingly, given the terms of reg.113(1) of the VAT Regulations, and knowing that no other relevant expenditure was likely, the appellant could not have intended or expected that the property would become a capital item in the

hands of the purchaser.... we find that the disapplication provisions are not engaged and we must therefore dismiss the appeal for the reasons given."

So, because the taxpayer knew that the supply would not be taxable, it was taxable.

First-Tier Tribunal (TC06539). *David Moulsdale*

3.2.2 Belated notification

A dispute arose over whether a property company had opted to tax a property at an informal board meeting on 30 June 2016, as the director claimed, or had only considered the option when the property was sold in September. The director said that it was routine to opt to tax non-residential properties, and the minutes would only make specific reference to the matter if it was decided not to opt. She said that the company's management accountant had completed the option form online on 1 July and printed it for her to sign. She believed that it had been posted the next day, but no records of posting were kept because of the volume of correspondence dealt with by the office. HMRC did not receive the form, and on the basis of a lack of evidence, they ruled that the option had not been made on 30 June.

At the hearing, the appellant's representative demonstrated the process involved in completing the VAT 1614A form on HMRC's website. The form must be completed online and then printed. It was demonstrated that the date of signature included in the form is not allowed by HMRC's systems to be backdated: an error message is shown in red on the screen, stating that "The date must not be earlier than today", where "today" is the date on which the form is being completed. It was also demonstrated to the Tribunal that the form cannot be printed whilst there are errors outstanding on the form. The Tribunal was provided with a copy of the VAT 1614A form on which the date of signature was shown as 1 July 2016. For the appellant, it was submitted that given the restrictions imposed by HMRC's systems as to the signature date, the form could not have been completed later than 1 July 2016.

HMRC accepted that they had discretion to accept a belated notification, which meant that they had to have a good reason to refuse to accept one; however, they considered that the evidence provided by the appellant was insufficient to support a decision that the option had actually been exercised when the company said it was.

Judge Anne Fairpo found that the decision to reject belated notification, and the review decision confirming it, failed to take into account the evidence provided by the taxpayer. She found as a fact that the form had been completed on 1 July 2016, and that no reasonable officer could have concluded otherwise. The appeal was allowed.

First-Tier Tribunal (TC06669): *Rowhildon Ltd*

3.3 Developers and builders

3.3.1 Updated Notice

HMRC have updated their Notice *Buildings and construction* from the August 2016 version with minor corrections to paragraphs 7.6 and 8.4, and also clarification in para.2.1 that a "dwelling" can consist of more than one dwelling.

VAT Notice 708

3.3.2 VAT on damp-proofing products

HMRC have issued a Brief to make explicit that they do not regard damp-proofing products, such as paints, creams or gels, as energy-saving materials (ESMs) that qualify for the reduced rate of VAT. Consequently, with effect from 1 September 2018, HMRC will require businesses to account for VAT at the standard rate on all sales and applications of these products.

HMRC are aware that some businesses have used the lower rate following a FTT decision that a particular product was "insulating material" in *Safeguard Europe Ltd* (TC02543). HMRC have reviewed the VAT treatment of these products following the *Safeguard* decision. It has concluded that these products do not qualify as ESMs for the following reasons:

- the dominant purpose of these products is to water-proof exterior walls rather than improving thermal efficiency;
- there is no conclusive evidence that these products improve the thermal efficiency of brickwork;
- if such evidence became available, it is likely that any improved thermal efficiency would be incidental to the dominant purpose of the products which is water-proofing;
- the products are not normally described as insulators;
- the products are sold (or 'held out for sale') as water-and-damp proofing products and not insulators;
- the legislation refers to ESMs being "installed", which indicates that the legislation more naturally refers to typical insulators such as cavity wall insulation rather than the damp proofing products which are 'applied'.

HMRC does not regard damp proofing paints, creams or gels as ESMs. Therefore, the sale and services of applying these products to the walls of residential accommodation are standard rated for VAT purposes.

Revenue & Customs Brief 9/2018

3.3.3 Charitable annexe

HMRC ruled that certain works carried out at a Catholic church were standard rated. The church had been remodelled following an amalgamation of a number of churches. The works had involved adding an upper storey, removing a dividing wall that had been built in the 1970s to separate the worship area from an area used as a church hall, reinstating

the main entrance, and constructing an extra space at the side of the church for use as a hall in the future.

The Tribunal described the new construction as follows: "The Hall occupies a site at the corner of the Church. To accommodate the Hall parts of two walls of the Church (and the accompanying roof) were demolished; that left the internal space open and this was infilled with a new internal wall (which then formed the wall between the Hall and the main church building). The Hall occupies around 120 square metres, around 40 square meters of which overlaps the site of the demolished part. The Hall comprises a meeting room, a kitchen, and toilets (including disabled facilities). The main entrance to the Hall is direct from outside (not through the main church building); access from the main church building is possible through lockable double doors. The central heating thermostat for the Hall is located in the Hall; the Hall is served by a boiler separate from the boiler serving the main church building; as part of the works the Hall boiler was installed by the contractor adjacent to the other boiler in the Sacristy store (in the main church building); that location was unsuitable and (in January 2018) it was replaced by a boiler located in the Hall's kitchen."

The key argument for the appellant was that the church had followed the guidance in Notice 708 and concluded that the Hall was an annexe capable of functioning independently, and it therefore qualified for zero-rating. HMRC considered that the Hall constituted an alteration, enlargement or extension of the existing building, and thus excluded from zero-rating by Note 16. In the alternative, the Hall was not a qualifying annexe within Note 17. HMRC accepted that the Hall was used for a relevant charitable purpose, and that it had a separate main entrance. However, the Hall was not capable of functioning independently from the existing building. In *Chelmsford Sixth Form College* it was held that the new building could not function independently as it shared a heating system, and the boiler was in the main building although each building was thermostatically controlled separately. Here, the Hall boiler had been located in the main church building at practical completion of the works (in November 2016), and was moved to the Hall only later, in January 2018.

The judge considered that the first step was to carry out an objective examination of the physical characteristics of the building as it was before and as it was after completion of the works, having regard (inter alia) to similarities and differences in appearance, the layout and how the building or buildings are equipped to function; the terms of planning permissions, the motives behind undertaking the works and the intended or subsequent actual use are largely irrelevant. The second step was to ask whether (as at the date of supply) the completed works amount to the enlargement of or extension of the existing building, or the construction of an annexe to the original building. In deciding whether the construction was an annexe, it was permissible to make a wider enquiry than just the physical appearance and functionality, to determine if the construction was an adjunct or accessory or supplementary structure.

This was the key: because the project had enlarged the worship space to fill the whole of the existing building, the Hall was added as a supplementary structure to accommodate the non-devotional activities

separately from the worship areas. The judge concluded that the Hall was an annexe.

The question was then whether it was capable of functioning independently. Although the Hall boiler was originally located in the church, it was nevertheless always a separate boiler, and it was controlled from inside the Hall. Taking all the facts together, the judge was satisfied that the tests in Note 17 Group 5 Sch.8 VATA 1994 were satisfied, and allowed the appeal.

First-Tier Tribunal (TC06692): *Roman Catholic Diocese of Westminster*

3.3.4 Article

In an article in *Taxation*, Rob Durrant-Walker and Alex Millar discuss the concept of a "dwelling" in relation to CGT and VAT. When advising on transactions in residential property the concept of dwelling is important. There is a degree of consistency between the taxes but the definition varies in places. It is important to distinguish between dwellings and other types of buildings used for residential purposes (such as residential accommodation for children or a care home for older people), to know when to apportion, and when there is a cliff edge approach to the tax calculations.

Taxation, 6 September 2018

3.4 Input tax claims on land

3.4.1 DIY claim (third time of asking)

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

The individual asked for a review and subsequently appealed to the FTT (TC05128), arguing that his intention had changed during the course of the project and the conditions had been removed. He now occupied the property as his family home. He had never actually used it for any business.

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

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

The individual appealed to the Upper Tribunal, where he represented himself (late 2017). The judges analysed the FTT's reasoning and decisions on the different conditions of Note 2 Group 5 Sch.8. The FTT had appeared to believe that Note 2(c) was not satisfied – however, the

restriction did not amount to a prohibition on separate use or disposal, as the FTT had concluded, and the conclusion that retrospective removal of that condition was somehow relevant to Note 2(c) was a mistake.

Turning to Note 2(d), the judges noted that there is a slight difference between Group 5 (which specifically requires construction in accordance with the statutory planning consent) and s.35(1)(b), which requires that carrying out of the works must be lawful. There is an overlap, because non-compliance with the consent would result in unlawful works, but the UT considered that s.35(1)(b) imposed wider conditions.

The FTT did not record any findings of fact in relation to a change of intention by the appellant. It appeared that he had decided to occupy the cottage as a permanent home during the early stages of construction, and that intention was eventually realised. The FTT should have considered whether and when that intention arose, and then consider in the light of that conclusion whether the construction had been carried out in accordance with the statutory planning consent.

Further, the FTT had misunderstood the condition in s.35(1)(b) that the works should not be carried out in the course or furtherance of a business. This issue had been decided in the appellant's favour on the grounds that no business had ever been carried on; however, that was not the requirement. Once again, the FTT ought to have considered the appellant's intentions at the time the construction was carried on, and then decide whether that constituted a business for VAT purposes.

The UT was not in a position to make the necessary findings of fact. The appeal was allowed, but the case would be remitted to a differently constituted FTT for a rehearing.

The new FTT considered the matter afresh, setting out the history of the construction project. In particular, construction started in late May 2014, and the application to remove the "tourism only" restriction was submitted to the local authority in March 2015. The appellant represented himself again, and cited a number of precedents in support of his argument.

The judge did not agree with his interpretation of the planning consent, which clearly contemplated business use. However, she also disagreed with HMRC that the planning consent imposed a requirement to run a business; it permitted use as holiday accommodation or as a private residence. The judge described this as an "occupancy condition".

The condition "otherwise than in the course or furtherance of a business" meant that some private use was not enough to allow the claim; for a refund to be available under s.35, the construction must not have any connection with an existing or planned business.

The question to be established was whether the appellant ever had an intention to carry on a business, and if so, whether and when that intention changed. The judge was satisfied that it was possible for a DIY claimant to recover VAT after such a change of intention – the initial intention did not rule out the claim for all time.

After considering the history of the project and the evidence presented by the appellant to the Tribunal, the judge made a number of findings of fact. Most significantly, the appellant had a business purpose when the construction started, and had not completely put this aside by the time the

construction finished. As a result, HMRC were correct to refuse the claim. The appeal was dismissed.

First-Tier Tribunal (TC06711): *Richard Akester*

3.5 Other land problems

Nothing to report.

4. INTERNATIONAL SUPPLIES

4.1 E-commerce

4.1.1 Changes to MOSS

Two changes are being made to MOSS from 1 January 2019. The first is to implement the Commission's relaxation that businesses whose total supplies of digital services across the EU below a €10,000 (£8,818) threshold may apply the VAT rules of their home country, rather than those of the country where their customers are located.

www.gov.uk/government/publications/vat-changes-to-the-supply-of-digital-services-2019

The second change relates to non-established taxable persons (NETPUs). HMRC issued for consultation a draft *VAT (Special Accounting Schemes) (Supplies of Electronic, Telecommunication and Broadcasting Services) Order 2018*. Currently, NETPUs who are registered for VAT in the UK are not permitted to use MOSS. The proposal is that they will, if they provide digital services to consumers, be allowed to register under the non-Union MOSS from 1 January 2019.

www.gov.uk/government/consultations/draft-legislation-vat-supplies-of-electronic-telecommunication-and-broadcasting-services-orders-2018

A Tax Information and Impact Note covering this instrument has also been published on the website.

4.1.2 Infringement proceedings against UK on VAT MOSS

The EU Commission has sent a reasoned opinion to the UK, requesting the UK to share with other member states the bank account details of traders registered for the VAT mini one-stop-shop, in order to comply with the EU administrative cooperation regulation. The Commission issued a letter of formal notice in January.

The Commission points out that at the moment, Member States who want to refund taxable persons in the UK have to collect additional information on a case-by-case basis, which is burdensome and delays refunds.

europa.eu/rapid/press-release_MEMO-18-4486_en.htm

4.2 *Where is a supply of services?*

4.2.1 Chequers proposal

In July the government published a White Paper setting out proposals for the future relationship between the EU and the UK. It does not include a great deal of detail on VAT, and is subject to so much controversy and opposition that it seems better to wait for more concrete material before commenting on what is likely to happen.

www.gov.uk/government/publications/the-future-relationship-between-the-united-kingdom-and-the-european-union

There is an article by Tarlochan Lall discussing the proposals in *Tax Adviser* for September 2018.

Tax Adviser, September 2018

4.2.2 No-deal Brexit

The technical note described in more detail below at 4.3.1 also has a section on supplies of services. As expected, there would be fewer consequences for supplies of services in a "no-deal Brexit": the place of supply rules will operate much as they do now, when there is not a great deal of difference between buying or selling services across the UK border or across the EU border.

One interesting comment is "For UK businesses supplying insurance and financial services, if the UK leaves the EU without an agreement, input VAT deduction rules for financial services supplied to the EU may be changed. We will update businesses with more information in due course." This shows that they are considering extending the Specified Supplies Order to cover such supplies to EU customers. However, there is no mention of the possibility that the old "Schedule 5" services (e.g. accountancy, legal) will become outside the scope if supplied to EU non-business customers.

Suppliers of digital services to EU consumers will no longer be able to use the UK MOSS. They will have to register for the non-Union MOSS in another Member State, or register separately with the authorities in each country where they make supplies.

The problem of TOMS is mentioned, but no detail is given beyond that "HMRC has been engaging with the travel industry and will continue to work with businesses to minimise any impact."

https://tinyurl.com/ybpv7k85

4.2.3 Reinvoiced expenses

In March 2009 a German company (the first appellant, TG) registered for VAT in Portugal as a non-resident person without a fixed establishment in the country for the purpose of carrying out a one-off transaction, being the acquisition of shares. A month later a branch of TG (the second appellant, TS) was registered for VAT in Portugal as a non-resident entity with a fixed establishment in the form of a branch.

TG went on to form a European Interest Grouping with a Portuguese company. The EIG was allocated another Portuguese VAT number. The

objective of the EIG was to implement the planned extension of a natural gas terminal in Portugal. The terminal belonged to another Portuguese company.

EIGs are subject to special arrangements in Portugal. An EIG is required to pass on to its constituent parties, in the proportions agreed in the articles of association, the profits made or losses incurred during an accounting year. Those profits or losses are taken into account in the taxable income of the members of the EIG with regard to income tax.

The articles of association of this EIG determined the other owner's contribution at 85% and that of TG at 15%. In addition, the EIG's internal agreement and rules attributed 64.29% of the obligations and liabilities to TG, with the remaining 35.71% being attributed to the co-owner.

In May 2009, TS concluded a subcontract with the EIG. According to the contract, the EIG recharged all the invoices resulting from this subcontract (and also from the other member of the EIG) to the owner of the terminal. For the purposes of the attribution and reinvoicing of its costs, the EIG used the tax reference of TS, not TG. The EIG therefore referred, in the debit notes which it sent to TS, to the tax identification number of TS and charged VAT on that basis. The EIG attributed 64.29% of its costs to TS, which deducted the VAT paid on the debit notes issued by the EIG.

Following a tax audit, the tax authority ruled that TS and TG were two different entities. TS was not a member of the EIG, so the EIG could not attribute costs to it and it could not deduct the VAT relating to those costs. TS appealed, and questions were referred to the CJEU.

The CJEU referred to precedent decisions on branches and head offices. Although it is not spelled out in the factual background section of the decision, it is clear from the discussion that TS is the Portuguese branch of TG – they are a single legal entity, even though they have different VAT numbers in Portugal.

It therefore followed that the tax authority would be required to allow deduction of input tax where the substantive conditions of art.168 were met, in particular that the costs had been incurred by a taxable person acting as such. It would be for the national court to determine whether the other conditions for deduction were met, but it was not permissible for a member state to deny input tax deduction merely on the grounds that the invoices should have been raised to one VAT number rather than the other, where both belonged to the same legal entity.

The court also noted the emphasis in the *Welmory* decision (Case C-605/12) on the use of "place of establishment" as the first criterion for determining the place of B2B supplies in art.44 PVD. This was because it offered legal certainty, being an objective criterion that was simple and practical. By contrast, the connection to the taxable person's fixed establishment, referred to in the second sentence of art.44, is a secondary point of reference which is an exception to the general rule.

CJEU (Case C-16/17): *TGE Gas Engineering GmbH – TGE Sucursal en Portugal v Autoridade Tributaria e Aduaneira*

4.2.4 Changes to specified supplies

A draft Statutory Instrument (*The Value Added Tax (Input Tax) (Specified Supplies) (Amendment) Order 2018*) has been issued to prevent future recovery of input tax in circumstances similar to those in the *Hastings Insurance* case. Intermediary services will be excluded from the specified supplies that confer the right of input tax recovery where they are supplied to persons outside the EU, if the final customer (the insured) belongs in the UK.

The wording changes as follows:

Present version

Services

(a) which are supplied to a person who belongs outside the member States;

(b) which are directly linked to the export of goods to a place outside the member States; or

(c) which consist of the provision of intermediary services within the meaning of item 4 of Group 2, or item 5 of Group 5, of Schedule 9 to the Value Added Tax Act 1994 in relation to any transaction specified in paragraph (a) or (b) above,

provided the supply is exempt, or would have been exempt if made in the United Kingdom, by virtue of any item of Group 2, or any of items 1 to 6 and item 8 of Group 5, of Schedule 9 to the Value Added Tax Act 1994.

Revised version

Services

(a) which are supplied to a person who belongs outside the member States;

(b) which are directly linked to the export of goods to a place outside the member States; or

(c) which consist of the provision of intermediary services within the meaning of item 4 of Group 2, or item 5 of Group 5, of Schedule 9 to the Value Added Tax Act 1994 in relation to any transaction specified in paragraph (a) or (b) above,

provided the transaction specified in paragraph (a) or (b) above is an exempt supply, or would have been an exempt supply if made in the United Kingdom, by virtue of item 1 of Group 2, or any of items 1 to 4, 5A, 6 and 8 of Group 5, of Schedule 9 to the Value Added Tax Act 1994.

The effect of that appears to be that intermediary services (covered by (c)) are only eligible for input tax credit if they relate to an underlying supply to a person belonging outside the member states (covered by (a) and (b)).

In a written ministerial answer on 19 July, the Financial Secretary to the Treasury, Mel Stride MP, commented that further steps would be taken to counter tax avoidance through "offshore looping".

www.gov.uk/government/publications/draft-legislation-amendment-of-the-vat-input-tax-specified-supplies-order-1999

4.3 International supplies of goods

4.3.1 No deal Brexit

The UK government has published a number of technical notes about the possible consequences of a “no-deal Brexit”. The notes emphasise that this is merely contingency planning: the government hopes and expects to reach a deal by 29 March 2019.

The technical note “VAT for businesses if there’s no Brexit deal” does not give very much new or detailed information, but the following are points of interest:

If the UK leaves the EU without an agreement, the government will introduce postponed accounting for import VAT on goods brought into the UK. This means that UK VAT registered businesses importing goods to the UK will be able to account for import VAT on their VAT return, rather than paying import VAT on or soon after the time that the goods arrive at the UK border. This will apply both to imports from the EU and non-EU countries.

Goods arriving as parcels coming into the UK will be chargeable to VAT without the benefit of Low Value Consignment Relief. For parcels valued up to and including £135, a “technology-based solution” will allow VAT to be collected from the overseas business selling the goods into the UK. Overseas businesses will charge VAT at the point of purchase and will be expected to register with an HMRC digital service and account for VAT due. The online service will be available for businesses to register in early 2019, prior to 29 March.

On goods worth more than £135 sent as parcels VAT will continue to be collected from UK recipients in line with current procedures for parcels from non-EU countries in accordance with the guidance in HMRC Notice 143. VAT will also continue to be collected in line with current procedures for all excise goods sent as parcels and potentially in cases where their supplier is not compliant with HMRC’s new parcels policy. HMRC is working with the relevant industry stakeholders and will provide further information in due course.

The NOVA system will continue to apply to vehicles being brought into the UK, and DVLA will continue to refuse to register a vehicle for use on UK roads unless there is evidence that the correct VAT has been paid.

Exporters will see the following changes:

- supplies to EU businesses will still be zero-rated, but Sales Lists will not be required (the more significant changes will apply to the purchaser, who will now be buying an import);
- supplies to EU consumers will no longer be subject to the distance selling rules, so they will in all circumstances be zero-rated on export (subject to the normal rules on proof of transport out of the country) – the responsibility for paying the VAT will fall on the purchaser in line with personal imports at the moment;

There are large gaps in the information, covered by such comments as “Individual EU member states may have different rules for import VAT for non-EU countries and import VAT payments may be due at the border

when importing goods. UK businesses should check the relevant import VAT rules in the EU Member State concerned."

There will be no change in the liability to register of a UK trader holding goods for sale in another Member State, but the detailed procedures may be different for a non-EU business.

UK businesses should still have access to the EU VAT number validation service to check the validity of EU business VAT registration numbers and HMRC is developing a service so that UK VAT numbers can continue to be validated.

The technical note comments on the work that is being done on the problem of Irish and Northern Irish businesses trading across the land border, but says "we will provide more information in due course" and "We would recommend that, if you trade across the land border, you should consider whether you will need advice from the Irish government about preparations you need to make."

The overall comment "You should consider whether you need separate professional advice before making specific preparations" begs the question of where the professional advisers will get any better information than this in order to provide more detailed advice.

https://tinyurl.com/ybpv7k85

A separate technical note has been issued on "Trading with the EU if there's no Brexit deal" dealing with the likely changes to customs and excise procedures.

If the UK left the EU on 29 March 2019 without a deal there would be immediate changes to the procedures that apply to businesses trading with the EU. It would mean that the free circulation of goods between the UK and EU would cease.

For businesses trading with the EU, the impacts would include:

- businesses having to apply the same customs and excise rules to goods moving between the UK and the EU as currently apply in cases where goods move between the UK and a country outside of the EU (customs duty may also become due on imports from the EU – see the separate 'Classifying your goods in the UK Trade Tariff if there's a no Brexit deal' technical notice). This means customs declarations would be needed when goods enter the UK (an import declaration), or when they leave the UK (an export declaration). Separate safety and security declarations would also need to be made by the carrier of the goods (this is usually the haulier, airline or shipping line, depending on the mode of transport used to import or export goods).
- the EU applying customs and excise rules to goods it receives from the UK, in the same way it does for goods it receives from outside of the EU. This means that the EU would require customs declarations on goods coming from, or going to, the UK, as well as requiring safety and security declarations.
- for movements of excise goods, the Excise Movement Control System (EMCS) would no longer be used to control suspended movements between the EU and the UK. However, EMCS would continue to be used to control the movement of duty suspended

excise goods within the UK, including movements to and from UK ports, airports and the Channel tunnel. This will mean that immediately on Importation to the UK, businesses moving excise goods within the EU, including in duty suspension, will have to place those goods into UK excise duty suspension, otherwise duty will become payable.

After the UK leaves the EU, in the event of a 'no deal' scenario, businesses importing goods from the EU will be required to follow customs procedures in the same way that they currently do when importing goods from a country outside the EU. This means that for goods entering the UK from the EU an import declaration will be required, customs checks may be carried out and any customs duties must be paid.

Before importing goods from the EU, a business will need to:

- register for an UK Economic Operator Registration and Identification (EORI) number. Businesses do not need to do anything now. There will be further information available later in the year. For those businesses that sign up for the EU e-mail updates, they will be contacted when this service becomes available.
- ensure their contracts and International Terms and Conditions of Service (INCOTERMS) reflect that they are now an importer.
- consider how they will submit import declarations, including whether to engage a customs broker, freight forwarder or logistics provider (businesses that want to do this themselves will need to acquire the appropriate software and secure the necessary authorisations from HMRC). Engaging a customs broker or acquiring the appropriate software and authorisations form HMRC will come at a cost.
- decide the correct classification and value of their goods and enter this on the customs declaration.

Customs duties, and excise duties on excise goods, will have to be paid "at the docks" or through duty deferment (even if the VAT will be payable on the next VAT return), unless the goods are entered into a suspension scheme.

Similar considerations apply to exporters, who will need an EORI number, changes to INCOTERMS and procedures for submission of export declarations. They may also need export licences for certain specific types of goods.

The note contains brief descriptions of various customs procedures that may mitigate the impact of the withdrawal of free circulation within the EU, including customs warehousing, inward processing, temporary admission and authorised use.

https://tinyurl.com/yavybzy3

4.3.2 Commission comments on Brexit

The European Commission has published the latest in its series of 'stakeholder' notices setting out its view of the consequences of UK withdrawal in the area of customs and taxation. The latest notice

concerns EU VAT rules and is intended to complement the notice on customs and indirect taxation published on 31 January 2018.

The new notice is divided into sections setting out the application of EU rules to the UK as a 'third country' in respect of:

- supplies of goods;
- supplies of services;
- submission of returns through the mini one-stop shop scheme (VAT MOSS); and
- VAT refunds.

Each section now contains specific advice to taxable persons on 'preparing for a withdrawal without withdrawal agreement'.

ec.europa.eu/taxation_customs/uk_withdrawal_en

4.3.3 Exemption on importation

A Lithuanian company imported fuel from Belarus between 2010 and 2012. It was entered into a customs procedure for excise goods that would be supplied on to a customer in another EU Member State, which entitled the company to exempt the import from VAT under PVD art.143(1)(d) (which cross-refers to the onward supply being exempt under art.138). The company made import declarations specifying the VAT registration numbers of its intended customers in Poland, Slovakia and Hungary.

The fuel was supplied on to customers "ex works", meaning that the supplier was only obliged to hand over the fuel to the purchasers in Lithuania. Confirmation of transactions and transport was sent by e-mail. In 2012, the Lithuanian authorities carried out an enquiry and noted some discrepancies in the VAT numbers, which were corrected. In 2013, the tax authorities in the other three countries notified suspicions of fraud in relation to the customs procedure being used for this fuel oil. They could not certify that the purchasers had received the goods, and also noted that the purchasers had not accounted for VAT on the arrival of those goods.

The Lithuanian authorities carried out a further check, and concluded that the goods had left Lithuania and there was no evidence that the company had acted negligently or imprudently. However, following yet another check carried out in 2014 and 2015, the authorities concluded that the company had not supplied the fuel to the customers shown on the import declarations, or had not shown that the fuel had been supplied within the meaning of the VAT Directive to the persons whose names were stated on the VAT invoices.

Questions were referred to the CJEU on a number of issues:

1. whether the fact that one customer's VRN had been included on the import declaration, but the goods had been despatched to a different customer, was enough on its own to deny exemption of the importation under art.143(1)(d);
2. whether the electronic documents were sufficient evidence of transportation to another Member State;

3. whether a tax authority could deny exemption if the right of disposal was transferred to customer not directly, but through other persons (transport undertakings and tax warehouses);
4. whether the Lithuanians' apparent different interpretation of the concept of "transfer of right of disposal" under art.143 (exemption on importation) and art.167 (right of deduction of input tax) was permitted;
5. whether the principle of "good faith" as established in the *Teleos* case, protecting a taxpayer's right to exempt a despatch under art.138, extended to exempting the related import under art.143;
6. whether the Lithuanians were entitled to make a presumption of "means of knowing of connection to fraud" where the undertaking communicated with contractual partners only by electronic means;
7. whether the competent authorities in other Member States were required to provide relevant information about transfers which it could access, if the taxpayer could not obtain it by other means.

In answering the first question, the CJEU drew the familiar distinction between the "substantive" and "formal" conditions for exemption. The VRN of the customer was a formal condition. It was therefore not possible to refuse exemption only on the ground that one VRN was shown on the import declaration and another on the despatch. Denial of exemption could only follow if that discrepancy indicated knowledge of fraud; a penalty for breach of a mere formal requirement should be administrative in nature and proportionate to the seriousness of the infringement.

The answer to the second question was that documents showing despatch, not to a purchaser but to a tax warehouse in another Member State, could be acceptable proof that goods had left the country. The other documents considered could also be taken into account as relevant evidence.

The third and fourth questions were considered together. The concept of "supply of goods" had to be interpreted consistently. Where the right to dispose of goods as owner was transferred indirectly from the trader to a customer via a transport undertaking or tax warehous, the tax authorities could not deny the treatment that followed – exemption of the import under art.143 and exemption of the despatch under art.138.

The fifth and sixth questions were also answered together. The principle of the *Teleos* case applied: an importer acting in good faith cannot be refused the right to the VAT exemption on importation where the conditions for the exemption of the subsequent intra-Community supply are not satisfied, because of tax evasion on the part of the purchaser, unless it is shown that the importer knew or ought to have known that the transaction was involved in tax evasion committed by the purchaser and did not take all reasonable steps in his power to avoid participation in the evasion. The mere fact that the importer and the purchaser communicated by electronic means of communication cannot allow it to be presumed that the importer knew or could have known that he was participating in tax evasion.

All those answers were favourable to the taxpayer. The answer to the last question was less so: it is up to the trader to provide evidence to support a

claim for exemption, and the tax authorities are not obliged to collect information to which only the public authorities have access. It is not clear what effect that will have on the outcome of the proceedings when they return to the Lithuanian court.

CJEU (Case C-108/17): *UAB 'Enteco Baltic' v Muitinės departamentas prie Lietuvos Respublikos finansų ministerijos*

4.3.4 Sales out of bond

A company appealed against assessments for a total of £733,940 in relation to sales that it claimed had been made to cash customers from bonded warehouses in France. It had received the cash and banked it in the UK, but claimed that its customers had used cash couriers to transport the money. HMRC decided that this was not credible.

HMRC did not allege fraud or "the means of knowledge", but simply argued that the company had not discharged the burden of proof to show that the goods were outside the UK when supplied. In HMRC's view, the goods were part of an "inward diversion fraud", in which goods are recorded as being sold at low French duty rates, but are in fact being smuggled back to the UK and sold for cash to evade UK VAT and duty.

Judge Sarah Falk examined the evidence, including witness statements from the owner of the business and reports from the French authorities. She concluded that in respect of some of the sales, where there were records from the warehouses that supported the assertion that the goods were present at the time payment was received, she concluded that the burden of proof was satisfied and the appeal was allowed to that extent. In respect of other goods, where the evidence was that the goods had left the warehouse before receipt or where there was insufficient evidence, she concluded that the company had not satisfied the burden of proof, and could not dislodge the assessments. She also dismissed an argument that one of the assessments was out of time, because it had been issued within one year of the officer having sufficient information to justify it.

The appeal was allowed in part.

First-Tier Tribunal (TC06577): *Dale Global Ltd*

4.3.5 Evidence of export

A company appealed against HMRC's refusal to allow credits totalling £35,164 for its return periods 01/13 and 04/13. The claims related to four sales orders of various car parts to customers in other EU member states.

HMRC formed the initial view that there was insufficient evidence of despatch; by the time of the hearing, they had decided that the goods did not exist. Judge Christopher McNall noted that HMRC's actual decision was the subject of the appeal, and that was based on the lack of evidence; although their skeleton argument referred to the current belief that the goods had not existed, that was not part of the dispute that lay before the Tribunal. Accordingly, the Tribunal had to consider whether the decision to refuse the claim was reasonable based on the evidence available at the time.

There were significant problems with disclosure of documents at successive hearings which started in 2017. HMRC introduced new

documents into the bundles without notifying the appellant; the judge ordered them to be removed and struck out any questions and answers that related to them.

The judge considered the director who gave evidence to be a "dynamic individual" who knew a great deal about his core business of importing and selling premium cars. However, his evidence about the disputed transactions was much less impressive. His argument was that the totality of the evidence presented was enough to meet the statutory requirements, but the judge did not agree. On the judge's understanding of his jurisdiction, he could not fault the decision of the officer that the evidence was inadequate; if he was wrong on his jurisdiction, he considered in the alternative that the law had not been complied with. The appeal was dismissed.

First-Tier Tribunal (TC06612): *Shaks Specialist Cars Ltd*

A similar problem arose in another case in which HMRC argued that there was insufficient evidence of export of cars to the Republic of Ireland, and that the trader did not take all reasonable steps to prevent its own participation in a tax fraud. The two separate arguments were referred to in the decision as the "Lack of Evidence denial" (based on the law) and the "Mecsek denial" (based on the decision of the CJEU in *Mecsek-Gabona Kft* Case C-273/11). The trader had the burden of proof on lack of evidence, and HMRC had the burden of proof on means of knowledge.

The Mecsek denial related to 38 vehicles sold in VAT period 10/12; 40 in 01/13; 27 in 07/12, and 22 in 04/13. HMRC submitted that the evidence clearly established that there had been substantial VAT losses as a result of the vehicles in the appeal being sold to a series of missing or defaulting traders in the Republic of Ireland. The evidence also showed that those losses resulted from fraud, including the presence of some of the vehicles in contemporaneous parallel supply chains. The necessary connection to that fraud was plain because the appellant sold the vehicles to the missing or defaulting traders; and the appellant had the means of knowing that this connection existed. The list of 14 factors that suggested the appellant should have recognised that this was not proper commercial trading appeared damning, although the appellants did have a response to each one.

The judge identified the main factors as:

(1) Lack of knowledge and due diligence in relation to customers

(2) Rapid rise in turnover

(3) Profit per sale

(4) Third party payments

(5) Awareness of risk of fraud

(6) Attempted registration of sales company

(7) Absence of disclosure

(8) Significant errors and discrepancies in sales and dispatch documents

The judge considered the arguments about these in detail, and concluded that (6) and (7) did not carry much weight, and (5) should be discounted because there was little knowledge of MTIC fraud in the car sector at the

time. However, the other factors, taken together in the context, were enough to satisfy the balance of probabilities that the appellant knew that the sales were connected to fraud, and failed to take all reasonable steps in its power to prevent its own participation in that fraud.

The judge also concluded after further examination that the "Lack of Evidence denial" also applied: the appellants had not complied with the statutory requirements of Notice 725. The judge noted that there were documents where the delivery address bore no relation to the buyer; where there was no address on the delivery note; where there was no delivery note at all, or an unsigned note, or a note signed illegibly. There was also in some cases troubling evidence of delivery before dispatch or of multiple deliveries.

The appeal was dismissed on both of the grounds.

First-Tier Tribunal (TC06652): *Taylors Service Centres Ltd*

4.3.6 Export conditions

A company appealed to the FTT (TC05378) against assessments for just over £200,000 in relation to transactions which had been zero-rated as exports to the Republic of Ireland. The trader had been registered for some time as a "vehicle consultant"; he had been visited and had discussed due diligence with officers. The disputed transactions involved purchases of cars from Germany, Cyprus and Malta, which were then sold to business customers registered in Eire. HMRC were not satisfied that the evidence was sufficient to show that the goods had left the UK as stated by the trader.

The appellant argued that the cars were in fact not in the UK at the time that the invoices were raised to the customer. This meant that UK VAT was not due, and the Tribunal should not consider whether VAT had been correctly accounted for elsewhere, because that was not relevant to the question before it. Alternatively, the evidence was sufficient to show that the goods had left the UK; or, under *Teleos*, the trader should be entitled to zero-rating on the basis of having done everything reasonable to ensure that the goods had left the UK.

The Tribunal was not satisfied that the evidence proved that the goods were outside the UK at the time of supply. Even if they were, the Tribunal considered that the place of supply would still be the UK under s.7(7) VATA 1994: the place of supply cannot be determined under the preceding provisions and the Appellant's supply involved the removal of the goods from the UK. The supplies were not therefore made directly from Germany, Cyprus and Malta. Although the facts were not the same as those in the *Euro Tyre Holdings* case, the Tribunal considered its conclusion was strengthened by that precedent.

The evidence was not sufficient to show that the goods had left the UK. The Tribunal did not accept that *Teleos* applied, because the trader had not taken all reasonable steps to be satisfied that the documents reflected what had happened: his due diligence was very poor. In any case, *Teleos* was different in that it involved a change of position by HMRC, who had originally accepted documentation and then sought to assess on the basis that it was forged. The appeal was dismissed.

The company appealed to the Upper Tribunal, disputing the FTT's decisions on place of supply (including the relevance of s.7(7)). The company also limited its appeal to some of the vehicles concerned, having accepted that some were in the UK at the time of supply.

The UT disagreed with the fundamental premise of the company's case: that if its supplies took place at a time when the relevant vehicles were outside the UK, the place of supply of those vehicles was outside the UK and no UK VAT could be charged on them. If that were to be upheld, there would have been successive supplies from the suppliers in Malta and Cyprus to ICW, and then by ICW as intermediate supplier to its customers. That led to a consideration of *EMAG Handel Eder* (Case C-245/04), *Euro Tyre Holding BV* (Case C-430/09) and *VSTR* (Case C-587/10) on successive intra-community transactions.

Where there has been no acquisition in another Member State on which VAT has been paid by virtue of the laws of that other Member State (to which s 13(4) may apply), s.13(3) VATA 1994 treats the acquisition by a person who has used their UK VAT identification number for the purpose of the acquisition of the goods as an acquisition of the goods in the UK. The result is that, in circumstances where, as in this case, ICW acquired the vehicles from its Maltese and Cypriot suppliers using its UK VAT identification number, and did not inform those suppliers that the vehicles would be sold on before the goods left Malta or Cyprus respectively, the intra-Community transports from Malta and Cyprus are ascribed to the supplies by the Maltese and Cypriot suppliers, and not to ICW. That is the case whether or not it can be established that ICW's own supplies took place before the vehicles left Malta or Cyprus, as the case may be. ICW is treated for VAT purposes as having acquired the vehicles in the UK, and there is no taxable acquisition by ICW in Malta or Cyprus. It is equally the case that, the intra-Community transport having been ascribed to the supplies by the Maltese and Cypriot suppliers respectively and there having in each case been a deemed acquisition by ICW in the UK, the place of ICW's supplies must be deemed to have been in the UK (art.31 PVD as confirmed by EMAG).

The UT did not agree with the FTT that s.7(7) had any relevance, but that did not change the decision. The company's argument that s.7(7)(b) operated to take the place of supply out of the UK was also misconceived.

The FTT's conclusions on the location of the Cyprus vehicles at the time of supply was unsatisfactory, as the decision did not fully explain the basis of the conclusion. However, the UT's decision on the law on place of supply meant that it was not necessary to remake or remit the decision. The criticisms of the decision in relation to the location of the Maltese vehicles were rejected. For these reasons, the company's appeal was rejected.

Upper Tribunal: *I C Wholesale Ltd v HMRC*

4.3.7 Personal export scheme

A car dealer supplied a car to a customer resident in Jersey. He rang HMRC to enquire how the Personal Export Scheme could be used to zero-rate the supply. HMRC sent a form VAT 410 which was completed and submitted. However, HMRC refused the claim to zero-rate the supply

"because the PES is a pre-approval scheme and the car had already been supplied when the scheme was applied for."

The law is in SI 1995/2518 regs.132 and 133 and in Public Notice 707. Both sides accepted that mistakes had been made in the processing of the application, but HMRC said that the only remedy available was through their complaints department – the Tribunal could not require zero-rating where the law was not satisfied.

The judge set out the relevant requirements of the law as follows (with appropriate paragraphs of PN 707 referred to in brackets):

(1) The supplier must make sure that the customer is entitled to use the scheme (8.3);

(2) The supplier must give the customer a copy of sections 1 – 7 of PN 707 and form VAT 410 (8.3);

(3) Once the customer has completed form VAT 410, the supplier must send the blue copy of the form (which is carbonated and has 4 different coloured copies) to HMRC's personal transport unit (PTU) at least two weeks before the date of delivery of the vehicle (8.4);

(4) If the form is completed accurately, HMRC will send the supplier VAT form 412 (8.4);

(5) The supplier must not zero rate the sale in their records until they have received form 412 (8.4);

(6) If the supplier needs to supply the vehicle urgently, the PTU can phone the supplier with the approval number, but only after they have received:

(a) the completed form 410 (8.4); and

(b) a Certificate for Urgent Delivery, which must be sent at least three working days before the date of delivery of the vehicle (10.3).

The judge did not agree with HMRC that the Notice was clear, and commented specifically that the absence of the requirement for pre-approval in the checklist for suppliers in paragraph 13 is unhelpful. However, this did not alter the conditions. The company had not complied with them because form 410 was not sent to HMRC until after the export had been completed, and form 412 had never been received; the company had not made an application for urgent delivery.

The Tribunal had no jurisdiction to take into account HMRC's mistakes or the "legitimate expectations" that might arise from misleading comments on the VAT Advice Line. The judge therefore made no findings in relation to that question. The appeal had to be dismissed.

First-Tier Tribunal (TC06721): *Hofmanns Henley Ltd*

4.3.8 Brexit bills

The *Taxation (Cross-border Trade) Act 2018* received Royal Assent on 13 September. The purpose of the Act is to allow the government to create a standalone customs regime when the UK leaves the EU and provide for amendment of existing VAT and excise legislation.

Provisions are made to impose and regulate a duty of customs by reference to the importation of goods into the UK, to confer a power to

impose and regulate a duty of customs by reference to the export of goods from the UK, to make other provision in relation to any duty of customs in connection with the withdrawal of the UK from the EU, and to amend the law relating to value added tax, and the law relating to any excise duty on goods, in connection with that withdrawal, and for connected purposes.

Taxation (Cross-border Trade) Act 2018

The House of Lords library published a briefing paper on the Bill before its second reading in the House on 4 September. It explains that the Bill allows for a range of outcomes in the Brexit negotiations, including the UK leaving without a transition period or negotiated outcome.

The Delegated Powers and Regulatory Reform Committee's criticised the Bill in relation to the balance between the government's use of the affirmative procedure and the negative procedure for making secondary legislation. The negative procedure does not require detailed parliamentary scrutiny. Mel Stride MP, the Financial Secretary to the Treasury, responded in a letter. He accepted that it would be appropriate for clauses 30 (import duty), 42 (VAT) and 47 (excise duty) to be subject to the 'made affirmative' procedure. In all other cases, the minister argued that: 'adopting the affirmative procedure would produce impractical results ... having regard to the frequency and speed with which regulations may need to be updated'.

publications.parliament.uk/pa/ld201719/ldselect/lddelreg/181/18104.htm and www.parliament.uk/documents/lords-committees/constitution/GovernmentResponse/government-response-to-taxation-cbt-bill.pdf

As well as sponsoring a private member's bill to reduce VAT on domestic energy supplies, Christopher Chope MP has put forward another Bill to "make provision for the reduction of tariffs on goods imported into the United Kingdom". It seems unlikely to make any difference to the result of the Brexit negotiations.

Import Tariff (Reduction) Bill

4.3.9 Fulfilment houses

HMRC have issued a Notice to provide guidance on applying for approval under the new scheme for fulfilment businesses storing goods in the UK for sellers established outside the EU. Certain sections of the notice have force of law from 1 April 2018. New businesses must register by 30 September 2018. Registration can now be cancelled, or details amended, using the online service. Record-keeping, due diligence and penalty obligations begin in April 2019.

Notice FH1

4.3.10 Union Customs Code

HMRC have updated their published guidance on the UK implementation of the new Union Customs Code from 1 May 2016, setting out the main changes to import and export procedures, including some transitional arrangements that will operate until 2020. The changes made in September 2018 are not identified in a "what's changed" section. Nor does the guidance refer to Brexit.

www.gov.uk/guidance/introduction-of-the-union-customs-code-ucc

4.3.11 Confusion over distance sales

A trader appealed against an assessment in relation to sales he had zero-rated on the grounds that he was making zero-rated sales to customers in the Republic of Ireland. He did not attend the hearing (having postponed an earlier hearing at the last minute) and, as he had stated an intention to give evidence in person without a witness statement in advance, the judge struggled to understand his grounds of appeal. He appeared to be under a number of misapprehensions about the way VAT worked on international sales and on the evidence required to secure zero-rating; he also appeared not to appreciate that the assessment required him to pay HMRC £17,500, rather believing that he was due a repayment.

Judge Heidi Poon set out the requirements of the law as clearly as possible so the trader would understand why his appeal would be dismissed, and also would understand that the result was that he owed HMRC the amount stated on the assessment. HMRC had not sought a penalty.

First-Tier Tribunal (TC06705): *James Murphy t/a Ebuzz*

4.3.12 Updated Notices

HMRC have updated the November 2016 version of their Notice *The single market*, with a link to guidance on how to make changes to VAT registration details, including return periods (paragraph 17.9).

Notice 725

HMRC have updated the October 2017 version of their Notice *VAT personal export scheme*. The amendments only appear to relate to contact telephone numbers.

Notice 707

4.4 European rules

4.4.1 SME VAT scheme

The EU Parliament's economic and monetary affairs (ECON) committee has put forward amendments to the Commission's proposal for simplification of VAT for SMEs in the EU, which forms part of the Commission's wider moves towards creation of a single EU VAT area. The committee's recommendations include creating an online portal for claiming exemption in other member states, removing the proposed requirement for annual VAT returns and ensuring that exempt SMEs do not need to file VAT returns. The committee also proposes bringing forward introduction of the scheme to 1 January 2020.

The committee's proposed amendments to the Commission's January 2018 outline include:

- setting both an upper limit (at EU level) and a lower limit (by member states) for the VAT exemption threshold;
- dropping the proposed requirement for SMEs to submit annual VAT returns;

- preventing member states from requiring exempt SMEs to submit VAT returns;
- creating an online one-stop-shop allowing SMEs to register for the exemption across member states; and
- implementing the scheme from 1 January 2020 (rather than 1 July 2022 in the original proposal).

www.europarl.europa.eu/sides/getDoc.do?type=REPORT&reference=A8-2018-0260&format=XML&language=EN

4.4.2 EU VAT system proposals

The EU Parliament economic and monetary affairs (ECON) committee has tabled its report containing amendments to the Commission's proposal for creation of a definitive EU VAT system, in advance of the debate and vote in Strasbourg on 2/3 October. The committee published a draft report on 3 May.

The Commission's proposal contains four "cornerstones" and four short-term "quick fixes". The cornerstones are:

- countering fraud by charging VAT on cross-border trade within the EU;
- a one-stop shop to enable cross-border declarations;
- the destination principle, where VAT is paid to the consumer's member state;
- simplified invoicing, allowing traders to use their own country's rules even for cross-border sales.

The quick fixes are mainly limited to certified taxable persons:

- requiring the customer's VRN as a substantive condition for exempting intra-community supplies of goods;
- simplifying rules for chain transactions that do not involve physical movements of goods;
- simplifying the rules on call-off stock;
- simplifying the rules on proof of transport for exempting intra-community supplies of goods.

Among the amendments put forward in the report, the committee calls for:

- 'certified taxable person' status to be clearly defined in regulations and comprehensive guidelines, and aligned as closely as possible with the criteria for authorised economic operators;
- simplified procedures for applications by SMEs;
- an appeals procedure for rejected applications to be put in place by 1 June 2020 (with applicants having to wait at least six months before making another application);
- the authorities to review certified taxable person status at least every two years;

- introduction of a VAT dispute resolution mechanism, based on the current EU VAT cross-border ruling pilot project, to operate alongside national VAT dispute mechanisms; and
- introduction of a mechanism to provide taxpayers with automatic notifications of changes to applicable VAT rates.

www.europarl.europa.eu/sides/getDoc.do?type=REPORT&reference=A8-2018-0280&format=XML&language=EN

ECON has also put forward amendments to the Commission's proposal for allowing member states more flexibility on rates. The Commission's proposal, published in January, would allow member states to apply a reduced rate of between zero and 5%, in addition to the two reduced rates currently permitted of no less than 5%, and one zero rate (subject to an overall weighted average VAT rate of at least 12%). It would also replace the current list of goods and services to which reduced rates can be applied, with a new list of products to which the standard rate would always be applied.

ECON suggests that a maximum standard rate of 25% should be imposed, as well as the current minimum standard rate of 15%; and also calls for member states to be prevented from applying lower rates to "harmful or luxury products".

It is intended that the definitive system and the greater flexibility on rates should come into force in 2022.

www.europarl.europa.eu/sides/getDoc.do?type=REPORT&reference=A8-2018-0279&format=XML&language=EN

4.4.3 VAT Terminal Markets Order

The EU Commission has issued a reasoned opinion to the UK on what it considers to be non-compliance with the PVD in the UK's zero-rating for certain commodity derivatives under the UK's Terminal Markets Order. The UK government has stated: "The tax treatment of commodity derivatives is unchanged. UK tax law stands unless and until such time as it is changed and therefore past and current trading activity under the Terminal Markets Order is not affected by the issuance of the Article 258 letter."

www.gov.uk/government/news/statement-on-infraction-proceedings-on-vat-treatment-of-certain-commodity-derivatives-trading

4.4.4 VAT fraud crime investigation

The results of Operation OCTOPUS II, which investigated criminal networks importing clothing and footwear from China into the EU by misusing the Customs Procedures 4200, have been made public. This procedure allows third country importations to be released into free circulation with a deferred payment of import VAT until the goods' arrival with the consignee. The investigation found that value of the goods was often under declared, or the goods went missing.

www.europol.europa.eu/newsroom/news/pan-european-vat-fraud-crime-group-dismantled

4.4.5 UK failure to collect customs duty

The European Commission has sent a reasoned opinion to the UK, marking the second stage of infringement proceedings against the UK's failure to pay over €2.7bn in customs duty (plus interest and minus collection costs) lost through fraud between 2011 and 2017, involving imports of textiles and footwear from China. The Commission began these proceedings with a letter of formal notice sent on 8 March. The UK now has two months to respond to the opinion.

In 2017 the EU's anti-fraud organisation, OLAF, published a report stating that importers in the UK had evaded customs duties by using fictitious and false invoices and incorrect valuation declarations on importation. According to the Commission, the UK failed to take appropriate action to prevent this fraud, in spite of being warned of the risks and the scale by the Commission since 2007.

europa.eu/rapid/press-release_IP-18-5807_en.htm

4.4.6 EU VAT gap

The latest report into the EU VAT gap suggests that member states lost in total almost €150bn in VAT during 2016. This is a reduction to 12.3% of total VAT revenues from 13.2% in 2015. The Commissioner responsible for taxation stated that the improvement should be commended but the amount remains unacceptable, particularly given that €50bn is estimated as being lost to criminals.

The VAT gap decreased in 22 member states, but increased in the other six, which included the UK, Ireland and France.

europa.eu/rapid/press-release_IP-18-5787_en.htm

4.4.7 Compatibility of sales tax with VAT

A dispute arose in Estonia about the imposition of a sales tax applicable to goods and services. A number of traders argued that it was contrary to art.401 PVD, which prohibits the imposition of any "VAT-like" tax in addition to VAT. However, art.401 allows other taxes to be imposed:

Without prejudice to other provisions of Community law, this Directive shall not prevent a Member State from maintaining or introducing taxes on insurance contracts, taxes on betting and gambling, excise duties, stamp duties or, more generally, any taxes, duties or charges which cannot be characterised as turnover taxes, provided that the collecting of those taxes, duties or charges does not give rise, in trade between Member States, to formalities connected with the crossing of frontiers.

Questions were referred to the CJEU to determine whether the disputed sales tax contravened this provision. This depended on whether the sales tax could be "characterised as a turnover tax", and in particular whether it had the essential features of VAT. The CJEU noted that VAT has been held in the past to have four components:

- VAT applies generally to transactions relating to goods or services;
- it is proportional to the price charged by the taxable person in return for the goods and services which he has supplied;

- it is charged at each stage of the production and distribution process, including that of retail sale, irrespective of the number of transactions which have previously taken place; and
- the amounts paid during the preceding stages of the production and distribution process are deducted from the VAT payable by a taxable person, with the result that the tax applies, at any given stage, only to the value added at that stage and the final burden of that tax rests ultimately on the consumer.

The tax at issue did not meet the third or fourth conditions. However, the referring court considered that it possibly produced a similar result, in that the burden of the tax fell on the final consumer.

The CJEU did not agree. Because there was no requirement to add the tax to the sale price, or to issue an invoice specifying the amount of the tax, it was not clear that the final consumer bore it – it could equally well be borne by the business making the supply. In the CJEU's view, the effect of the tax depended on the behaviour and decisions of the traders who had to charge it, not on the essential nature of the tax itself. As a result, it was not a turnover tax within the meaning of art.401, and was not incompatible with the Directive.

CJEU (Case C-475/17): *Viking Motors and Others v Tallinna linn, Maksu- ja Tolliamet*

4.4.8 Inactive registration

A Romanian company was engaged in the business of the assembly, installation and maintenance of wind farms. For the purpose of carrying out its economic activity, it acquired various goods and services from suppliers established and registered for VAT purposes in Romania and in other Member States of the European Union. It exercised its right to deduct VAT in respect of the goods and services acquired by submitting a VAT return. From 7 October 2010 to 24 May 2011, the company was declared an 'inactive taxpayer' for the purposes the Romanian VAT law on the ground that, for half a calendar year, it had not filed any of the returns required by law.

Subsequently it put matters right, but when it received a VAT inspection in 2014/15, the authorities sought to disallow input tax claimed on expenditure incurred during the period that the registration had been suspended. The court considered the reasons for which a VAT deduction may be validly refused, but this did not fall within them. Denial of deduction was disproportionate in relation to a mere "formal" failure. Where the substantive requirements had been met and the right of deduction was not being invoked fraudulently or abusively, national law could not deny it in the circumstances of the case.

CJEU (Case C-69/17): *Siemens Gamesa Renewable Energy Romania SRL v Agenţia Naţională de Administrare Fiscală — Direcţia Generală de Soluţionare a Contestaţiilor*

4.5 *Foreign refund reclaims*

4.5.1 No-deal Brexit

The technical note described in more detail above at 4.3.1 also has a section on VAT refund claims. It makes the obvious point that the current electronic refund system will no longer be available; UK businesses wishing to make claims in the EU will have to use the existing processes for non-EU businesses. This process varies across the EU and businesses will need to make themselves aware of the processes in the individual countries where they incur costs and want to claim a refund

https://tinyurl.com/ybpv7k85

4.5.2 No economic activity

A company incorporated in the Cayman Islands leased, and then bought, tools from a UK VAT registered company, and then leased them to a Netherlands group company for no consideration. It made a claim for repayment of the input tax (about £5.4m) under the 13th Directive; HMRC refused the claim on the grounds that there was no economic activity, because there was no consideration.

In the FTT (TC05806), the company argued that it had an overall economic activity that included no non-economic activities and no exempt activities. It made taxable sales of spare parts (separate from the tools that it leased in and leased out intra-group). On the basis of *Sveda*, the input tax on the leasing of the tools related to the whole of its economic activities and should be allowed.

The judge (Jonathan Richards) said that the CJEU had set out two tests in *Sveda*. The claimant must have incurred the input tax in the capacity of a taxable person and there must be a direct and immediate link to the person's taxed outputs. That link does not have to be individual and specific, as it can apply to the taxed outputs as a whole; however, it must exist.

The judge considered precedents including *Sveda* and *Associated Newspapers*. He commented that the facts of those cases were clear and it was easy to see a direct link between the claimed tax and the outputs of the business as a whole. It was less clear in the current case. No clear explanation had been given for the decision to obtain the tools at a cost and then lease them to a group company for no consideration. The company's witness had speculated that it might be something to do with direct tax, but whatever it was, the judge considered that it was not economic. There was no direct and immediate link between the tool costs and the taxed sales of spare parts, because they were a separate activity. The decision to incur cost and not to make onward charges was not the decision of an economic operator. Accordingly, neither of the *Sveda* tests was satisfied, and HMRC were correct to refuse repayment of the tax.

The company appealed to the Upper Tribunal. The Upper Tribunal summarised the facts again, noting that the various leases had arisen as part of a corporate reorganisation in which tools and intellectual property were shifted around the group. The company argued that there was an overall economic purpose, and that the company would not have purchased the intellectual property (necessary for sales of spare parts)

without purchasing the tools. The company's counsel added the *Iberdrola* decision (Case C-132/16) to the precedents relied on. It was released after the FTT decision. He submitted that it was authority for a "but for" test of causation; the court rejected the opinion of A-G Kokott that a particular "use" for the purpose of taxable transactions was necessary, and instead held that it was sufficient that the relevant inputs were "essential" or "necessary" for the taxable person to carry out its economic activities. The FTT was also wrong to conclude that the existence of the package deal requiring JDI to buy the tools as well as the Intellectual Property was a subjective rather than objective matter that should be ignored.

The Upper Tribunal (Mr Justice Roth and Judge Sarah Falk) considered the *Iberdrola* decision in some detail. They rejected the taxpayer's argument that it approved a "but for" test: Article 17 of the Directive and Article 168 of the PVD both require the relevant goods or services to be "used" for the purposes of taxable (or taxed) transactions. This has been expressed both in terms of a "direct and immediate link" and in terms of a cost component of output transactions, and the concept of direct and immediate link has been treated as applying to general costs which are components of the price of goods or services supplied rather than being linked to a specific output, but the underlying requirement is one based on use. This is reflected in paragraph 27 of the judgment in *Iberdrola*, and is entirely consistent with previous case law including *Sveda*.

In particular, the court in *Iberdrola* stated that only costs that were "objectively necessary" to allow the company to carry out its taxed transactions could be deducted. The statutory test is one of use, and the CJEU made clear that this test was satisfied only to the extent that the reconstruction allowed Iberdrola's own properties to be connected to the pump station, and thereby operate as viable dwellings.

In relation to the relevance of subjective intentions, the UT agreed that they were relevant, but the test was rather an objective one, requiring consideration of the taxpayer's economic activities to determine why the relevant input was acquired, and whether in economic terms the input could properly be regarded as a cost of taxable supplies. The UT did not consider that the FTT had made any error of law in this respect.

The CJEU precedent *Bastova*, concerning links between the costs associated with breeding and training racehorses and economic activity, was also considered. This also required objective evidence of a link. The Court of Session in *Frank Smart Ltd* had also considered intended use, but that was a case in which there had not yet been any actual use; in the present situation, there was no doubt about what the company had used the tools for.

After further detailed consideration of the FTT's conclusions and the company's criticisms of it, the UT concluded that there was no error of law. It was a conclusion that the FTT was entitled to reach, and indeed was bound to reach given that it had found no link between the purchase and the taxable transactions of the company.

Upper Tribunal: *JDI International Leasing Ltd v HMRC*

5. INPUTS

5.1 Economic activity

5.1.1 Another holding company

Another case has come before the CJEU relating to the deduction of input tax on the acquisition of subsidiaries. The most recent significant precedents have established:

- that a holding company that is engaged in economic activity can regard acquisition costs as general overheads, and deduct them in accordance with the principles of partial exemption;
- that only exempt supplies have to be taken into account in the partial exemption calculation, not investment activities or investment income that are outside the scope;
- economic activities include supplying management services to the subsidiaries in question for consideration;
- where a holding company supplies such management services to some subsidiaries, but not to others, the subsidiaries to which services are not supplied will be treated as held in a non-economic capacity, and input tax should be restricted in accordance with the principles of business and non-business transactions (which are left to Member States to determine).

[*Cibo Participations* (Case C-16/00), *Larentia + Minerva and Marenave Schiffahrt* (Cases C-108/14 and C-109/14, MVM (Case C-28/16)]

In the present case, the holding company did not charge for supplies of management services, but let property to its subsidiaries. The question was whether this constituted "direct involvement in the management of its subsidiary" in line with the precedents, so that the VAT on acquisition costs would be deductible.

The court examined the precedents and concluded that the letting of property to subsidiaries was to be treated in the same way as the provision of management services for consideration. The holding company would be treated as engaged in economic activity in relation to any subsidiary to which it made such taxable supplies, and would therefore be able to deduct input tax on acquisition costs. The refusal of input tax was acceptable where it was necessary to counter tax evasion or fraud, but any other restriction risked undermining the neutrality of the tax.

Where a holding company only involved itself in the management of some subsidiaries (presumably, in only letting property to some), a Member State should apply general principles (rather than the Directive) to determine what was a fair proportionate recovery in the circumstances.

CJEU (Case C-320/17): *Marle Participations SARL v Ministre de l'Économie et des Finances*

5.1.2 Article

In an article in *Taxation*, David Jacob and Tom Jarvis discuss the recent CJEU cases on recovery of input tax by holding companies and recommend the provision of management services for consideration in

order to secure recovery. Those services should be provided from completion of the acquisition, and the intention to provide them should be documented from the outset.

Taxation 23 August 2018

5.2 Who receives the supply?

Nothing to report.

5.3 Partial exemption

5.3.1 Public authority and capital item

In the case of *Waterschap Zeeuws Vlaanderen* (Case C-378/02), the CJEU held that a public authority, which bought a capital item for use in its non-business activities, could not subsequently make adjustments under the capital goods scheme even though it had started to use the item for taxable supplies. The right to deduct input tax was established at the time the VAT was incurred; at that time, the authority was not acting in the capacity of a taxable person, and therefore had no right of deduction. The adjustments under the capital goods scheme depended on there being something to adjust.

A new case has refined this principle. The municipality in the case had been registered as a taxable person since 2005. During 2009 and 2010 it incurred VAT on the construction of a community centre. On completion, it was managed by a non-business entity. In 2014, the municipality decided to transfer ownership of the building into its assets and manage it directly, including renting it out for consideration. The Polish authorities applied the *Waterschap* decision and refused any deduction.

The Polish courts asked for clarification of the point, because the later case *Gmina Międzyzdroje* (Case C-500/13) appeared to allow an adjustment in similar circumstances. In that case, *Waterschap* does not appear to have been considered; the question and answer were rather concerned with the taxpayer authority's suggestion that it should be able to make an adjustment in a single year, rather than applying the capital good scheme.

In the present case, the CJEU reiterated the importance of deduction as a fundamental part of the VAT system. If deduction was not allowed, it would undermine the neutrality of the tax. It therefore seems that the CJEU was keen to find a reason to distinguish the situation from *Waterschap* and allow the deduction. The tax authorities wanted to make something of the fact that the municipality had not declared its intention to use the item for taxable purposes when it incurred the VAT; this was rejected as not of overriding importance. What was more significant was that the municipality was already registered as a taxable person at the time, and the fact that the asset (a building) was capable of economic use. The referring court should carry out an objective assessment of whether

the municipality had been acting as a taxable person when it incurred the VAT, but it was not in principle prevented from enjoying deductions by adjustment under the capital goods scheme.

CJEU (Case C-140/17): *Szef Krajowej Administracji Skarbowej v Gmina Ryjewo*

5.3.2 Article

In an article in *Taxation*, Neil Warren examines the attribution of VAT on purchased goods to non-business, exempt and taxable activities, and gives some practical examples.

Taxation, 13 September 2018

5.3.3 Framework for NHS bodies

HMRC have published an updated version of the "framework" that NHS trusts may use in designing partial exemption methods. The revised version contains more detail on the standard method override adjustment where a trust has not sought approval for a special method, and on the process for obtaining approval.

www.gov.uk/guidance/partial-exemption-frameworks

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 Right of deduction where supply not completed

Two German individuals contracted to buy a combined heat and power unit from suppliers (GA and GB). They were issued with tax invoices and made payment on accounts. They both registered for VAT and claimed the input tax. GA and GB then went into insolvent liquidation; the persons acting for them were convicted of 88 counts of fraudulent trading practices and conspiracy to defraud. The goods were never delivered.

Questions were referred to the CJEU to determine what adjustments, if any, were required to the individuals' claims for input tax. Although the supply had never taken place, there was a chargeable event triggered by the issue of the invoice and the payment. They had acted in good faith, and the payment on account had not been refunded. It was possible that the principles of *Reemtsma Cigarettenfabriken* (Case C-35/05) required the tax authorities to make a direct refund to the individuals, if they had received the output tax from the fraudulent supplies, as they could not exercise their right to repayment by any other means.

The CJEU noted that the obligation of supplier and recipient are not symmetrical in relation to payments and deductions of VAT: output tax shown on an invoice must be paid to the authorities, but input tax can only be deducted in relation to the receipt of an actual supply.

The court first considered the right of a trader to deduct input tax at the time that a payment on account is made. The mere possibility that the goods might not be delivered was not enough to rule out the right of recovery. A potential buyer may not be refused the right to deduct the VAT relating to a payment on account in respect of the goods in question where that payment has been made and received and where, at the time that payment was made, all the relevant information concerning the future supply could be regarded as known to that buyer and the supply of those goods appeared to be certain. However, that buyer may be refused that right if it is established, having regard to objective elements, that, at the time the payment on account was made, he knew or should reasonably have known that that supply was uncertain.

Those objective elements include the fact that the goods were specifically identified. This has been a point of argument in cases in the UK: where the goods existed and were identified, a UK Tribunal has held that they were actually "supplied" for VAT purposes, even if they were never delivered to the customer (*David Peters Ltd* (TC01819)). However, that was an unusual decision that seemed to go against the conclusions of many other cases in this area.

The next question was then whether the input tax, properly deducted at the time of the payment on account, had to be adjusted under art.184 to 186 PVD once it became apparent that the goods would never be delivered. The answer given by the court is "Articles 185 and 186 of Directive 2006/112 must be interpreted as not precluding, in circumstances such as those at issue in the cases in the main proceedings, a national law or practice which has the effect of making adjusting the value added tax relating to a payment on account for the supply of an item conditional upon that payment being refunded by the supplier." That

appears to presume that the German law is so generous, but the extract from the German law appears to require an adjustment to input tax simply if the goods have not been supplied.

Nevertheless, the judgment appears clear that the court believes the trader should enjoy the deduction. It suggests that an adjustment under art.184, where the payment on account is not recoverable because of the supplier's insolvency, should lead to a *Reemtsma* right against the tax authorities. "However, it would be manifestly unreasonable to require those buyers to adjust those deductions and then to bring an action against the tax authorities in order to obtain a refund of the VAT paid in respect of the payments on account in question."

There is one further curiosity in the decision. The court distinguishes the circumstances from the earlier case of *Firin* (Case C-107/13) in that this did not appear to be a VAT fraud (just a different kind of fraud), and that the claimants had "already derived revenue from the goods in respect of which they had made the payments on account even before those goods had actually been delivered. It is apparent from the orders for reference that the buyers had rented out the goods in question and had received rent in respect of those goods. Thus, those goods, in respect of which input tax was paid, were indeed used, to a certain extent, for taxable output transactions." No further details are given: it is not clear how the traders could have rented out goods that did not exist, or whether they were obliged to refund the rent that they had received in respect of a supply that must have been without value.

Nevertheless, the overall conclusion appears to be that a person who pays a deposit to a supplier who then becomes insolvent has a greater chance of keeping the input tax deduction than they did previously.

CJEU (Case C-660/16 and 661/16): *Finanzamt Dachau v Achim Kollroß and Finanzamt Göppingen*

5.8.2 Right of deduction where no supply made

By contrast with the above decision, the CJEU ruled in two cases referred from France that "in order to deny a taxable person in receipt of an invoice the right to deduct the VAT appearing on that invoice, it is sufficient that the authorities establish that the transactions covered by that invoice have not actually been carried out."

The appellants were two companies that purported to have leased some equipment for onward supply to customers in the foreign French possession Reunion. The companies claimed that there would have to be an allegation of knowledge or means of knowledge of fraud to deny input tax. This appeared to be the judgment of the court in *Stroy Trans* (Case C-642/11): "if, taking account of fraud or irregularities committed by the issuer of an invoice or upstream of the transaction relied upon as the basis for the right to deduct, that transaction is considered not to have been actually carried out, the recipient of an invoice can be denied the right to deduct VAT only if it is established, on the basis of objective factors and without requiring the recipient of the invoice to carry out verifications which are not his responsibility, that he knew, or ought to have known, that the transaction was connected with VAT fraud, this being a matter which is for the referring court to determine."

The court distinguished the present cases from the precedent. In that earlier case, the tax authorities relied on irregularities committed by the issuer of the invoice or by one of its suppliers, and the question referred related to the consequences, regarding the exercise of the right of the recipient of an invoice to deduct VAT declared by the issuer of that invoice, of the absence of rectification by the tax authorities, in a tax adjustment notice addressed to the issuer of that invoice. The appellant had tried to draw an inference from the tax authorities' apparent "acceptance" of the supplier's returns – if the tax authorities had not corrected them, then they had "accepted" that the transactions had taken place. The CJEU ruled that the claimant was not entitled to draw that inference.

Nevertheless, the earlier case did appear to imply that the authorities would have to argue the "*Kittel*" grounds to disallow an input tax deduction. The present case suggests that they do not.

CJEU (Case C-459/17 and 460/17): *SGI and Valériane SNC v Ministre de l'Action et des Comptes publics*

5.8.3 Scrap dealing

A company appealed against a refusal by HMRC of a claim to input tax of £70,993 for its 08/13 quarter. HMRC argued that the claim related to purchases of scrap metal that were associated with fraudulent trading by a "missing trader".

The company had only engaged in scrap metal dealing in the previous quarter, when extended verification had not been applied. The circumstances of these deals were considered relevant by the Tribunal, even though the input tax had been allowed and was not the subject of the appeal.

The Tribunal examined the history of the deals and concluded that the first three tests for *Kittel* were not ultimately in dispute: there was a tax loss, it arose from fraudulent evasion, and the transactions were connected with that loss. The only disputed matter was whether the trader knew or ought to have known of that connection.

HMRC put forward a number of arguments based on the pattern of trade being "so far removed from ordinary commercial practice that either the appellant knew that the deals were connected with fraud but was prepared to proceed regardless or should have known that the deals were connected with fraud."

The Tribunal heard extensive witness evidence from the directors, a husband and wife. The judge considered the husband to be "nobody's fool" but "profoundly incurious" about the transactions he was entering into. In all the circumstances, the company ought to have asked more questions, and that satisfied the fourth test for *Kittel* to apply. The appeal was dismissed.

First-Tier Tribunal (TC06702): *MD Construction (Bradford) Ltd*

5.8.4 Car dealing

A car dealer bought 29 VAT "qualifying" cars in the quarter to 09/12, of which 13 were sold in the Republic of Ireland and zero-rated. HMRC denied the input tax on all 29 on the basis that the supplier was a missing trader and the dealer knew or ought to have known that the purchases were connected with an intention to defraud the revenue.

The trader did not dispute that HMRC had proved that there was a tax loss, that the tax loss resulted from fraudulent evasion, and that his transactions were connected with that evasion. The sole issue was therefore whether he knew or ought to have known of that connection. HMRC's primary case was that the trader actually knew, as his explanations for his conduct were otherwise not credible. Their secondary case was that he should have known.

Judge Richard Chapman examined the history of the dealings and found that the trader did not have direct knowledge of the fraud. There were some inconsistencies in his evidence, but overall he was doing his best to answer probing questions, albeit not immediately. His evidence should not be rejected wholesale.

On the other hand, the trader should have known of the connection with fraudulent evasion. He accepted that he had a general knowledge of MTIC fraud, and was on guard when entering the initial deals with the supplier and one of the Republic of Ireland customers. Nevertheless, his due diligence checks were superficial, and should not have given him the comfort that he claimed he obtained. There were a number of other features in the conduct of dealing that suggested that the trader closed his eyes to warning signs.

The appeal was dismissed in respect of 29 cars and allowed in respect of a thirtieth.

First-Tier Tribunal (TC06665): *Roy Wilson (t/a Roy Wilson Car Sales)*

5.8.5 Updated Notice

HMRC have updated their Notice *Local authorities and similar bodies*. "What's changed" lists the following:

- the contact details for HMRC and the procedure for 'Putting things right' have been updated;
- the overview has been changed to give a better understanding of the work of public bodies and the general provisions for VAT reclaims;
- the name and number of public notices has been updated;
- further information has been given on the calculation of VAT attributable to exempt supplies;
- new rules on occasional breaches of the insignificance test;
- paragraphs 12.3, 12.4, and 12.6 have been amended (dealing with reclaims by bodies not registered for VAT).

Notice 749

6. ADMINISTRATION AND PENALTIES

6.1 Group registration

6.1.1 Group registration eligibility criteria

Legislation in Finance Bill 2019 will allow non-corporate entities, such as partnerships or individuals, to join VAT groups. The non-corporate entity must control all of the members of the VAT group and be UK established and VAT registered. The change is being made in response to judgments of the CJEU and has been the subject of consultation. An amendment will be made to SI 2004/1931 *VAT (Groups: eligibility) Order* to prevent 'misuse' of the new rules.

A new "control test" is inserted as s.43AZA VATA 1994:

(1) This section applies for the purposes of s.43A (and expressions used in this section have the same meaning as in that section).

(2) A body corporate ("X") controls a UK body corporate if –

(a) X is empowered by statute to control the UK body corporate's activities, or

(b) X is the UK body corporate's holding company.

(3) An individual ("Y") controls a UK body corporate if Y would, were Y a company, be the UK body corporate's holding company.

(4) Two or more relevant persons carrying on a business in partnership ("the partnership") control a UK body corporate if the partnership would, were it a company, be the UK body corporate's holding company.

(5) In this section "holding company" has the meaning given by s.1159 of, and Sch.6 to, the Companies Act 2006.

www.gov.uk/government/publications/vat-grouping-eligibility-criteria-changes/vat-grouping-eligibility-criteria-changes

6.2 Other registration rules

6.2.1 Compulsory registration

HMRC decided in November 2016 that a trader should have been registered from 1 July 2011 to 30 November 2012, and imposed a penalty under FA 2008 Sch.41 of £1,937. The trader did not dispute the "rolling turnover" figures, but considered it unreasonable that an excess over the threshold of £5,000 had resulted in a "fine" (VAT plus penalty) of £11,622.

The judge noted that the officer did not have enough information to raise the assessment until the last tranche of business records were made available in January 2016. The assessment was therefore in time.

The judge examined the trader's argument that registration should have been for a shorter period because the excess had arisen due to unforeseen circumstances. He rejected it, and also criticisms of the way in which

HMRC had operated the rules. The law was clear, and HMRC had only done what the trader ought to have done. There was no reasonable excuse or special circumstance that would remove the penalty; and the disproportionality of the penalty was not within the Tribunal's jurisdiction. The appeal was dismissed in its entirety.

First-Tier Tribunal (TC06609): *Timothy Hughes*

6.2.2 Online marketplaces

HMRC have updated their guidance for online marketplaces and the new joint and several liability rules with more detail on how to register for VAT, either online or by post using form VAT1.

www.gov.uk/guidance/vat-overseas-businesses-using-an-online-marketplace-to-sell-goods-in-the-uk

HMRC have published further signatories to the new cooperation agreement under which online marketplaces will exchange certain information about their sellers in the interests of promoting VAT compliance. Current signatories are: Amazon Europe Services Sarl; eBay EMEA; Fruugo.com Ltd; Wolf & Badger Ltd; Etsy Ireland UC; ASOS plc; and Flubit Ltd.

www.gov.uk/government/publications/hmrc-and-online-marketplaces-agreement-to-promote-vat-compliance

6.2.3 Updated Notice

HMRC have updated the February 2017 version of their Notice *Registration scheme for racehorse owners*, adding syndicates to the list of those who can be 'owners' of racehorses.

Notice 700/67

6.3 Payments and returns

6.3.1 Online filing

Two companies appealed against 2015 directions by HMRC requiring them to file their VAT returns online. The director who represented the taxpayer had asked for one hearing to be postponed, but did not provide sufficient medical evidence; he asked for a further postponement, which HMRC resisted; they did not object to him participating by telephone, but technological problems made this impossible. The judge decided to proceed with the hearing because of the substantial delay that had already occurred; the director had not provided medical evidence, but he had sent a written skeleton argument based on the European Convention on Human Rights which the Tribunal could consider.

In rejecting the taxpayer's request to be allowed to file on paper, HMRC had noted that online filings had been made previously. It was therefore not impractical for the trader to continue to do so.

The judge considered the history of the dispute, which had been through an earlier hearing in relation to the "religious objection" ground. She considered that HMRC had incorrectly interpreted the "age" exemption as

relating to "infirmity in old age", which would be separately covered by the "disability" heading; however, that minor issue had not led HMRC to make an unreasonable decision. If she was wrong and had a full appellate jurisdiction, she would also have agreed with the decision that the traders did not qualify for the exemption.

The appeals were dismissed.

First-Tier Tribunal (TC06596): *Glen Lyn Generations Ltd and another*

6.3.2 Interest harmonisation

The government is proposing new rules to harmonise the sanctions for late payment of tax across a range of taxes, at the same time as introducing new penalties for late submission of returns (see 6.8 below). The VAT rules will change to become similar to those that exist in income tax and corporation tax. This will lead to the abolition of default surcharge.

The government wants to revise the interest rules for VAT to ensure they follow similar rules to those for Corporation Tax and ITSA. Provisions similar to the current FA 2009 s.101, s.102, Schedules 53 and 54 will be enacted to apply to VAT accounting periods starting after April 2020.

The measure will ensure that in VAT, late payment interest will be payable where a payment is made after the due date from the date that payment became due and payable until the date it is received by HMRC. Late payment interest will also apply to VAT returns, VAT amendments and assessments and VAT Payments on Account.

Additionally, repayment interest will be payable in VAT either from the last day the return was due to be received or the day it was received, until the date the repayment to the taxpayer is authorised/offset. Where a VAT repayment return has been received HMRC will not pay interest:

- for periods of reasonable enquiry where a full response has not been received;
- for periods where HMRC needs to correct errors or omissions in the return;
- where security has been requested and not provided.

The CIOT has objected to the exclusion of "periods of enquiry" from the accrual of interest, because it would remove the incentive for HMRC to determine enquiries promptly.

The late payment penalties will consist of two separate charges. The first charge will become payable 30 days after the payment due date and will be based on a set percentage of the balance outstanding. However the precise amount of that charge will be dependent on what payments are made or the Time to Pay (TTP) arrangements that are agreed during those first 30 days.

The first and second charge

Days after due	Action by taxpayer	First charge penalty
0 – 15	Tax paid	No penalty
	TTP agreed	Penalty suspended
16 – 30	Tax paid	Reduced percentage
	TTP agreed	Reduced/suspended
30+	None	First charge

The second charge will also become payable and will be calculated on amounts outstanding from day 31 after the payment due date until the outstanding balance is paid in full. Any TTP agreed during this period will also result in future penalties being suspended from the date the TTP was agreed.

www.gov.uk/government/publications/interest-harmonisation-and-sanctions-for-late-payment/interest-harmonisation-and-sanctions-for-late-payment

The government also published a summary of responses to the December 2017 consultation on MTD interest and sanctions for late payment.

www.gov.uk/government/consultations/making-tax-digital-interest-harmonisation-and-sanctions-for-late-payment

6.3.3 Interest rates

HMRC raised the interest rates for corporation tax quarterly instalments paid late from 13 August 2018 and for other taxes and duties from 21 August 2018, following the Bank of England's announcement of a rise in the base rate. Repayment interest rates remain unchanged.

www.gov.uk/government/news/hmrc-late-payment-interest-rates-to-be-revised-after-bank-of-england-rate-rise

6.4 Repayment claims

6.4.1 Holding company claims

The long and tortuous tale of the *Taylor Clark* repayment claim has reached its conclusion in the Supreme Court, with HMRC left holding the money: the company entitled to claim had not claimed, and the company that had made a claim was not entitled to do so.

Background and FTT

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

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

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

The FTT (TC02443, December 2012) reviewed the complex background and a number of precedent cases. It concluded that T could not take over C's timely claim when it had not itself made any claim at all. Any claim made by T as part of the appeals process was after the *Fleming* time limit; C had not made the claim on behalf of T or acting as its agent, and T could not take the benefit of the fact that C had made a claim in time.

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

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

Upper Tribunal

T appealed to the Upper Tribunal, arguing that the 1990 agreement had not assigned the right to reclaim VAT; and even if it had, the fact that T was the representative member of the group at all material times, it would still have had the right to make a claim. Both HMRC and the appellant agreed with the reasoning of the FTT in the subsequent case of *Standard Chartered plc* and disagreed with the FTT's decision in *MG Rover Group Ltd* – it was the representative member, and not the "real world supplier" (in Judge Mosedale's expression) that accounted for VAT and should be entitled to reclaim it.

T's representative argued that it was not necessary for a claim to have been made by the appellant: s.80 only required "a claim being made for the purpose", which could be made by someone else. She also argued that the principles of equivalence and effectiveness supported her construction.

HMRC responded that the meaning of s.80 was clear, and in accordance with its purpose: a claim had to be made by or on behalf of the person to whom the money was to be repaid. T had not made a claim by the time limit; it was unaware of the claim that had been made. The principles of equivalence and effectiveness did not assist the appellant, as the time-bar had been held to comply with EU legislation in principle. The judge preferred HMRC's as the more natural construction of the law. The appellant's version could lead to absurd results.

The one area in which the UT disagreed with the FTT was in relation to the question of entitlement to claim. As the judge agreed with the FTT in *Standard Chartered*, he considered that the representative member was the person entitled to claim, even after the trade had been transferred in 1990. He did not accept that the 1990 agreement assigned the right to make such reclaims to C.

The appellant's action was dismissed. The language suggested that neither C nor T would be entitled to a repayment: the judge stated that "*Prior to 1 April 2009 the appellant as representative member of the VAT group would have been entitled to claim repayment of output tax overpaid by it in respect of the period 1973 – 3 December 1996. The appellant made no s. 80 claims before the expiry of the limitation period. Its claims are time-barred.*" The implication was that C was not a person entitled to make a claim, so presumably the claims that it made – and that HMRC accepted, in part – were not valid.

Court of Session

The company appealed to the Court of Session. The essential issue before the court was whether the claim made by C could be regarded as made on

behalf of the representative member of its former VAT group, T. If so, T was entitled to the repayment; if not, no one would be entitled to it.

The court considered that the contents of the correspondence between C and HMRC, as well as the statutory scheme of s.43 VATA 1994, supported the company's contention. C had quoted T's VAT number and name on some of its claims, and HMRC had clearly regarded the claim as made on T's behalf as they paid the money to T. Claims could be made by tax advisers on behalf of clients; there was no reason why a subsidiary should not make a claim on behalf of the representative member. Everything done by a member of the group was regarded as done by the representative member, and this was a mere extension of that statutory principle.

The court confirmed that C was not entitled to the repayment. T had been responsible for paying the VAT in the period for which the repayment was claimed, and only T had therefore overpaid VAT. T was entitled to regard the timely claims made by C as made on its behalf, and it was entitled to the repayment. Its appeal was allowed.

Supreme Court

HMRC appealed to the Supreme Court. Lord Hodge gave the leading judgment and the other four judges unanimously agreed. The judge considered the way in which the UK has implemented the optional "single taxable person" treatment in art.11 PVD. It was clear from the words of s.43 VATA 1994 that the UK regarded the representative member of the VAT group as "the single taxable person"; the VAT group was not some other form of "quasi-person" with a separate existence. The law treats the supplies made and received by all group members as made and received by the representative member for the time being. The law also requires the person who has overpaid the VAT to make the claim for repayment.

The FTT had correctly found that C had not made the claims on behalf of T. There were several reasons for this and the decision was amply justified. C could not act as T's agent, because it had no actual or implied authority to make claims on its behalf; there was no basis for a contention that T had or could have retrospectively authorised C to claim as its agent.

There was no need for a reference to the CJEU. The judges did not consider that any explanation of the EU concept of "single taxable person" was necessary for the determination of the appeal. HMRC's appeal was allowed.

Supreme Court: *HMRC v Taylor Clark Leisure plc*

6.4.2 VAT in postal charges

Zipvit's argument about input tax implicit in charges treated as exempt by Royal Mail has been rejected again by the Court of Appeal.

Background and FTT

In 2014, the FTT (TC03773) dismissed an argument that a company should be entitled to input tax as the VAT fraction of money paid to Royal Mail in respect of supplies which were regarded by the UK law as exempt, but which were of a kind held by the CJEU not to qualify for exemption under EU law. The particular claim related to consideration paid of £120,000, but there are a number of other similar claims with a large

amount of money riding on them. Judge Mosedale gave her decision acknowledging that it would surely be subject to appeal, and probably an eventual reference to the CJEU. She therefore set out the facts and her understanding of the law, and her reasoning for her decision, with the stated intention of making everything clear for those who would review the decision later.

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

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

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

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

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

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

Upper Tribunal

The company appealed to the Upper Tribunal. In 2016, Mrs Justice Proudman rehearsed the legislative background to the claim in the PVD, the VAT Act and the regulations. She went on to state the two issues before her: whether VAT was "due or paid" within art.168(a) PVD; and whether, in the absence of invoices, HMRC should nevertheless exercise discretion in the company's favour. It was accepted by all sides that the UT had jurisdiction to consider the exercise of HMRC's discretion.

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

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

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

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

- if the decision maker reached a decision that no reasonable decision maker could have reached, the appeal should be allowed and the appellant's claim for input tax should be upheld; but

- if HMRC's decision would inevitably have been the same had it been properly undertaken, then the appeal should be dismissed;
- in any other case HMRC should be required to reconsider their decision, taking into account such matters as they should take into account and leaving out of account those matters which they ought not to have taken into account.

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

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

Court of Appeal

The company appealed further, arguing first that new evidence should be considered by the CA. This is unusual for an appellate court, but the judges considered that it would be right to admit new relevant material in a case on which litigation of possibly £1 billion depended. It was not clear who was to blame for the fact that this material (relating to details of the contracts entered into between Zipvit and Royal Mail) had not been put before the FTT. Henderson LJ held that it was appropriate to admit it, but also to consider the position on the alternative hypotheses with and without the new material.

The judge notes the confusing wording of VATA 1994 s.19(2), which appears at first sight to be a grossing up provision: "the value of a supply is such amount as, with the addition of the VAT chargeable, is equal to the consideration". The judge comments that this is not what it means – it is a rewording of art.78(a) PVD, which excludes the VAT from the taxable amount. He goes on to say:

"There is no difficulty in principle with this analysis if the consideration for a taxable supply is agreed to be £100 plus VAT, or if the agreement says nothing about VAT, with the consequence that the agreed consideration of £120 must be treated as inclusive of VAT. But what if the parties agree a price which is *exclusive* of VAT, perhaps because it is unclear whether VAT is properly chargeable on the supply? In that kind of case, it will be a matter of construction of the agreement between the parties to determine whether the customer is contractually liable to pay an amount equal to the VAT, if and when it turns out to be properly chargeable. Assuming that to be the correct construction, and if it emerges that VAT is chargeable on the supply, the supplier will probably then send a VAT-only invoice to the customer (which would be for £24, if the agreed VAT-exclusive price were £120).

Does s.19(2) then have the effect that the original payment of £120, made on a VAT-exclusive basis, must be retrospectively split into a taxable amount of £100 plus VAT of £20, and that the subsequent payment of £24 (assuming that the customer honours his contractual obligation) must likewise be split into a further taxable amount of £20 and VAT of £4? As

a matter of first impression, there is much to be said in favour of an affirmative answer to this question. There is still only one supply, and a single overall consideration for it, albeit paid in two instalments; and since the supply is (on this hypothesis) taxable, each of the sums paid on account of the total price should be regarded as including VAT at the appropriate rate. The function of s.19(2) is to ensure that the total consideration is split into a taxable value of £120 and tax of £24, not to treat the first payment of £120 as exclusive of VAT and the second payment of £24 as consisting entirely of VAT. That may be how the supplier and the customer view the matter in commercial terms, but the correct analysis for VAT purposes could well be that there has been a single taxable supply for a total consideration for £144, comprising a taxable amount of £120 and VAT of £24, paid in two instalments."

This construction was put forward by the taxpayer, supported by the 2013 decision of the Court of Session in *Simpson & Marwick v HMRC*. That concerned a situation in which a firm of solicitors had failed to account for unpaid "VAT only" invoices, and sought to argue that it was entitled to bad debt relief on the full amount – if the amount involved was £120 gross, £100 had been paid by an insurance company, and the whole amount outstanding (£20) was the VAT. The CS held that the £100 received from the insurance company included some VAT, and bad debt relief could not operate in this way.

The judge noted that this case turned on the construction of the bad debt relief rules, and did not settle the question on which the present case depended. That was the consequence for VAT of an agreement between the parties that a price was "VAT-exclusive", followed by the determination some time later that VAT should have been charged. This had not been addressed by the CJEU, and the judge considered that a reference might have been necessary on the following question: "whether the original purchase price paid by the customer to the supplier should be treated as VAT-inclusive, in circumstances where the supplier has a contractual right to obtain payment of the VAT from the customer, but (for whatever reason) has failed or chosen not to enforce that right."

He then summarised his conclusions on whether VAT had been "due or paid" for the purposes of art.168. If Royal Mail had a contractual right to recover the VAT from Zipvit, a reference would have been necessary. If it clearly had no such right, the price paid would have had to be treated as VAT-inclusive, and Zipvit would have had a right of recovery. This followed from the CJEU decision in *Tulica* (Cases C-249/12 and 250/12), even though that dealt with the position of a supplier, and would have been "acte clair". Similarly, if the contract had stated explicitly that the price was VAT-inclusive, that would confirm the right of recovery.

The judge moved on to the second question, which was whether the absence of a VAT invoice was fatal to the claim. This was required by PVD art.178, with further details provided in art.226 and art.219; articles 180 and 182 empower Member States to authorise a deduction without an invoice, as enacted by the UK in SI 1995/2518 reg.29.

The company argued that the invoices supplied by Royal Mail were defective VAT invoices that ought to have been corrected in accordance with the CJEU decision in *Barlis 06* (Case C-516/14). All that was

missing was the VAT element that should have been included in the consideration.

The judge disagreed. In *Barlis*, the question was whether the description of the services was adequate. There was no dispute about the liability to VAT, or about whether the VAT had been accounted for by the suppliers. In the present case, the invoices described the supplies as zero-rated or exempt, and there was no doubt that Royal Mail had not accounted for output tax. The judge noted that the function of the VAT invoice, as confirmed by CJEU case law, was to enable the authorities to monitor the payment by suppliers of the VAT claimed by purchasers. It was not a mere formal requirement, as the company argued.

The absence of a VAT invoice was fatal to the claims whether or not the new contractual material was admitted, and there was no need for a reference to the CJEU. The other two judges agreed, and Zipvit's appeal was dismissed again.

Court of Appeal: *Zipvit Ltd v HMRC*

6.4.3 Golf club claim

A golf club's claim was allowed by the Tribunal in February 2018. HMRC applied for leave to appeal, and the FTT decided to review the decision itself, having identified an error of law. The judge stated "the Tribunal has considerable sympathy with the Appellant's position. The Appellant had very good reason to believe it had won its appeal as of 7 February 2018. Further, the reasons relied upon by the Tribunal in now dismissing the appeal are based upon arguments which were not raised by HMRC at the hearing of the appeal but only in the subsequent application for permission to appeal. The Tribunal pointed out HMRC's failure to raise many of these arguments at the hearing in its notification to the parties that it was conducting a review." Nevertheless, HMRC were entitled to raise points of law in applying for leave to appeal; no new issues of fact were raised, so while it was unsatisfactory that the decision was changed by matters that had not been raised at the first hearing, nevertheless it was correct.

The club had made a timely *Fleming* claim in March 2009, and had appealed to the Tribunal when its claim was refused. Accordingly, when *Bridport* was finally accepted by HMRC, its claims for periods up to 12/08 were allowed. In November 2013, the company applied for payment of further amounts for periods from 12/07 to 09/13. HMRC eventually accepted the claims for periods from 12/07 to 12/08 as amendments to the existing valid *Fleming* claim, but ruled that 03/09, 06/09 and 09/09 were out of time as over four years before the date of the claim.

The question before the Tribunal was therefore whether the 2013 claim was an amendment or extension of the original claim (arising out of the same issue) or was a new claim (as HMRC argued). The judge considered a range of arguments put forward by the club's representative, but based on precedents including *Bratt* and *Reed Employment*, he concluded that the requirements of reg.37 were not met in respect of the disputed periods by the original claim. The judge examined in some detail what is meant by "within the contemplation of the original claim" and concluded that it must be objective and derived from the wording of the written request.

That had related to specific periods with an end date of 12/08. Therefore the November 2013 claim was a new claim in respect of periods that the original claim had not covered, and it was out of time for the disputed periods as HMRC contended. The appeal was dismissed.

First-Tier Tribunal (TC06549): *Longcliffe Golf Club*

6.4.4 Connected company invoice

A company (P) provided adult entertainment services on the internet, generating revenue through premium telephone numbers. Another company (F) collected payments from telecommunication companies on its behalf and paid them over less a VATable commission. In fact, the whole of the receipts were paid over without the deduction of the commission, for reasons that were never explained. F raised invoices to P and accounted for output tax; P deducted input tax. P was dissolved in 2012.

In early 2012, the director of F discovered that the commission charged by F had been based on the whole receipts from the telecommunications company, when it should have been based on P's 28.5% share of these (the balance belonged to the "partners" who provided the adult entertainment). There was correspondence between F and the accountant to both companies reflecting an intention to correct the overcharged commission.

In August 2012 the accountant wrote to HMRC explaining the error, stating that F had overpaid and P had underpaid VAT as a result. The amount was quantified in August 2013 at £109,856.

Correspondence followed, in which it was acknowledged by HMRC that they had contributed to delays. Formal claims by Error Correction Notice were submitted by F on 13 March 2016 for the output tax (rejected as out of time, because the outputs all related to periods up to 02/2012) and a bad debt claim for £38,665 submitted in the VAT return for 05/2017, also rejected as out of time.

HMRC applied for strike-out of certain aspects of the subsequent appeal on the grounds that it had no reasonable prospect of success. The judge considered a number of arguments put forward for the appellant, but concluded that nothing in the history of the case or in the legislation made it "excessively difficult or practically impossible" for the company to exercise its rights. The Tribunal had no jurisdiction to extend the time limit, or to consider an alternative common law remedy against HMRC. Accordingly, the strike-out application was granted.

Turning to the substantive issues, the judge had to consider what constituted "the claim" for the purposes of s.80. HMRC said that a letter dated 19 February 2016 was not a valid claim, and necessary information was only received in April, rendering 02/2012 out of time. Relying on the CA judgment in *Bratt*, the Tribunal noted that "claim summaries" analysing the overpayment by return period had to be included in the February letter if it was to be valid; the question was whether, on the balance of probabilities, they had been included.

Three different versions of the February letter were produced. After considering the circumstances and arguments in great detail, the judge

found as a fact that the summaries had not been submitted with the original letter when it was sent to HMRC.

This meant that the only adjustment still in time related to 05/2012. HMRC had rejected even this because the conditions of reg.38 had not been satisfied. The judge again examined all the circumstances and concluded that, even if there had been an agreement between F and P to reduce the consideration, no repayment had been made by P, nor had the accounts been adjusted to reflect this. There was therefore no actual "adjustment in the course of business".

The judge further considered the bad debt relief claim, and for completeness held that it was also made out of time and did not meet the conditions of s.36 VATA 1994. The appeals were dismissed in their entirety.

First-Tier Tribunal (TC06593): *First Agency Ltd*

6.4.5 Lennartz

The Tribunal heard a lead appeal in respect of a number of claims based on the same arguments. The appellant had claimed a repayment of over £1.5m of overpaid VAT. It concerned what the Tribunal decided should be called "the *Lennartz* treatment", and the consequences of the CJEU decision in *VNLTO* (Case C-515/07) that the treatment was not available where a trader had non-business use within the scope of the entity's objects, rather than "private use or use otherwise than for the purposes of the business" as required by the Directive.

HMRC issued R&C Brief 02/2010 to set out their response to *VNLTO*. In essence, taxpayers who had utilised *Lennartz* treatment in circumstances where (in the light of *VNLTO*) it was not properly available, could choose to unravel that treatment, adjusting both over-deducted input VAT and over-declared output VAT. However, HMRC had decided not to insist on unravelling in all cases, even where the unravelling would have been advantageous to HMRC. Instead, taxpayers were free to retain the benefit of over-claimed input VAT deductions (on the basis of the law as it was understood pre-*VNLTO*), but only on the basis that the taxpayer continued to treat itself as making deemed supplies, and to account for output VAT on those deemed supplies. This was provided for by FA (no.3) 2010 Sch.8 para.4.

The appellant had applied *Lennartz* to the costs of a new building project from November 2009 onwards. It received substantial repayments of VAT on the costs of the project, then accounted for output tax on the supposed "non-business use". In April 2014, its VAT advisor submitted a claim for over-declared output tax, net of overclaimed input tax, from 04/10 to 01/14, totalling £1.522m.

The basis of the claim was that the provision of education to students was a business activity, irrespective of how it was funded. In consequence no part of the buildings within the scope of the project were put to non-business use, and there was no requirement for the college to account for deemed output VAT. Output tax could therefore be reclaimed, subject to the four-year cap; input tax should also be adjusted, but most of that had been claimed over four years before.

HMRC refused the claim on alternative grounds: either the provision of education was properly regarded as non-business and the R&C Brief 2/2010 approach was valid, or else HMRC were entitled to offset the claim against the excessive input tax recovered earlier.

The college's grounds of appeal were as follows:

(1) the provision of education and vocational training by the college is a "business activity" for the purposes of reg.116E, irrespective of whether it is a supply for consideration.

(2) the provision of education and vocational training by the college is a supply for a consideration because the grant income received by the college from government agencies must constitute consideration (within the meaning of art.2(1)(c) PVD and s5(2) VATA) for the provision of that education and vocational training.

(3) it is not possible to split the activities of the college between business and non-business activities. All the activities of the college amount to a single business activity.

(4) a distinction can be drawn between the "provision" of education and vocational training, and the "supply" of education and vocational training – and that the provision of education and vocational training does not require consideration.

(5) HMRC's publicly stated policy is that the provision of vocational training is an exempt supply for VAT purposes – and as it is a "supply", it must by definition be a business activity.

(6) Even if the college is wrong on points (1) to (3) above, the payments made by funding agencies amount to consideration for the provision of education and vocational training, and in consequence the education and vocational training funded by such payments must amount to a business. The college submits that for a payment to amount to consideration, it does not have to be student-specific.

The Tribunal then set out the issues that arose from the designation of the case as a lead appeal, and HMRC's arguments in relation to them. The judge agreed with HMRC that "business" in VATA 1994 Sch.4 para.5(4) (the deemed supply rule) does not have the same meaning as "business" in VATA 1994 s.4 (scope of VAT on taxable supplies). Accordingly, the term "business" as used in:

(1) s.4 must be interpreted consistently with the concept of "economic activity" as used in art.9(1) PVD; and

(2) para.5(4) must be interpreted consistently with art.26(1) (as interpreted in *VNLTO* by the CJEU).

Therefore, "business" in para.5(4) extends beyond economic activities, whereas "business" in s.4 VATA 1994 refers only to economic activities. The judge agreed with HMRC that the provision of education and vocational training by the college amounted to "business activities" for the purposes of art.26(1) PVD and para.5(4).

Next, the judge held that education and vocational training funding provided by government agencies did not amount to consideration for any supplies made by the college. It was a public block grant provided subject to conditions, rather than a payment for particular services. The scale of

the college's activities, and the amount of them that were funded by the agencies, meant that the activities were not economic activities and were therefore outside the scope of VAT.

The college's argument that it was engaged in a single activity that was all business was examined and rejected. The judge agreed with HMRC's submission that the key distinction between economic and non-economic activities are whether services are provided for consideration, and that there is nothing in the VAT legislation that prevents someone from engaging in both economic and non-economic activities.

In summary, the Tribunal held that the provision of education and vocational training, to the extent that it is funded by the funding agencies, is not an "economic activity" within art.9 PVD and is outside the scope of VAT for the purposes of the PVD; it is not a "supply of services for consideration" within art.2(1)(c) PVD and is not treated as such by the VATA; it is not a "supply as defined by s.5(2)(a) VATA 1994"; and that in relation to goods for which "*Lennartz* treatment" has been previously adopted by a person, such a person is liable to account for output tax pursuant to Sch.4 para.5(4) and Part 15A of the VAT Regulations.

The appeal against HMRC's preferred decision was dismissed, making it unnecessary to consider HMRC's alternative decision.

First-Tier Tribunal (TC06657): *Colchester Institute Corporation*

6.4.6 Historic claim succeeds

A company made a *Fleming* claim in respect of fleet leasing bonuses it would have received from manufacturers during the period 1988 to 1995. Following the CJEU decision in *Elida Gibbs* (Case C-317/94), HMRC invited businesses that had accounted for standard rated output tax on such bonuses to make reclaims. The company did so, and appealed against a decision dated 3 April 2013 to refuse that claim. The Tribunal was not concerned with the quantum of the claim (£5.6m) but with the principle.

As a preliminary matter, HMRC sought to introduce an argument that the wrong company was making the claim. The claimant had been the representative member of the VAT group at some times, but not when the relevant transactions were undertaken. The appellant argued that it was prejudicial for HMRC to introduce this argument at a late stage; from other cases it appeared that it had been HMRC's view of the law for a long time, and if they had raised the point earlier, the company could have investigated whether there had been an effective transfer of rights when the company that overpaid the VAT was bought by the claimant in 1999. It was harder to find evidence of that now. The claim was first made in 2003; if HMRC had raised this ground of objection then, the correct claimant could have met the requirements of the *Fleming* window in 2009. Judge Mosedale allowed the amendment to HMRC's statement of case, because she did not accept that there was significant procedural prejudice to the appellant.

HMRC argued that the *Elida Gibbs* claims should be rejected because the company sold its leased cars to finance houses. It would therefore have recovered input tax on the full price of the cars before taking the fleet bonuses into account. It accounted for output tax on those bonuses rather

than reducing input tax deducted on the purchase; the two errors cancelled each other out.

Judge Mosedale was asked to rule on whether, in the circumstances, the appellant would have been entitled in law to claim the input tax on the purchase of the cars. The company accepted that, if that was the case, it would not be able to produce any evidence that it had not in fact done so. If it had not been entitled to claim, HMRC accepted that it would not have done so. The judge was therefore asked to reach a conclusion on what the industry practice in relation to VAT recovery was before 1995, and whether it was probable that the company followed it.

This was a technical argument about the operation of para.7(2) of the Input Tax Order 1992: in financing the purchase of cars through a sale to a finance house and taking it back on HP terms to lease to customers, the company argued that it was not making a sale to the finance company that qualified for input tax deduction. They did not buy the cars "for the purpose of selling them"; and the car would not be "unused" at the time of the sale to the finance house, because it would already have been leased to the customer.

The judge considered a variety of evidence from accounts, published guides and witnesses. Given the passage of time, it was not surprising that the evidence was "rather thin"; however, she considered that it was enough to show that fleet leasing companies did not recover input tax on purchases of cars before 1 August 1995, and the appellant would have followed the industry practice.

The question was then whether this was correct in law. This in turn depended on the order of events: whether the leasing company sold the cars to the finance house before or after they were leased to the customer. The evidence on this was confused by some correspondence around the time of the refusal of the claim in 2012. Statements had been made on behalf of the appellant that suggested that the sales were in "the wrong order" (from their point of view). The judge concluded that the statements were wrong – they were made by people who did not understand in detail how the business operated, and who did not realise the significance of the order of the transactions. They were not intended to mislead, and they did not change the underlying position. The documentation showed that the lease to the customer preceded the sale to the finance house in each case. The witnesses gave a convincing commercial rationale for this.

After further detailed consideration of the "purpose" of buying the cars, the judge concluded that this related to the first transaction following that purchase – leasing to the customer, not selling to the HP company. As a matter of law, therefore, it was not entitled to the input tax.

There were three appellants in the case. Two of them won their appeals in principle and were left to discuss the quantum with HMRC. The third won for the period 1988 – 1993, but not for 1994 – 1995; and its appeal was stayed behind the final determination of the appeal in *MG Rover*, because it also depended on whether the correct company had made the claim.

First-Tier Tribunal (TC06648): *Bramall Contracts Ltd and others*

6.4.7 Calculation too vague

FTT decision TC05971 concerns a Scottish NHS Board that made a claim for repayment of input tax incurred on taxable supplies by its laboratories during the period 1974 to 1997. Its appeal was heard in 2015 and 2016 by Judge Kenneth Mure, who unfortunately died before giving a decision. The decision was, with the agreement of the parties, prepared by the side member of the Tribunal, Peter Sheppard. His decision records the evidence and discussion in considerable detail.

The first contention by HMRC was that the claim now under dispute was "new", i.e. made after March 2009 and therefore time-barred. The Tribunal disagreed. The calculations and revisions had been made in the course of correspondence and discussion in the period since March 2009, but they all remained valid clarifications of an existing valid claim.

Next, the FTT accepted that the Board did make taxable supplies in the course of business throughout the period of claim. There were specific supplies that were not covered by the exemption, in line with the *d'Ambrumenil* decision of the CJEU.

However, it was not possible to draw a conclusion about the calculation of the claim. A figure had been agreed for the 2006/07 year (14.7%) in relation to a non-*Fleming* claim, but the Tribunal could not accept that extrapolation of this figure back into the distant past could be justified. Extrapolation might be valid over a long period if there were at least some contemporaneous figures from prime records – for example, over a 25-year period, the Tribunal suggested that verified calculations could be carried out every 5 years and applied to the intervening periods, if there was no great variation. However, to take a figure from 2006/07 and apply it without any other evidence to all the years from 1974 to 1997 could not satisfy the balance of probabilities.

The appeal was therefore dismissed by the FTT; the Board appealed to the Upper Tribunal, where it came before Lord Tyre. The grounds of appeal were essentially that the FTT had applied the criteria appropriate to a dispute about partial exemption (where the law prescribes the method of calculation, including direct attribution) rather than business/non-business (where the only requirement is for a fair result).

The judge accepted, on the basis of the CJEU precedent *SECURENTA* (Case C-437/06), that the distinction between partial exemption and business/non-business methods was valid. It would therefore constitute an error of law if the FTT had purported to apply partial exemption methods in reaching a decision on a business/non-business split. However, the judge considered that the FTT had been quite clear about the distinction between the two, and had applied the correct test. Comments about partial exemption at the end of the decision were not part of the reasoning that had led to the refusal of the appeal, and did not indicate an error of law. Nor was it incumbent on the FTT to carry out alternative calculations to those supplied by the appellant with a view to arriving at an acceptable figure, because there was insufficient material before it to do so.

The appeal was refused.

Upper Tribunal: *NHS Lothian Health Board v HMRC*

6.5 Timing issues

Nothing to report.

6.6 Records

6.6.1 Making Tax Digital for VAT

HMRC have published the new *Notice Making Tax Digital for VAT*, providing information on the digital record-keeping and return requirements of making tax digital for VAT, which will apply to businesses with a taxable turnover above the VAT registration threshold from April 2019. Parts of the notice have the force of law from 1 April 2019. From 1 April 2020, there must be a 'digital link' for any transfer or exchange of data between software applications used as 'functional compatible software', without the need for any manual intervention.

The Notice sets out the requirements in some detail, and makes the point that the MTD rules only apply to the records that are specified in the Notice or are required to complete the VAT return. Other records do not have to be kept in functional compatible software. Some software will record all your VAT records and accounts information. However, there are some records that by law must be kept and preserved in their original form either for VAT purposes or other tax purposes. For example you must still keep a C79 (import VAT certificate) in its original form.

Functional compatible software is a software program, or set of software programs, products or applications, that must be able to:

- record and preserve digital records;
- provide to HMRC information and returns from data held in those digital records by using the API platform;
- receive information from HMRC via the API (Application Programming Interface) platform.

The complete set of digital records to meet Making Tax Digital requirements does not all have to be held in one place or in one program. Digital records can be kept in a range of compatible digital formats. Taken together, these form the digital records for the VAT registered entity.

Data transfer or exchange within and between software programs, applications or products that make up functional compatible software must be digital where the information continues to form part of the digital records. Once data has been entered into software used to keep and maintain digital records, any further transfer, recapture or modification of that data must be done using digital links. Each piece of software must be digitally linked to other pieces of software to create the digital journey. It follows that transferring data manually within or between different parts of a set of software programs, products or applications that make up functional compatible software is not acceptable under Making Tax Digital – for example, noting down details from an invoice in one ledger

and then using that handwritten information to manually update another part of the business functional compatible software system.

HMRC will allow a period of time ("the soft landing period") for businesses to have in place digital links between all parts of their functional compatible software. For the first year of mandation (VAT periods commencing between 1 April 2019 and 31 March 2020) businesses will not be required to have digital links between software programs. The one exception to this is where data is transferred, following preparation of the information required for the VAT Return, to another product (for example, a bridging product) that is API-enabled solely for the purpose of submitting the 9 Box VAT Return data to HMRC. The transfer of data to this product must be digital.

HMRC recognise that there may be points during preparation of a VAT return when calculations will have to be made outside of any software used to keep the digital records, or there may be a need to enter data into software from particular sources. For example a capital goods scheme adjustment calculation done in a separate spreadsheet may need some form of input by hand into the software that will send the VAT return information to HMRC.

The following details are worth noting in full:

The records listed in the following paragraphs must be kept, maintained and preserved in digital form. The regulations refer to this information as your "electronic account". The exact way you must enter the information will depend on the software package you have. Contact your software provider if you are unsure how to enter information into your software. HMRC can only provide advice on the legal requirements of Making Tax Digital.

You will need to keep additional records, such as invoices. You do not have to keep these digitally but you may choose to do so. For more information on the additional records that must be kept for VAT purposes, see VAT Notice 700/21: keeping VAT records.

3.3.1 Designatory data

You must have a digital record of:

- *your business name*
- *the address of your principal place of business*
- *your VAT registration number*
- *any VAT accounting schemes that you use*

3.3.2 Supplies made

For each supply you make you must record the:

- *time of supply (tax point)*
- *value of the supply (net value excluding VAT)*
- *rate of VAT charged*

This only includes supplies recorded as part of your VAT Return. Supplies that do not go on the VAT Return do not need to be recorded in functional

compatible software. For example intra-group supplies for a VAT group are not covered by these rules.

The time of supply is the date that you must declare output tax on. Typically this is when you send a VAT invoice or, if you are on cash accounting, when you receive payment for the supply. For more information on time of supply, see VAT Notice 700: VAT guide, section 14 and section 15.

Where more than one supply is recorded on an invoice and those supplies are within the same VAT period and are charged at the same rate of VAT you can record these as a single entry.

You must also have a record of outputs value for the period split between standard rate, reduced rate, zero rate, exempt and supplies which are outside the scope of UK VAT. However, you only need to keep a digital record of 'outside the scope' supplies that you are required to include in your VAT Return.

In relation to supplies received, the Notice requires the following:

3.3.3 Supplies received

For each supply you receive you must record the:

- *time of supply (tax point)*
- *value of the supply*
- *amount of input tax that you will claim*

This only includes supplies recorded as part of your VAT Return, supplies that do not go on the VAT Return do not need to be recorded in functional compatible software. For example, wages paid to an employee would not be covered by these rules.

There is no requirement under the regulations to record inputs for the period split by VAT rate.

The time of supply is typically the date on the VAT invoice or, if you are on cash accounting, when you pay for the supply. However you must also hold the associated evidence to claim deduction of input tax. For more information on time of supply, see VAT Notice 700: VAT guide, section 14 and section 15 and also paragraph 10.5 of that same Notice for information on timescales for claiming input tax.

If more than one supply is on an invoice you can record the totals from the invoice. Where the amount of input tax that you will claim is not known at the time you record the supply you have received, you can record:

- *the total amount of VAT and adjust for any irrecoverable VAT once calculated*
- *no VAT and adjust for any recoverable VAT once calculated*
- *VAT recoverable based on an estimated percentage and adjust for any VAT once calculated*

Where an invoice includes supplies with different times of supply that are within the same VAT period, you may record all supplies on the invoice as being at the same date.

Adjustments such as those required by partial exemption do not have to be carried out within the software, nor do they require an amendment to the record of the original supply. Error corrections are also made in the current period without changing the original records.

There are numerous examples in the Notice of how the rules are expected to work. There are also detailed points about:

- sales made or received by third party agents;
- reverse charge transactions;
- retail schemes;
- flat rate scheme;
- gold special accounting scheme;
- margin schemes.

The MTD features "voluntary updates" and "supplementary data" will be made available at a later date.

Traders may authorise HMRC to receive data from (and send data to) an agent in relation to any Making Tax Digital service. Agents will need to sign up to a new agent services account to use Making Tax Digital services on behalf of their clients. The agent must have software of their own or have access to the software that holds the client's digital records.

Notice 700/22

HMRC have also published a short introduction *Preparing VAT-registered businesses for Making Tax Digital*, which outlines the main requirements. It still appears that many businesses are not aware of the significance of the changes coming. There is more help and support for MTD on GOV.UK, including webinars and a video.

www.gov.uk/government/publications/making-tax-digital-how-vat-businesses-and-other-vat-entities-can-get-ready

The House of Lords economic affairs Finance Bill sub-committee intends to examine progress on MTD since its March 2017 report on 'Making Tax Digital for Business'. Particular areas of interest for this inquiry include:

- What key improvements have occurred, or new concerns have arisen, since the Sub-Committee's report on Making Tax Digital for Business was published in March 2017?
- How prepared are HMRC, businesses (small and large) and software providers for the implementation of Making Tax Digital for VAT in April 2019, and what are the challenges of concurrent preparations for Brexit?
- What are the potential costs of Making Tax Digital for VAT for businesses?

The committee is also examining HMRC's powers, and wishes to hear from a wide range of people with views on these two lines of inquiry.

www.parliament.uk/business/committees/committees-a-z/lords-select/economic-affairs-finance-bill-sub-committee/news-parliament-2017/call-for-evidence/

6.6.2 MTD: Pilot extension and deferred start date

HMRC had been running a MTD for VAT pilot for a group of invited businesses since April. They have now extended this pilot to include around half a million businesses whose affairs are straightforward and up to date.

On 17 October 2018, they announced that "As part of planning for the VAT pilot, HMRC have continued to listen to concerns about business readiness for MTD" and, as a result of those concerns, businesses with more complex requirements will defer their start date by 6 months.

To defer their start date to 1 October 2019, businesses must fall into one of the following categories:

- Trusts;
- 'Not for profit' organisations that are not set up as a company;
- VAT divisions;
- VAT groups;
- Those public sector entities required to provide additional information on their VAT return (Government departments, NHS Trusts);
- Local authorities;
- Public corporations;
- Traders based overseas;
- Those required to make payments on account;
- Annual accounting scheme users.

https://www.gov.uk/government/publications/making-tax-digital/overview-of-making-tax-digital

6.6.3 Articles

In an article in *Taxation*, Neil Warren discusses some of the issues arising from MTD for small and medium-sized enterprises. He highlights the fact that the requirements relate only to accounting entries that affect the VAT return. For example, a flat rate scheme trader does not need to keep a digital record of expenditure, unless it relates to capital expenditure goods on which input tax can be claimed, or relevant goods that determine whether the limited cost trader rate applies.

Taxation 9 August 2018

In an article in *Taxation*, Brian Palmer reviews some of the practical aspects of MTD and the approaching implementation of the new rules.

Taxation 2 August 2018

6.7 Assessments

6.7.1 Hidden purchases

A takeaway owner appealed against assessments based on suppressed takings. The Tribunal reviewed the history of the investigation, which included discovering that a supplier operated two accounts for the business, one “named” and one “unnamed”. The supplier said that this was normal practice and he did not consider it his business to check whether his customers met their VAT obligations, as long as he did. None of the purchases in the unnamed account appeared in the business records of the appellant.

The appellant denied that there was a second account; even though it had been clearly part of HMRC’s case since 2015, his representative applied during the hearing for a witness summons to be sent to the supplier’s director to be cross-examined. Judge Kevin Poole refused to do this, and found as a fact that the second account existed. The continued denials of any wrongdoing confirmed dishonesty. The appeals against assessment and penalty were dismissed.

First-Tier Tribunal (TC06564): *Yew Kai Lee*

6.7.2 Best judgement

A trader appealed against assessments for VAT of £34,131 and associated penalties for deliberately understated sales from a grocery shop between 2009 and 2013. HMRC had noted sales from a cash-and-carry business to the trader which did not appear in his accounting records; his declared mark-ups also appeared to be unusually low. The resulting assessment took into account underclaimed input tax as well as underdeclared output tax on the suppressed purchases.

The trader claimed that the accountants who had acted for him were responsible for omitting invoices. They were questioned in the Tribunal in relation to the advice that they had given: they denied any role in “cooking the books”. The Tribunal accepted their evidence and held that the trader was responsible. The appeals against penalty and assessment were dismissed.

First-Tier Tribunal (TC06703): *Kandasamythurai Pathmanathan*

Another appeal was equally unsuccessful against assessments relating to understatement of shop takings. The trader did not attend the hearing and offered no evidence. It seems quite surprising that the Tribunal bothered to consider the matter in any detail, but as the assessments had been appealed the judge considered the questions of best judgement and the time limits. She was satisfied that HMRC had complied with the law on both points, and formally dismissed the appeals.

First-Tier Tribunal (TC06667): *Saima Khalid*

6.7.3 Split of sales

A Subway franchisee appealed against assessments totalling £47,875 covering the periods 05/12 to 01/15. HMRC had carried out invigilations on three days in 2015 and noted that the proportion of standard rated sales on these days was much higher than that disclosed by previous VAT

returns. The average proportion of 82% was used to calculate the assessment, extrapolated back over the previous periods.

There was a breakdown in communications between the officer and the trader. The trader offered to have further invigilations to support his contention that the results had not been representative, but the officer had now raised an assessment and considered that further invigilations would be inappropriate. Accordingly the trader appealed, arguing that the methodology was unreliable: all three invigilations were carried out at the same time of day and at a cooler time of year when more people might order hot food. He also contended that the invigilations at least showed that sales were entered into the till correctly, there was no evidence to suggest that sales had been deliberately entered incorrectly and there was no evidence to support any errors in the operation of the till.

The till had a touchscreen and was programmed by Subway. It prompted the user to select the various options that would lead to classification of a supply as standard or zero rated. The judge was satisfied that there was no deliberate manipulation of the records, or incorrect programming. That left the possibility that the periods of invigilation were not representative of the appellant's trade over the previous VAT periods. The judge was satisfied that the appellant's trade could be subject to daily variations, variations arising from the time of day and/or seasonal variations. He acknowledged that the appellant had not carried out any exercise to demonstrate what the effect of such variations might be. He still had to consider whether he could be satisfied on the basis of the evidence before him that the invigilation results were explicable by reference to such variations.

The officer said that he based his view partly on the proportions of standard rated sales in other Subway shops in the area, but no evidence was put before the judge. Overall, and considering all the evidence, the judge concluded that the sample was not representative. He did not criticise the officer for his choice of sample dates, but he allowed the appeal.

First-Tier Tribunal (TC06666): *Golden Cube Ltd*

6.8 *Penalties and appeals*

6.8.1 Default surcharge

A company appealed against surcharges totalling £12,605 from August 2015 to March 2016, during which time it submitted monthly returns. By the time of the hearing the amount in dispute had been reduced to £9,947. The surcharge liability notice and surcharges were all sent to a previous address of the company, even though PAYE and corporation tax correspondence went to the correct address, and a meeting regarding VAT had been held at the new office. Also, the company had moved to monthly accounting to keep its VAT debt at a manageable level; although it had been late making monthly payments, it argued that it was still paying much of the VAT earlier than it would have done under quarterly accounting.

These reasons were rejected on review. In the appeal to the Tribunal, the company added a bad debt causing cash flow difficulties to its grounds of appeal. Judge Peter Sheppard did not consider this to have created sufficient difficulty to warrant a reasonable excuse. However, he was satisfied that HMRC had not properly served a surcharge liability notice until after the relevant periods. It was not clear why they had sent notices to a different address from the one their officer visited. A facility for making a single notification of changes of address on the GOV.UK website was misleading, because a notification to Companies House was forwarded to HMRC's corporation tax department but not to VAT.

As the notices had not been served, the appeal was allowed.

First-Tier Tribunal (TC06552): *Excel Commercial Cleaning Services Ltd*

A company appealed against a 15% surcharge of £5,883 imposed in respect of its 08/17 period. It paid the VAT due in two instalments, one of £30,000 on Monday 9 October and the balance of £9,222.64 a week later. It accepted the surcharge on the second payment, but in respect of the first, claimed that it had been prevented from making the payment on Friday 6 October by a fault in HMRC's system.

Judge Tony Beare concluded that this was a misunderstanding of the operation of s.59. There was no dispute that there had been a default; "reasonable excuse" operated to extinguish the default, but no excuse was offered for the second part of the payment. Once it was established that there was a default without an excuse, the calculation of the surcharge was based purely on the "outstanding VAT", which was clearly in this case the full £39,222. In other words, it was not possible to have a reasonable excuse for part of a VAT payment when the other part was definitely paid late.

The appeal was dismissed. There has been at least one other decision in which the judge took a different view.

First-Tier Tribunal (TC06695): *London Needs Cooling Ltd*

A trader appealed surcharges for all the periods from 02/14 to 02/17. By the time of the hearing, only the surcharges for 11/15, 02/16 and 05/16 were still in dispute. VAT had been paid late for all these periods, as well as 05/17. The appellant put forward excuses that included misunderstandings of the due date by his accountant and a "reasonable

belief" following a phone call in late 2015 that the situation had been resolved. The judge did not agree that any of this constituted a reasonable excuse. It was the trader's responsibility to ensure that the returns and payments were on time, and the due dates were clearly set out in guidance and correspondence.

First-Tier Tribunal (TC06679): *William Stuart Crawford*

A company in the surcharge regime discovered in February 2017 that it had overpaid VAT for 11/15. HMRC agreed, adjusted the VAT due for that period and reduced the surcharge that had been levied. The company's VAT account with HMRC was credited with £13,975 of VAT and £2,096 in surcharge as at 24 March 2017. The company then argued that the credit for 11/15 should reduce the amounts outstanding for periods in 2016, so reducing the surcharges for those periods as well. The total in dispute was just over £12,000.

The judge examined the operation of s.80 and concluded that credits arising on a claim cannot be backdated in this way. It only arises when the claim is made, so it cannot be set against earlier liabilities. The decision of the Upper Tribunal in *Swanfield* on allocation of actual payments dealt with a different situation, where actual payments might be set against later liabilities when there was already an old balance owing. The UT held that the taxpayer did have that choice, but would have to exercise it positively. HMRC had no obligation to make an allocation that would be favourable to the taxpayer, and would as a matter of routine allocate receipts to the earliest available liability.

The muddle that led to the overpayment was not a reasonable excuse, and the surcharges were not disproportionate. The appeal was dismissed.

First-Tier Tribunal (TC06672): *K D Media Publishing Ltd*

A company appealed against a 5% surcharge of £404.46 for its period 07/17. The excuse was that the director had simply forgotten to pay. The director argued that he had followed his normal quarterly procedures and therefore had "a reasonable expectation that HMRC would receive the payment". Judge Anne Fairpo did not accept that this could be a reasonable expectation if the company did not initiate the payment. The appeal was dismissed.

First-Tier Tribunal (TC06661): *Nicholson, Griffin And Charlton Ltd*

A connected company made a similar mistake for 07/17, leading to a surcharge of £713.06. The excuse was the same and so was the result.

First-Tier Tribunal (TC06660): *Nicholson & Griffin Ltd*

A company appealed against a 15% surcharge of £1,372 for its 08/17 period. The defence was a combination of "payments made on a Saturday not received until Monday" and disproportionality. The judge considered that a conscientious taxpayer, understanding the system (as the taxpayer acknowledged he did) and aware that he was in the surcharge regime, would have checked how long payments took to arrive. The surcharge at 2.9% of the appellant's turnover for the quarter was "a long way from being not merely harsh but plainly unfair". The appeal was dismissed.

First-Tier Tribunal (TC06646): *Clear Cut Consulting Ltd*

6.8.2 New penalties coming

The government has issued a technical note about the proposal for "points-based" late submission penalties (note: the web address below appears to relate to a specific aspect of the proposal, but it is where the whole document is at least for the time being).

The new regime is likely to initially apply to regular VAT and ITSA (income tax self-assessment) obligations. Other excise, environmental, indirect and transport taxes are included within the scope of legislation since the government intends to introduce the new regime more widely after VAT and ITSA. The government intends to bring Corporation Tax within the scope of the regime at a later date.

A taxpayer will automatically receive a point every time they fail to make a return on time. HMRC will notify them of this point. At a certain threshold of points, a financial penalty will be charged and notified (value to be confirmed in due course).

The level of the points threshold will depend on how often a taxpayer is required to file a return, to recognise the demands of more frequent obligations. Once a taxpayer has reached the threshold a penalty will be charged for every subsequent failure to make a return on time but their points total will not increase.

The intention is that the threshold will be 2 points for annual returns, 4 for quarterly returns and 5 for monthly returns. Points will "expire" after 2 years, but will not do so if the taxpayer is at the penalty threshold – that is, it will take two years of good compliance to reset the points. In effect, this means that there will have to be 2 timely annual returns, 4 quarterly returns or 6 monthly returns, provided that all returns due for the preceding 24 months have been filed (whether or not on time).

The most complicated aspect appears to be this: "Taxpayers will normally have one points total for each frequency of return they are required to file. So if they are required to provide an annual ITSA return and quarterly VAT returns and both returns are late, they will incur 2 points applying to 2 different totals: one for ITSA and one for VAT. Where a taxpayer has 2 or more businesses and files separate returns for each business each business will have a separate points total. If a taxpayer provides a single return for multiple businesses they will have a single points total."

There are rules to adjust the points total where a trader moves from one filing frequency to another, as may happen in VAT.

The proposals are intended to apply from 1 April 2020.

www.gov.uk/government/publications/technical-note-on-capital-gains-tax-and-corporation-tax-for-non-residents-on-uk-property/technical-note-on-capital-gains-tax-and-corporation-tax-for-non-residents-on-uk-property

6.8.3 Penalty

A trader was assessed to £15,663 of VAT and £7,831 in a dishonesty penalty for the periods from 12/03 to 12/08 on the basis that taxable services had been misdescribed as outside the scope MOT tests. The director admitted that he had done this from January 2009 in an attempt to keep his business afloat, but denied that he had done so before that.

The judge examined the basis of the extrapolation that HMRC had undertaken, and concluded that they had shown, on the balance of probabilities, that the dishonest behaviour had started earlier than 2009. The assessment was raised to best judgement, and the penalty was confirmed. In particular, the mitigation for penalties that was allowed for post-2009 penalties would not be applied to pre-2009 periods, because the trader had not cooperated by admitting the dishonesty.

First-Tier Tribunal (TC06712): *Derbyshire Motors Ltd*

6.8.4 Late appeals

A golf club made *Fleming* claims through its accountants in late March 2009. The claims were rejected in August 2009; the accountants wrote to HMRC to "appeal", which HMRC took as accepting the offer of a formal review. This was carried out and concluded on 2 October 2009. The accountants wrote back with a "further appeal" and asking for a second review. HMRC responded that this was not possible, and if the matter was to be taken further, it would be necessary to appeal to the Tribunal without delay. The accountants stated that they did not receive this reply, nor a further reply to a letter sent in August 2011 chasing a response. They submitted further claims in May and September 2014, and wrote to HMRC in March 2016 asking why no repayment had been made to the club in respect of the 2009 claims.

Further correspondence followed in which HMRC stated that they considered the matter closed in October 2009; the accountants had clearly received that letter because HMRC had a copy of their request for a "re-review" on file, and no appeal had been lodged with the Tribunal. After appointing new agents, the club finally made a formal appeal in October 2017.

The club's representative put forward several arguments to persuade the Tribunal to admit the late appeal. The review letter had only been sent to the agents, even though the law requires it to be sent to the taxpayer as well. The non-receipt of HMRC's replies should be taken into account. The amount of money was substantial, and the claim would certainly succeed following the *Bridport* decision.

The Tribunal considered that the arguable irregularities in the way the review was offered were not enough to vitiate the decision. The appellant wanted to "cherry pick" the law in interpreting some provisions strictly while taking a looser approach to others. The judge was satisfied that the review was properly notified.

The judge considered the exercise of the Tribunal's discretion. He noted that, whether or not the letters in 2009 and 2011 had gone astray, the club and its agents had clearly received the reply in 2016; even then, "the penny did not appear to drop". Rather than appealing immediately to the Tribunal, they chose to argue that the earlier dispute was still "live" – this was "wishful thinking". HMRC's conduct had been clear and consistent throughout; balancing all the factors required by precedent, the judge rejected the application to admit a late appeal.

First-Tier Tribunal (TC06604): *Kingsgate Golf Club Ltd*

In 2014 HMRC obtained a judgment debt in the County Court against an individual who had apparently failed to account for income tax and CGT

for most, if not all, his working life, together with some VAT. The total liability was over £2.5m. HMRC applied in the High Court for orders to sell the individual's property; he sought to challenge the judgment debt, and proceedings were stayed while he also applied for leave to appeal against the assessments and determinations out of time.

A large part of the taxpayer's excuse for delay was that he had no permanent address, and HMRC had failed to communicate with him properly. The judge examined the background to the assessments in detail and rejected this claim. Overall, there was insufficient reason for the delay to excuse it, and leave to appeal was not granted, apart from a few of the items on a long list where HMRC had agreed that adjustments should be made.

First-Tier Tribunal (TC06689): *John Patrick Walsh*

6.8.5 Procedure

A company was assessed to £1.4m of input tax it had claimed in circumstances HMRC alleged related to MTIC fraud. The company disputed whether it should be required to deposit the tax before an appeal could be heard. The UT dismissed this appeal in 2014, but the company was granted leave to appeal to the Court of Appeal on the grounds of a new legal argument, that the requirement to deposit disputed tax infringed the EU legal principle of equivalence. The company argued that deposit of tax is not required for income tax or SDLT appeals.

Lady Justice Arden gave the leading judgment in the CA in late 2016, dismissing the appeal. She set out several differences between VAT appeals and other tax appeals in relation to:

- prepayment of tax (only required for VAT);
- hardship applications (only available for VAT, but held not to be available to this appellant);
- postponement applications (relevant to direct taxes);
- taxpayer appeals to the Upper Tribunal from the FTT (which will generally require payment of tax that the FTT held to be due).

She cited Lord Hope's statement of the equivalence principle from the case of the FII Group Litigation: "The principle of equivalence requires that the rules regulating the right to recover taxes levied in breach of EU law must be no less favourable than those governing similar domestic actions."

The matters in dispute included what actions and taxes could be regarded as "similar" for this purpose. The judge referred to the 'no "most favourable treatment" principle', by which she meant that equivalence did not require an EU-based claim to enjoy the most favourable of any available regimes in domestic law; it was permitted under EU precedent for there to be a range of different comparators and for the equivalent claim to fall within them, rather than always enjoying the most favourable.

She said that this was enough to dispose of the appeal, but she went on to conclude that VAT appeals were not similar to other tax appeals for the

purpose of the equivalence test, and identified specific points from precedent CJEU cases that supported this approach.

The company appealed to the Supreme Court, with the same unanimous result. Lord Briggs gave the leading judgment, and agreed that the other taxes were not proper comparators with VAT for the purposes of "equivalence". VAT's economic burden falls upon the consumer, but it is collected by the trader from the consumer and accounted for by the trader to HMRC. Taxpayers appealing income tax or corporation tax are being required to pay something of which the economic burden falls on them and which they have not collected from anyone else. Therefore, it is no less than appropriate that traders assessed to VAT should be required to pay or deposit the tax in dispute, which they have or should have collected. If there is no true comparator for the disputed claim, the concept of equivalence has no application.

Supreme Court: *Totel v HMRC*

HMRC assessed a fish and chip shop owner to £28,323 of VAT and a penalty of £26,913 (95%) in respect of underdeclared takings. The FTT (TC05332) examined the evidence and the arguments put forward by both sides, and was satisfied that the assessment was made to the best of the officer's judgement. There was no reason to disturb the quantum. It was also clear that there had been deliberate behaviour with concealment and very little cooperation, so the appeals against both the assessment and the penalty were dismissed.

The trader applied for leave to appeal, which was initially refused. It was later granted on limited grounds, being the apparent withholding of evidence that was in HMRC's possession but not disclosed to the taxpayer. This did not relate to whether the assessment was valid, but concerned the decision on quantum, because the evidence (original till rolls) was relevant to determining whether certain credit card transactions had been included in the records.

HMRC had apparently refused or ignored several requests for return of the original documents. The UT quoted the following as an example of HMRC's responses to requests for disclosure:

"HMRC is not bound to disclose specific information or reasons for suspecting dishonest conduct, or any other evidence held. It is sufficient to identify the matters that are the subject of the enquiry. It is entirely a matter for the taxpayer to decide whether or not to take the opportunity to make a full disclosure."

This was described as "wholly unmeritorious" and "a totally inappropriate response to a proper request from the taxpayer". HMRC provided no explanation of why they considered such a response to be appropriate. The FTT had only considered the failure to return the till rolls "unfortunate", which was a gross understatement.

It was not clear that the new evidence would have had a material effect on the FTT's decision on quantum, because there was very little in the FTT decision to explain how that decision was taken. However, the UT could not be sure that the decision would have been the same, and accordingly the UT decided that the new material should be admitted. The case should be remitted to a new panel of the FTT, and appropriate directions should be issued in due course to clarify the issues in dispute and to

ensure proper disclosure. A new hearing could be avoided if the parties could come to an agreement on quantum.

Upper Tribunal: *Kyriakos Karoulla (trading as Brockley's Rock) v HMRC*

A company applied for an appeal to be consolidated with two other connected appeals in a "missing trader" case concerned with alcoholic drinks. Although the judge did not accept all of HMRC's arguments in the case, he did agree that the facts were not sufficiently common between the "extant appeals" and the present one; HMRC said that the "extant appeals" were "trial ready", and adding the new case would lead to delay. There would not be significant overlap in witness evidence. The appellant's application for joinder was rejected.

First-Tier Tribunal (TC06553): *Morgan Drinks Ltd and another*

A case came before Judge Mosedale in which the appellant had been given an "unless order" to provide further witness evidence. This appeared to relate to the split between hot and cold takeaway food sold by a food outlet. The appellant did not attend a strike-out hearing and was not represented; his representative had notified the Tribunal a week earlier that he was too ill to attend but had not applied for a postponement, then informed the Tribunal the day before that he had resigned and would notify the client. No request for postponement was received from the taxpayer.

The judge was satisfied that the appellant was aware of the date of the hearing and it would not be contrary to the interests of justice for the hearing to proceed. She considered that the witness statement that had been submitted in response to the "unless order", while containing some new evidence of facts, was of so little relevance to the case that it did not meet the terms of the order. It was therefore arguable that the case was already struck out for failure to comply with the direction.

However, the judge went on to consider that the appeal had no reasonable prospect of success, and struck it out on those grounds as well.

First-Tier Tribunal (TC06581): *Footlong Subs Ltd*

A company (now in liquidation) made various appeals to the Tribunal during 2016 and 2017. Ten of these appeals were consolidated, and HMRC produced a detailed consolidated Statement of Case in relation to them. The appeals related to three excise duty assessments, three related penalty assessments, four VAT assessments and a decision to refuse approval to carry on the wholesale of alcohol. The total amount at issue was over £2.6m. The liquidator withdrew these appeals after being appointed, then later applied to reinstate them under rule 17 of the 2009 Tribunals Rules. HMRC objected to the reinstatement.

The judge noted that the company had another appeal in progress with the Tribunal in relation to a *Kittel* argument about input tax. That appeal was not affected by the current dispute.

HMRC argued that s.85(4) VATA 1994 meant that the Tribunal had no power to reinstate the appeal. The judge agreed: "S.85 is quite clear in its terms. If an appellant, or someone on its behalf, notifies HMRC that it desires not to proceed with an appeal and there is no objection from HMRC under s.85(4)(b), then the parties are deemed to have agreed that the appeal is [dismissed], with the same consequences as if the Tribunal

had determined it. This is the effect of s.85(4), read with s.85(1). The only caveat to this is where the appellant notifies HMRC within 30 days of the original notification (being the date of the deemed agreement) that it no longer wishes to withdraw. In that case the effect of s.85(2) is that the deemed Tribunal determination created by the withdrawal does not take effect. There is no power in s.85 for this 30 day time limit to be extended, and in my view rules 5 and 17 of the Tribunal Rules cannot supply such a power."

That was enough to dispose of the application, but as the exercise of the Tribunal's discretion to extend time and to reinstate (if it had had such discretion) had been fully argued, the judge gave her views. She considered that, in all the circumstances, she would not have refused to grant an extension of time, as the delay was not particularly long and the prejudice to HMRC (who had already produced a Statement of Case) was, on balance, outweighed by the prejudice to the taxpayer's shareholder. This was substantial, as she had been served with a personal liability notice for the amount owing.

On the other hand, the shareholder would still have the opportunity to challenge the personal liability notices on their merits, even though the appeals had been withdrawn. Her situation was therefore not a sufficient reason to allow reinstatement. The judge would therefore not have been minded to reinstate the appeals.

However, the reason for refusing the application was the lack of jurisdiction.

First-Tier Tribunal (TC06675): *OWD Ltd t/a Birmingham Cash & Carry (in liquidation)*

KPMG applied to the Tribunal for access to HMRC's statement of case and both parties' skeleton arguments in the *Hastings Insurance* case. The firm was not a party to the appeal nor did it represent any party, but requested the documents in order better to understand HMRC's arguments in the appeal which, they stated, were relevant to their arguments in a different case in which they were instructed. Both the appellants and HMRC objected to the documents being made available, and the question of whether they should nevertheless be effectively published came before Judge Greg Sinfield.

In the civil courts, Rule 5.4C of the Civil Procedure Rules ('CPR') provides that a person who is not a party to civil proceedings may obtain certain documents from the records of the court as of right and other documents with the permission of the court. The Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 ('FTT Rules') make no provision for granting a non-party access to documents. Accordingly, the FTT can only allow a non-party to have access to documents if it has an inherent jurisdiction to do so.

The judge considered that the principles of open justice were applicable to the FTT. Although the FTT Rules did not make any reference to allowing access, rule 14 allows prohibition of disclosure, which suggests that documents may be disclosed. Rule 32 provides that, subject to limited exceptions that were not relevant in *Hastings*, all hearings must be held in public. The judge considered that this confirmed that the principles of open justice applied.

HMRC's first objection was based on "taxpayer confidentiality" as required by s.18 of the Commissioners for Revenue and Customs Act 2005. The judge said this was misconceived, as it only prohibited an officer of HMRC from disclosing information. This was an application to the Tribunal. The second objection was that the FTT Rules made no provision for disclosure, but the judge had concluded that did not restrict its jurisdiction.

The appellant wanted the Tribunal to be sure that the applicant had a "legitimate purpose" in requesting access to the documents. The judge considered that involvement in related litigation was such a purpose.

The appellant also argued that the skeletons were in the end not particularly relevant because both counsel departed significantly from them in their oral submissions to the court. In effect, the appellant's point was that "open justice" applied to what happened at the hearing, not the skeletons submitted beforehand. The judge disagreed: the skeletons were deployed by the parties at an open hearing and were read by the Tribunal. The reasons for departing from them in oral submissions could be various, but not to provide access to those parts of the skeleton argument would mean that the member of the public would not have a full and complete understanding of the arguments deployed by that party.

Other reasons for restricting or redacting the disclosure were mainly rejected. The appellant's only success was to have the annexures to HMRC's statement of case (copies of decision letters that related to earlier appeals) excluded from the disclosure, because they were not relevant to the current decision and were not referred to by the Tribunal.

First-Tier Tribunal (TC06656): *Hastings Insurance Services Ltd*

6.8.6 Disputed ADR

A charity operated a number of supporter schemes. Income from some of these schemes was the subject of an appeal to the FTT (TC03992, 2014), where Judge Mosedale decided that the income constituted standard rated consideration for the right to partake in exclusive events and offers, rather than outside the scope donations. The treatment of other schemes was the subject of an Alternative Dispute Resolution meeting in July 2013. In her decision, Judge Mosedale commented that she considered the agreement that appeared to have been reached at the ADR was "wrong in law" and "inconsistent with HMRC's published position". HMRC wrote to the charity in January 2015, stating that they had not intended to agree to anything that was contrary to their published policy. In December 2015, they raised an assessment for 04/13 to 12/14 amounting to £65,268. The charity appealed to the Tribunal.

The parties agreed that the issues for the Tribunal were:

(1) whether the Tribunal has the jurisdiction to rule on the issues in dispute; and if so

(2) whether the paragraph about the Schemes which had been included in the document exchanged between the parties at the end of the ADR meeting had the meaning relied on by the Appellants, or the meaning relied on by HMRC;

(3) whether HMRC and the Appellant had concluded a contract, and in particular whether there was:

(a) agreement between the parties;

(b) an intention to create legal relations ("ITCLR"); and/or

(c) the omission of an essential term, so as to void the contract;

(4) if there was a contract between the parties, whether a unilateral mistake had been made by HMRC;

(5) if there was no unilateral mistake, whether HMRC had the power to make the agreement, or whether it was ultra vires.

Judge Anne Redston summarised her decision as follows:

(1) the Tribunal has jurisdiction to rule on the issues;

(2) the meaning of the words in the document exchanged between the parties is that advanced by the Appellant;

(3) the parties had concluded a contract;

(4) there was no unilateral mistake by HMRC; but

(5) the term of that contract which concerned the Schemes was void as ultra vires.

The charity had also applied for judicial review based on a legitimate expectation that it could rely on the terms of the contract it had concluded with HMRC. That application was stayed pending the outcome of the appeal, and would now proceed.

The disputed agreement was whether it was possible for the charity to separate out a "donation" from a "VATable payment for benefits" in taxing receipts, if it was not in practice possible to receive the benefits without making the donation as well. There was a dispute over the meaning of the following paragraph from the ADR agreement:

"From 1/4/13 where the value of the 'benefits' package for supporter schemes is identified and this is clearly stated (both in the application forms and on the website), this will be treated as the consideration. Any sums paid above the price charged for the benefits package is to be treated as a donation."

HMRC's counsel said that the word "value" in the first sentence meant "price". In the second sentence the words "price charged" implies that there will be a separate, expressly stated, price charged for the benefits package, and this in turn requires the Appellant's scheme literature to make clear that the benefits are available at a given price, in line with HMRC guidance. He submitted that the relevant background included para.5.14 of Public Notice 701/1, which was known to both parties to be HMRC's published guidance, and the HMRC witness evidence showed there had been no movement away from that guidance during the ADR meeting. Para.5.14 stated "If a patron or supporter pays more than the minimum amount you can treat the excess as a donation and outside the scope of VAT as long as the patron or supporter is aware that the scheme benefits are available for a given amount, and that anything in excess of that amount is a voluntary donation. This should be explicit in the patron or supporter scheme literature."

The judge agreed with the taxpayer and with Judge Mosedale that HMRC's interpretation of the agreement was wrong. It did not require that the benefits should be separately available for purchase.

She went on to consider the requirements for a contract, and concluded that there was one; it was not void for a mistake by HMRC. However, according to a range of precedents, HMRC could not be bound by an agreement that was ultra vires (beyond their legal powers to make). The judge distinguished between four types of agreement between HMRC and a taxpayer:

(1) those for which specific vires is given to HMRC by Parliament; the retail scheme considered in *GUS* is a good example;

(2) published extra-statutory concessions ("ESCs"). HMRC has the power under TMA s 1 to make such concessions, but only if it is not "in conflict with its statutory duty", which is to act in "the best manner of obtaining for the national exchequer the highest net return that is practicable", see *Wilkinson* at [45] and *Al Fayed* at [78];

(3) contracts between individual taxpayers and HMRC which are stated to be binding for a stated future period, or to be irrevocable. These purported contracts are ultra vires because they do not allow HMRC to take account of changes in the law or of the taxpayer's circumstances, see *Gresham* and *Al-Fayed*; and

(4) contracts between individual taxpayers and HMRC, which prevent HMRC from applying a taxing provision (other than in circumstances where the reason for that concession is for the purpose of HMRC's overall task of collecting taxes). Such contracts are ultra vires and a change of position by HMRC can only be challenged by judicial review, as Lord Templeman said in *Preston* at p 262.

The present arrangement fell within the fourth category. It could not bind HMRC, so the only way to object to them resiling from it was to apply for judicial review. The judge dismissed the appeal to the FTT.

First-Tier Tribunal (TC06719): *The Serpentine Trust Ltd*

6.9 Other administration issues

6.9.1 Draft legislation

The government has published an overview of draft legislation and measures in Finance Bill 2018-19. In relation to VAT, this includes:

VAT grouping eligibility criteria changes (covered in 6.1 above)

Late payment interest (covered in 6.3 above)

Late submission penalties (covered in 6.8 above)

VAT treatment of vouchers (covered in 2.12 above)

www.gov.uk/government/collections/finance-bill-2018-19

6.9.2 HMRC annual report and accounts 2017/18

HMRC's latest annual report and accounts show total revenues collected in 2017/18 of £605.8bn, an increase of £30.9bn (5.4%) over 2016/17. Compliance interventions yielded £30.3bn. These figures also show segmentation by "customer" groups: individuals; small businesses; wealthy individuals; mid-sized businesses; and large businesses.

VAT (£128.6bn, 21% of total revenue) increased by 3.4% due to higher receipts from oil, gas and mining, as well as from the leisure and business sectors.

An interesting detail is the analysis of the costs per pound of collection or payment. VAT costs 57p per £1 to collect, compared to 79p for income tax, 61p for corporation tax and 20p for National Insurance Contributions.

Another note shows the results of requests for reviews:

	2017/18	2016/17
VAT Penalty cases including default surcharge cases		
Dealt with in the year	17,700	15,753
Original decision upheld	5,354	5,440
Varied	1,957	2,025
Cancelled	10,379	8,288
Other	10	–
Percentage where original decision was upheld	30%	35%
All other reviews		
Dealt with in the year	16,414	13,826
Original decision upheld	11,314	8,795
Varied	472	495
Cancelled	4,613	4,528
Other	15	8
Percentage where original decision was upheld	69%	64%

The VAT figures are skewed by default surcharge, where a large number of automatically issued surcharge notices are cancelled when the trader puts forward an excuse.

Another interesting note relates to "remission of tax under care and management powers": *There was a bulk remission of £20 million relating to 12 VAT cases. These liabilities related to services provided by lawyers between 2009 and 2012. There was a clear legitimate expectation that at the time these supplies were exempt from VAT. Therefore recovery was not seen to be justified nor prudent to pursue on a value for money basis.*

www.gov.uk/government/publications/hmrc-annual-report-and-accounts-2017-to-2018

The National Audit Office report on the accounts is also available. It does not focus on any VAT issues this year.

www.nao.org.uk/press-release/her-majestys-revenue-customs-annual-accounts-2017-18/

6.9.3 HMRC's tax avoidance litigation in 2017/18

HMRC have published a list of cases decided during 2017/18 in which tax avoidance was involved. HMRC won 23 of the 24 decisions listed, with one producing a mixed result. None of the listed cases concerned VAT.

www.gov.uk/government/publications/tax-avoidance-litigation-decisions

6.9.4 Compliance check leaflets

HMRC have issued or updated three leaflets in the CC/FS series (compliance checks):

- CC/FS38a – general information about the "serial tax avoidance regime" (STAR);
- CC/FS1b – general information about checks by campaigns and projects;
- CC/FS1a – general information about compliance checks.

The third has been updated to give greater prominence to the paragraph about publicly-available 'open source' information HMRC may collect and use when dealing with compliance checks, as explained in the next item.

www.gov.uk/government/publications/compliance-checks-serial-tax-avoidance-regime-ccfs38a;
www.gov.uk/government/publications/general-information-about-checks-by-compliance-centres-ccfs1b;
www.gov.uk/government/publications/general-information-about-compliance-checks-ccfs1a

6.9.5 Criminal investigation procedures

HMRC's online guide to criminal investigation policy and procedures was updated in September 2018 with information on the type of publicly-available 'open source' material HMRC may monitor and retain.

HMRC may observe, monitor, record and retain internet data which is available to anyone. This is known as 'open source' material and includes:

- news reports
- internet sites
- Companies House and land registry records
- blogs and social networking sites where no privacy settings have been applied

www.gov.uk/government/publications/criminal-investigation

6.9.6 Directors banned over VAT scams

Two company directors who involved their companies in complex VAT scams, attempting to cheat HMRC of millions of pounds, have received lengthy director bans – of 13 and 15 years – following investigations by the Insolvency Service. The two directors, Nadeem Ahmed and Ulhaque Ahtamad, were involved in complex MTIC fraud schemes. Interestingly, Ahtamad, who was banned for the maximum period allowed by the law, was a director of Masstech Ltd, which visited the FTT twice in relation to different allegations of MTIC involvement; neither of them related to the fraud described in the banning order, which concerned carbon emissions allowances.

www.gov.uk/government/news/directors-banned-after-attempting-to-cheat-millions-in-complex-vat-scam

6.9.7 OTS further review

The Office of Tax Simplification has issued a "scoping document" for a second review into the life cycle of businesses, focusing on smaller enterprises and covering the following issues:

- the accessibility and clarity of guidance and support in relation to the process of setting up a business, including the information on gov.uk (linking to the OTS's wider work on guidance), including issues arising from the interaction between an individual's personal and business affairs;
- how a business works out and administers its taxes (taking into account matters such as Making Tax Digital, record-keeping, filing returns, understanding allowable deductions);
- sources of error and unnecessary complexity, and ways these could be eased or mitigated;
- the way the tax system handles unprofitable years or shorter-term cash flow issues (for example through the loss rules and time to pay arrangements) and the extent to which the tax system helps businesses manage the cash flow demands of paying tax more generally;
- the impact of taking on the businesses' first employee and subsequent employees (with regard to payroll taxes, completing P11Ds in relation to benefits, employment allowance);

- the impact and any distortive effect of thresholds (recognising the significance of issues of this kind that the OTS drew attention to its 2017 VAT report);
- issues arising in relation to relevant tax reliefs such as R&D tax credits;
- making overseas sales or purchasing goods or services from abroad for the first time;
- issues arising as the business develops, for example moving to new premises.

www.gov.uk/government/publications/ots-scoping-document-for-further-review-of-business-life-cycle

6.9.8 Articles

In an article in *Taxation*, Andrew Hubbard examines the concept of ‘blockchain’ and how it might be used to record VAT transactions.

Taxation, 16 August 2018